Capital strength: the common equity tier 1 fully loaded ratio stood at 11.4% at 2015 year-end.

A capital increase of €1,607 million was implemented in April 2015.

Capital management

Capital management is the result of an ongoing capital planning process. This process considers expected economic, regulatory and industry performance, as well as adverse scenarios. It factors in projected capital consumption in the various businesses under a number of scenarios as well as market conditions that may determine the efficacy of measures that may be taken. The process is conducted in line with the bank's strategic goals and the pursuit of attractive returns for shareholders, while always ensuring that own funds are sufficient to attend to the risks inherent in the business.

In terms of capital management, as a general policy, the bank aims to ensure the adequacy of the available capital to the organisation-wide level of risks incurred.

The group follows the guidelines established by the Basel Capital Accord as a basic principle which closely ties the requirements of banks' own funds to the risks that are actually incurred, based on internal risk measurement models which must first be independently assessed.

The group has been authorised by the Supervisor to use the majority of its internal models to calculate regulatory capital requirements. Based on the risk measures that provide these new methodologies, the group has a comprehensive risk measurement model under an internal measurement unit in terms of assigned capital.

The capital mapping by risk type at 2015 year-end is shown in Table T14.

%

T14

	2015
Credit risk	80
Structural risk	7
Operational risk	7
Market risk	2
Other	4
Total	**100**

The risk assessment in terms of the necessary contributed capital allows it to be compared with the profitability obtained from operational and customer levels to the business unit level. The group has implemented a system to analyse return adjusted to risk (RaRoC) provided by this assessment, allowing homogeneous comparisons to be made and enabling their inclusion within the price fixing process of operations.

The group has a complex measurement system in place for each type of risk faced by the bank and some integration methodologies for each of these risks, from an overall point of view and taking into account all possible stress scenarios and corresponding financial planning. These risk assessment systems have been adapted to the corresponding best practices.

The group carries out an annual internal capital assessment process, envisioned in the new framework set out by the NBCA, and more specifically in the regulations on the adequacy of regulatory own funds, which is reported to the Supervisor.

This process is based on a wide inventory of previously identified risks and on the qualitative internal assessment of policies, procedures, risk acceptance, measurement and control systems and their corresponding mitigation techniques.

A global quantitative assessment is subsequently carried out on the necessary capital based on internal parameters using models used by the bank (for example, borrowers' credit rating systems in the form of ratings and scorings), as well as other internal estimates suited to each type of risk. The assessments of each risk type are subsequently included and a figure is set using an indicator in terms of allocated capital. Furthermore, the business and financial plans of the bank and its stress tests are taken into account in order to verify whether the business trends and possible adverse scenarios may endanger the bank's level of solvency by comparing it with available own funds.*

For further information on capital management, refer to the document published annually containing information with prudential relevance, which is available on the bank's website (www.grupobancosabadell.com) under the section Shareholder and Investor Information/Financial Information.

* **For more details see the consolidated financial statements (note 4).**

Qualifying capital and capital ratios

Regulations

On 1 January 2014, the new regulatory framework known as Basel III entered into force. It will be implemented in phases (phase-in model) until 1 January 2019. This new framework is made up of Directive 2013/36/EU, generally known as CRD-IV, and Regulation (EU) 575/2013, generally known as the CRR, which regulates minimum own funds that credit institutions need to maintain, both at an individual and a consolidated level, and the way in which these own funds are to be calculated, as well as different internal capital assessment processes which should be carried out and the public information to be disclosed to the market.

As a Spanish credit institution, the group is subject to Directive CRD-IV, which has been implemented in Spain through various standards and regulations (for further details of these regulations, see Note 5 of the consolidated annual accounts for 2015).

In accordance with the requirements established in the CRR Regulation, credit institutions should have a total capital ratio of 8% at all times. However, it should be noted that Regulators may exercise their powers under the new regulatory framework and require banks to have additional levels of capital.

It should be noted that in 2015, new regulations have been published which supplement the CRR Regulation in matters related to own funds, liquidity, pillar I risks and capital requirements.

Ratios

At 31 December 2015, the group's qualifying capital amounted to €11,417.4 million, entailing a surplus of €4,315.9 million, as shown in table T15.

€ million

T15

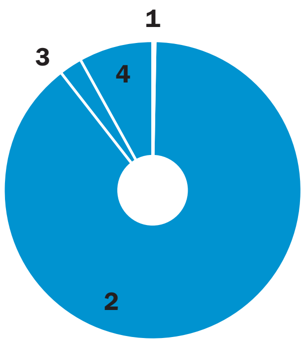
	2014	2015	% 15/14
Capital	503.1	679.9	35.1
Reserves	8,855.7	11,428.7	29.1
Bonds convertible into shares	—	—	—
Non-controlling interests	28.9	24.3	(15.9)
Deductions	(684.5)	(1,923.5)	181.0
Recursos core capital (Common equity Tier 1)	**8,703.2**	**10,209.4**	**17.3**
Core capital (Common equity Tier 1) (%)	11.7	11.5	—
Preferential shares, convertible bonds and deductions	—	—	—
Tier 1 funds	**8,703.2**	**10,209.5**	**17.3**
Tier I (%)	11.7	11.5	—
Tier 2 funds	**838.7**	**1,207.9**	**44.0**
Tier II (%)	1.1	1.4	—
Capital base	**9,541.9**	**11,417.4**	**19.7**
Minimum eligible funds	5,953.4	7,101.5	19.3
Surplus funds	**3,588.5**	**4,315.9**	**20.3**
Total capital ratio (BIS Ratio) (%)	**12.8**	**12.9**	**0.31**
Risk Weighted Assets (RWAs)	**74,417.8**	**88,768.7**	**19.3**

Core capital own funds make up 89.4% of qualifying capital.

Under Basel III, Tier 1 comprises core capital, convertible bonds and deductions of intangible assets of the same value.

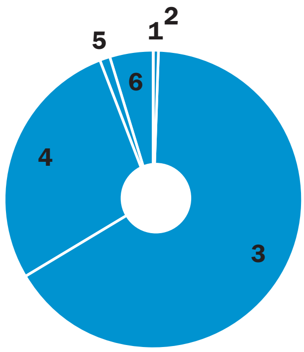
Tier 2 funds, which contribute 10.6% of the BIS ratio, are comprised mainly of subordinated debt and general provisions (with regulatory qualifying capital limits), as well as the remaining required deductions.

The distribution of own funds requirements by risk type and geographical location at 2015 year-end is shown in figure G12 y G13.



G12 Own resources requirements per risk type 31.12.2015 (%)

1	Credit valuation adjustment risk	0.3 %
2	Credit risk	89.2 %
3	Market risk	2.6 %
4	Operational risk	7.9 %



G13 Own resources requirements per geography 31.12.2015 (%)

1	Rest of OECD	0.1 %
2	Rest of the world	0.6 %
3	Spain	65.8 %
4	Rest of EU	27.8 %
5	Latin America	1.1 %
6	North America	4.6 %

Capital-raising issues

Over the last five years, the bank has increased its capital base through issuances which qualify as Tier 1 capital, which have allowed the capital to increase by over €6.6 billion euros. These include a capital increase with pre-emptive subscription rights of €1,607 million carried out in April 2015, as a result of the acquisition of TSB (T16).

During 2015, mandatorily convertible subordinated bonds have been converted into shares valued at €789 million, which have not impacted the capital ratios.

The change in phased-in common equity tier 1 (CET1) for 2014 (€8,703 million) and 2015 (€10,209 million) is mainly due to the aforementioned capital increase, the retained profit for the year and larger deductions as a consequence of the acquisition of TSB.

Risk weighted assets (RWA) for the year amount to €88,768.7 million, a 19.28% increase compared with the previous year due mainly to the acquisition of TSB and, to a lesser extent, to changes in deferred tax assets (DTA).

All of these capital-raising issues and events have allowed Banco Sabadell to reach a 11.5% phased-in common equity tier 1 (CET1) in December 2015, and a total capital ratio of 12.9%, amply exceeding the standards required by the regulatory framework.

In 2015 the bank received a notification from the European Central Bank with its decision on prudential minimum requirements applicable to the bank, after the supervisory review and evaluation process (SREP), stating that Banco Sabadell must maintain a common equity tier 1 (CET1) ratio of 9.25% of phased-in regulatory capital. This requirement includes the minimum required by Pillar 1 (4.50%) and Pillar 2 (4.75%), including the capital conservation buffer.

CET1 phased-in

+11.5%

Based on the note published by the Bank of Spain on 28 December 2015, it has set a countercyclical capital buffer of 0% for 2016 and a prudential capital buffer of 0% for systemically important institutions, which is applicable to Banco Sabadell (despite it being considered to be an O-SII - other systemically important institution).

€ million

T16

		Amount	Impact on capital
February 2011	Debt-for-equity swap (equity through accelerated book building and repurchase of preferential and subordinated shares)	411	+68 bp of *core tier* I
February 2012	Preferential shares swapped for ordinary shares	785	+131 bp of *core tier* I
March 2012	Capital increase	903	+161 bp of *core tier* I
July 2012	Preferential debt instruments and Banco CAM subordinated shares swapped for ordinary shares	1,404	+186 bp of *core tier* I
September 2013	Accelerated book building and capital increase with subscription rights	1,383	+178 bp of *core tier* I
October 2013	Issuance of mandatorily convertible subordinated bonds for hybrid swap of B. Gallego	122	+17 bp of *core tier* I
April 2015	Capital increase with pre-emptive subscription right - TSB	1,607	+181 bp of *core tier* I

Note: The impact on capital (in basis points) is calculated using the year-end data for each year; these figures have varied significantly due to the increase in the scope of consolidation of the group in the last few years.