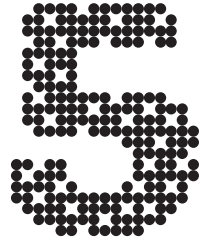


Risks



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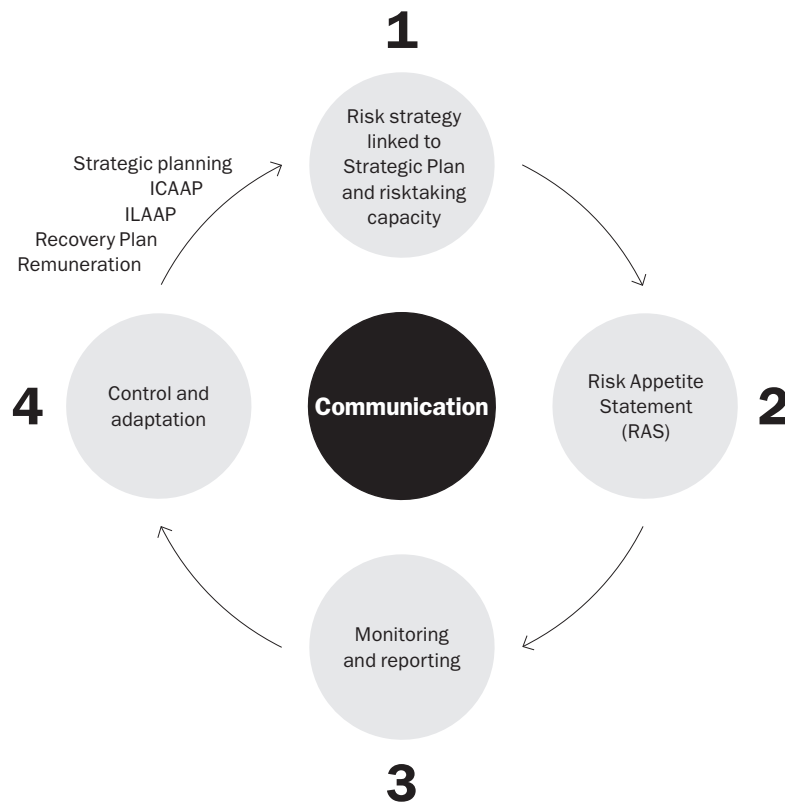
In 2022, Banco Sabadell Group continued to strengthen its Global Risk Framework by making improvements in line with best practices in the financial sector.

The Group continues to have a medium-low risk profile, in accordance with the risk appetite defined by the Board of Directors.

The Group's risk strategy is fully implemented and linked to the Strategic Plan and the Group's risk-taking

capacity, articulated through the Risk Appetite Statement (RAS), under which all material risks are monitored, tracked and reported, and the necessary control and adaptation systems are in place to ensure compliance:

Strategic risk management and control processes



Main 2022 milestones in risk management and control

The most salient aspects concerning the management of the first-tier risks identified in the Banco Sabadell Group risk taxonomy and concerning the actions taken in this regard in 2022 are set out below:

Strategic risk

Definition:

the risk of losses (or negative impacts in general) materialising as a result of strategic decisions or their subsequent implementation. It also includes the inability to adapt the Group's business model to changes in the environment in which it operates.

Key 2022 milestones:

(i) Strategy and reputation

- Supporting customers in the transition to a more digital model and in the adoption of good practices and initiatives in terms of greater consumer protection.
- The Bank has finished implementing the Efficiency Plan, with a significant cost reduction that has contributed to an improvement in the cost-to-income ratio and levels of profitability in excess of the target disclosed to the market for 2023.
- The performance of the Bank's business and its results are reflected in various reputational indicators, including the stock market performance, which is above the average of Spanish banks.

(ii) TSB

- Throughout 2022, TSB has been completing the actions of its Strategic Business Plan to improve profitability and efficiency.

(iii) Improvement in the capital position

- The CET1 ratio improved to 12.55% in fully-loaded terms as at 2022 year-end, driven significantly by organic capital creation. Generalised fulfilment of regulatory capital requirements.
- Total capital remained stable, ending 2022 at 17.02%, and the leverage ratio decreased from 5.81 to 4.59% year-on-year (in fully-loaded terms).

(iv) Profitability

- The Group's net profit amounted to 859 million euros as at the end of 2022. It is particularly worth mentioning the good performance of core results (net interest income + fees and commissions – recurrent costs), which showed a 26.3% increase year-on-year, as a result of the good performance of net interest income and the growth in fees and commissions, as well as the cost reduction.
- The Group achieved a year-end ROTE of 7.8%, exceeding the May 2021 guidance of ROTE >6% by 2023.

Credit risk

Definition:

Credit risk refers to the risk of losses being incurred as a result of borrowers' failure to fulfil their payment obligations, or of losses in value taking place due simply to the deterioration of borrower quality.

Key 2022 milestones:

(i) Non-performing assets

- Decrease in the NPL ratio in the year, from 3.7% to 3.4%, due to a reduction in stage 3 assets as a result of an improved credit quality.

(ii) Concentration

- From a sectoral point of view, the loan portfolio is diversified and has limited exposure to the sectors most sensitive to the current environment and shows a downward trend.
- Similarly, in terms of individual concentration, the metrics relating to concentration of large exposures do show a slight upward trend but nevertheless remain within the target level. The credit ratings of top segments improve significantly as more recent balance sheets with a more diluted impact of the health crisis are introduced.
- Geographically speaking, the portfolio is positioned in the most dynamic regions, both in Spain and worldwide. International exposure accounts for 36% of the loan book.

(iii) Lending performance

- Performing loans continue to increase year-on-year in all geographies, factoring out the impact of the performance of currencies, with annual growth figures of 1.7% in Spain, 3.3% in the UK (TSB) and 1.4% in Mexico.
- In Spain, the year-on-year growth is primarily driven by loans to individuals (the increase in the mortgage portfolio is noteworthy) and by business loans.

(iv) TSB lending performance

- In TSB, at a constant exchange rate, annual growth was 3.3%, supported by the positive evolution of the mortgage book.

Financial risk

Definition:

Possibility of obtaining inadequate returns or having insufficient levels of liquidity that prevent an institution from meeting future requirements and expectations.

Key 2022 milestones:

(i) Robust liquidity position

- Solid liquidity position, where the LCR (Liquidity Coverage Ratio) stands at 234% at the Group level (196% at TSB LMU and 270% at Banco Sabadell Spain) and the NSFR (Net Stable Funding Ratio) stands at 138% at the Group level (151% at TSB LMU and 132% at Banco Sabadell Spain) both at 2022 year-end, after having optimised the funding sources with access to long-term financing, having borrowed 22 billion euros from the ECB and 6,201 million euros from the Bank of England, as well as increasing the funding gap in 2022.
- The loan-to-deposit (LtD) ratio as at 2022 year-end was 95.6% with a balanced retail funding structure.
- Moreover, Banco Sabadell has fulfilled the capital markets issuance plan, which it had set for itself for 2022, with strong investor appetite. This allowed it to optimise the associated financing costs.

(ii) Structural interest rate risk

- The Institution continued to accommodate higher levels of new fixed rate lending in an environment of higher interest rates in all relevant currencies, where in particular the euro interest rates went from negative to positive. The variable rate loan book has gradually included the revaluation of benchmark indices (mainly the 12-month Euribor). On the liabilities side, there is a customer deposit base, predominantly comprising sight deposit accounts.

Operational risk

Operational risk is defined as the risk of incurring losses due to inadequacies or failures of processes, staff or internal systems or due to external events.

Operational risk remains a material risk for the Group, with impacts that, although acceptable, have increased in recent years due to the problems associated with conduct risk. The current scenario of high awareness and increased regulatory pressure, aimed especially at providing greater protection for consumers and vulnerable customers, places conduct risks as the main focus of attention. Its current relevance and the expectation that this scenario will likely continue requires the focus to remain fixed on these risks, monitoring their evolution and adequately monitoring the planned mitigation measures.

The focus remains on complaints related to floor clauses, mortgage application and arrangement fees, high interest charges associated with revolving credit cards and appropriate assistance for vulnerable customers, especially in the UK, given the demanding regulatory environment. The creation of the new financial customer protection authority planned for the first few months of 2023 could have an impact on the complaints received, as it facilitates this process. The materialisation of conduct risk involves a potential reputational risk for the Institution, although it remains in line with the sector.

Compliance risk

Compliance risk, which is part of operational risk, is defined as the risk of incurring legal or administrative penalties, significant financial losses or reputational damage as a result of an infringement of laws, regulations, internal rules or codes of conduct applicable to the banking business, minimising the possibility of any infringements occurring and ensuring that any that do occur are identified, reported and dealt with diligently.

Main milestones of 2022:

(i) Continue to promote a culture of ethics and compliance among employees

Compliance has developed a training model that contributes to:

- (i) learning for the compliance team, as its employees can obtain official compliance certifications and participate in courses and events.
- (ii) learning for the entire Institution, through training courses aimed at the branch network and other divisions, as well as Senior Management, and the design of compliance courses and follow-up on their completion.
- (iii) the compliance culture, in relation to which it is worth highlighting: (a) the role of the Regulatory School, which symbolises a change of paradigm, a friendly, pleasant and very graphic space in which to convey mandatory and regulatory standards, (b) the daily

distribution to all employees who are part of Compliance of relevant news that may be of interest in their areas of work, (c) the weekly sending of communications to all the Bank's employees by Human Resources, which include relevant aspects related to Compliance, and (d) the quarterly sending of a newsletter from Risk Control and Regulation with relevant news on compliance.

(ii) Planning and monitoring

The Compliance function establishes, applying the principle of proportionality in accordance with the nature, volume and complexity of its activities, a compliance programme which includes a detailed schedule of its activities. This programme covers all services provided and activities carried out by the Institution and defines its priorities based on the assessment of compliance risk and in coordination with the Risk Control function.

In order to guarantee the effectiveness of the Programme, Monitoring Plans have been drawn up, which include two types of information: those that illustrate the activities carried out from a quantitative perspective, with KPIs linked to the operational execution of the programme, and those that deal with qualitative variables.

(iii) Relationship with supervisors

Management maintains constant interaction with the main authorities supervising the Bank's activities.

All requests received from the various supervisors have been dealt with within the established deadlines.

(iv) Evolution of the Senior Management reporting model

Compliance has adapted its Senior Management reporting model during 2022. To this end, the number of reports has been increased, as has their frequency.

For more details on the corporate risk culture, the global risk framework and the overall organisation of the risk function, as well as the main risks, see Note 4 to the consolidated annual financial statements for 2022.