

Risks



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Risks

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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 remediation systems are in place to ensure compliance therewith:

5.1 Strategic risk management and control processes



5.2 Main milestones achieved in 2024 in relation to risk management and control

The most salient aspects concerning the management of the first-tier risks identified in Banco Sabadell Group's risk taxonomy and concerning the actions taken in this regard in 2024 are set out below:

Strategic risk

Definition: the risk of losses (or negative impacts in general) materialising as a result of making strategic decisions or of 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 milestones in 2024:

(1) Strategy and reputation

- Although there were macroeconomic factors at play in 2024 that threatened to have a negative impact on the Bank's profitability, those threats did not materialise as (i) inflation has stabilised, (ii) global growth was better than expected, (iii) the interest rate cutting cycle began, and (iv) there were signs of improvement in both demand for credit and economic activity, with a better outlook for Spain. Similarly, the successful implementation of levers by the Institution, the stronger credit profile and the delivery of record-breaking results are all reflected in several reputational indicators, for example, (i) the improved outlooks of investors and rating agencies with regard to the Institution and (ii) solid performance of the Institution's shares, which appreciated by 68.64% over the year.
- The Group is exposed to reputational risk inherent in the sector in which it operates, characterised by significant visibility among customers and the general public.
- In recent years, a series of events has led to a change in the relationship model of financial institutions with their customers and investors, with a shift towards reduced face-to-face service in retail banking which has accentuated the materiality of this risk.
- Banco Sabadell Group bases its business model on corporate values such as ethics, professionalism, rigour, transparency, quality and, in general, long-term business relationships that are beneficial to both the Group and its counterparties.

(2) Capital position

- The CET1 ratio stood at 13.02% as at 2024 year-end, particularly driven by organic capital generation. Regulatory requirements in relation to capital are generally being met.
- The Total Capital ratio has improved, ending 2024 at 17.60%.
- As at the end of 2024, the leverage ratio stood at 5.20%, representing an increase of 12 basis points compared to 2023.

(3) Profitability

- In 2024, global growth was better than expected, inflation stabilised and the central banks began to cut interest rates. Demand for credit and economic activity also showed signs of improvement.
- With regard to the tender offer launched by Banco Bilbao Vizcaya Argentaria (BBVA) in May 2024 for the acquisition of 100% of Banco Sabadell's share capital, to date, there has been no indication that the risks posed by this situation will materialise.
- The geopolitical environment appears somewhat unstable due to the conflicts in Ukraine and in the Middle East, and because of the result of the presidential election in the United States, which could exacerbate trade and/or financial tensions at a global level.
- In 2024, the Institution successfully delivered on a number of strategic initiatives introducing, among other things, a series of improvements that have helped to reduce its cost of risk, such as the improvements made to its risk acceptance models for both companies and individuals.
- Against this backdrop, in year-on-year terms, Banco Sabadell has significantly increased its net earnings, driven by (i) sound core results, (ii) increased net interest income, (iii) reduced cost of risk, (iv) an active and growing commercial dynamic, and (v) contained growth of costs.
- All these aspects are clearly reflected in the Group's improved profitability, shown by an improvement of its ROTE, which increased from 11.50% as at 31 December 2023 to 14.93% as at 31 December 2024.

Credit risk

Definition: risk of incurring losses as a result of borrowers failing to fulfil their payment obligations, or of losses in value materialising due simply to the deterioration of borrowers' credit quality.

Key milestones in 2024:

(1) Non-performing assets

- During 2024, non-performing assets were reduced by 1,068 million euros. The NPL ratio for the year stands at 2.84%.

(2) Concentration

- From a sectoral point of view, the loan portfolio is diversified and has limited exposure to the sectors most sensitive to the current economic environment.
- Similarly, in terms of individual concentration, the risk metrics relating to concentration of large exposures showed a slight downward trend and remained within the appetite level. The credit rating of large exposures also improved over the year.
- Geographically speaking, the portfolio is positioned in the most dynamic regions, both in Spain and worldwide. International exposures account for 37% of the loan book.

(3) Lending performance

- Gross performing loans ended the year 2024 with a balance of 156,913 million euros, increasing by 4.7% year-on-year.

- In Spain, gross performing loans in year-on-year terms posted a 5.3% improvement, driven by the increase in lending to corporates and individuals, as well as the healthy performance of foreign branches.

(4) TSB lending performance

- In TSB, at a constant exchange rate, gross performing loans remained stable.

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 milestones in 2024:

(1) Sound liquidity position

- Sound liquidity position in which the Liquidity Coverage Ratio (LCR) stands at 210% at the Group level (200% at TSB LMU and 248% at Banco Sabadell Spain) and the Net Stable Funding Ratio (NSFR) stands at 142% at the Group level (153% at TSB LMU and 137% at Banco Sabadell Spain), both as at 2024 year-end, having repaid the remaining 5 billion euros of the amount drawn down from the ECB's TLTRO III facility, and having optimised long-term funding of up to 1.67 billion euros secured with the Bank of England.
- The Loan-to-Deposit ratio (LtD) as at the end of 2024 was 93.2%, with a balanced retail funding structure.
- Moreover, Banco Sabadell has fulfilled the capital markets issuance plan that it had set itself for 2024, with strong investor appetite, allowing it to optimise the associated funding costs.

(2) Structural interest rate risk

- In 2024, the Institution's loan book continued to trend towards a higher proportion of fixed-rate transactions, mainly mortgages and business loans, while on the liabilities side, balances of interest-bearing demand deposits (mainly of wholesale customers) and term deposits have increased, contrasting with a reduction in the balance of non-interest-bearing demand deposits, whilst costs have been kept at low levels relative to interest rate trends over the year. In addition, other balance sheet variations in 2024 included the increase in the fixed-income portfolio on the asset side, which acts as a natural balance sheet management and coverage lever, and the implementation of management actions to defend net interest income amidst interest rate cuts.

Operational risk

Definition: risk of incurring losses due to inadequate or failed internal processes, people and systems or due to external events. This definition includes but is not limited to compliance risk, model risk and Information and Communications Technology (ICT) risk and excludes strategic risk and reputational risk.

Key milestones in 2024:

- Operational risk remains a significant risk for the Group, with impacts that can be absorbed in the normal course of the business.
- The current situation of high awareness and increased regulatory pressure, aimed especially at providing greater protection for consumers and vulnerable customers, requires conduct risks to be the main focus of attention. Its current materiality and the expectation that this situation will likely continue requires the focus to remain fixed on these risks, tracking their evolution and adequately monitoring the planned mitigation measures.
- The focus remains on complaints related to floor clauses, mortgage application and arrangement fees, interest rates connected 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, which is not yet in operation, could have an impact on the complaints received, as it facilitates this process. The materialisation of conduct risks involves a potential reputational risk for the Institution, although it remains in line with the sector.

Compliance risk

Definition: risk of incurring legal or regulatory sanctions, material financial loss or loss to reputation as a result of failing to comply with laws, regulations, internal rules and codes of conduct applicable to the Group's activities.

In accordance with Banco Sabadell's Compliance Policy and observing the EBA's Guidelines on Internal Governance, a Compliance Programme is drawn up, applying the principle of proportionality according to the nature, volume and complexity of activities, containing a detailed schedule of activities, including the review of policies and procedures, risk assessment, control plans and staff training in relation to compliance. This programme covers all services provided and activities carried out by Compliance and defines its priorities based on the risk assessment, in coordination with the Risk Control function. Monitoring exercises are conducted and regular reports on them are made to the Group's governing bodies in order to identify any deviations and resolve them quickly and effectively.

In 2024, efforts continued to be made to promote a culture of ethics and compliance among employees, interacting on an ongoing basis with the main supervisory authorities in connection with the Bank's compliance activity.

Priorities in 2025:

- Ensure the continuing development of the supervision model for subsidiaries and foreign branches in order to reinforce a homogeneous and grouped view of the entities under the scope of supervision.
- Continue to promote the plan to digitalise processes in the area of Anti-Money Laundering and Countering the Financing of Terrorism.
- Develop monitoring metrics to prevent compliance risks at the level of the governing bodies.
- Integrate research and the use of artificial intelligence models in the management and prevention of customer data protection risks.