RISKS

IDENTIFICATION, MEASUREMENT, MANAGEMENT, CONTROL AND INTERNAL COMMUNICATION OF RISKS TO WHICH ARE OR MAY BE EXPOSED THE ENTITY.

Our risk management and control model is underpinned by a set of common principles together with a risk culture embedded throughout the Group, a solid governance structure and advanced risk management processes and tools.

Our risk principles are mandatory and must be followed at all times. They take into account regulatory requirements and market best practices. They are the following:

1. **A strong risk culture (Risk Pro),** as part of 'The Santander Way', which is followed by all employees, covers all risks and promotes socially responsible management that contributes to Santander's long-term sustainability.
2. **All employees are responsible for managing risk.** They must be aware of, and understand, the risks generated in their day-to-day activities, avoiding risks where the impacts are unknown or exceed the Group's risk appetite limits.
3. **Engagement of senior management,** ensuring consistent management and control of risk through their conduct, actions and communication. They also promote our risk culture and assess its degree of implementation, overseeing that the risk profile is kept within the levels defined by our risk appetite.
4. **Independence of the risk management and control functions,** consistent with our three lines of defence model.
5. **A forward-looking and comprehensive approach to risk management and control** across all businesses and risk types
6. **Complete and timely information management,** enabling risks to be appropriately identified, assessed, managed and reported to the corresponding level.

These principles, combined with a series of tools and processes that are embedded in the Group's strategic planning, such as our risk appetite statement, risk profile assessment, scenario analysis and our risk reporting structure, annual planning and budget process, provide a holistic control structure for the entire Group.

1. Risk factors

Santander has established the following key risk types in its risk framework:

- Credit risk: is the risk of financial loss arising from the default or credit quality deterioration of a customer or other third party, to which Santander has either directly provided credit or for which it has assumed a contractual obligation

- Market risk: is the risk incurred as a result of changes in market factors that affect the value of positions in the trading book.

- Liquidity risk: is the risk that Santander does not have the liquid financial resources to meet its obligations when they fall due, or can only obtain them at high cost.

- Structural risk: is the risk arising from the management of different balance sheet items, not only in the banking book but also in relation to insurance and pension activities. It includes the risk of Santander not having an adequate amount or quality of capital to meet its internal business objectives, regulatory requirements or market expectations.

- Operational risk: is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including conduct risk.

- Regulatory Compliance risk: risk of non-compliance with legal and regulatory requirements as well as supervisors expectations, which may result in legal or regulatory sanctions, including fines or other financial implications.

- Model risk: is the risk of loss arising from inaccurate predictions, causing a sub-optimal decision, or from a model being implemented or used inappropriately.

- Reputational Risk: the risk of current or potential negative economic impact to the bank due to damage to its perception on the part of employees, customers, shareholders/investors and the wider community.

- Strategic Risk: is the risk of loss or damage arising from strategic decisions or their poor implementation that impact the medium and long term interests of our key stakeholders, or from an inability to adapt to external developments.

In addition, climate-change related risk drivers – whether physical or transition-led, have been identified as factors that could aggravate the existing risks in the medium and long term.

The classification of risks is critical to ensure an effective risk management and control. All identified risks should be therefore referenced to the aforementioned risk categories in order to organise their management, control and related information.

2. Risk governance

The Group has a robust risk governance structure, aimed at ensuring the effective control of its risk profile in accordance with the risk appetite defined by the board of directors.

This governance structure is underpinned by the distribution of roles among the three lines of defence, a robust structure of committees and a strong relationship between the Group and its subsidiaries. All supported by our Group-wide risk culture, Risk Pro.

The **Group Chief Risk Officer** (Group CRO) is responsible for the oversight of all risks and for challenging and advising the business lines on how they manage risks, with direct access and reporting to the board risk committee as well as to the board of directors.

Risk appetite and structure of limits

At Santander, we define risk appetite as the amount and type of risks that are considered prudent to assume for implementing our business strategy, so that the Group can maintain its ordinary activity in the event of unexpected circumstances. When establishing the risk appetite, adverse scenarios that could have a negative impact on capital and liquidity levels, profitability and/or the share price are taken into account.

The risk appetite statement (RAS) is annually set by the board for the entire Group. Additionally, the boards of our subsidiaries also set their own risk appetite on an annual basis, aligned and embedded within the Group's consolidated statement.

Each subsidiary's statement is then further cascaded down in the form of management limits and policies by risk type, portfolio and activity segment, within the common standards defined by the Group.

Risk Profile Assessment (RPA)

The Group carries out identification and assessment tests on the different risks that it is exposed to, involving all the lines of defence, establishing management standards that meet regulatory requirements and reflect best practices in the market and reinforce our risk culture.

The results of the risk identification and assessment (RIA) exercises are integrated to evaluate the Group risk profile through the risk profile assessment (RPA). This exercise analyses the development of risks and identifies areas for improvement:

- **Risk performance**, enabling the understanding of residual risk by risk type through a set of metrics and indicators calibrated using international standards.
- **Control environment assessment**, measuring the degree of implementation of the target operating model, as part of our advanced risk management.

- **Forward-looking analysis**, based on stress metrics and identification and/or assessment of the main threats to the strategic plan (Top risks), enabling specific action plans to be put in place to mitigate potential impacts.

Scenario Analysis

Another fundamental tool that is used by the Group to ensure robust risk management and control is the analysis of potential impacts triggered by different scenarios related to the environment in which the Group operates. These scenarios are expressed both in terms of macroeconomic variables, as well as other variables that may affect our risk profile.

This "scenario analysis" is a robust and useful tool for risk management at all levels. It enables the Group to assess its resilience under stressed conditions and the identification of possible mitigating actions to be implemented in case the projected scenarios start to materialise. The objective is to reinforce the stability of income, capital and liquidity.

In this respect, the role of our Research and Public Policy team in terms of the generation of the different scenarios as well as the governance and control processes around these exercises, including the review by senior management as well as the three lines of defence are fundamental.

The robustness and consistency of the scenario analysis exercises are based on the following pillars:

- Development and integration of models that estimate the future performance of metrics, such as credit losses.

- Challenge and backtesting of model results.

- Inclusion of expert judgement and expert knowledge of our portfolios.

- Robust governance covering models, scenarios, assumptions and results, as well as management mitigation actions.

The application of these pillars in the European Banking Authority (EBA) stress test exercise, has enabled Santander to comfortably meet the defined quantitative and qualitative requirements, contributing to the excellent results obtained by the Group.

Reporting

Our reporting model continues to evolve and we continue to simplify and optimise our processes, controls and the communication to senior management. The enterprise wide view of all risks is regularly consolidated allowing the Group's senior management to assess the risk profile and take actions needed.

Our risk reporting taxonomy contains three types of reports that are released on a monthly basis: the Group risk report (which is distributed to senior management), the subsidiaries risk reports, and the reports on each of the risk factors identified in the Group's risk framework.

This taxonomy is characterised by the following:

- All risk factors included in the Group's risk framework are covered.

- Balance between data, analysis and qualitative comments is maintained throughout the reports, including forward-looking measures, risk appetite information, limits and emerging risks.

- The holistic view is combined with a deeperanalysis of each risk factor and geographic area and region.

- A homogenous structure and criteria. A consolidated view is provided to enable the analysis of all risks based on common definitions.

- All the metrics reported follow RDA criteria, ensuring the quality and consistency of the data included in all risk reports.

For further details of the issues discussed above, see the Risk management and control chapter of the annual report. Likewise, the evolution of the risk profile is available on a regular basis in the quarterly financial reports (http://www.santander.com).