

Report of the Directors of Banco Santander, S.A. on the Common Draft Terms of Merger

BETWEEN

BANCO SANTANDER, S.A.

(as absorbing company),

AND

BANCO ESPAÑOL DE CRÉDITO, S.A.

(as absorbed company)

Santander, 18 February 2013

1. INTRODUCTION

The Boards of Directors of Banco Santander, S.A. (“**Santander**”) and Banco Español de Crédito, S.A. (“**Banesto**”), at their respective meetings held on 9 January 2013, prepared and signed common draft terms of merger (*proyecto común de fusión*) regarding the merger by absorption (the “**Merger**”) of Banesto by Santander (the “**Draft Terms of Merger**” or the “**Draft Terms**”).

The Draft Terms of Merger were prepared and approved by the Boards of Directors of such companies and signed by their members (with such exceptions as are indicated therein) in accordance with the provisions of section 30 *et seq.* of Law 3/2009 of 3 April on Structural Modifications of Mercantile Companies (the “**Structural Modifications Act**”). The Draft Terms of Merger have been included in Santander’s corporate website (www.santander.com) since 9 January 2013 and in Banesto’s corporate website (www.banesto.es/webcorporativa) since 10 January 2013, from which they can be downloaded and printed. The fact of the inclusions and the dates thereof were published in the Official Gazette of the Commercial Registry on 17 January 2013 in the case of Banesto and on 18 January in the case of Santander.

For purposes of section 33 *et seq.* of the Structural Modifications Act, the members of the Board of Directors of Santander have prepared this report on the Draft Terms of Merger (the “**Report**”), within which, in accordance with the provisions of the aforementioned sections, they explain and provide a detailed rationale regarding the legal and financial aspects of the Draft Terms of Merger.

The Draft Terms shall be subject to the approval of the shareholders at the General Shareholders’ Meetings of Santander and Banesto, in accordance with the provisions of section 40 of the Structural Modifications Act.

Additionally, as a part of the integration process under the Santander brand of banking activity by the Santander Group in Spain, the business of Banco Banif, S.A. Unipersonal (“**Banif**”) will be integrated in a separate operation. This integration will also take place through the absorption of Banif by Santander, the corresponding draft common terms of merger having been approved by the Boards of Directors of Santander and Banif on past 28 January. These draft terms shall be subject to the approval of the shareholders at the same General Shareholders’ Meeting of Santander to which the Draft Terms of Merger are submitted, but the approval thereof at a General Shareholders’ Meeting of Banif shall not be necessary, as the merger is special due to Banif being a company wholly-owned by Santander.

2. RATIONALE FOR THE MERGER

As detailed in the Draft Terms of Merger, the merger by absorption of Banesto by Santander occurs within the context of a profound restructuring of the Spanish financial system, which involves a major reduction in the number of institutions and the creation of larger institutions.

In addition, the Spanish financial system has lost profitability over the last five years due to a drop in margins, which has adversely affected efficiency despite an improvement in costs, as well as to cyclically high provisions. In brief, the financial sector needs to optimise its income, margins, and fees, normalise provisions, and, in sum, improve efficiency.

Within this context, the merger by absorption of Banesto by Santander and the integration of Banif will allow, on the one hand, for an improvement in the efficiency of the Group through a structural modification that maximises economies of scale and, on the other, for a strengthening of the position of the Santander Group in Spain, selectively increasing its market share under a single brand.

- A) The Draft Terms explain that **efficiency improvements** can be achieved by integrating structures, through: (i) a single corporate centre and a single management structure, (ii) integration of intermediate structures, and (iii) total integration of back offices, information technology systems, and operations. The estimated time frame for operational integration of Santander and Banesto is one year. The foregoing will result in an optimisation of branches, albeit at a slower pace than that of the competition, which will help to increase market share.

The synergies to be achieved with the integration of the Banesto and Banif businesses within Santander are expected to be approximately 520 million euros before taxes per year as from the third year following the Merger, broken down as follows:

- (A) **Cost synergies**: 30 million euros in technology, 69 million euros in real estate, 32 million euros in operations, 8 million euros in advertising and brand image, and 27 million euros in other expenses, which, together with an approximate saving of 16 million euros in amortisation and depreciation, would entail total savings of approximately 183 million euros.

Furthermore, pre-tax savings of approximately 237 million euros are expected from progressively reducing the Group's personnel in Spain over three years.

Overall, cost synergies are expected to reach approximately 420 million euros.

- (B) **Revenue synergies**: the goal is to improve income by approximately 100 million euros through the single brand and new business structure, leveraging the strength of Banesto's traditional businesses such as SMEs and corporate offices.

- B) As regards **strengthening the Group's position in Spain**, a national network with a balanced market share and one of the strongest brands in the international financial system will be achieved with the Merger. In particular, the Merger will entail the existence of a single brand, with a more powerful network of approximately 4,000 branches throughout Spain, with the same corporate identity, providing a wider range of products and better quality of service.

It is therefore expected that average market share in Spain will rise from 11% in 2012 to 13% in 2015, and that the share in deposits will rise from 14% currently to 16% in 2015. It is also expected that the interest margin will increase by approximately 30 basis points in 3 years.

In sum, the goal of the Group is to achieve in 3 years a return on equity (ROTE) of between 12% and 15% on the business in Spain.

In other respects, the business improvements will be accompanied by the advantages for the shareholders of Santander and Banesto that are detailed in the Draft Terms:

- Shareholders of Banesto become shareholders of Santander, a diversified international group with a presence in high-growth markets, very liquid shares, an attractive remuneration policy, and a firm strategy of creating value for shareholders. As indicated in section 5.1 of the Draft Terms of Merger, this conversion into shareholders of Santander will be accomplished pursuant to an exchange ratio of 0.633 shares of Santander for each share of Banesto, which is a very significant premium for Banesto shareholders taking into account the listing prices of both shares prior to publication of the merger initiative. Banesto shareholders will also benefit, as Santander shareholders, from the synergies arising from the Merger.
- For the shareholders of Santander, the transaction has a low execution risk and will create significant synergies from integration (as stated, cost and income synergies are expected to reach approximately 520 million euros). The Merger is also expected to be positive from the earnings per share viewpoint, with a 3% improvement by the third year.

3. LEGAL ASPECTS OF THE DRAFT TERMS OF MERGER

3.1 Structure of the Transaction: Merger by Absorption

The legal structure chosen to integrate the businesses of Santander and Banesto is that of a merger, upon the terms set forth in section 22 *et seq.* of the Structural Modifications Act.

The Merger shall be accomplished by means of the acquisition of Banesto (absorbed company) by Santander (absorbing company), with the termination by means of dissolution without liquidation of the former and the *en bloc* transfer of all of its assets and liabilities to the latter, which shall acquire by universal succession all of the rights and obligations of Banesto. The shareholders of Banesto other than Santander shall receive shares of Santander in exchange as a result of the Merger.

3.2 Analysis of the legal aspects of the Draft Terms of Merger

3.2.1 Identification of the entities participating in the Merger

In accordance with the provisions of section 31.1 of the Structural Modifications Act, section 3 of the Draft Terms of Merger identifies the companies participating in the Merger by indicating their registered name, corporate structure, registered office, tax identification number, and registration details in their respective Commercial Registries.

3.2.2 Merger exchange ratio

(A) Exchange ratio

In accordance with section 31.2 of the Structural Modifications Act, the Draft Terms state the exchange ratio for the shares of Santander and Banesto, which has been determined based on the fair value of their corporate assets and shall be 0.633 shares of Santander for each share of Banesto. Section 4 of this Report includes greater detail regarding the exchange ratio, as well as a financial analysis and rationale.

(B) Method for covering the exchange

As set forth in section 5.2 of the Draft Terms of Merger, Santander will cover the exchange of Banesto shares with outstanding shares held as treasury shares, and will therefore not increase the share capital of Santander.

(C) Shares forming part of the exchange

The outstanding shares of Banesto shall form part of the exchange, except for those that may not be included by application of section 26 of the Structural Modifications Act, i.e. neither the Banesto shares owned by Santander nor the Banesto shares held as treasury shares. As of 31 December 2012, Banesto held, through its subsidiary DUDEBASA, S.A., 4,982,936 treasury shares, which represented 0.7249% of its share capital.

(D) Exchange procedure

As set forth in section 31.2 of the Structural Modifications Act and section 5.3 of the Draft Terms of Merger, the procedure for exchanging Banesto shares for Santander shares shall be carried out taking the following into account:

- (i) once the Merger has been approved at the General Shareholders' Meetings of Santander and Banesto, the equivalent documentation referred to in section 41.1. c) and related provisions of Royal Decree 1310/2005 of 4 November has been submitted to the National Securities Market Commission (*Comisión Nacional del Mercado de Valores*) (hereinafter, the "**CNMV**"), the conditions precedent referred to in section 3.2.9(D) below have been met, and the deed of merger has been registered with the Commercial Registry of Cantabria, the Banesto shares shall be exchanged for Santander shares;
- (ii) the exchange shall take place as from the date indicated in the announcements to be published in one of the widely-circulated newspapers in the autonomous communities of Cantabria and Madrid, respectively, in the Official Gazettes (*Boletines Oficiales*) of the Spanish Stock Exchanges, and in the Official Gazette of the Commercial Registry. Santander shall act as agent for such purpose, which shall be indicated in the aforementioned announcements;
- (iii) the exchange of the shares of Banesto for shares of Santander shall be implemented through the participants in the *Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores, S.A. Unipersonal* ("**Iberclear**") that are depositaries thereof, in accordance with the procedures established for the book-entry system pursuant to the provisions of Royal Decree 116/1992 of 14 February, and with the application of the provisions of section 117 of Royal Legislative Decree 1/2010 of 2 July, approving the Restated Text of the Companies Act (*Ley de Sociedades de Capital*) (the "**Companies Act**"), to the extent applicable;
- (iv) the Banesto shareholders holding a number of shares that will not give them the right to receive a whole number of Santander shares under the agreed exchange ratio may acquire or transfer shares in order that the resulting shares give them the right to receive a whole number of Santander shares in accordance with such

exchange ratio. The decision whether to buy or to sell shall be for each individual shareholder to make; and

- (v) without prejudice to the foregoing, and as indicated in the Draft Terms of Merger, it is stated for the record that the companies participating in the Merger have agreed to appoint an odd-lot agent as a mechanism aimed at facilitating the exchange by such Banesto shareholders. It is envisaged that Santander Investment Bolsa, Sociedad de Valores, S.A., acting on the behalf of Santander, exercises the function of odd-lot agent in accordance with the procedure described in section (E) below (the “**Odd-lot Agent**”).

(E) Procedure for odd-lot acquisitions

- (i) As the exchange ratio established in the Draft Terms would in unitary terms be equivalent to the delivery of one Santander share for every 1.579778831 Banesto shares, at the close of Banesto’s final trading session on the Spanish Stock Exchanges, each Banesto shareholder that, in accordance with the previous figure and according to their resultant overall position in Banesto, does not have the right to receive a whole Santander share (due to having only one Banesto share) or has the right to receive a whole number of Santander shares but is left with a number of Banesto shares which do not give the right to an additional Santander share (an “**Odd-lot**”) may transfer said Odd-lot to the Odd-lot Agent.

By way of example, a Banesto shareholder holding 50 shares would have the right to 31.65 Santander shares (50×0.633). In accordance with the above, such shareholder would receive 31 Santander shares and would continue to have the right to 0.65 Santander shares. That fraction of a Santander share corresponds to 1.02685624 Banesto shares (0.65×1.579778831). The 1.02685624 Banesto shares would constitute the Odd-lot which the Odd-lot Agent would acquire as odd-lot agent, at the price established in section (ii) below.

As shall be set forth in the announcement to the market regarding the specific exchange procedure, each of the Banesto shareholders shall be presumed to accept this system of odd-lot acquisition. Those who are entitled to a fraction of a Santander share and voluntarily decide not to accept the system or to balance their position in accordance with the preceding section (D) (iv) shall receive, under the joint ownership system, the part of a Santander share corresponding to that fraction.

- (ii) The acquisition price of the Odd-lot shall be the result of multiplying such Odd-lot by the arithmetic mean of the weighted average exchange rate of the Banesto shares on the Automated Quotation System (*Sistema de Interconexión Bursátil*) (Continuous Market) during Banesto’s final three trading sessions on the Spanish Stock Exchanges.
- (iii) The Odd-lot Agent shall acquire the Odd-lots of shares left over in the positions existing at the close of Banesto’s final trading session on the Spanish Stock Exchanges.

- (iv) In accordance with the provisions of section 26 of the Structural Modifications Act, the Banesto shares or parts thereof acquired in this manner by the Odd-lot Agent shall not form part of the exchange.

The shares of Banesto will be cancelled as a result of the Merger.

3.2.3 Ancillary obligations, special rights, and securities other than those representing capital

As indicated in section 6 of the Draft Terms, for purposes of sections 31.3 and 31.4 of the Structural Modifications Act, there are no ancillary obligations (*prestaciones accesorias*), special preferred shares, or persons with special rights at Santander or Banesto other than simple ownership of the shares, for which reason there is no need to grant any special right or offer any options.

The Santander shares delivered to Banesto shareholders as a result of the Merger will not give the holders thereof any special rights.

3.2.4 Benefits extended to independent experts and to the directors

With respect to section 31.5 of the Structural Modifications Act, section 7 of the Draft Terms of Merger indicates that no benefits of any type will be extended to the independent expert that will participate in the Merger process or to the directors of Santander or Banesto.

3.2.5 Date as from which the holders of shares delivered in exchange will have the right to participate in the profits of Santander

Section 8 of the Draft Terms establishes that, as from the date on which they are delivered, the shares delivered by Santander to Banesto shareholders in order to cover the exchange shall give their holders the right to participate in the profits of Santander upon the same terms as the other shares of Santander outstanding on such date. As indicated in section 4.2.2 of this Report, Banesto shareholders will not have the right to participate in the Santander Scrip Dividend (*Santander Dividendo Elección*) programme of April/May 2013.

3.2.6 Date of accounting effects of the merger

Section 9 of the Draft Terms of Merger establishes 1 January 2013 as the date from which the transactions of Banesto shall be deemed for accounting purposes to have taken place on behalf of Santander.

For such purposes as may be appropriate, it is stated for the record that the retroactive effect thus determined for accounting purposes is in accordance with the requirements of the General Chart of Accounts (*Plan General de Contabilidad*) approved by Royal Decree 1514/2007 of 16 November.

3.2.7 Amendment of the Bylaws of Santander

In compliance with the provisions of section 31.8 of the Structural Modifications Act, the Draft Terms establish that the Bylaws of Santander will not be amended as a result of the Merger. Therefore, upon completion of the Merger, Santander, as the absorbing company, will continue to be governed by its current Bylaws, the text of which appears on Santander's corporate website (www.santander.com) (and a copy of which was attached to the Draft Terms of Merger as annex 1 reflecting the Bylaws in force at the date thereof).

Without prejudice to the foregoing, and independently of the Merger, it is stated for the record that the Board of Directors of Santander has resolved today to include in the agenda for the General Shareholders' Meeting the proposed bylaw amendment contained in the notice of meeting that it has also approved, and with respect to which it will publish the information required by law.

3.2.8 Impacts of the Merger on employment, impact on gender within management bodies, and impact on corporate social responsibility

Section 12 of the Draft Terms of Merger sets forth the possible impacts of the Merger with respect to employment, as well as possible impacts on gender within management bodies and the impact, where applicable, on Santander's corporate responsibility. The Draft Terms therefore comply with the provisions of section 31.11 of the Structural Modifications Act.

Section 5 of this Report analyses the impacts of the Merger on shareholders, creditors, and employees of the participating companies.

3.2.9 Other information in the Draft Terms of Merger

In addition to the information required as a legal minimum, the Draft Terms of Merger address other issues that have been included based on standards of relevance or significance in the opinion of the Boards of Directors of Santander and Banesto. These are as follows:

(A) Appointment of independent expert

As set forth in section 13 of the Draft Terms of Merger, on 11 January 2013 the Boards of Directors of Santander and Banesto asked the Commercial Registry of Cantabria (where Santander is registered) to appoint an independent expert to prepare a single report regarding these Draft Terms of Merger, pursuant to the provisions of section 34.1 of the Structural Modifications Act.

(B) Banesto Merger Committee

Section 14 of the Draft Terms of Merger stated for the record that the Draft Terms were the result of a process of analysis and decision-making carried out by the management bodies of both Santander and Banesto. As regards the latter company, such analysis has been entrusted to an ad hoc informational and consultative committee within its Board of Directors, without executive duties, the main purpose of which has been to lead and protect the investigation and decision-making process for the sole purpose of this Merger.

This committee (the creation of which was the subject of a notice of significant event sent to the CNMV on 19 December 2012 (registration number 178,973)) is made up of three independent directors (José Luis López Combarros, Juan Antonio Sagardoy Bengoechea and Carlos Sabanza Teruel) and is called the "Merger Committee".

(C) Tax regime

Section 15 of the Draft Terms establishes that the Merger is subject to the tax regime established in chapter VIII of title VII of Royal Legislative Decree 4/2004 of 5 March, approving the Restated Text of the Company Income Tax Act (*Ley del Impuesto sobre Sociedades*) and section 3 of additional provision two thereof, as well as to section 45,

paragraph I. B.) 10. of Royal Legislative Decree 1/1993 of 24 September, approving the Restated Text of the Asset Transfer and Documentary Stamp Tax Act.

To that end, notice of the choice of such tax regime shall be given to the Tax Authority within three months of the registration of the deed of merger, upon the terms established by the relevant regulations.

(D) Conditions precedent

As stated in section 16 of the Draft Terms, the effectiveness of the Merger is subject to the following conditions precedent:

- (i) the authorisation of the Ministry of Economy and Competitiveness for the absorption of Banesto by Santander, pursuant to the provisions of section 45.c) of the Banking Act of 31 December 1946;
- (ii) the acquisition of the other authorisations that must be obtained from the Bank of Spain, the CNMV, or any other governmental body or other supervisory entity by reason of the business activities of Banesto or subsidiaries thereof.

3.3 Development of the Legal Procedure for the Merger by Absorption

In order to properly understand the process for the transaction, it is appropriate to identify and outline its main milestones in chronological order.

3.3.1 Approval and signing of the Draft Terms of Merger

The starting point for the process was the preparation of the Draft Terms of Merger by the directors of Santander and Banesto, in compliance with section 30 *et seq.* of the Structural Modifications Act.

3.3.2 Independent expert report regarding the Draft Terms of Merger

Pursuant to the provisions of section 34 of the Structural Modifications Act and section 338 *et seq.* of the Commercial Registry Regulations, on 11 January 2013 Santander and Banesto asked the Commercial Registry of Cantabria to appoint a common independent expert in order to issue a single report regarding the Draft Terms of Merger.

On 11 January 2013, the aforementioned Commercial Registry of Cantabria appointed BDO Auditores, S.L. as independent expert. Today, 18 February 2013, BDO Auditores, S.L. has issued the mandatory report regarding the Draft Terms of Merger.

3.3.3 Directors' report regarding the Draft Terms of Merger

The directors of Santander have prepared this Report in compliance with the requirements of section 33 of the Structural Modifications Act.

3.3.4 Call to the General Shareholders' Meetings of Santander and Banesto

The Board of Directors of Santander has resolved today to call the annual General Shareholders' Meeting to be held in Santander on 22 March 2013 (in anticipation of a lack of quorum on the first call to meeting, scheduled for 21 March). It is expected that Banesto, for its part, will call its annual General Shareholders' Meeting to be held in Madrid on 21 March 2013.

The agenda for the General Shareholders' Meeting of Santander includes the following items, among others not inconsistent therewith:

Approval of the merger by absorption of Banesto by Banco Santander, with termination of the absorbed company and the *en bloc* transfer of its assets and liabilities, by universal succession, to the absorbing company, with the express provision that the exchange be covered by the delivery of treasury shares by Banco Santander in accordance with the draft terms of merger formulated by the respective Boards of Directors of such companies as included on their respective websites, and for such purpose:

- (a) Approval of the common terms of merger between Banco Santander and Banesto, and approval of the balance sheet of Banco Santander ended as of 31 December 2012 as the merger balance sheet.
- (b) Approval of the resolution on the merger by absorption of Banesto by Banco Santander, with termination of the former by means of dissolution without liquidation and the *en bloc* transfer of all of its assets and liabilities to the latter, which shall acquire them by universal succession, expressly providing that the exchange shall be covered by means of the delivery of treasury shares of Banco Santander, all in compliance with the provisions of the common draft terms of merger.
- (c) Adherence of the transaction to the tax regime established in chapter VIII of title VII of the Restated Text of the Company Income Tax Act and section 3 of additional provision two thereof, as well as in section 45, paragraph 1. B.) 10. of the Restated Text of the Asset Transfer and Documentary Stamp Tax Act (*Impuesto sobre Transmisiones Patrimoniales y Actos Jurídicos Documentados*).

In addition, in accordance with the provisions of the Draft Terms of Merger, the items on the agenda for the General Shareholders' Meeting of Banesto shall include deliberation on and, if applicable, approval of the resolution on the merger by absorption of Banesto by Santander.

At the time of the publication of the calls to the respective General Shareholders' Meetings, the documents specified in section 3.4 below shall be made available on the corporate websites of Santander and Banesto.

3.3.5 Documentation equivalent to a prospectus

The offer of Santander shares to the Banesto shareholders to cover the exchange ratio shall not require the publication of an informational prospectus, but shall require the submission to the CNMV of the document with equivalent information referred to in section 41.1.c) of Royal Decree 1310/2005, which shall be made available to the shareholders on the CNMV website (www.cnmv.es) at the appropriate time.

3.3.6 Merger resolution and publication of announcements

Pursuant to section 40 of the Structural Modifications Act, the Merger must be approved by the shareholders at the General Shareholders' Meetings of Santander and Banesto, strictly in accordance with the Draft Terms of Merger.

Following the adoption of the resolution on the merger by absorption of Banesto by Santander, the text thereof shall be published in the Official Gazette of the Commercial Registry, in a widely-circulated newspaper in the autonomous community of Cantabria, and in

another widely-circulated newspaper in the autonomous community of Madrid, as required by section 43 of the Structural Modifications Act.

These announcements shall state: (a) the right of the shareholders and creditors of Santander and Banesto to obtain the full text of the resolution adopted and of the merger balance sheet, as well as (b) the creditors' right of opposition.

In accordance with section 44 of the Structural Modifications Act, upon the publication of the last of the announcements, the mandatory one-month time period shall commence within which creditors and bondholders of Santander and Banesto whose credit rights arose before the date of the inclusion of the Draft Terms of Merger in the corporate websites of Santander and Banesto and were not due and payable as of such date may oppose the Merger until such credit rights are secured, so long as, in the case of bondholders, the Merger has not been approved by the corresponding General Bondholders' Meeting. Creditors whose credit rights are already sufficiently secured shall have no right of opposition.

3.3.7 Execution and registration of the deed of merger

Following adoption of the corresponding merger resolution, publication of the announcements, and compliance with the step referred to in section 44 of the Structural Modifications Act, the deed of merger by absorption of Banesto by Santander will be executed.

Prior to the registration of the deed of merger, the deed shall bear a statement by the Commercial Registry of Madrid to the effect that there are no obstacles to the registration of the proposed Merger. The deed of merger shall be filed for registration with the Commercial Registry of Cantabria, and the Commercial Registry of Madrid shall be asked to cancel the entries corresponding to Banesto.

3.3.8 Completion of the exchange

Once the deed of merger is registered at the Commercial Registry of Cantabria, the exchange of Banesto shares for Santander shares shall take place on the terms established in the Draft Terms of Merger and in sections 3.2.2.(D) and 3.2.2.(E) of this Report.

3.4 Information regarding the planned transaction

In accordance with the provisions of section 39 of the Structural Modifications Act, before the publication of the call to the General Shareholders' Meeting of Santander, the following documents regarding the Merger shall be included in the corporate website of Santander, from which they can be downloaded and printed:

- (i) the Draft Terms of Merger;
- (ii) this Report and the report of Banesto's directors regarding the Draft Terms of Merger;
- (iii) the independent expert's report;
- (iv) the annual accounts and management reports of Santander and Banesto for the last three financial years, together with the corresponding audit reports. The Santander and Banesto balance sheets forming part of the annual accounts as of 31 December 2012 shall serve as merger balance sheets;

- (v) the current Bylaws of Santander and Banesto; and
- (vi) the identity of the directors of Santander and Banesto and the date from which they have held their respective positions.

For purposes of the provisions of section 39.1.7 of the Structural Modifications Act, it is also stated for the record that, as set forth in section 10 of the Draft Terms and in section 3.2.7 of this Report, the Bylaws of Santander will not be amended as a result of the Merger.

In accordance with the provisions of section 518 of the Companies Act and its implementing regulations, the proposed resolutions, together with their rationale and the reports that are required or that the Board of Directors decides to make available, shall also be available for consultation as from the dates of the respective calls to meeting at the corporate websites of Santander (www.santander.com) and of Banesto (www.banesto.es/webcorporativa).

4. FINANCIAL ASPECTS OF THE DRAFT TERMS OF MERGER

4.1 Merger Balance Sheets, Annual Accounts, and Amendments

Section 11.1 of the Draft Terms of Merger specifies that for purposes of section 36.1 of the Structural Modifications Act, the merger balance sheets shall be considered to be the balance sheets of Santander and Banesto, respectively, as of 31 December 2012.

The Board of Directors of Santander prepared such balance sheet on 28 January 2013. For its part, the Board of Directors of Banesto is to prepare its balance sheet at its meeting today.

The Santander and Banesto balance sheets, duly verified by their auditors, shall be submitted to the shareholders for approval at the respective General Shareholders' Meetings at which a decision on the Merger will be adopted, prior to the approval of the merger resolution itself.

Pursuant to the provisions of section 31.10 of the Structural Modifications Act, section 11.2 of the Draft Terms of Merger states for the record that the conditions upon which the Merger is undertaken have been determined taking into consideration the annual accounts of the merging companies for the financial year ending 31 December 2012, the merging companies' financial year being the same as the calendar year.

4.2 Rationale for the Exchange Ratio

4.2.1 Exchange ratio

In accordance with section 31.2 of the Structural Modifications Act, the Draft Terms state that the exchange ratio for the shares of Santander and Banesto shall be 0.633 Santander shares, each with a nominal value of 0.5 euro, for every Banesto share, each with a nominal value of 0.79 euro each, without provision for any supplementary cash compensation.

In conformity with section 25 of the Structural Modifications Act, the exchange ratio in a merger reflects an agreement between the merging entities at the time of signing the draft terms of merger regarding the financial valuation of each entity.

The Board of Directors of each of the participating entities must separately evaluate the fairness of the agreed exchange ratio for the entity and its shareholders, and the independent expert appointed by the Commercial Registry must provide an opinion regarding whether the exchange ratio is fair for the entities participating in the Merger. Furthermore, the Boards of

Directors may (if they consider it appropriate, as in this Merger) seek opinions from financial experts regarding the fairness of the exchange ratio.

Pursuant to the provisions of section 25 of the Structural Modifications Act, the exchange ratio has been determined based on the fair value of the assets and liabilities of Santander and Banesto and, in turn, has been agreed to and calculated based on the methodologies explained and for which a rationale is set forth below.

4.2.2 Rationale

Valuation by reference to the listing price tends to be the method considered preferable for determining the fair value in the case of listed securities (by way of example, for purposes of determining the fair value of the shares to be issued in the event of capital increases excluding pre-emptive rights, section 504.2 of the Companies Act deems the fair value to be that which results from the listing price except where proven otherwise). The use of a standard based on valuation of the listing price is also justified as being the most commonly used standard applied in mergers of listed companies.

The shares of both Santander and Banesto are listed on official securities markets. Therefore, in order to determine the fair value of the assets of both companies in order to set the exchange ratio, the reference method applied by the directors was based on their listing prices.

At the close of trading on 14 December 2012 (the trading day immediately preceding the first public announcement regarding the Merger), the share price of Santander was 5.90 euros and the share price of Banesto was 2.99 euros. As regards these listing prices, the exchange ratio entails a valuation of the Banesto shares at 3.73 euros per share. The premium offered to Banesto's shareholders over the market price on such date is 25%. These valuations are reflected in the following table:

Santander		Banesto	
Euros per share	Value in euros (millions)	Euros per share	Value in euros (millions)
5.90	60,895	3.73	2,568

In determining the exchange ratio, with the aforementioned premium over the listing price as of 14 December 2012, Santander and Banesto have considered the following aspects, among others:

- The synergies to be achieved with the Merger of both companies, as detailed in the Draft Terms as well as in section 2 of this Report.
- The fact that Banesto shareholders will not be able to receive the compensation that Santander shareholders will receive within the framework of the Santander Scrip Dividend (*Santander Dividendo Elección*) programme, in January/February and April/May 2013, in either cash or shares of Santander, because it is expected that the Merger will be completed in the month of May. Banesto does not plan to distribute any dividends.

Deutsche Bank, S.A.E., as the financial adviser of Santander for the Merger, has stated to the Board of Directors of the company in a fairness opinion that, from a financial point of view,

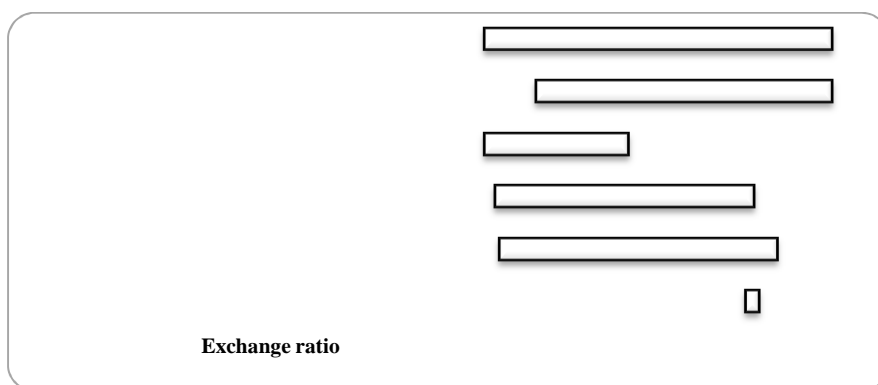
the agreed exchange ratio is fair to Santander. The opinion of Deutsche Bank S.A.E., financial adviser of Santander for the transaction, is attached to this Report as **Annex 1**.

Barclays Bank PLC and Goldman Sachs International, as financial advisers for Banesto, have submitted to the Board of Directors of such company their respective fairness opinions with respect to the consideration that results from the agreed exchange ratio and that is to be received by the shareholders of Banesto other than Santander and the companies of its group and affiliates within the framework of the Merger. According to such opinions, as of 9 January 2013 the agreed exchange ratio is fair from a financial point of view for the shareholders of Banesto other than Santander and its affiliates.

4.2.3 Other valuation methods

The Board of Directors of both banks analysed and weighted the resulting values of applying other valuation methods in order to contrast that the exchange ratio was consistent with the ranges provided by those alternative valuation methods. The contrasting methods selected by Santander, which are developed more fully below, provide a range of possible exchange ratios from 0.439 to 0.706 Santander shares for every Banesto share and therefore includes the exchange ratio of 0.633 Santander shares for every Banesto share provided in the Draft Terms. Indeed, in the chart and graph set forth below it may be observed that the exchange ratio chosen is clearly included in the total range resulting from the contrasting methods and in the actual ranges provided by four out of five of the methods used (including the dividend discount model).

Method	Range of Exchange ratios resulting from the contrasting methods	
	Minimum	Maximum
Historical listing prices	0.479	0.706
Target price of analysts	0.439	0.549
Comparable listing prices	0.448	0.646
Precedent transactions	0.451	0.664
Dividend discount model	0.640	
Total range of the contrasting methods	0.439	0.706



In the following are developed the contrasting methods used:

(A) Historical listing prices

The implied value of Santander and Banesto is calculated taking into account the average listing price for different periods and the number of outstanding shares as of the date of the Draft Terms of Merger.

	Santander		Banesto		Implicit Exchange ratios
	Euros per share	Value in euros (millions)	Euros per share	Value in euros (millions)	
Average last month	5.79	59,760	2.80	1,923	0.483
Average last three months	5.80	59,863	2.88	1,980	0.497
Average last six months	5.49	56,663	2.63	1,808	0.479
Average last year	5.29	54,599	3.03	2,086	0.574
Average last three years	7.48	77,202	5.28	3,629	0.706

Source: *Bloomberg*, 14 December 2012

As a result of the above, it would result a range of possible exchange ratios from 0.479 to 0.706 Santander shares for every Banesto share, range that therefore includes the exchange ratio of 0.633 Santander shares for every Banesto share provided in the Draft Terms.

(B) Target price of analysts

This valuation method calculates the implied value of Santander and Banesto taking into account the target prices assigned to the shares in the reports of financial analysts published since 1 October 2012, considering the number of outstanding shares as of the date of the Draft Terms of Merger.

	Santander		Banesto		Implicit Exchange ratios
	Euros per share	Value in euros (millions)	Euros per share	Value in euros (millions)	
Median	5.975	61,669	3.080	2,117	0.515
Average	5.905	60,943	3.053	2,009	0.517
Maximum	9.110	94,026	5.000	3,437	0.549
Minimum	4.100	42,317	1.800	1,237	0.439

It should be borne in mind that the target prices published by financial analysts do not necessarily reflect the current listing prices of the shares of Santander and Banesto. Such estimates are subject to uncertainties, such as the future financial evolution of the companies or future market conditions.

As a result of the above it would result a range of possible exchange ratios from 0.439 to 0.549 Santander shares for every Banesto share, range that therefore does not include the exchange ratio of 0.633 Santander shares for every Banesto share provided in the Draft Terms, but it should be observed that in any case the target price of

analysts, by its very nature, does not take into account circumstances such as the synergies that would be achieved in a corporate transaction as the merger.

(C) Comparable listing prices

Also taken into account has been the valuation method using multiples of various companies that are comparable to Santander and Banesto, using the adjusted price book value valuation multiple, as it is considered to be more appropriate in the Spanish current market environment. To do this, it has been estimated the impact of the application of a stress test similar to that carried out by Oliver Wyman in last September for the Spanish banks over Banesto's capital.

	Santander		Banesto		Implicit Exchange ratios
	Euros per share	Value in euros (millions)	Euros per share	Value in euros (millions)	
Average	5.557	57,355	2.921	2,008	0.526
High	6.454	66,613	4.168	2,865	0.646
Low	5.091	52,545	2.279	1,567	0.448

- (1) Price calculated applying the price book value multiple of comparable banks to the book value of Santander and Banesto. In the case of Banesto, its book value has been adjusted applying similar criteria to those applied by Oliver Wyman (adverse scenario) in the stress test carried out last September 2012.
- (2) Comparables used: Caixabank, Sabadell, Popular, and Bankinter in the case of Banesto; and HSBC, BNP Paribas, and BBVA in the case of Santander.

As a result of the above, it would result a range of possible exchange ratios from 0.448 to 0.646 Santander shares for every Banesto share, range that therefore includes the exchange ratio of 0.633 Santander shares for every Banesto share provided in the Draft Terms.

(D) Precedent transactions

The valuation method based on comparable precedent transactions that have recently taken place in Spain has also been considered in calculating the implied value of Banesto, taking into account the prices at which the aforementioned transactions have been completed and the premium/discount that they represented with regard to the listing prices at the time of the transaction. The selection of precedents for use excluded those transactions for which public assistance was received (for example, asset protection schemes). Specifically, the integrations of Caixabank with Banca Cívica, of Banco Popular with Banco Pastor, and of Banco Sabadell with Banco Guipuzcoano have been taken into account.

		Euros per share	Value in euros (millions)	Implicit Exchange ratios
Banesto	Average value	3.209	2,206	0.544
	High	3.917	2,692	0.664
	Low	2.661	1,829	0.451

As a result of the above, it would result a range of possible exchange ratios from 0.451 to 0.664 Santander shares for every Banesto share, range that therefore includes the exchange ratio of 0.633 Santander shares for every Banesto share provided in the Draft Terms.

(E) Dividend discount model

Finally, the dividend discount model has been used in order to assess the value in use of the companies. Such method consist on calculating the value of a company based in the present value of future dividends that such company may pay once its annual capital needs have been covered. It has been used to this as a basis the existing business plans.

Taking the above into account, this method would provide a value for Banesto of 4,917 million euros and a value for Santander of 115,348 million euros and an exchange ratio of 0.640 Santander shares for every Banesto share, which is very close to the exchange ratio of 0.633 Santander shares for every Banesto share provided in the Draft Terms.

5. IMPACTS OF THE MERGER ON SHAREHOLDERS, CREDITORS, AND EMPLOYEES

5.1 Impacts on Shareholders

As a result of the Merger, Banesto shareholders will cease to have such status and will become shareholders of Santander. This will be achieved through the allotment of Santander shares to Banesto shareholders (other than Santander) in proportion to their respective participation in Banesto's share capital, in accordance with the agreed exchange ratio. The exchange shall be carried out on the terms set forth in the preceding sections 3.2.2 (D) and 3.2.2 (E).

For Banesto shareholders, the Merger involves the assignment, on a par with the existing Santander shareholders, of the rights and duties corresponding thereto under law and the Bylaws from the time the Merger becomes effective.

5.2 Impacts on Creditors

The merger by absorption of Banesto by Santander will involve the transfer in favour of Santander, by universal succession and in a single act, of all of Banesto's assets, rights, and obligations. The obligations Santander has entered into with its creditors prior to the Merger shall remain unaltered. Banesto's legal relationships, including those that it has entered into with its creditors, shall remain in force despite their transfer to Santander. Therefore, Santander will become the debtor under the obligations that Banesto has incurred to its creditors.

With the publication of the announcements of the Merger resolution, the creditors of Santander and Banesto whose credit rights meet the requirements established in section 44 of the Structural Modifications Act may, within a period of one month, exercise their right of opposition on the terms set forth in the aforementioned section 44.

5.3 Impacts on Employees

With relation to the impact of the Merger on employment, section 12.1 of the Draft Terms establishes that, pursuant to the provisions of section 44 of the Restated Text of the Statute of Workers Act (*Ley del Estatuto de los Trabajadores*), Santander shall become subrogated to the labour rights and obligations of the employees of Banesto and Banif.

The entities participating in the Merger shall comply with their obligations to provide information to, and, if applicable, to consult with the legal representatives of the workers of each entity, in accordance with the provisions of labour regulations. Notice of the Merger shall also be given to public agencies where appropriate, and in particular to the General Social Security Revenue Office (*Tesorería General de la Seguridad Social*).

The Draft Terms state that the optimisation of the network resulting from the Merger will entail a reduction in the number of employees, which would take place progressively through relocation to other units of the Santander Group, both in Spain and abroad, naturally-occurring turnover of the work force, and incentivised redundancies.

It is also stated for the record that, in any event, the integration of employees shall take place with respect for applicable legal provisions in each case, especially with respect to the rights of the representatives of the workers to information and consultation, holding relevant meetings and negotiations with them to allow for the development of such employee integration with the greatest possible consensus among the parties. In this regard, Santander and Banesto have held meetings with the employees' main trade union representatives regarding the Merger, as a result of which, on 15 January, a protocol labour agreement was signed with the trade union representatives of 89.31% of Santander's employees and 93.20% of Banesto's employees, which will be effective for 3 years and establishes the principles and basic rules that will govern the reorganisation and rationalisation processes to take place following the Merger.

* * *

This Report has been prepared by the directors of Santander in accordance with section 33 of the Structural Modifications Act.

ANNEX 1
Fairness Opinion Issued by Deutsche Bank, S.A.E. for the Board of Directors of Santander

The Board of Directors
Banco Santander, S.A.
Ciudad Grupo Santander
28660 Boadilla del Monte
Madrid
Spain

-9 January 2013-

Dear Sirs:

Deutsche Bank, S.A.E. ("**Deutsche Bank**") is acting as financial advisor to Banco Santander, S.A. ("**Red**") in connection with the proposed merger (the "**Merger**") of Banco Español de Crédito, S.A. ("**Blue**") with and into Red pursuant to the terms and conditions to be set forth and agreed in a merger agreement (*Proyecto Común de Fusión*) to be entered into between Red and Blue (the "**Merger Agreement**"). Deutsche Bank has, with Red's permission, assumed for the purposes of rendering its opinion contained in this letter, that the Merger Agreement will provide that, among other things, Blue will be merged by absorption into Red and each shareholder of Blue will, upon completion of the Merger in accordance with its terms, exchange each outstanding ordinary share of Blue (the "**Blue Shares**"), for 0.633 ordinary shares of Red (the "**Red Shares**") (the "**Exchange Ratio**").

Blue is a quoted company listed in the Madrid Stock Exchange (*Mercado Continuo*). As of the date of this letter, Red owns, directly or indirectly, approximately 88.99% of Blue's issued and outstanding share capital at the date of this letter.

Red has requested Deutsche Bank to provide an opinion addressed to the board of directors of Red (the "**Board**") as to whether the Exchange Ratio proposed is fair, from a financial point of view, to Red.

In connection with Deutsche Bank's role as Fairness Opinion provider to Red, and in arriving at its opinion, Deutsche Bank has reviewed certain publicly available financial and other information concerning Blue and Red and has performed certain analyses of other information furnished to it by Red. Deutsche Bank has also held discussions with members of the senior management of Red regarding the business and prospects of Red and Blue.

In addition, Deutsche Bank has: (i) reviewed the financial aspects of certain selected merger and acquisition transactions which Deutsche Bank has considered comparable to the Merger; (ii) reviewed certain historical and projected financial information of Blue (including, but not limited to, analyses and forecasts of certain estimated cost savings, operational efficiencies, revenue effects and financial synergies expected by Red to be achieved as a result of the Merger (collectively the "**Synergies**") provided by the management of Red and approved by the management of Red for use by Deutsche Bank for the purposes of rendering its opinion (the "**Projections**"); (iii) reviewed the reported prices and trading activity for Blue Shares and Red Shares; (iv) to the extent publicly available, compared certain financial and stock market information for Blue and Red with similar information for certain selected companies which Deutsche Bank has considered comparable to Red and Blue and whose securities are publicly traded; (v) reviewed an estimation of the results of Oliver Wyman's stress test of Blue provided by Red (the "**OW Stress Test Results**"); (vi) reviewed a draft of the Merger Agreement (*Proyecto Común de Fusión*) dated as of 9 January 2013 provided by Red (the "**Draft Merger Agreement**"); and (vii) performed such other studies and analyses and considered such other factors as it deemed appropriate.

In conducting its analyses and arriving at its opinion, Deutsche Bank utilized a variety of generally accepted valuation methods commonly used for these types of analyses. The analyses performed by Deutsche Bank were prepared solely for the purpose of enabling

Deutsche Bank to provide its opinion to the Board as to the fairness, from a financial point of view, of the Exchange Ratio to Red and do not purport to be appraisals or necessarily reflect the prices at which businesses or securities may actually be sold, which are inherently subject to uncertainty.

Deutsche Bank has not assumed responsibility for, and has not independently verified, any information, whether publicly available or furnished to it, concerning Blue or Red, including, without limitation, any financial information, forecasts or projections considered in connection with the rendering of its opinion. Accordingly, for the purposes of its opinion, Deutsche Bank has, with Red's permission, assumed and relied upon the accuracy and completeness of all such information (including, without limitation, the Stress Test Results, the Projections and the Synergies). In addition, Deutsche Bank has not had discussions with the management of, or conducted due diligence with respect to, Blue other than its review of certain publicly available information related to Blue. Accordingly, for the purposes of its opinion, Deutsche Bank has, with Red's permission, assumed that there is no non-public information with respect to Blue not made available to Deutsche Bank that would, or would reasonably be likely to, have an adverse impact on the price of the ordinary shares of Blue.

Deutsche Bank has not conducted a physical inspection of any of the properties or assets, and has not prepared or obtained any independent valuation or appraisal of any of the assets or liabilities (including any contingent, derivative, or off-balance sheet assets and liabilities), of Blue or Red or any of their respective affiliates, nor has Deutsche Bank evaluated the solvency or fair value of Blue or Red under any applicable law relating to bankruptcy, insolvency or similar matters. With respect to the financial forecasts and projections, including, without limitation, those contained in the Projections and the Synergies, made available to Deutsche Bank and used in its analyses, Deutsche Bank has assumed with Red's permission that they have been reasonably prepared on bases reflecting the best currently available estimates and judgements of the management of Red. In rendering its opinion, Deutsche Bank expresses no view as to the reasonableness of such financial information, forecasts and projections or the assumptions on which they are based.

For purposes of rendering its opinion, Deutsche Bank has assumed with Red's permission that the Merger will be consummated in accordance with its terms, without any material waiver, modification or amendment of any term, condition or agreement. Deutsche Bank has also assumed that all material governmental, regulatory or other approvals and consents required in connection with the consummation of the Merger will be obtained and that in connection with obtaining any necessary governmental, regulatory or other approvals and consents, no material restrictions will be imposed. Deutsche Bank is not a legal, regulatory, tax or accounting expert and has relied on the assessments made by Red and its advisors with respect to such issues. Representatives of Red have informed Deutsche Bank, and Deutsche Bank has further assumed, that the final terms of the Merger Agreement will not differ materially from the terms set forth in the Draft Merger Agreement Deutsche Bank has reviewed.

This opinion has been approved and authorized for issuance by a fairness opinion review committee, is addressed to, and for the use and benefit of, the Board and is not a recommendation to the holders of the Red Shares to accept or reject the Merger. This opinion is limited to the fairness, from a financial point of view, of the Exchange Ratio to Red, and is subject to the assumptions, limitations, qualifications and other conditions contained herein and is necessarily based on financial, economic, market and other conditions, and the information made available to Deutsche Bank, as of the date hereof. Red has not asked Deutsche Bank to, and this opinion does not, address the fairness of the Merger, or any consideration received in connection therewith, to the holders of any class of securities, creditors or other constituencies of Red, nor does it address the fairness of the contemplated benefits of the Merger. Deutsche Bank expressly disclaims any undertaking or obligation to advise any person of any change in any fact or matter affecting its opinion of which it become aware after the date hereof. Deutsche Bank expresses no opinion as to the merits of the underlying decision by Red to engage in the Merger. In addition, Deutsche Bank does not express any view or opinion as to the fairness, financial or otherwise, of the amount or nature of any potential compensation payable to or to be

received as a result of the Merger by any of the officers, directors, or employees of any parties to the Merger, or any class of such persons. This opinion does not address the prices at which the shares of Blue or Red or other securities will trade following the announcement or consummation of the Merger.

Deutsche Bank will be paid a fee for its services as financial advisor to Red, which is contingent upon delivery of this letter. Red has also agreed to indemnify Deutsche Bank against certain liabilities in connection with its engagement. In this letter, Deutsche Bank AG and its subsidiaries are referred to as the "DB Group". One or more members of the DB Group has, from time to time and as at the date hereof, provided investment banking, commercial banking (including extension of credit) and other financial services to Blue and Red or their respective affiliates for which it has received compensation. In the ordinary course of their business, members of the DB Group may actively trade in the securities and other instruments and obligations of Blue or Red for their own accounts and for the accounts of their customers. Accordingly, the DB Group may at any time hold a long or short position in such securities, instruments and obligations. For the purpose of this opinion, Deutsche Bank has not considered any information that may have been provided to it in those capacities or in any other capacity than fairness opinion provider.

Based upon and subject to the foregoing, it is Deutsche Bank's opinion as investment bankers that, as of the date hereof, the Exchange Ratio is fair, from a financial point of view, to Red.

This letter may not be reproduced, summarised or referred to in any public document or given to any person without the prior written consent of Deutsche Bank. Notwithstanding the foregoing, this opinion may, if required by law, regulation or any competent regulatory authority, be included in any disclosure document filed by Red with applicable securities regulatory authorities with respect to the Merger (including, but not limited to, the *Comisión Nacional del Mercado de Valores*), provided it is reproduced in full, and that any description of or reference to Deutsche Bank in such disclosure document is in a form reasonably acceptable to Deutsche Bank and its legal advisers.

Yours faithfully,

Deutsche Bank, S.A.E.

DEUTSCHE BANK, S.A.E.