S&P Global Ratings

RatingsDirect®

Banco Santander S.A.

Primary Credit Analyst:
Antonio Rizzo, Madrid + 34 91 788 7205; Antonio.Rizzo@spglobal.com

Secondary Contact:
Elena Iparraguirre, Madrid + 34 91 389 6963; elena.iparraguirre@spglobal.com

Table Of Contents

Table Of Contents (cont.)

Banco Santander S.A.

SACP	a
Anchor	bbb
Business Position	Very Strong +2
Capital and Earnings	Adequate 0
Risk Position	Strong +1
Funding	Average 0
Liquidity	Adequate

\+

Support	0
ALAC Support	0
GRE Support	0
Group Support	0
Sovereign Support	0

\+

Additional Factors	0

Issuer Credit Rating
A/Stable/A-1

Resolution Counterparty Rating
A+/--/A-1

Credit Highlights

Overview

Key strengths	Key risks
Wide geographic diversification and solid market positions in the markets where it operates.	Exposure to higher-than-average economic risk in some of the countries where it operates.
Focus on stable retail banking business, underpinning the bank's sound and resilient earnings.	Some countries and business segments are still vulnerable to potential pandemic-related setbacks.
Successful strategy and implementation.	Proven appetite for acquisitions.
Sound capitalization for the risks it faces.	

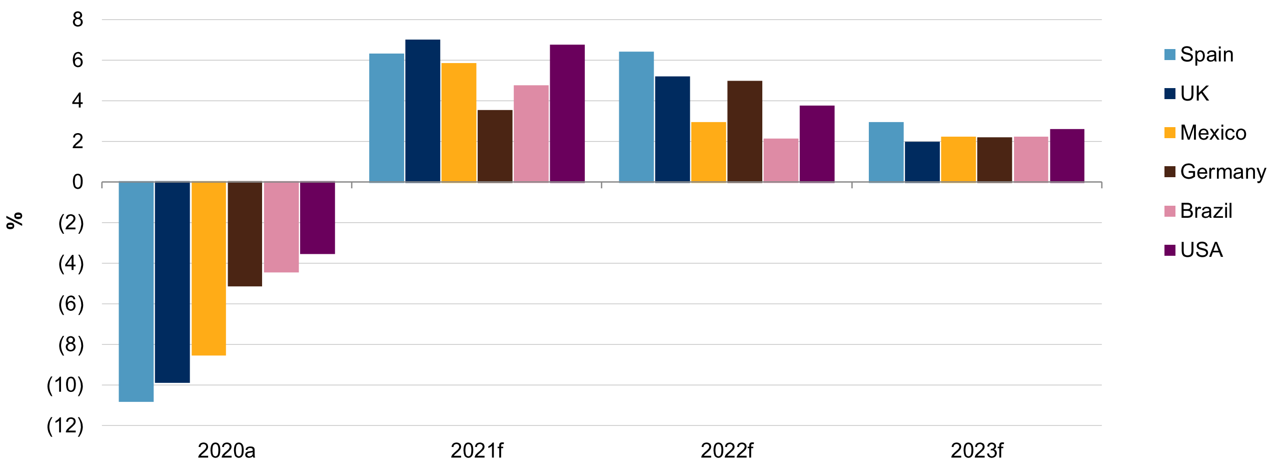
Santander's business model will remain a key rating strength. Santander enjoys a powerful, geographically diversified retail banking franchise, with a presence in both developed and emerging economies that generates strong, consistent operating earnings and is fairly efficient compared to peers. We believe that the global pandemic in 2020 demonstrated the effectiveness of the group's diversification and, in turn, its business resilience. Given that the economic fallout of the pandemic, in terms of scale and timing, has varied by country, the bank has been able to use different levers in each of them to better manage the impact (see chart 1).

We expect moderate capital strengthening on the back of improved profitability and selective growth. The bank's capital, which has strengthened over recent years, remained resilient in 2020. We project the bank's risk-adjusted capital (RAC) ratio to slowly climb above 8% by 2023 on the back of higher retained earnings (7.7% at end-2020) and 3.5% average loan growth. This already takes into account the recent capital redeployment toward more profitable businesses (namely the acquisitions of the minority interests in Mexico and the U.S., and a broker dealer). The improving economic conditions across the group's footprint--alongside the upfronting of provisioning completed in 2020--should support higher operating profits and lead to a sustained decline of cost of risk toward pre-pandemic levels in two years.

NPLs are likely to pick up given pockets of risk in Spain and Latin America, although deterioration will remain manageable. Though improving until March 2021, we expect the bank's asset quality to deteriorate once support from authorities recedes and we see the full extent of damage to the private sector. We see the small and midsize enterprise (SME) portfolios in Spain and Brazil as being potentially more vulnerable. Conversely, we expect residential mortgages, which account for over one third of Santander's loan book, to remain resilient, as demonstrated by loans that were under moratoria. We expect the bank's NPL ratio to increase to 4.5%-5% of gross loans in 2022 from 3.65% in 2020. We consider this level of deterioration to be manageable.

Chart 1

All Key Markets Where Santander Operates Face A Synchronized Recession



f--Forecast. a--Actual. Source: S&P Global Ratings.

Outlook: Stable

The stable outlook on Banco Santander S.A. reflects our view that its geographically diversified global franchise remains a rating strength and that the bank can absorb potential further asset-quality deterioration in some geographies and business segments, such as SMEs. We consider that the bank will continue to generate sustainable operating income in the next two years, maintain superior efficiency (below 50% cost-to-income), and prudent credit provisioning (about 105 bps-115 bps of cost of risk) to deliver its strategic priorities, notably improving profitability and capital. Specifically, we expect operating performance to improve on the back of business growth in the Americas and cost savings in the mature European market. We see the bank's ROE reaching about 8.5% and the RAC ratio strengthening and stabilizing just above 8% in the next two years.

Given the current negative sovereign outlook, the stable outlook on Santander implies that, in the event of a sovereign downgrade to 'A-', we are likely to rate Santander one notch above Spain. This reflects our view that in a hypothetical stress scenario of the Spanish sovereign defaulting, there is an appreciable likelihood that Santander would not automatically default considering its globally diversified exposures.

Since the bank complies with its total loss-absorbing capacity (TLAC) and minimum requirement for own funds and eligible liabilities (MREL), we project only a limited increase in the stock of bail-inable debt. Therefore, at this stage, we don't see the buffer of bail-inable debt sustainably exceeding 400 bps of its S&P Global Ratings' risk-weighted assets (RWA)--a level that would enable it to benefit from one notch of rating uplift.

Upside scenario

Although unlikely over the two-year outlook horizon, we could take a positive rating action if the bank demonstrates stronger build-up of loss-absorbing instruments than we currently expect. This could be because either it increases the stock of bail-inable debt as a percentage of our RWA, or the RAC ratio exceeds our current expectations. In that event, an upgrade of Santander would also depend on our confidence that the rating can remain two notches above its domestic sovereign.

Downside scenario

The ratings could come under pressure if the bank fails to maintain a track record of high and resilient operating profitability; its wide geographical and business diversification does not provide tangible benefits to its risk profile; or unexpected events (such as aggressive acquisitions) undermine its capital position.

Key Metrics

Banco Santander S.A.--Key Ratios And Forecasts

	--Fiscal year ended Dec. 31--				
(%)	**2019a**	**2020a**	**2021f**	**2022f**	**2023f**
Growth in operating revenue	1.9	(9.2)	0.8-1.0	0.2-0.2	1.4-1.7
Growth in customer loans	4.1	(1.5)	3.4-4.2	2.7-3.3	2.5-3.1
Growth in total assets	4.3	(0.9)	2.1-2.6	1.7-2.1	1.7-2.0
Net interest income/average earning assets (NIM)	2.9	2.6	2.5-2.8	2.5-2.7	2.5-2.7
Cost to income ratio	47.5	48.1	45.6-47.9	45.4-47.8	45.1-47.4
Return on average common equity	6.7	(9.7)	6.9-7.6	7.4-8.2	8.0-8.8
Return on assets	0.6	(0.5)	0.4-0.5	0.5-0.6	0.5-0.6

Banco Santander S.A.--Key Ratios And Forecasts (cont.)					
	--Fiscal year ended Dec. 31--				
(%)	**2019a**	**2020a**	**2021f**	**2022f**	**2023f**
New loan loss provisions/average customer loans	1.1	1.4	1.2-1.3	1.1-1.2	1.0-1.1
Gross nonperforming loans/customer loans	3.8	3.7	4.0-4.4	4.2-4.6	3.7-4.1
Net charge-offs/average customer loans	1.3	0.9	1.1-1.1	1.1-1.1	1.0-1.0
Risk-adjusted capital ratio	7.7	7.7	7.7-8.1	7.9-8.3	8.0-8.5

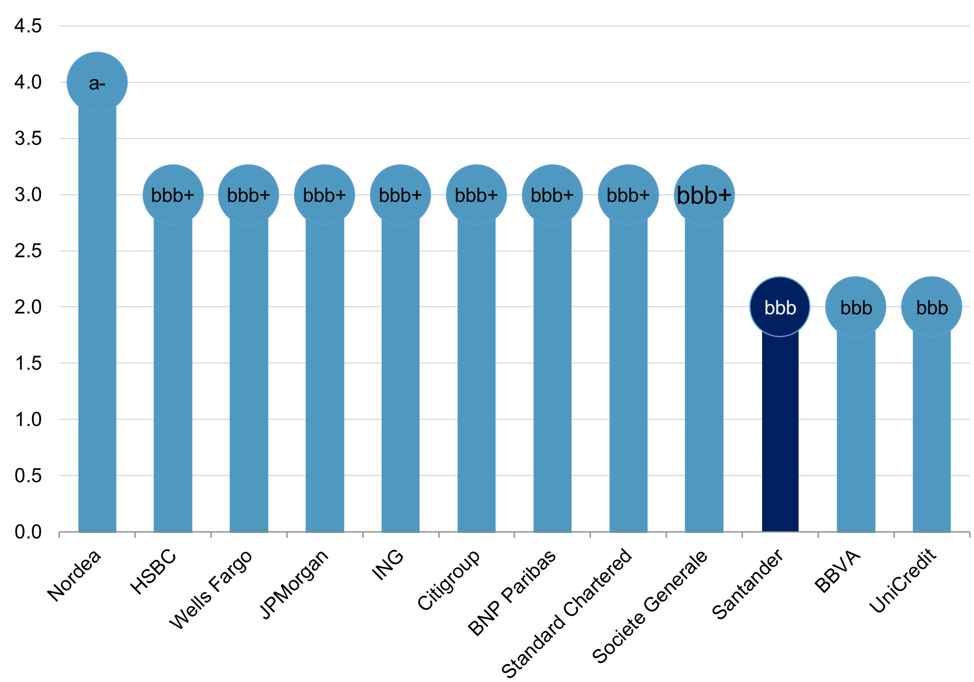
All figures are S&P Global Ratings-adjusted. a--Actual. e--Estimate. f--Forecast.

Anchor:'bbb', Reflecting The Higher-Than-Average Economic Risk Of The Markets Where The Bank Operates

Our anchor for Santander is currently 'bbb', weaker than that of most of its global peers, as chart 2 shows. We generally compare Santander with the following peers: HSBC, BNP, JP Morgan, Citigroup, Standard Chartered, ING, Societe Generale, Wells Fargo, BBVA, Nordea, and Unicredit.

Chart 2

Santander's Lower Than Peers' Anchor Reflects Higher Economic Risks Of Its Footprint



Data as of June 2021 Source: S&P Global Ratings.

The weighted-average economic risk to which Santander is exposed is not only higher than that of global peers, but also marginally higher than that faced by institutions operating primarily in Spain. The U.K. and Spain account for the group's largest credit exposures at about one-quarter each in March 2021. Both have an economic risk score of 4. Brazil (economic risk of 7) and the U.S. (economic risk of 3) each account for about 10%. The remaining exposures are split roughly evenly at about 5% each between Mexico (economic risk of 6), Portugal (economic risk of 6), Germany (economic risk of 1), other Latin American countries (economic risk of 7), and the rest of Europe (economic risk of 4). Weightings are rounded to the nearest 5% before averaging.

With regard to industry risk, our assessment of '4' reflects Spanish banks' balanced funding profiles and ample liquidity, as well as the profitability challenges ahead. Customer deposits now fund the bulk of banks' loan books, at historically low costs. Reliance on wholesale market funding is therefore limited and markets remain open. In addition, we expect the European Central Bank will continue to ensure banks' access to funding, if needed, at attractive prices. That said, the pandemic shock is aggravating existing profitability challenges resulting from low rates, limited business growth, and intense competition. The prospect of Spanish banks achieving returns in line with their cost of capital was already remote, particularly for midsize banks, and much so currently. Banks' profitability will only partially recover in 2021. However, we expect Spanish banks to remain efficient compared with peers.

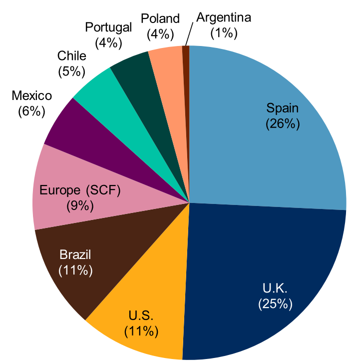
Business Position: A Powerful, Geographically Diversified, And Profitable Retail Banking Franchise

Santander benefits from a robust business model focused on a stable retail banking business that generates strong, consistent earnings. Its geographically diversified franchise gives it leading market positions in the countries where it operates and has helped the bank to weather the 2020 pandemic-induced economic downturn in all the markets Santander operates in.

Of the bank's global peers, only the ratings on French bank BNP Paribas and U.S. bank JP Morgan Chase benefit from these business model strengths to the same extent as Santander.

Chart 3

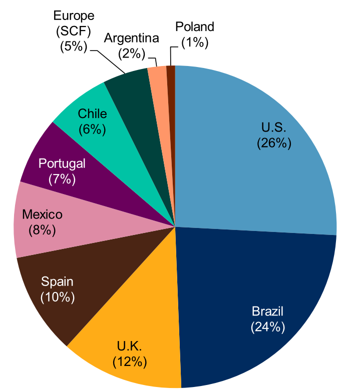
Santander Benefits From Wide Geographic Diversification, Weighted Toward Matured Economies
Geographical distribution of the group's asset base as of 1Q2021



Source: S&P Global Ratings.

Chart 4

Emerging Markets Are Key Contributors To The Group's Profitability
Geographical contribution to net attributable profits as of 1Q2021

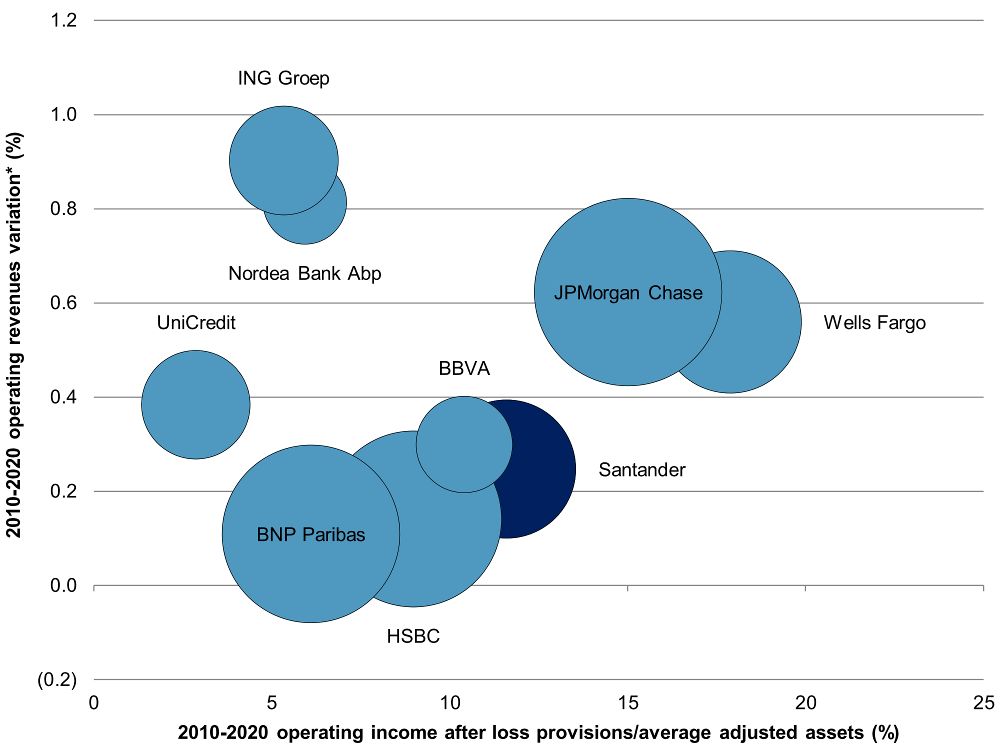


Source: S&P Global Ratings.

As a result of an intensive expansion strategy over the past two decades, Santander is currently one of the most geographically diversified banks in the world. Generally, no single country concentrates more than 30% of the group's net profits and credit. Its presence in developed economies outweighs its presence in emerging markets (accounting for 86% and 14% of loans in March 2021, respectively), but it is fairly balanced when measured in terms of profit contribution (about 55% and 45%, as of March 2021). Historically, the limited economic correlation of the countries in which it operates has allowed Santander to accommodate the ups and downs of the different economic cycles and achieve consistent, resilient results over time. This has also been confirmed during the recent pandemic, since the magnitude and timing of the economic impact in each country has varied, and the bank used different levers in each of them to mitigate the impact.

Chart 5

Santander's Profitability Resilience Versus Peers In 2020



*Standard Deviation. Bubble size represents Total Assets as of 2020. Source: S&P Global Ratings.

Santander also enjoys strong positions and franchises in most of its markets of operation, which provide it with pricing power and a loyal retail customer funding base. In addition to the 18% market share in loans that the bank holds in Spain, Santander is the third-largest mortgage lender in the U.K. (holding about 11% of the market). It owns the second-largest banks in Portugal, Poland, and Chile and the third-largest banks in Mexico and Brazil (excluding public banks). It has also built one of the largest pan-European consumer finance business. Santander is also present in the U.S., where it benefits from decent, though regional and still underperforming, market positions in several strong northeastern markets, and operates a consumer arm specialized in nonprime auto loans (SCUSA). The parent has recently announced its intention to acquire the minority stake of 20% of SCUSA to have full control of the subsidiary.

The group primarily focuses on retail banking activities, which support the bank's business and earnings stability. Compared with peers, Santander exhibits a track record of stronger, more-resilient earnings, and outstanding efficiency.

We also note that a rebound in operating income in the first quarter of 2021 following a decline over recent years. However, this was mainly due to negative FX effects in Latin America since we calculate an operating income increase of 6% CAGR since 2017.

Santander benefits from a clear, well-executed strategy, which has led to the transformation of what was once a domestic institution into a strong and well-diversified global banking group. Inorganic growth has been a key enabler of the bank's build-up of a global franchise over the years and we think Santander could, in principle, consider further mergers and acquisitions if opportunities were to arise, most likely in businesses or markets where it already operates. Specifically, this year the bank announced its intention to buy minorities in its Mexican and U.S. (consumer finance) subsidiaries, in addition to a U.S.-based broker-dealer, Amherst Pierpont Securities. We don't believe these transactions indicate a significant shift in the group's strategy but demonstrate that Santander manages its equity investments in foreign subsidiaries dynamically and is committed to deploying capital efficiently toward higher-growth countries and businesses.

The COVID-19 pandemic has not materially altered the strategic priorities of the bank, the focus of which remains:

- Improving the bank's operating performance;
- Maintaining a solid capital base, improving the allocation of capital to the more profitable businesses;
- Expanding the business by engaging further existing clients; and
- Accelerating the digitalization of the business.

The group has also committed to operate more cohesively across units, fostering collaboration, avoiding duplications, and facilitating synergies. With this aim, the bank announced:

- The creation of a single business and operating model for Santander units in Europe (One Santander) to streamline its operations; and
- The combination of SCF and Openbank to build up a purely digital consumer finance business and increase synergies and cross selling.

Capital And Earnings: Capital Has Remained Resilient And Could Strengthen Further, Despite Recent Acquisitions

Santander's level of capital, both measured by regulatory ratios and our own RAC measure, remains tighter than most international peers, but this is balanced by the predictability and quality of its earnings, which contribute to consistent capital buildup.

Santander managed to keep its level of capital broadly unchanged by our measure in 2020. Specifically, the RAC ratio stood at 7.7% at end-2020, in line with the previous year. This is despite the impact of the pandemic impact and €8.7 billion losses reported in 2020, which were largely related to the write-down of goodwill and deferred tax assets.

We expect Santander's RAC ratio to improve moderately in 2021 and increase above 8% going into 2022-2023, driven by higher retained earnings and selective loan growth. Our expectations also include the impact of recently announced deals (such as minorities in SCUSA and the Mexican subsidiaries, and the U.S.-based broker-dealer). Though these will strain the 2021 RAC ratio, albeit at a manageable level (20-25 bps), they will provide higher retained earnings going forward.

Although the pandemic has made it more challenging for the bank to achieve its medium-term target of 13%-15% underlying return on tangible equity and reducing the cost-to-income ratio to 42%-45%, these indicators stood at a promising 10% and 47%, respectively, at March 2021.

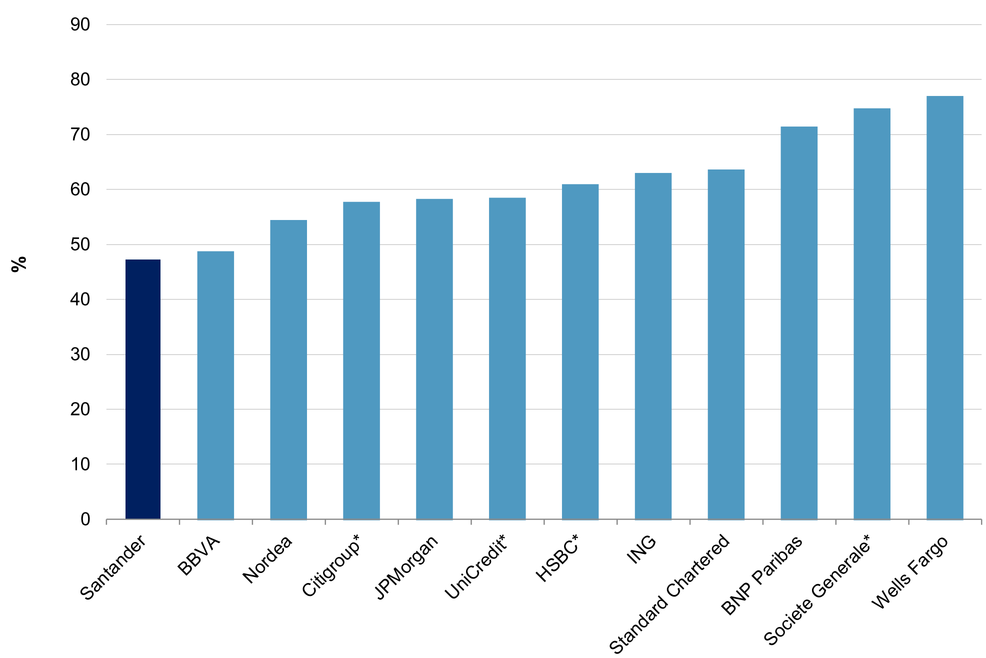
Overall, we expect net profits to reach pre-pandemic levels by 2022. Specifically, we expect:

- A mild increase in operating income (about 1% yearly growth on average in 2021-2023), on the back of both positive revenue trends and cost containment, with cost-to-income subsequently declining to 46% in 2023 from 48% in 2021.
- Lower credit impairments compared to 2020, returning to 2019 levels by 2023 (cost of risk declining to 105-110 bps of average loans).
- A dividend pay-out of around 40% of in 2021 moving to the upper end of the targeted dividend payout of 50% thereafter. We also project an average risk-weighted asset growth of 4% during 2021-2023.
- By region, Latin America and U.S. should continue to grow volumes and revenues. Meanwhile in Europe, controlling costs remains the priority, with an additional €1 billion in cost savings after the recently announced restructuring, mainly in Spain and the U.K.

Chart 6

Strong Efficiency Is A Key Attribute Of Santander

Cost to income ratio as of Mar. 2021



*Data as of Dec 2020. Source: S&P Global Ratings.

The bank's earnings buffer (which measures the capacity of the bank's earnings to cover normalized losses) remains a sound 165 bps of S&P Global Ratings' RWAs over 2021-2023, slightly below the 172 bps average reported over 2017-2019.

We forecast hybrid instruments to account for about 10% of Santander's total adjusted capital (TAC) over 2020-2022. Hybrid instruments included in TAC are now largely AT1 instruments--six issued by the parent and two by the U.K. subsidiary. The remaining legacy preference shares included in TAC are minimal, about €150 million. Based on the outstanding amount of AT1 and Tier II instruments, 1.55% and 2.38% respectively, there is little room to issue more.

The group's capital is usually allocated efficiently across subsidiaries, with higher resources dedicated to higher growth and profitable business areas. Although capital ratios are now higher than standard group levels in a number of geographies due to regulatory dividend restrictions during the pandemic, we expect sustained dividend upstreaming to the parent to resume in 2021 and current differences to reduce.

Santander reported a fully loaded common equity (CET1) ratio of 11.89% as of March 2021 (within its target range of 11%-12%), and above 11.58% in March 2020. As a result, Santander's regulatory capital ratios stand comfortably above the supervisory review and evaluation process (SREP) requirements, with an MDA buffer of 315 bps as of March 2021.

Our capital measure is weaker than the regulator's, reflecting the higher risks that we see in economies where Santander operates, and the still-large balance of DTAs resulting from timing differences outstanding on the bank's balance sheet. Indeed, our calculation of Santander's RWAs is almost 80% higher than the regulatory one.

Risk Position: Wide Geographic And Risk Diversification Ease The Repercussions Of The Global Recession

Despite Santander's capital ratios being lower than peers (both by regulatory and S&P Global Ratings' measures), we consider its capital base solid enough to manage the risks that it faces. Because of the countries where it operates, Santander faces higher-than-average risks, but its wide geographic diversification in economies that have historically been uncorrelated provides it with a benefit that our RAC calculation does not fully capture. Equally, the bank enjoys good diversification by risk and client type; it also has a track record of better-than-average asset quality in its main markets of operation. It achieved the latter through strong risk management, underwriting standards, and the close monitoring of risks.

The diversification benefit that we calculate for Santander is one of the highest in our sample of rated global banks. We calculate that RWAs after diversification at end-2020 stood almost 21% below those before diversification effects.

Our credit cost estimates of 125-130 bps are lower than last year (143 bps) and set to decline further toward pre-pandemic levels by 2023 (105-110 bps), alongside the gradual recovery of the economies in which the bank operates.

Despite the stock of NPAs continuing to decline in 2020, however, we still see pockets of risk in some asset classes and regions. For example, SMEs in Spain, including remaining loans under moratoria, and Brazil, while residential mortgages should remain solid. We expect NPAs to increase this year, reaching about 5.5% by 2022 from 4.5% last year. If we exclude the foreclosed real estate assets, nonperforming loans (NPLs) should peak at 4.4% by next year.

Unlike the stock of NPLs (Stage 3), which in 2020 declined 6% year-on-year, the stage 2 loans increased materially by 30% in the same period and represent about 8% of total loans, compared to 6% at the start of the COVID-19. We will monitor the evolution of the Stage 2 loans as we believe their migration into nonperforming could be the main driver of asset quality deterioration.

Furthermore, most loans under moratoria have expired, without having a material impact on credit quality. Out of the €93 billion loans under moratoria which expired, only 5% were then classified as nonperforming while about 20% went into Stage 2 bucket. There are €15 billion still outstanding as of March 2021, and they are largely secured and granted in Spain and Portugal.

The additional provisioning through 2020, with about €3 billion of so-called "post model adjustments" due to COVID-19, improves--although only temporarily--the group's reserves coverage to almost 72% of NPLs at March 2021, from 66% in 2019.

Santander's portfolio is granular, with exposures to the top-20 private creditors accounting for about a third of TAC in December 2020. It is also well diversified by business. Specifically, the group's exposure to consumer lending (25% of the loan book) is higher than that of peers, due to its large auto-lending business in Europe and the U.S. Only the latter has a higher-risk profile, however, as it is mostly subprime. Furthermore, its performance during the pandemic has proved more resilient that we expected. The residential mortgage book (35% of total credit) is primarily low risk, especially in the U.K., where most of Santander's mortgages originate. It will form a source of credit stability.

Given the nature of its business, the bank's main risk exposure is to credit risk. That said, Santander is also structurally exposed to foreign currency risks due to its local currency investments in subsidiaries abroad. The bank's policy is to largely hedge its equity investments' exposure to minimize the impact of adverse movement in the group's regulatory capital ratio. Hedging has historically proved effective when foreign currencies suffered large devaluations. With regards to the hedging of the subsidiaries' profit contribution to the group, Santander's stance is more opportunistic and depends on the bank's expectations of rate moves and prices. For instance, in 2020 the Brazilian results were not fully hedged, which left the group more exposed to adverse rate movements.

The group also actively manages its structural exposures to interest rate risk, through asset-liability committee portfolios or swaps across geographies. At present, most operations, other than Brazil and Chile, are positioned to benefit from interest rate increases.

Given its large size and operations in multiple jurisdictions, managing the group entails some complexity. However, we consider this to be manageable. We believe that Santander's retail business model, consistently replicated across its network, and its organizational structure, facilitate the bank's management.

Funding And Liquidity: A Structurally Balanced And Resilient Funding Profile

Santander enjoys a fairly balanced funding profile, weighted toward retail deposits. The group's loan-to-deposit ratio stood at 103% at March 2021. It also holds a manageable amount of wholesale funding, diversified by instrument, market, and investors; is exposed to limited refinancing risk as debt maturities are spread over several years; and has proved able to access market funding in times of market turbulence.

The bank's stable funding ratio, according to our calculations, stood at a solid 115% at March 2021, having improved from 101% at end-2019, particularly due to reduced leverage and market-share gains in deposits in matured markets.

The bank operates abroad through subsidiaries that are largely independent from the parent for funding purposes. However, in addition to SCF and UCI (a joint venture with BNP) which recurrently receive funding from the parent, other subsidiaries (e.g. Chile, Brazil, and U.S.) are now obtaining financing from the parent with the aim of optimizing the parent's ample liquidity available.

There are no significant differences in the funding profiles of subsidiaries within the group. The group entities/regions that are proportionally more dependent on wholesale financing are SCF, Chile, and SCUSA.

The group's wholesale debt outstanding in the market totaled €173 billion at March 2021, across a wide array of instruments: senior (31%), covered bonds (29%), senior nonpreferred (27%), subordinated debt (8%), and preferred securities (5%). If securitizations are added, total wholesale debt would exceed €200 billion. Banco Santander S.A. and Santander UK are the most active issuers in the group, accounting for about 85% of the group's wholesale debt outstanding. The calendar of debt maturities is well spread and thus manageable.

In recent years, Santander has opportunistically borrowed resources from the European Central Bank (ECB)'s targeted longer-term refinancing operation (TLTRO) programs to take advantage of attractive terms, and has done it again under the TLTRO III facility, which is almost entirely deposited back at the central bank. Similarly, some of Santander's subsidiaries access central bank facilities from host countries, though proportionally to a lower extent.

Santander benefits from sound liquidity, which it will preserve. We do not think the bank will make use of the flexibility provided by regulators to run the bank with tighter liquidity.

We estimate the group's liquidity ratio--by S&P Global Ratings' measure (broad liquid assets to short term wholesale funding)--at 2.15x at March 2021, up from 1.4x at end-2019. Broad liquid assets also amounted to 51% of customer deposits as of the same date. Liquidity is held in cash and liquid securities portfolios. The latter are primarily invested in government securities. The largest portfolios are those of Brazil, U.K., the U.S., Poland, and Chile. We also note that central banks' financing is flattening our liquidity ratios.

Support: No Notches Of Uplift For ALAC Or Government Support

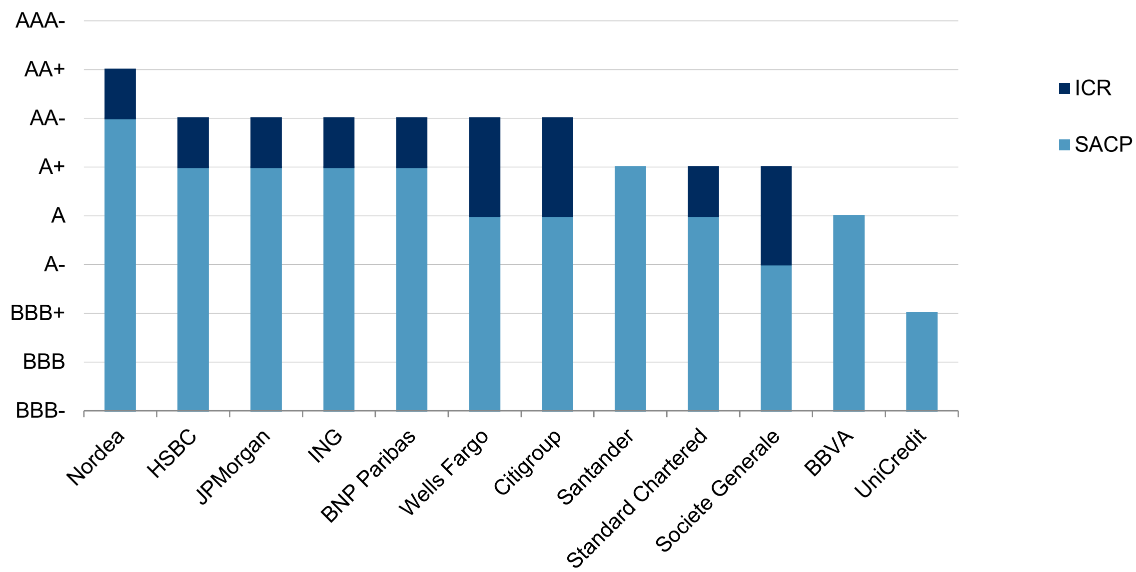
We consider Santander to have high systemic importance in the Spanish banking system, but consider the Spanish government's support toward the banking sector uncertain. As such, the bank is not eligible to benefit from government support.

Unlike most of its global peers, the ratings on Santander do not benefit from ALAC uplift either (see chart 7). The bank's ALAC buffer has grown over recent years, primarily through the issuance of senior nonpreferred debt--the latter reached a total of about €23 billion in March 2021. We forecast the ALAC buffer will remain around 350-375 bps during 2022-2023. Although further issuance of bail-inable instruments is planned for the next two years, it will largely replace maturing instruments, as the bank already complies with both minimum requirement for own funds and eligible liabilities (MREL) and total loss-absorbing capacity (TLAC) requirements. As a result, Santander's buffer of bail-inable instruments will still not be large enough to reduce the default risk of senior debt holders in resolution, as it will fall somewhat short of 400 bps, the minimum threshold to be eligible for a one-notch uplift.

Santander's MREL requirement is €109 billion (as of 2019), equivalent to 28.06% of RWAs and 16.81% of total liabilities and own funds of its resolution group. Of this, €74 billion should take the form of subordinated liabilities. As of March 2021, the MREL ratio of Santander was 34.2%. Moreover, the TLAC requirements is 21.5% from 2022 and--including the 2.5% allowed share of senior debt--Santander's TLAC of 24.9% at March 2021 already complies with future requirements.

Chart 7

Unlike Most Of Its Global Peers, Santander's Ratings Do Not Benefit From ALAC Uplift



Data as of June, 2021. HSBC--Hong Kong and Shanghai Banking Corporation. ING--International Netherlands Group. BBVA--Banco Bilbao Vizcaya Argentaria. SACP--Stand-alone credit profile. ICR--Interest coverage ratio. ALAC--Additional loss absorbing capacity. Source: S&P Global Ratings.

The ALAC buffer comprises senior nonpreferred and subordinated debt instruments, and, to a lesser extent, excess capital over the 7% threshold. We have only included bail-inable instruments issued (or to be issued) by Banco

Santander S.A., excluding those issued by subsidiaries abroad identified as separate points of entry in resolution (most notably, all instruments--including AT1s--issued out of the U.K. and U.S.). We have also excluded the fidelity bonds granted in 2017 to Popular's retail clients to compensate for the money lost in the bank's resolution.

For Santander, we request a lower-than-standard threshold to benefit from one notch of ALAC uplift (400 bps rather than 500 bps) to reflect the multiple point-of-entry approach for the bank's resolution strategy. The Single Resolution Board identified nine different points of entry for the Santander group, which will be subject to a separate resolution process from that of the parent. Those separate points of entry are:

- Spain, which is the largest as it also includes the European operations of Santander Consumer Finance, as well as all equity holdings in subsidiaries abroad; and
- Portugal, the U.K., Poland, the U.S., Mexico, Brazil, Chile, and Argentina.

Each point of entry would be required to build up its own cushions of bail-inable instruments to face a potential resolution scenario, provided that it is required to do so by host authorities. Indeed, the U.K. and the U.S. operations are already building their own TLAC/MREL cushions, and we understand that the Portuguese operations will also have their own plan soon. We understand that Santander's intention is to downstream ALAC to SCF, which will, in turn, further downstream it to its subsidiaries.

Environmental, Social, And Governance

We see ESG credit factors for Santander as broadly in line with those of industry and domestic peers.

Santander's governance, control standards, and transparency are high, which is very much needed given that its presence in several countries exposes the group to diverse risks. In recent years, it has been under the regulatory scrutiny of the U.S. authorities and was required to make meaningful adjustments to its risk management in the country. We understand that major issues have now been addressed. The bank also has large exposures to markets such as those in Latin America, where governance practices may be weaker than in Spain, Santander's domestic market, and therefore require constant monitoring. So far, the bank has managed those risks well. Santander's board of directors is diverse, fairly international, and includes several independent members. The representation of the Botín family, founder of the bank, looks high compared with the economic interest the family holds. Of the two seats the family holds, however, one belongs to Ana Botín in her role as executive chairman. In 2018, the decision-making process at the board level has raised some questions, as a new CEO was announced and reconsidered only three months later, which has led to a legal dispute still ongoing.

Social factors are increasingly relevant for a retail-focused bank like Santander. However, the bank has experienced fewer client claims or conduct issues than several other global banks in the past decade. It was not affected by Spanish customers' claims on mortgage interest rate floors and the bank managed to proactively reduce the risk of claims in other instances (arranging solutions to private banking clients affected by Bernie Madoff's case or to retail clients of Popular who lost their investments when the bank was resolved). In the U.K., misconduct charges largely originated from payment protection insurance cases at the bank that Santander acquired before the financial crisis, but it was also fined in 2018 for failing to effectively process the accounts and investments of deceased customers.

Environmental factors do not overly affect the bank's credit quality, and related risks are very much in line with those faced by peers. Of note, Santander is a large provider of auto loans (15% of the group's loan exposure), so the business and financial challenges that the auto industry faces could indirectly affect its business prospects. A substantial change in consumer preferences, such as favoring renting over ownership, could force the bank to adapt its product offer. The group has set a target to be carbon neutral by 2050.

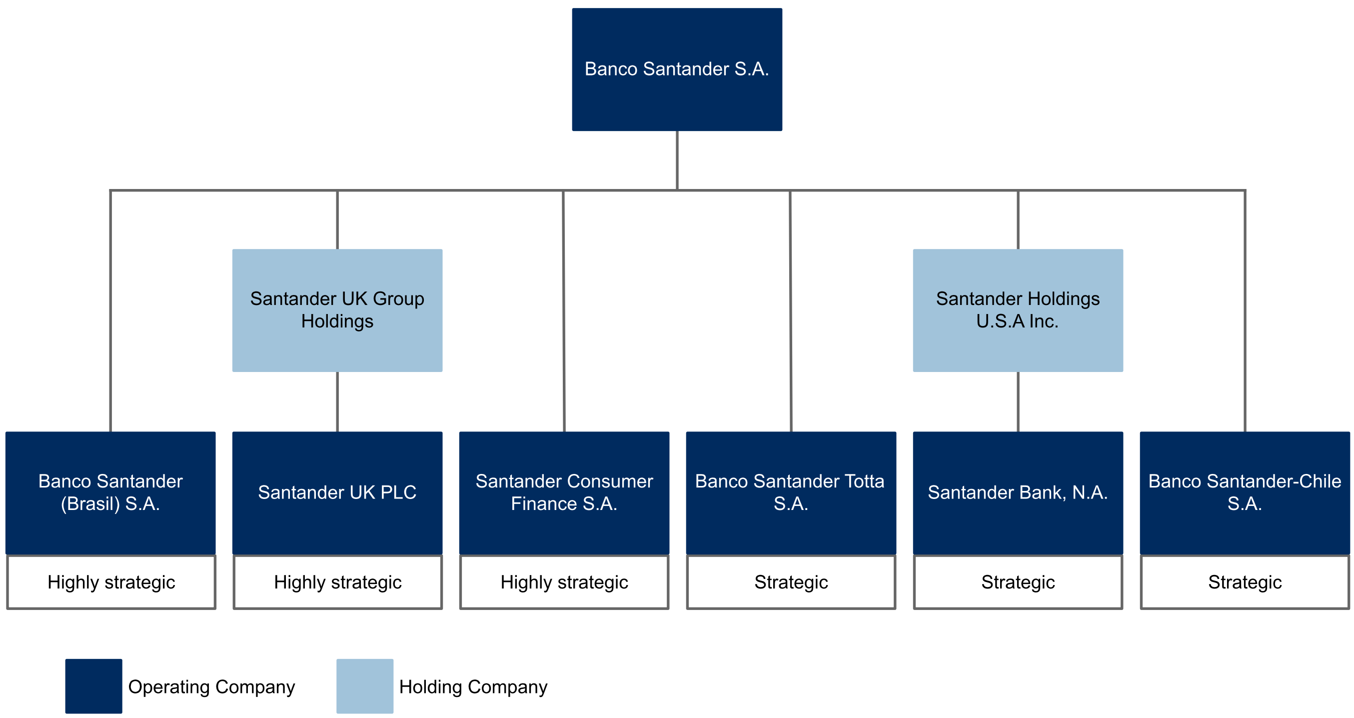
Group Structure, Rated Subsidiaries, And Hybrids

We rate six of Santander's operating subsidiaries globally (see chart below). In contrast to most other global banking groups, we do not consider any of Santander's subsidiaries as core (see "How We're Refining Our View Of The Strategic Importance Of Certain Spanish Bank Subsidiaries," published on Aug. 2, 2019).

At present, the ratings on only three of Santander's subsidiaries benefit from group support: Santander Consumer Finance S.A. (two notches of uplift), Banco Santander Totta, S.A. in Portugal (one notch), and Banco Santander N.A. in the U.S. (three notches).

We do not incorporate group support into the ratings on the remaining three subsidiaries for various reasons: the sovereign creditworthiness of the host country limits any upside potential (Brazil); the ratings benefit already from ALAC uplift (Santander UK PLC); or the stand-alone credit profile is already one notch lower than the parent's group credit profile (GCP) of 'a' (Santander Chile).

Santander's Simplified Organization Chart Including Rated Subsidiaries Only



Source: Banco Santander S.A., S&P Global Ratings.

Hybrid Ratings

We consider senior nonpreferred debt, nondeferrable subordinated debt, and preference shares as hybrid instruments and arrive at these ratings by notching down from the bank's 'a' SACP.

We therefore rate Banco Santander S.A.'s senior nonpreferred debt at 'A-', one notch below the bank's SACP to reflect subordination versus senior obligations.

We rate nondeferrable subordinated debt at 'BBB+', two notches below the bank's SACP. In addition to being subordinated, we believe that these instruments (capital instruments for regulatory purposes), could be written down to absorb losses ahead of resolution, that is, before the institution reaches the point of nonviability.

We rate junior subordinated debt at 'BBB-', four notches below the bank's SACP. In addition to the above, the wider notching compared with nondeferrable subordinated instruments reflects the risk of coupon suspension and these instruments computing as a Tier 2 regulatory capital (one notch), as well as the existence of a mandatory trigger for coupon suspension linked to the availability of enough profits in prior year's reporting--as opposed to enough distributable reserves (an additional notch).

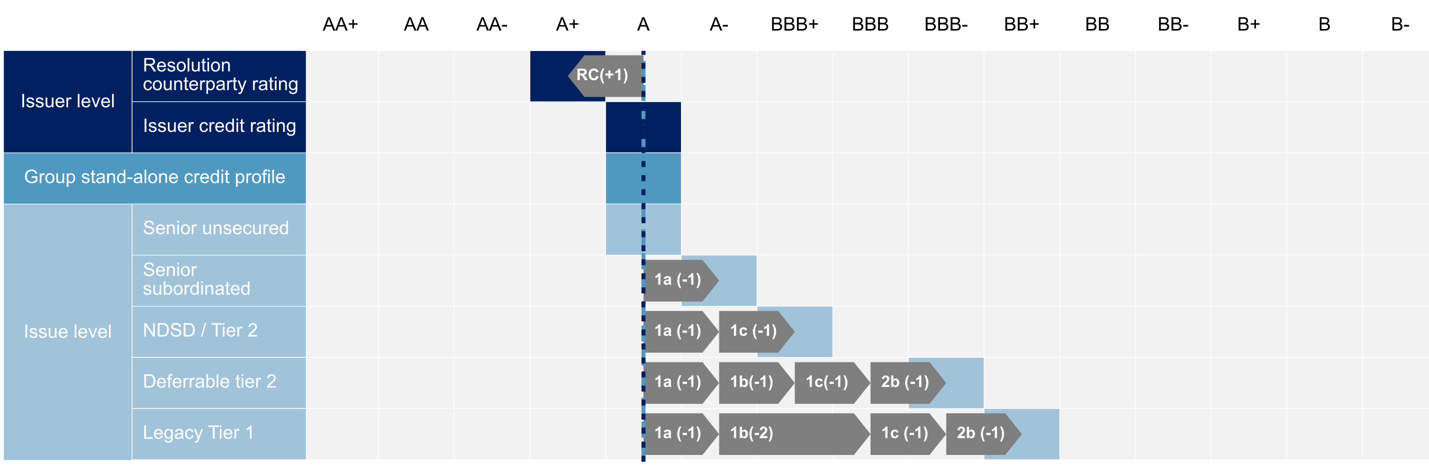
Finally, we rate the remaining two legacy preference shares five notches below the bank's SACP, at 'BB+'. The additional notch difference relates to preference shares computing as Tier I rather than Tier II capital. Despite these instruments having a mandatory coupon suspension clause in case of reported losses, we understand that the regulator allowed them to pay in 2020 regardless out of distributable reserves. We note, however, that the bank did not discontinue coupon payments on these remaining legacy preference shares in 2021, despite having reported losses in 2020 and thus having potentially reached the trigger for coupon suspension.

We do not rate the bank's AT1 instruments issued in the past few years.

Resolution Counterparty Ratings (RCRs)

We set the RCR of Banco Santander at 'A+'. The RCR is a forward-looking opinion of the relative default risk of certain senior liabilities that may be protected from default through an effective bail-in resolution process for the issuing entity. We therefore rate them one notch above the bank's long-term ICR to show their lower relative default risk. Santander's RCR also stands one notch above the long-term sovereign credit rating on Spain, indicating that we see a considerable likelihood that a sovereign default would not immediately trigger a default on the bank's RCR liabilities.

Banco Santander S.A.: Notching



Key to notching

Group stand-alone credit profile
Issuer credit rating

RC	Resolution counterpartyliabilities (senior secured debt)
1a	Contractual subordination
1b	Discretionary or mandatory nonpayment clause and whether the regulator classifies it as regulatory capital
1c	Mandatory contingent capital clause or equivalent
2b	Other nonpayment or default risk not captured already

Note: The number-letter labels in the table above are in reference to the notching steps we apply to hybrid capital instruments, as detailed in table 3 of our “Hybrid Capital: Methodology And Assumptions” criteria, published on July 1, 2019.
NDSD—Non-deferrable subordinated debt.

Key Statistics

Table 1

Banco Santander S.A. -- Key Figures

	--Year ended Dec. 31--				
(Mil. $)	**2021***	**2020**	**2019**	**2018**	**2017**
Adjusted assets	1,545,028.0	1,490,479.0	1,492,966.0	1,429,279.0	1,413,632.0
Customer loans (gross)	888,045.0	869,856.0	882,815.0	848,319.0	824,695.0
Adjusted common equity	71,634.0	68,907.0	73,486.0	67,385.0	65,106.0
Operating revenues	11,884.0	46,621.0	51,367.0	50,425.0	49,849.0
Noninterest expenses	5,613.0	22,433.0	24,379.0	23,410.0	23,080.0
Core earnings	2,579.0	N/A	12,292.0	12,277.0	12,601.0

*Data as of March 31. The data and ratios are S&P Global Ratings' adjustments or calculations of data from publicly disclosed financial statements, and may differ from the issuer's own data and ratios.

Table 2

Banco Santander S.A. -- Business Position

	--Year ended Dec. 31--				
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Loan market share in country of domicile	17.6	17.5	17.6	17.6	18.3
Deposit market share in country of domicile	18.1	18.3	18.9	18.2	18.9
Total revenues from business line (currency in millions)	11,884.4	46,735.3	52,657.6	50,453.0	50,541.0
Commercial banking/total revenues from business line	13.9	11.5	10.0	10.1	11.0
Retail banking/total revenues from business line	80.2	79.6	82.7	84.9	87.1
Commercial & retail banking/total revenues from business line	94.2	91.2	92.7	95.0	98.1
Other revenues/total revenues from business line	5.8	8.8	7.3	5.0	1.9
Return on average common equity	7.9	(9.7)	6.7	8.2	7.2

*Data as of March 31. The data and ratios are S&P Global Ratings' adjustments or calculations of data from publicly disclosed financial statements, and may differ from the issuer's own data and ratios.

Table 3

Banco Santander S.A.--Capital and Earnings

	--Year ended Dec. 31--				
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Tier 1 capital ratio	15.3	15.6	15.1	14.5	13.8
S&P Global Ratings' RAC ratio before diversification	N/A	8.4	8.8	7.3	7.6
S&P Global Ratings' RAC ratio after diversification	N/A	8.0	8.3	6.9	7.3
Adjusted common equity/total adjusted capital	97.3	100.0	100.0	100.0	100.0
Net interest income/operating revenues	61.3	62.3	60.1	60.5	59.8
Fee income/operating revenues	15.3	14.0	13.1	13.8	15.2
Market-sensitive income/operating revenues	6.5	5.7	5.6	5.9	4.9
Noninterest expenses/operating revenues	45.3	46.6	38.6	40.7	39.5
Preprovision operating income/average assets	2.0	2.0	2.7	2.6	2.5

Table 3

Banco Santander S.A.--Capital and Earnings (cont.)

	--Year ended Dec. 31--				
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Core earnings/average managed assets	0.9	0.4	1.7	1.7	1.1

*Data as of March 31. N/A--Not applicable. The data and ratios are S&P Global Ratings' adjustments or calculations of data from publicly disclosed financial statements, and may differ from the issuer's own data and ratios.

Table 4

Banco Santander S.A.--Risk-Adjusted Capital Framework Data

(Mil. US$)	**Exposure***	**Basel III RWA**	**Average Basel III RW(%)**	**S&P Global Ratings RWA**	**Average S&P Global Ratings RW (%)**
Credit risk					
Government & central banks	507,240.0	15,950.0	3.1	83,688.4	16.5
Of which regional governments and local authorities	14,283.0	212.5	1.5	2,116.2	14.8
Institutions and CCPs	80,397.0	13,337.5	16.6	29,447.8	36.6
Corporate	261,559.0	167,287.5	64.0	269,497.2	103.0
Retail	578,166.0	196,725.0	34.0	323,748.6	56.0
Of which mortgage	375,892.0	73,412.5	19.5	148,813.1	39.6
Securitization§	39,316.0	8,162.5	20.8	16,834.6	42.8
Other assets†	61,772.0	53,425.0	86.5	89,319.9	144.6
Total credit risk	1,528,450.0	454,887.5	29.8	812,536.6	53.2
Credit valuation adjustment					
Total credit valuation adjustment	--	725.0	--	2,831.7	--
Market Risk					
Equity in the banking book	8,011.3	10,725.0	133.9	67,902.2	847.6
Trading book market risk	--	18,012.5	--	26,291.3	--
Total market risk	--	28,737.5	--	94,193.4	--
Operational risk					
Total operational risk	--	55,862.5	--	94,947.4	--
	Exposure	**Basel III RWA**	**Average Basel II RW (%)**	**S&P Global Ratings RWA**	**% of S&P Global Ratings RWA**
Diversification adjustments					
RWA before diversification	--	562,600.0	--	1,004,509.1	100.0
Total Diversification/ Concentration Adjustments	--	--	--	(212,033.3)	(21.1)
RWA after diversification	--	562,600.0	--	792,475.8	78.9
		Tier 1 capital	**Tier 1 ratio (%)**	**Total adjusted capital**	**S&P Global Ratings RAC ratio (%)**
Capital ratio					
Capital ratio before adjustments		78,501.0	14.0	77,563.0	7.7
Capital ratio after adjustments‡		78,501.0	14.0	77,563.0	9.8

Table 4

Banco Santander S.A.--Risk-Adjusted Capital Framework Data (cont.)

*Exposure at default. §Securitization Exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. Sources: Company data as of 'Dec. 31 2020', S&P Global Ratings.

Table 5

Banco Santander S.A.--Risk position

	--Year ended Dec. 31--				
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Growth in customer loans	8.4	(1.5)	4.1	2.9	6.9
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	(21.1)	(19.4)	(23.4)	(24.3)
Total managed assets/adjusted common equity (x)	21.9	22.1	21.0	22.0	22.4
New loan loss provisions/average customer loans	1.0	1.4	1.1	1.1	1.2
Net charge-offs/average customer loans	0.9	0.9	1.3	1.3	1.5
Gross nonperforming assets/customer loans + other real estate owned	3.7	3.7	3.8	4.2	4.6
Loan loss reserves/gross nonperforming assets	72.1	74.3	65.8	65.3	63.7

*Data as of March 31 . N/A--Not applicable. The data and ratios are S&P Global Ratings' adjustments or calculations of data from publicly disclosed financial statements, and may differ from the issuer's own data and ratios.

Table 6

Banco Santander S.A--Funding and Liquidity

	--Year ended Dec. 31--				
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Core deposits/funding base	62.5	63.8	62.0	61.2	60.4
Customer loans (net)/customer deposits	103.2	103.9	109.6	110.3	110.5
Long-term funding ratio	85.9	86.4	80.3	83.5	81.4
Stable funding ratio	114.8	112.4	101.6	106.1	103.5
Short-term wholesale funding/funding base	14.9	14.5	21.0	17.6	19.9
Broad liquid assets/short-term wholesale funding (x)	2.1	2.1	1.4	1.6	1.5
Net broad liquid assets/short-term customer deposits	29.2	26.1	13.1	19.5	16.9
Short-term wholesale funding/total wholesale funding	39.1	39.3	54.3	44.5	49.3
Narrow liquid assets/3-month wholesale funding (x)	3.0	2.9	2.2	2.2	2.1

*Data as of March 31. The data and ratios are S&P Global Ratings' adjustments or calculations of data from publicly disclosed financial statements, and may differ from the issuer's own data and ratios.

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Criteria | Financial Institutions | Banks: Assessing Bank Branch Creditworthiness, Oct. 14, 2013
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- Bulletin: Banco Santander's Plan To Acquire Remaining Stake In U.S. Subsidiary Won't Hurt The Group's Capital, July 6, 2021
- Various Rating Actions Taken On Spanish Banks Amid Proven Resilience And Industry Challenges, June 24, 2021
- As Near-Term Risks Ease, The Relentless Profitability Battle Lingers For European Banks, June 24, 2021
- Spain 'A/A-1' Ratings Affirmed; Outlook Remains Negative On Fiscal And Structural Challenges, March 19, 2021
- Spanish Banks Need To Bolster Provisions, Cut Costs, And Preserve Capital In 2021, Jan. 25, 2021
- Bulletin: Extending Depositor Preference To All Depositors Would Not Trigger Rating Changes On Spanish Banks, Nov. 25, 2020
- Banking Industry Country Risk Assessment: Spain, June 18, 2020
- How We're Refining Our View Of The Strategic Importance Of Certain Spanish Bank Subsidiaries, Aug. 2, 2019

Anchor Matrix

Industry Risk	Economic Risk 1	2	3	4	5	6	7	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	**bbb**	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of July 26, 2021)*

Banco Santander S.A.	
Issuer Credit Rating	A/Stable/A-1
Resolution Counterparty Rating	A+/--/A-1
Commercial Paper	
Foreign Currency	A-1
Senior Subordinated	A-
Senior Unsecured	A
Short-Term Debt	A-1
Subordinated	BBB+
Issuer Credit Ratings History	
24-Jun-2021	A/Stable/A-1
29-Apr-2020	A/Negative/A-1
06-Apr-2018	A/Stable/A-1
09-Jun-2017	A-/Stable/A-2
09-Feb-2017	A-/Positive/A-2
Sovereign Rating	
Spain	A/Negative/A-1
Related Entities	
Banco Santander (Brasil) S.A.	
Issuer Credit Rating	BB-/Stable/B
Brazil National Scale	brAAA/Stable/brA-1+
Banco Santander-Chile S.A.	
Issuer Credit Rating	A-/Stable/A-2
Commercial Paper	
Foreign Currency	A-2
Senior Unsecured	A-

Ratings Detail (As Of July 26, 2021)*(cont.)	
Banco Santander SA (London Branch)	
Certificate Of Deposit	
Local Currency	A-1
Banco Santander S.A. (New York Branch)	
Commercial Paper	
Local Currency	A-1
Banco Santander Totta S.A.	
Issuer Credit Rating	BBB/Stable/A-2
Resolution Counterparty Rating	BBB/--/A-2
Senior Unsecured	BBB
PSA Banque France	
Issuer Credit Rating	BBB+/Stable/A-2
Commercial Paper	A-2
Senior Unsecured	BBB+
Santander Bank, N.A.	
Issuer Credit Rating	A-/Stable/A-2
Senior Unsecured	A-
Short-Term Debt	A-2
Subordinated	BBB+
Santander Consumer Bank AG	
Issuer Credit Rating	A-/Stable/A-2
Resolution Counterparty Rating	A/--/A-1
Commercial Paper	A-2
Senior Subordinated	BBB+
Senior Unsecured	A-
Santander Consumer Finance S.A.	
Issuer Credit Rating	A-/Stable/A-2
Resolution Counterparty Rating	A/--/A-1
Commercial Paper	
Local Currency	A-2
Senior Subordinated	BBB+
Senior Unsecured	A-
Short-Term Debt	A-2
Subordinated	BBB
Santander Financial Services PLC	
Issuer Credit Rating	A-/Stable/A-2
Resolution Counterparty Rating	A/--/A-1
Santander Holdings U.S.A Inc.	
Issuer Credit Rating	BBB+/Stable/A-2
Senior Unsecured	BBB+
Santander Totta SGPS, S.A.	
Senior Unsecured	BBB
Santander UK Group Holdings PLC	
Issuer Credit Rating	BBB/Stable/A-2

Ratings Detail (As Of July 26, 2021)*(cont.)	
Junior Subordinated	BB-
Senior Unsecured	BBB
Short-Term Debt	A-2
Subordinated	BB+
Santander UK PLC	
Issuer Credit Rating	A/Stable/A-1
Resolution Counterparty Rating	A+/--/A-1
Junior Subordinated	BB
Junior Subordinated	BB+
Preference Stock	BB
Senior Secured	AAA/Stable
Senior Unsecured	A
Senior Unsecured	A-1
Short-Term Debt	A-1
Subordinated	BBB-

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.