

# BBVA

*“Managing in an uncertain  
interest rate environment”*

GOLDMAN SACHS  
Banking Conference

Montecarlo, 10<sup>th</sup> June 2004

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 **Managing in a low interest rate environment in Spain**

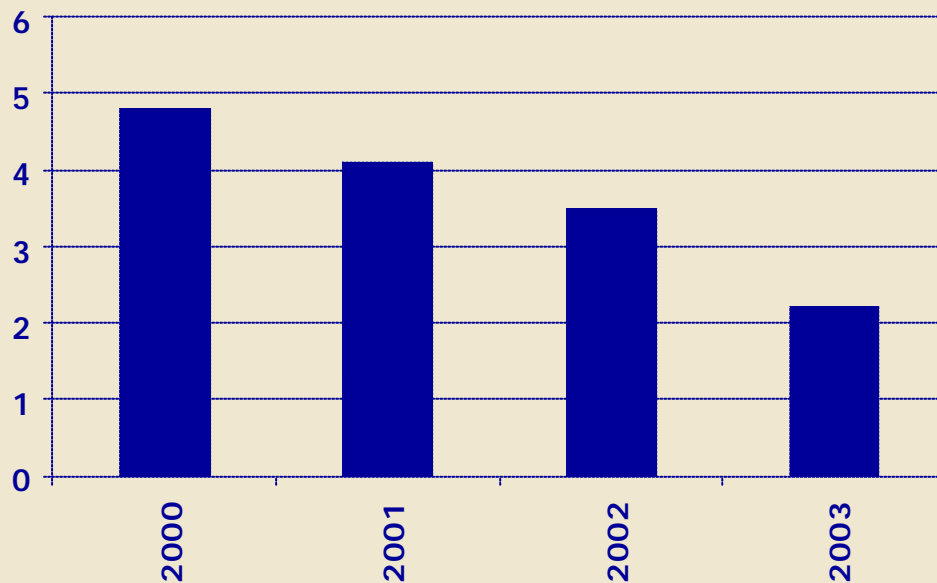
 Positioning for the new scenario

 The BBVA Bancomer case

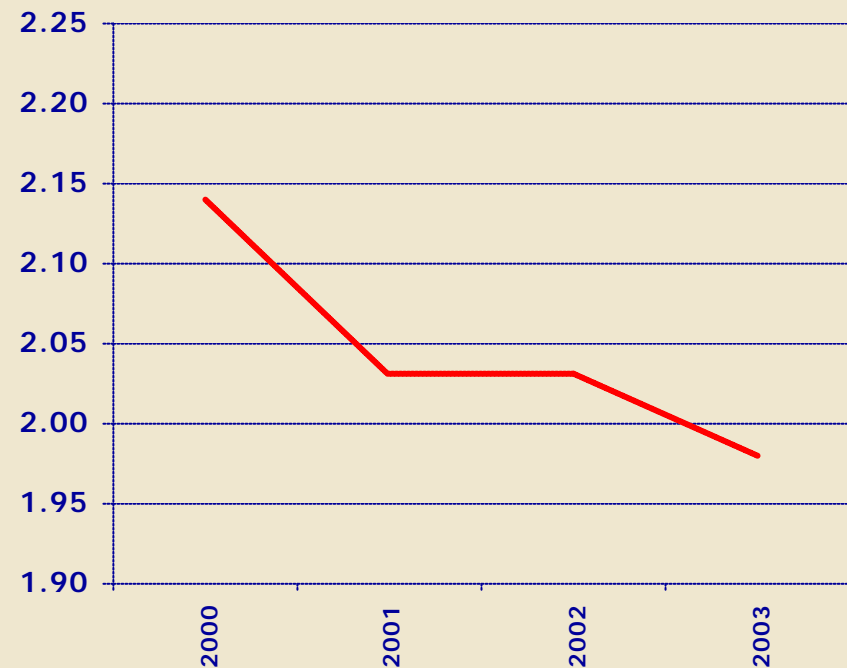
 Conclusions

# Interest rates in the Eurozone have been on a downward path for the last years

## Euribor 3 months



## Spanish Bankig System : Net interest margin (%)



Affecting negatively the net interest margins of the Spanish banks

# What has BBVA done to offset the negative impact of low interest rates?

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**We have focussed on:**

- 1. Increasing commercial activity and careful pricing policies**
- 2. Management of interest rate risks**
- 3. Improving fees**
- 4. Cost control**
- 5. Credit quality improvements**

1

# Retail Banking: a marketing offensive . . .

...driven by innovation and anticipation

June 03

Mortgage solutions

July 03

Solutions for SMEs

September 03

Fondo Extra 5

November 03

Pension solutions

January 04

Easy Mortgage

Feb – Mar 04

*Óptimo* and *Rentas* Funds

April 04

Credit card *Tarjeta diez*

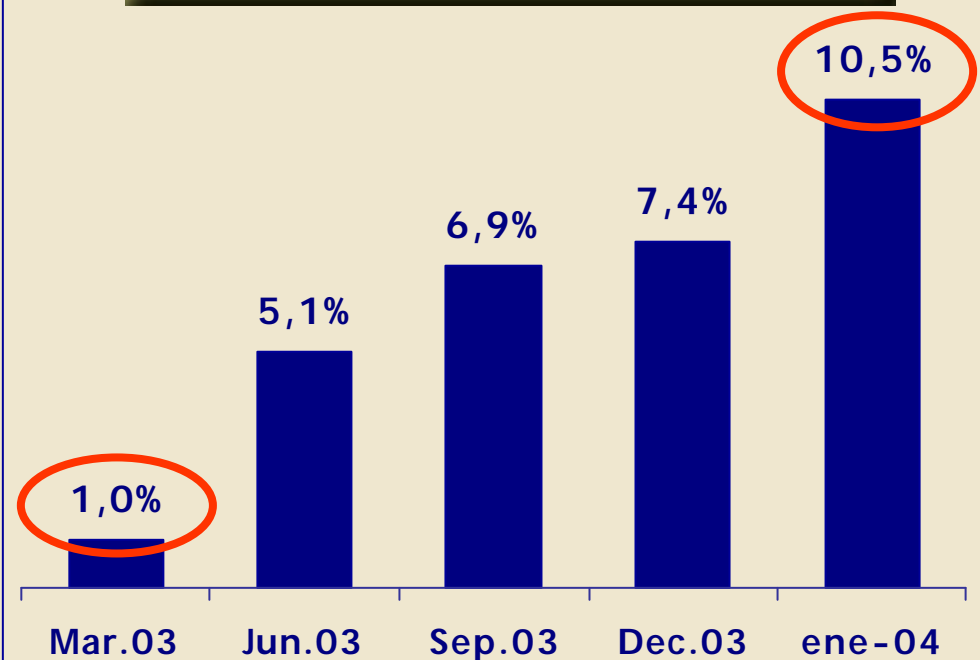
# ... that is contributing to boosting business activity

Year-on-year growth  
Average balances

## Lending



## Total customer funds deposits + funds



# ...with three pillars of the improvement

## 1. A steady mortgage demand

- ✍ Individuals +21%, developers +17%
- ✍ 1Q04: record quarter in new mortgage production (5.1 €Bn, +48%)

## 2. Accelerating volumes from SMEs

- ✍ +17% increase in SME's
- ✍ +19% increase in small businesses

## 3. Increase in off-balance sheet funds

- ✍ +19% increase in mutual funds
- ✍ Gaining market share

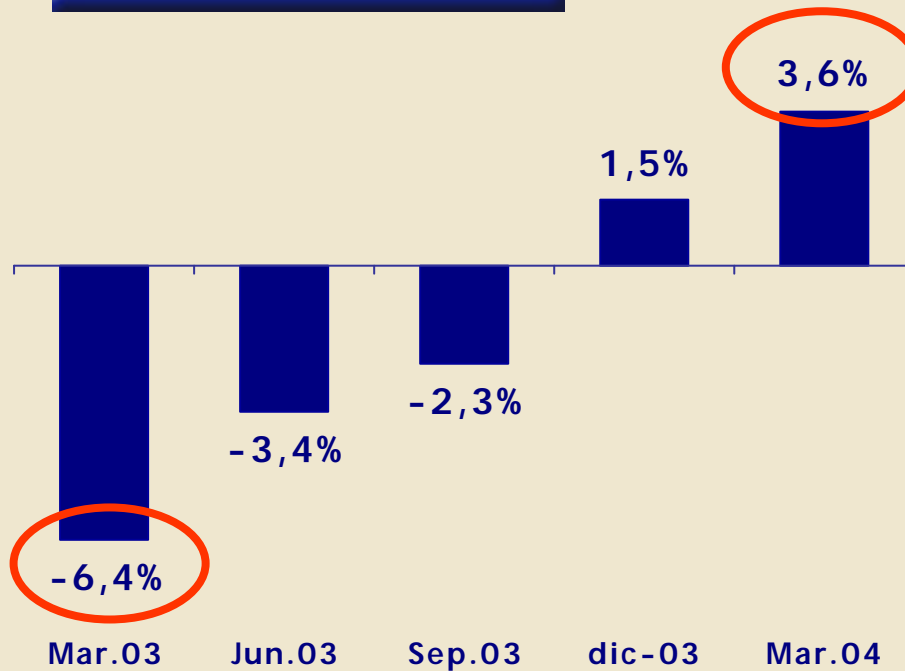


# In Wholesale Banking, selective recovery in lending

y-o-y change

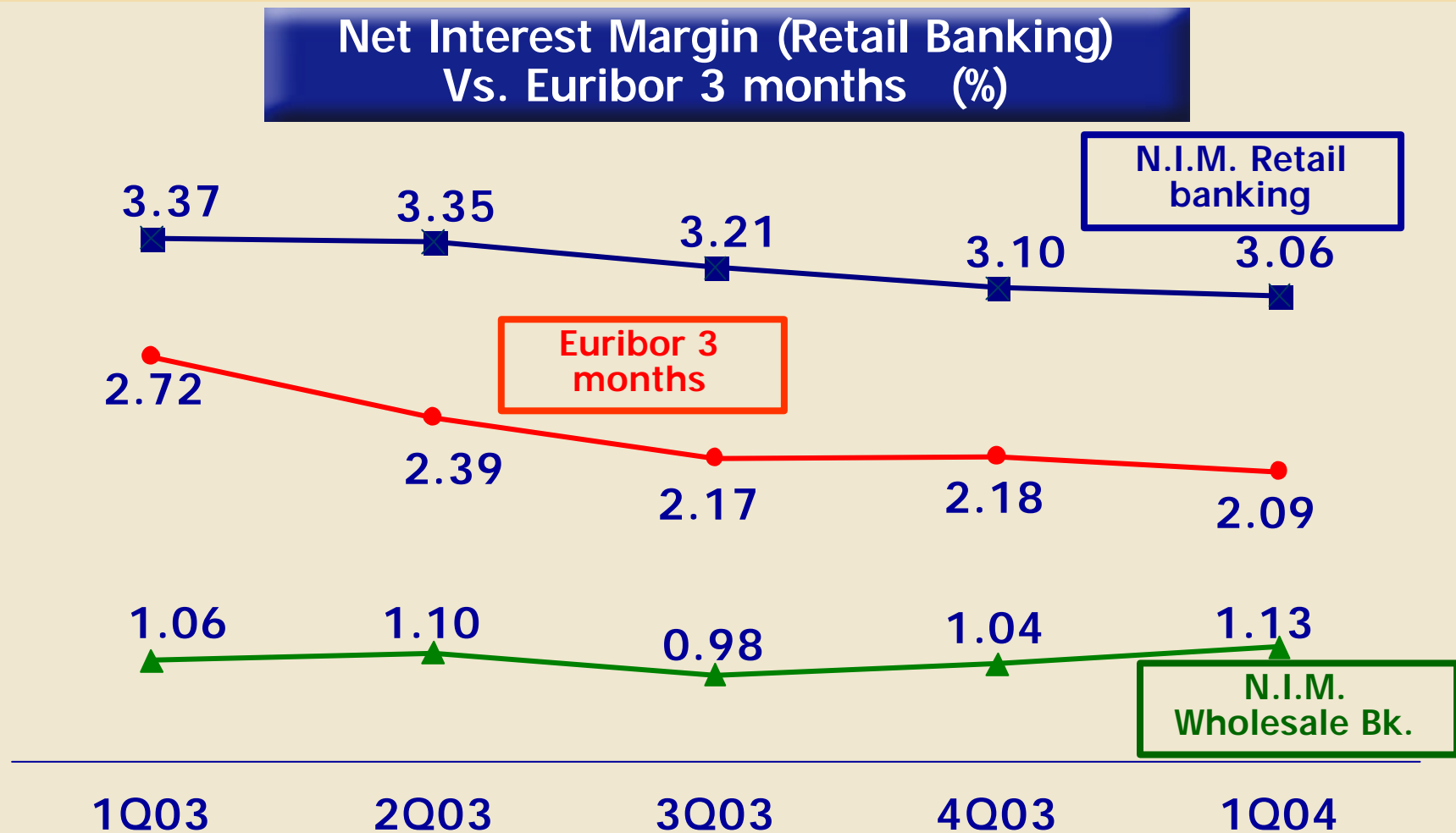
% growth by business unit

Average balances



	Mar-03	Dec-03	Mar-04
Global corporate	-12.7	-9.6	-1.9
Domestic	-6.8	-7.7	+4.3
International	-22.4	-11.9	-12.7
Institutional	+2.5	+9.3	+10.2
<b>TOTAL</b>	<b>-6.3</b>	<b>+1.5</b>	<b>+3.6</b>

# Careful pricing allows for a satisfactory evolution of net interest margins



...despite interest rates at record lows

## 2

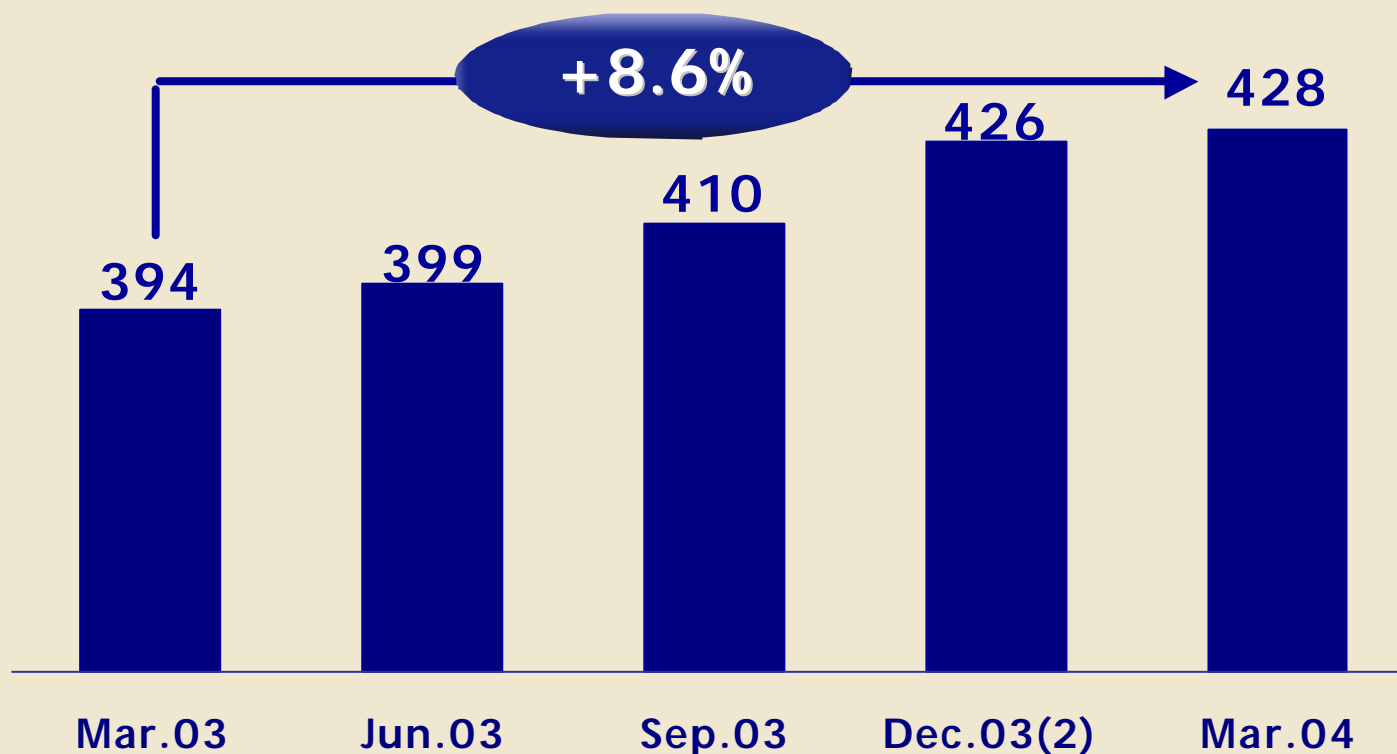
# Active management of interest rate risks

- ✍ The ALCO maintains a portfolio of government securities
- ✍ Target: To offset the negative effect on the Group's N.I.I. of a fall in interest rates
- ✍ The size of the portfolio was €24 bn as of March 2004. Short duration: 1.8 years (2.6 years beginning 2003)
- ✍ 65% of latent capital gains are locked in
- ✍ Additionally, €8 bn IRS to hedge the spread 3-12 month Euribor

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## Strong focus in fee generation, driven by asset management

Domestic Businesses (1) Net fee income  
(€ million)



(1) Retail and Wholesale & Investment Banking in Spain  
12(2) Excluding preferred fees (as extraordinary in December 2003)

**BBVA**

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## Cost control in both Retail and Wholesale businesses

Total expenses (€ million)

Retail Banking

Wholesale & Investment Banking

586

567

566

84

73

75

Mar.02

Mar.03

Mar.04

Mar.02

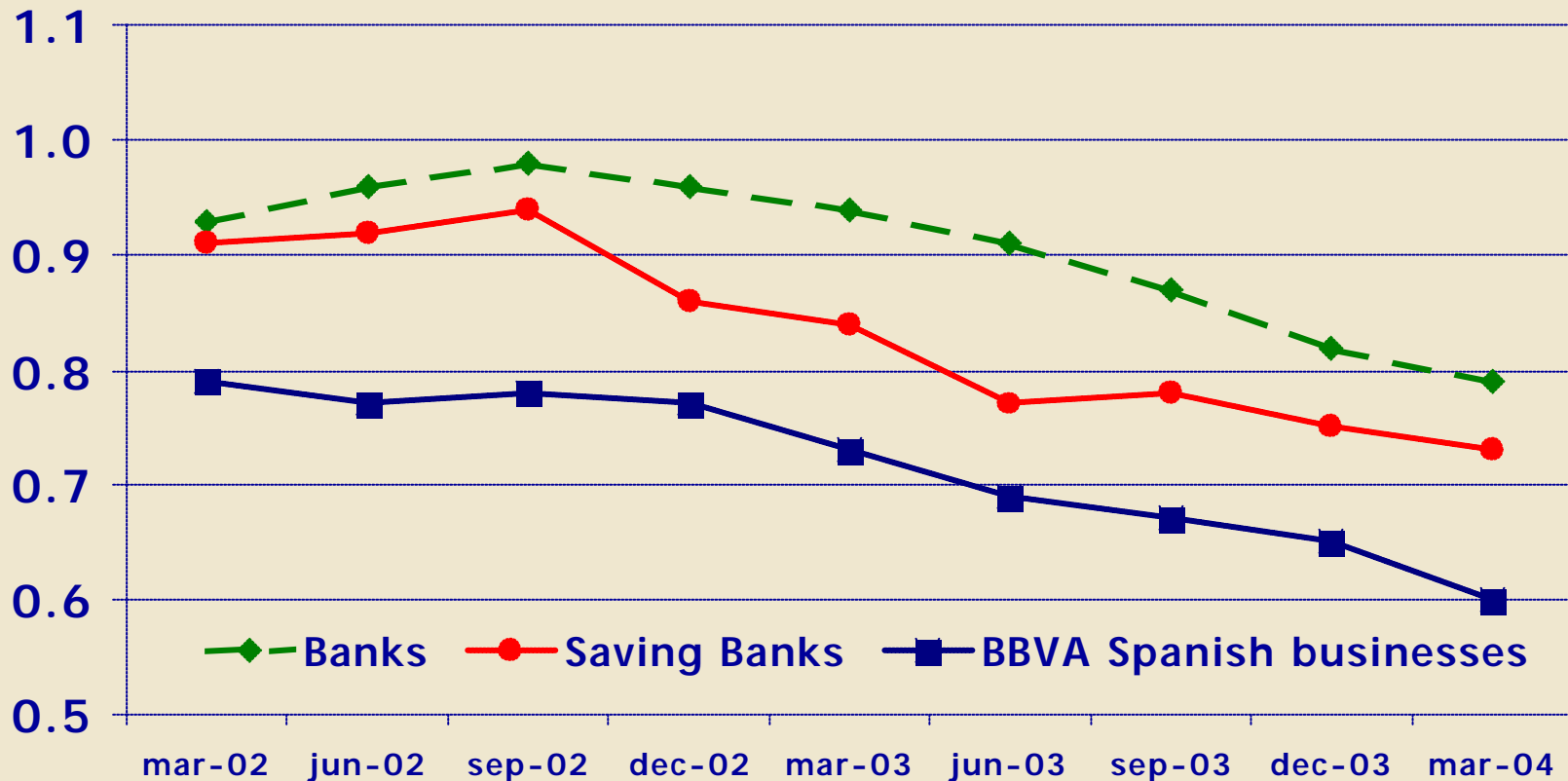
Mar.03

Mar.04

5

# ... with better asset quality than the Spanish Banking System

NPL ratio (%) (Domestic Sector)



✍ Improvements in risk management techniques

✍ Increase in less risky assets (mortgages)

## As a result, healthy growth in operating profit of domestic businesses ...

Current € million	1Q03	1Q04	Chg. %
Net interest income	897	985	9.9
Core revenues	1,274	1,383	8.6
Ordinary revenues	1,402	1,493	6.5
<b>Operating Profit</b>	<b>606</b>	<b>696</b>	<b>15.0</b>

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 Managing in a low interest rate environment in Spain

 **Positioning for the new scenario**

 The BBVA Bancomer case

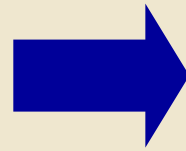
 Conclusions



# What has changed in the macro environment recently?

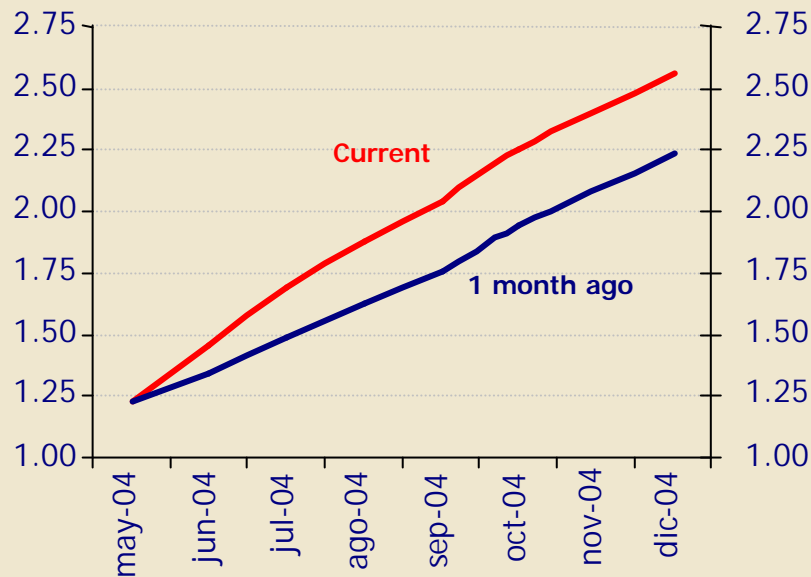
1.- Higher GDP growth and higher interest rates expectations

 **Strong growth recovery in 1Q04**

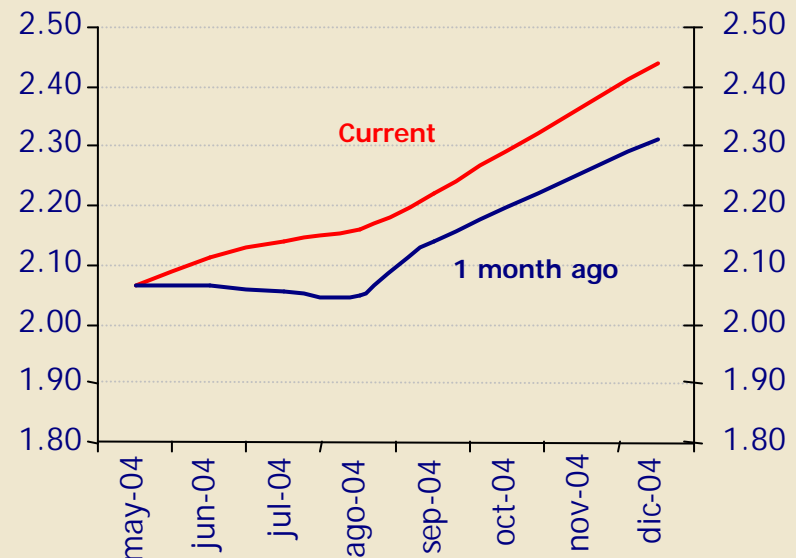


 **Faster shift towards neutral monetary policies**

**USA: 3m interest rates discounted by futures**




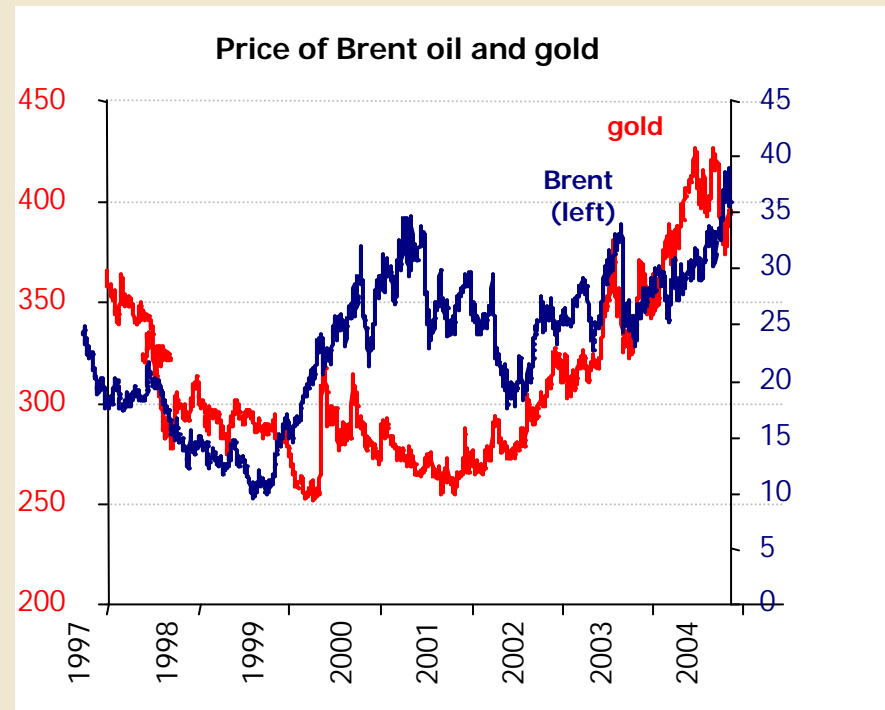
**Euro: 3m interest rates discounted by futures**



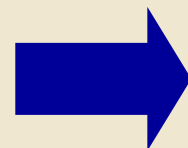
# What has changed in the macro environment recently?


## 2.- Higher oil prices

 **Cyclical increase in demand and lower inventories**




 **Geopolitical risks and speculative positions**



 **Adds further pressure to the oil price and becomes the main source of uncertainty**

# Financial scenarios to year end 2004

 Geopolitical risk is diluted, as in previous occasions

 Price of oil falls

 Economies continue to grow, albeit more moderately (end of positive temporary effects)

 Geopolitical risk is maintained or intensifies further

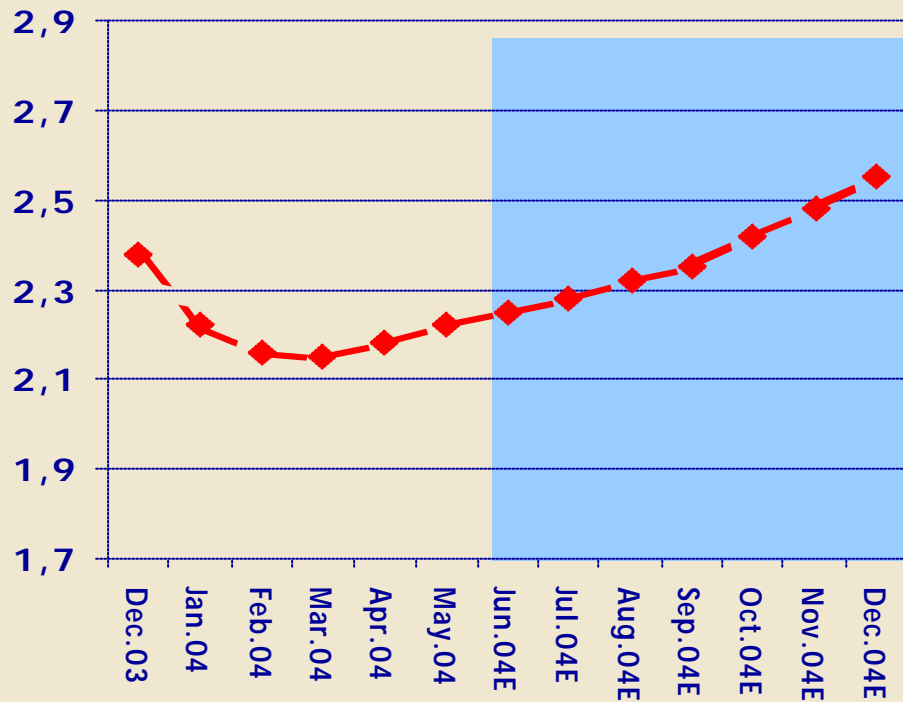
 The price of oil remains high

 Confidence levels decrease and economic activity adjusts downwards

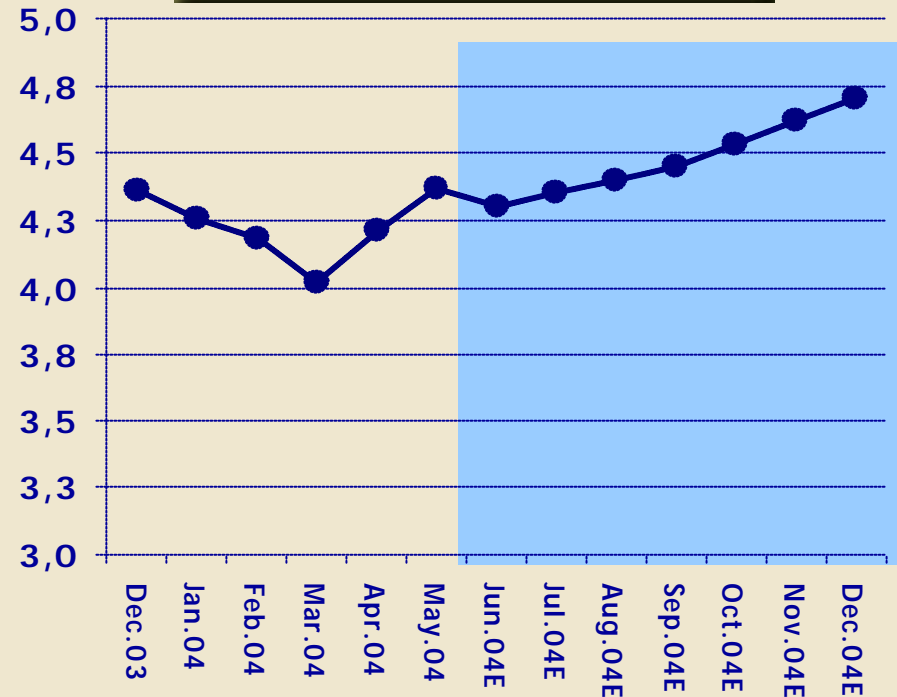
**Geopolitical risk thus becomes the catalyst for a series of pending adjustments**

# With rates at a trough, higher economic activity will likely lead to moderate increases in interest rates

### 12 Month interest rates

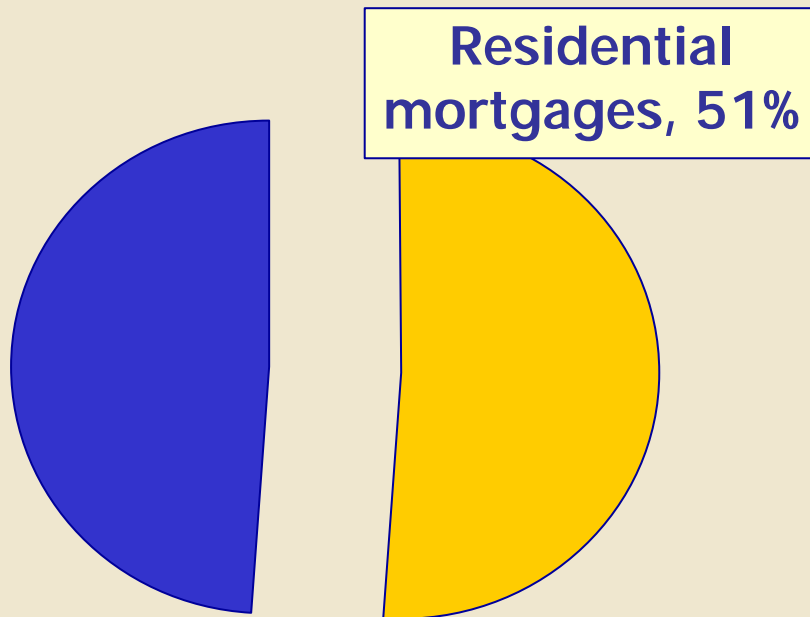


### 10 year interest rates

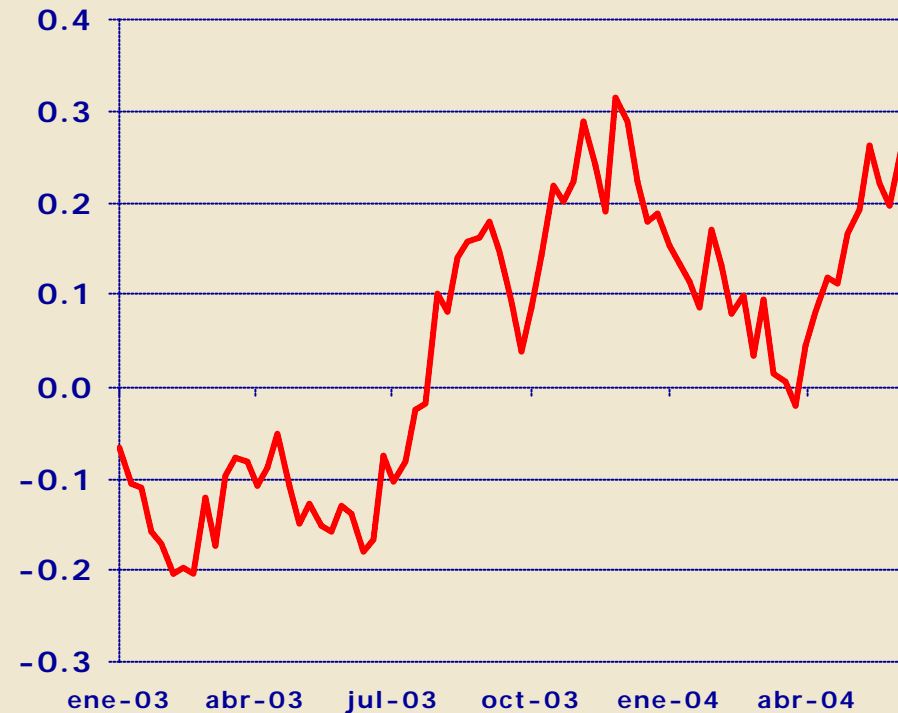


# In this scenario, BBVA is well placed given the structure of its assets ...

## Retail banking loans structure



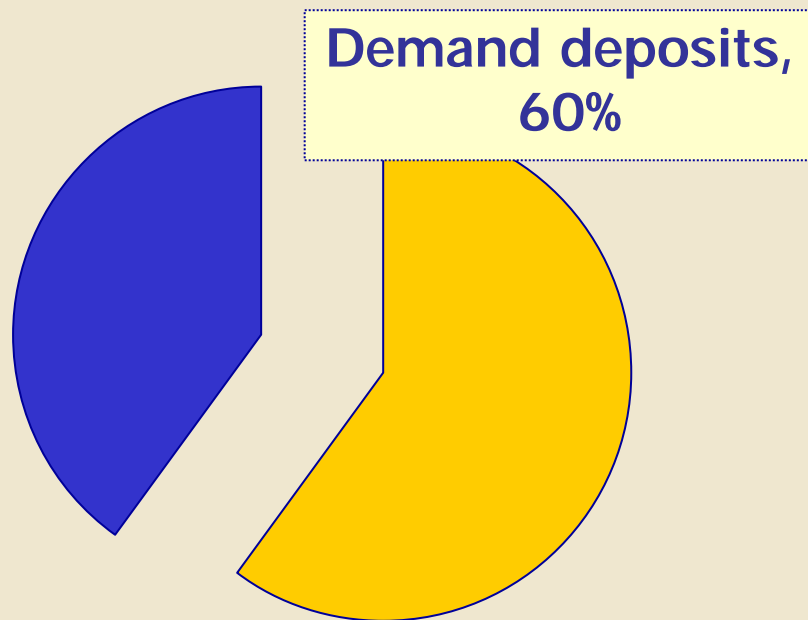
## Yield curve 12M-3M Euribor



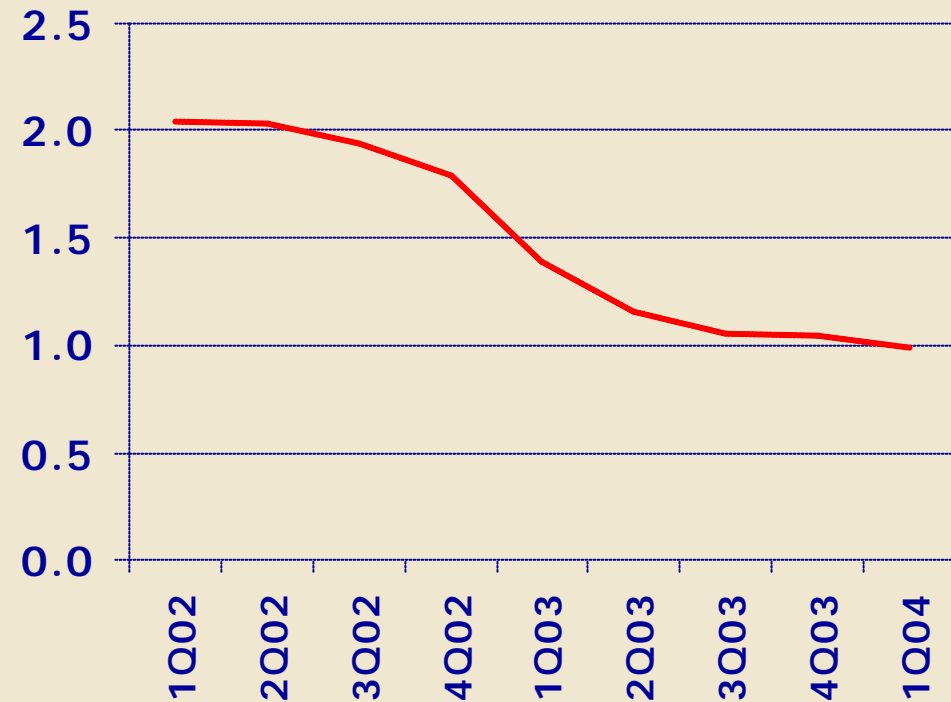
Current steepening of the 3-12m slope enhances profitability of mortgage book

# ... and its liabilities

## Retail Bk. deposits structure



## Deposit spread \* (%)



Liquid deposits: spread stabilisation

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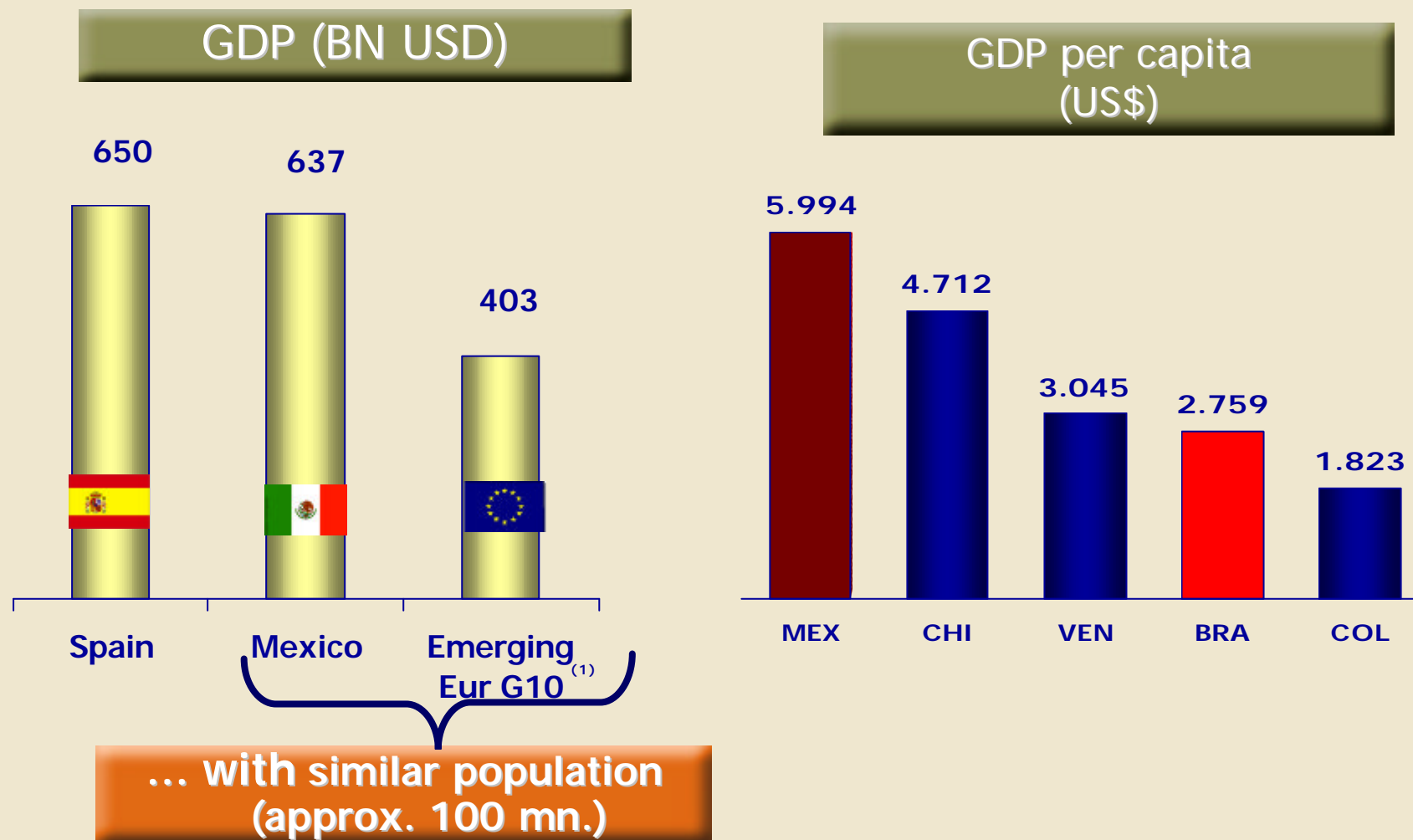
✍ Managing in a low interest rate environment in Spain

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✍ **The BBVA Bancomer case**

✍ Conclusions

# Mexico: a sizeable economy



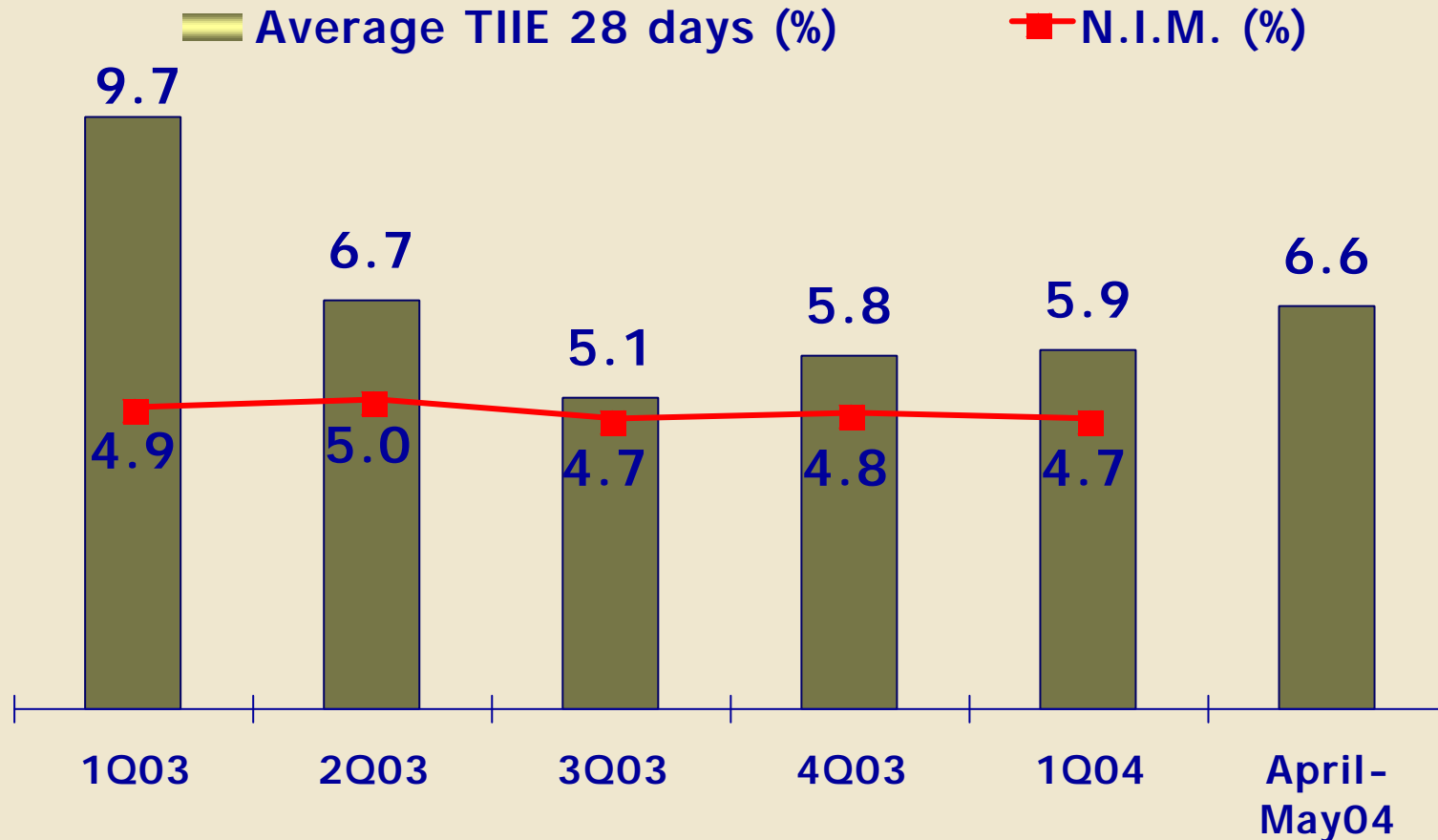
**Emerg. Eur. G10:** Group of 10 emerging countries in Eastern Europe, with 100 M inhabitants: Czech Republic, Estonia, Cyprus, Latvia, Lithuania, Hungary, Malta, Poland, Slovenia and Slovakia.



# ...entering a growth phase



# Despite lower rates, BBVA Bancomer has succeeded in defending the net interest margin ...

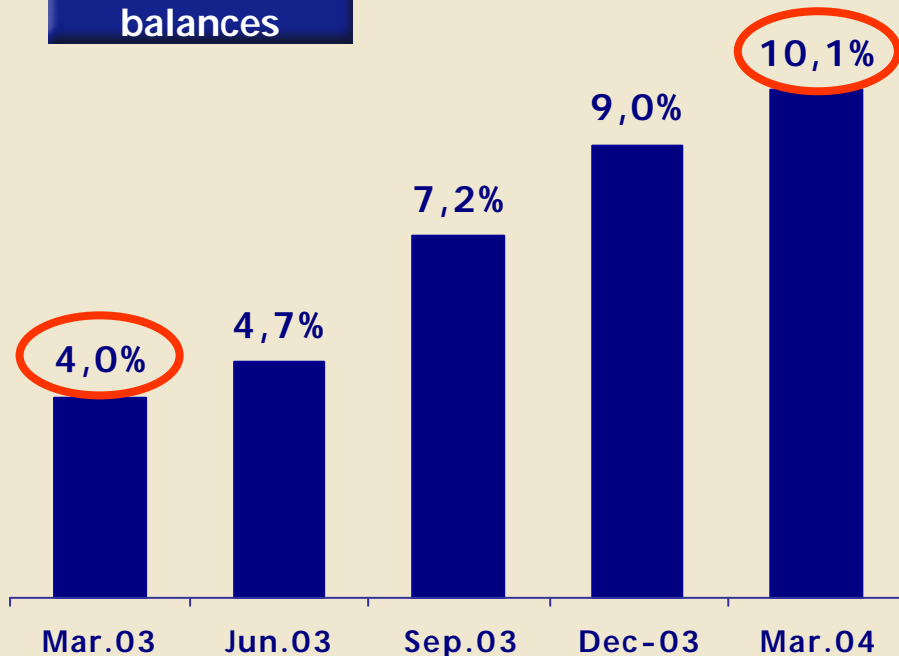


# ... growing its customer deposit base, while also improving the mix

y-o-y change

% growth by product

Average balances



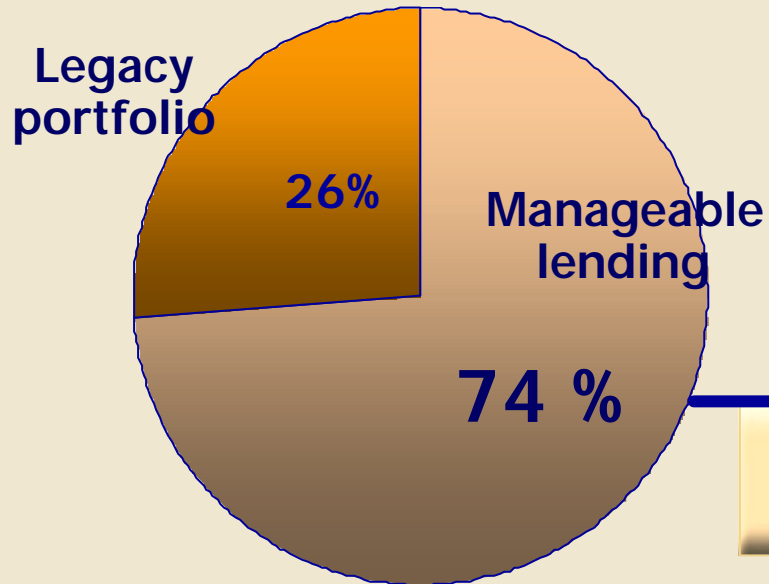
	Mar-03	Dec-03	Mar-04
Sight a/cs	+13.0	+18.1	+16.8
Term deposits	+14.7	+9.6	-6.5
Mutual funds	-6.9	+5.8	+23.7
<b>TOTAL (*)</b>	<b>+4.0</b>	<b>+9.0</b>	<b>+10.1</b>

\* Including repos

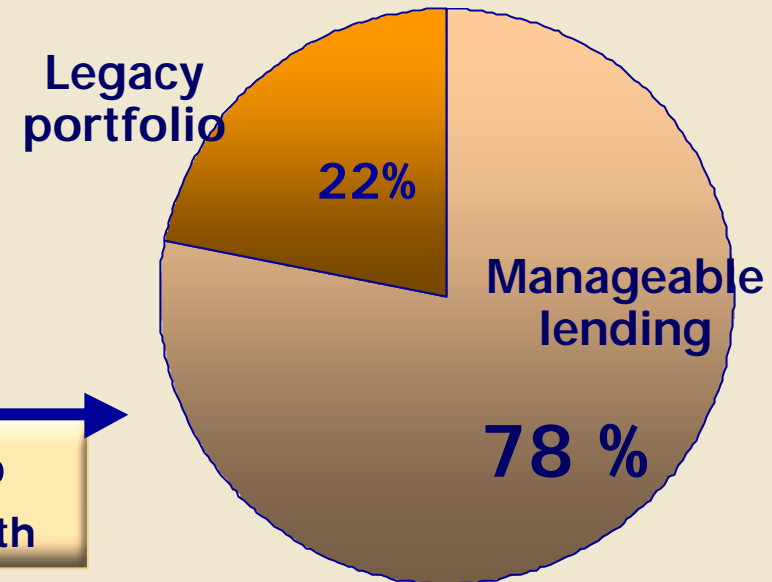
...with strong support from sight and savings accounts and funds

# ... and expansion of lending with focus in the most profitable segments

March 2003



March 2004



+15%  
Yoy growth

Commercial&Government

+12%

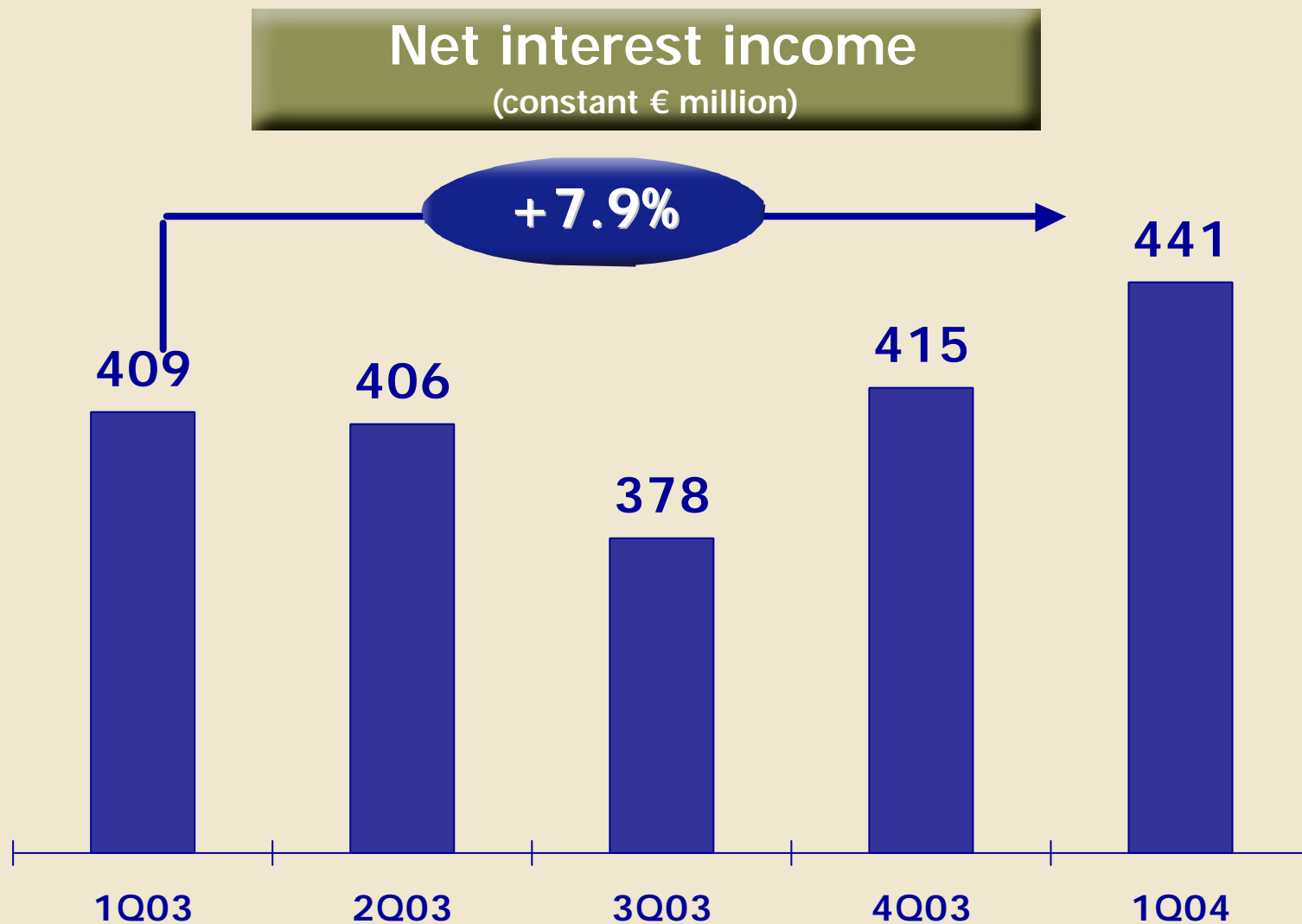
Consumer&Cards

+31%

Mortgages

+10%

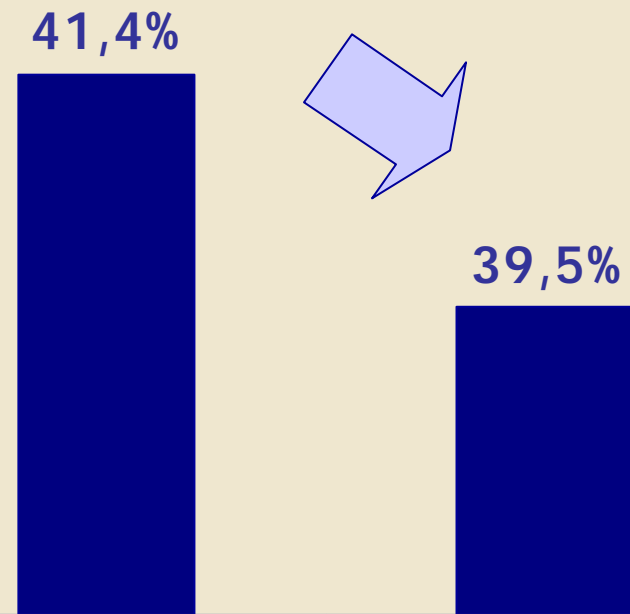
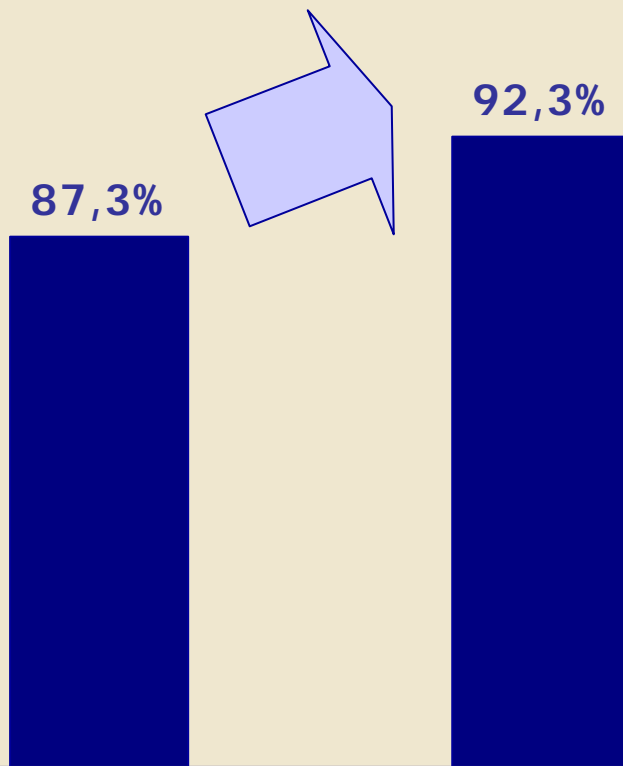
# Thus BBVA Bancomer has shown a significant increase in net interest income



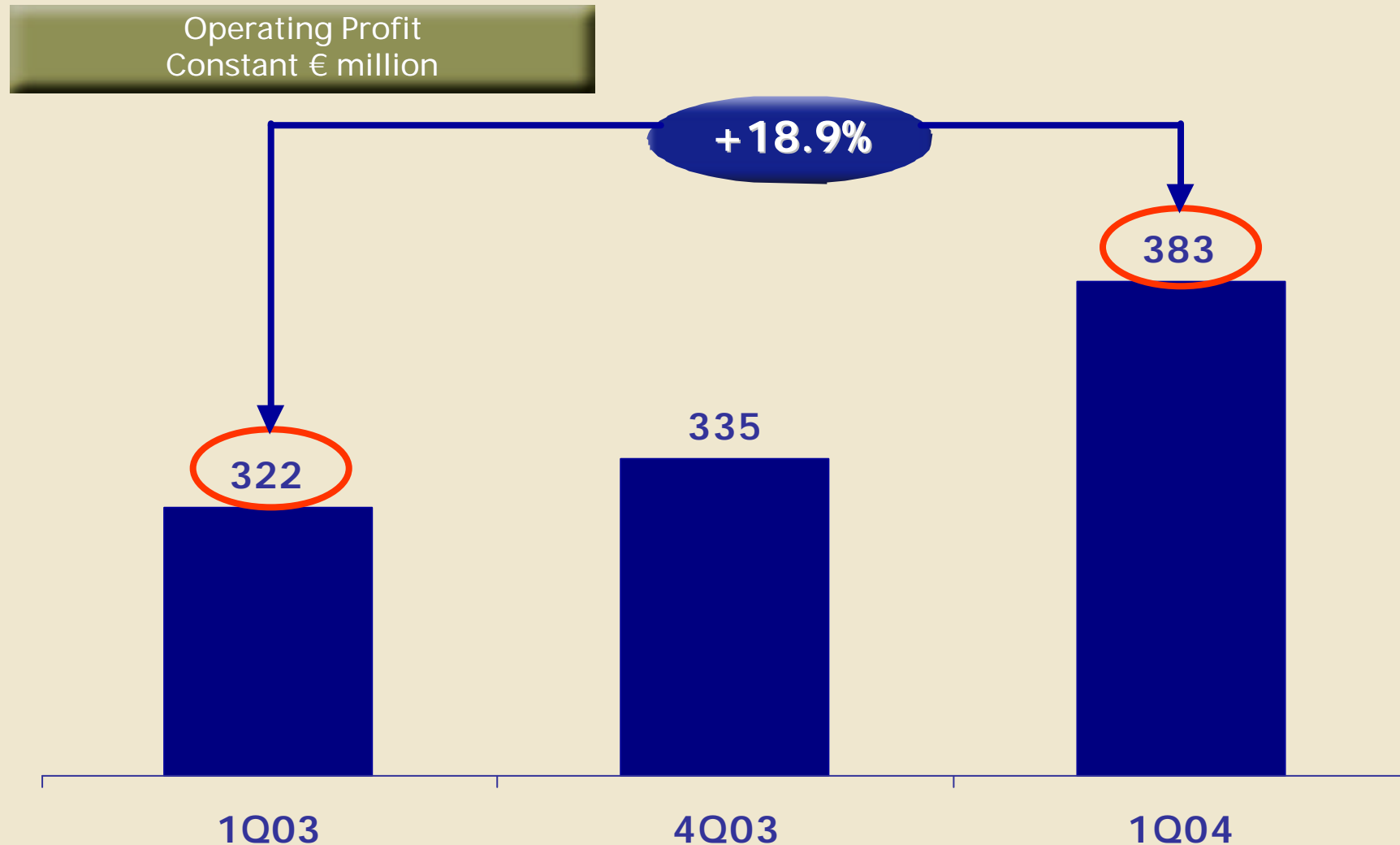
# In this context special emphasis in fees and gains in efficiency

Fee income / costs (%)

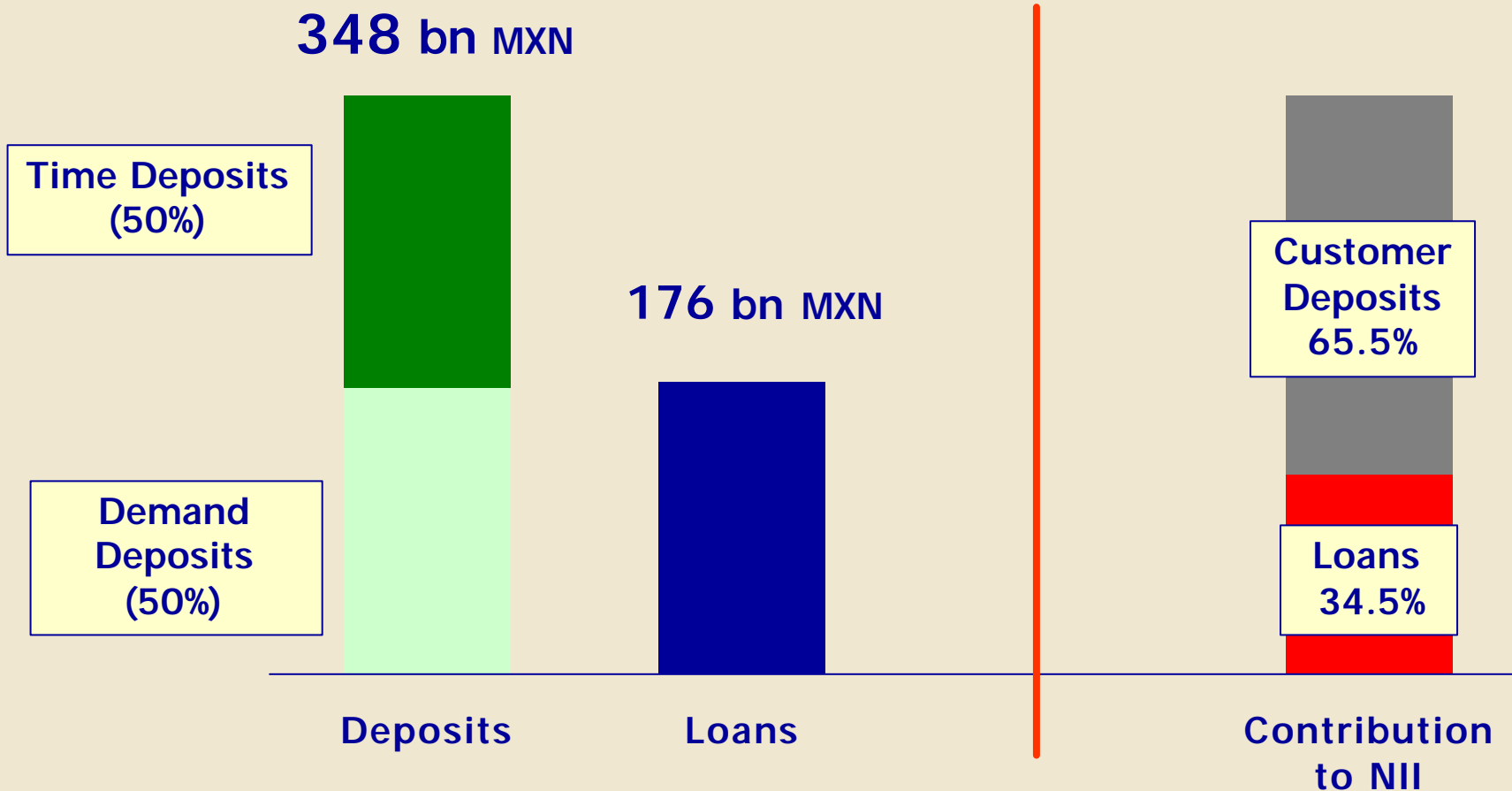
Cost / income ratio



# ... achieving the highest operating profit of recent quarters



# BBVA Bancomer: a deposit rich franchise

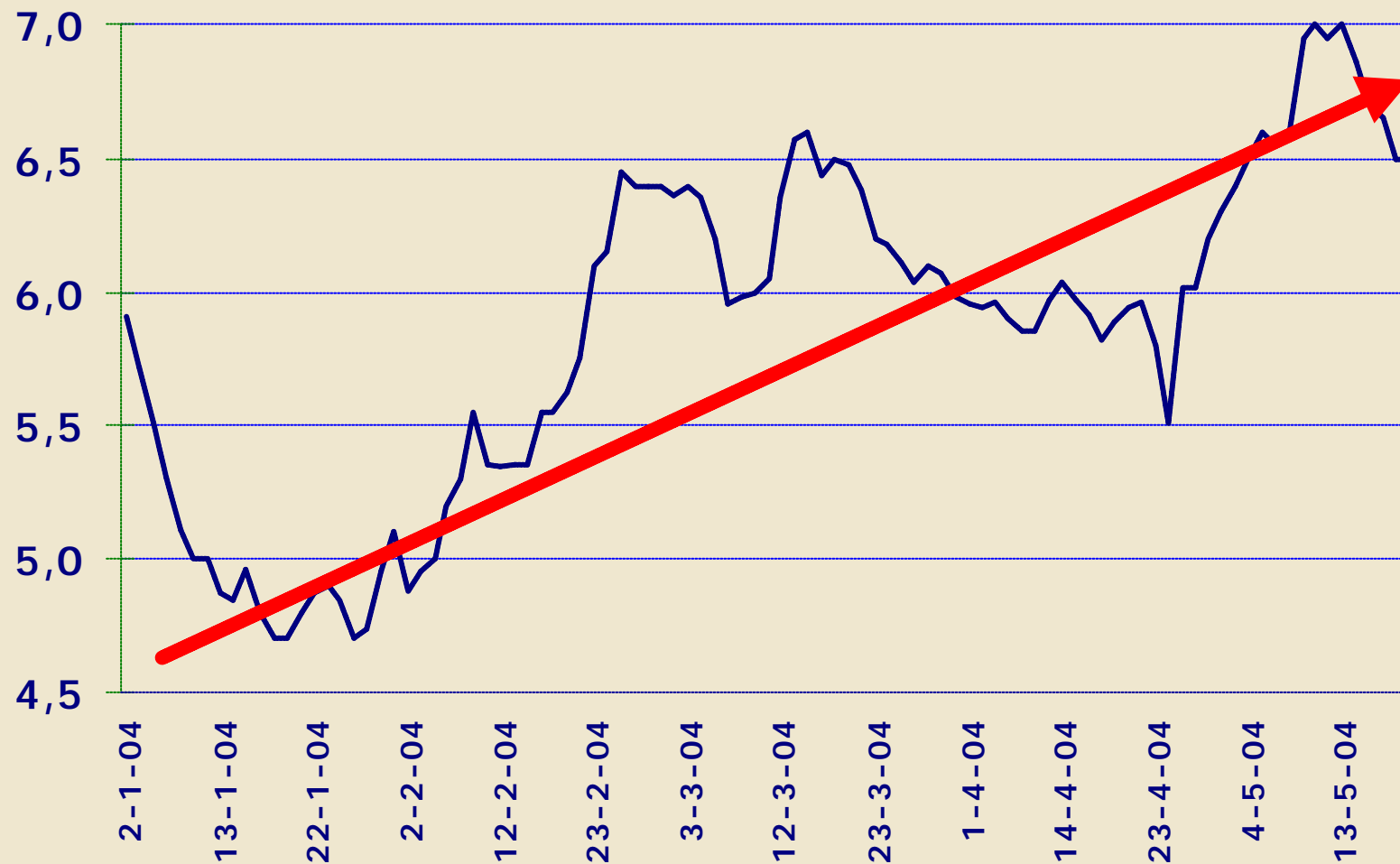


Well positioned for higher interest rates



# ... and the trend in interest rates has already changed

Cetes 28 days: 2004 evolution



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- ✍ Managing in a low interest rate environment in Spain
- ✍ Positioning for the new scenario
- ✍ The BBVA Bancomer case

✍ **Conclusions**

# We are creating a very solid Group

High Profitability

ROE

20.3%

Highly productive

Efficiency

46.0%

Controlled risks

NPL Ratio

1.23%

Coverage

209.8%

Solvency

BIS Ratio

12.1%

Rating

AA- / Aa2

...and growth in EPS of 25.1%

# Conclusions

- ✍ **BBVA has successfully implemented commercial and interest rate risk policies with good results, despite low interest rates**
- ✍ **Cost control and credit quality have also made a significant contribution**
- ✍ **The Group will benefit from the current steepening of the yield curve**

**On course to deliver a good evolution of results**

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