



*Sociedad de Gestión de Activos
Procedentes de la Reestructuración
Bancaria, S.A.*

ANNUAL ACTIVITY REPORT 2018



Sareb presents its 2018 Annual Activity Report

The orientation and approach of the content were determined by the conclusions of the materiality assessment, in line with the commitment undertaken by the company for continuously improving the transparency and quality of the information that is to be presented to its stakeholders.

The prospective information presented in this Activity Report is subject to the analysis of the current context and its expected evolution, without compromising those objectives for achieving it.



Cover Photo:

Sareb apartment building development in the centre of Madrid.



ANNUAL ACTIVITY
REPORT
2018

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1. INTERVIEW JAIME ECHEGOYEN



"Sareb is fulfilling the function for which it was created: to acquire problematic assets from financial institutions undergoing restructuring, to provide them with liquidity channels through the delivery of bonds, and to contribute to the normalisation of the property market without price distortions"



What is your overall assessment of 2018?

It has been another very demanding year, markedly affected by the market environment in which we operate. The major Spanish financial institutions have tried to make progress towards fulfilling the capital requirements demanded by the European Central Bank (ECB) by selling heavily discounted 'macro portfolios' of assets linked to the real estate sector. Given this situation, Sareb has opted to preserve the value of its loans and reduce sales in the institutional market, and this has affected its activity and results during the year.

These circumstances, together with the reduced likelihood of recovering debts from the financial asset portfolio after six years of activity and negotiation with debtors, have led us to focus on the conversion of loans into more liquid real estate assets to sell in the retail market.

On the property side, 2018 saw us reach a record number of sales, with the sale of 21,150 units, which is 12% more than in 2017. All this within the context of an asymmetric market in which some areas continue to show slow growth, in sharp contrast to the expansion seen in Madrid, Barcelona and some large coastal cities. A large part of Sareb's portfolio is located in these secondary markets, and this explains why we have implemented specific marketing plans, which led to a 68% increase in sales in certain provinces.

These figures are impressive in themselves, but we must not lose sight of the fact that we still have a great deal of work to do to fulfil our mandate.



After six years of activity, how far has the company progressed towards fulfilling its mandate?

We entered our seventh year having achieved a 44% reduction in the developer loan portfolio we acquired from financial institutions that were recipients of public aid. Taking into account the global portfolio of loans and real estate, our balance sheet has been reduced by more than 32%, meaning around €16,500 M.

We have also repaid about one third of the Government-guaranteed senior debt that we issued at the time of our incorporation, in order to acquire the assets. Overall, this liability has decreased by more than €15,000 M since 2012.

This has all been made possible by professional management that has enabled us to reduce Sareb's original number of debtors by more than 4,100, and to sell over 89,400 properties in the retail market, which has also contributed to the growth of the real estate sector.



As well as serving as a vehicle for restoring confidence in the financial sector and reactivating the real estate market, what additional impact has Sareb's activity had during its first years of operation?

"Sareb has also provided public administrations with 4,000 affordable rental housing units, in order to contribute, as far as is possible, to solving the social housing problems of vulnerable groups at risk of exclusion"

Looked at chronologically, it seems clear, and the Spanish and European economic authorities have highlighted as much, that Sareb continues to work to fulfil the function for which it was created: to acquire problematic assets from financial institutions undergoing restructuring, to provide them with liquidity channels through the delivery of bonds, and to contribute to the normalisation of the property market without price distortions.

Our activity between 2012 and 2018 also contributed more than €27,300 M to the Spanish economy, equating to 0.41% of the combined GDP for that period, according to estimates in the 'Report on the Social and Economic impact of Sareb (2013-2018)', published by the EY consultancy firm. All this has contributed, in turn, to the growth of local economies and the creation of employment throughout the various Spanish regions.

But the impact of our work in the economic sphere is not solely limited to the repayment of debt, contributing to the State coffers via taxes and the growth of the real estate market. Sareb has also provided public administrations



More information on the social and economic impact of Sareb

https://www.sareb.es/file_source/web/contentinstances/documents/informesactividad/contribucion-sareb-6-anos.pdf

with 4,000 affordable rental housing units, in order to contribute, as far as is possible, to solving the social housing problems of vulnerable groups at risk of exclusion. More than 2,300 of these homes have already been assigned to autonomous regions and local councils, providing housing for nearly 5,900 people.

Within the framework of its activity, Sareb is committed to the implementation of responsible management and compliance with the guidelines of the ten principles of the United Nations Global Compact, with a view to promoting sustainable development in areas relating to human rights, workers' rights, the environment and the fight against corruption.



How does Sareb plan to fulfil its divestment mission in the years it has remaining?

"We intend to achieve this objective by speeding up the process of converting our loans into properties, which are easier to sell in the retail market and also allows us to avoid the large discounts demanded in the institutional loan market"

It's a very demanding challenge that requires us to adapt to new market circumstances. We are approaching this stage with a new strategy that is especially focused on protecting the value of our assets. We intend to achieve this objective by speeding up the process of converting our loans into properties, which are easier to sell in the retail market and also allows us to avoid the large discounts demanded in the institutional loan market.

We have provided a strong impetus to this conversion in 2018, as collateral properties worth €1,400 M have entered our balance sheet, and we expect this figure to rise to €3,800 M in 2020.

At the same time, we will continue to work with top specialist managers to manage specific assets in our portfolio. This is the case with the vast majority of our ongoing property development projects and the land on which we want to build, which following on from our partnership with Värde Partners, will soon be managed by Aelca, a leading property developer. This partnership will allow us to continue to boost the recovery of real estate development, which has already led to approval for the construction of almost 7,000 homes since Sareb was created.

With this in mind, in 2017, we created the REIT Témopre Properties in order to optimise the management of real estate assets that are mainly rental properties. This vehicle, which has allowed us to divest part of our real estate portfolio, has attracted the interest of various investors, and we hope to sell our stake at some point in 2019. This experience demonstrates that we need to come up with specific solutions to manage each of the different assets we hold.

We will also pay special attention to our most singular properties, such as hotels and shopping centres, and ensure further progress with the territorial reorganisation of our structure, in order to be closer to our properties and customers.

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What is Sareb

Sareb was founded in November 2012, as part of the Memorandum of Understanding (MoU) signed between the Spanish and international authorities to assist the restructuring and recapitalisation of the Spanish banking sector.

The agreement established that a management company would be set up to which the properties awarded and developer loans would be transferred from banks undergoing difficulties due to their excessive exposure in the real estate sector, so that they could liquidate their assets in an orderly manner.

A key part for the recovery of the financial and real estate sector in Spain

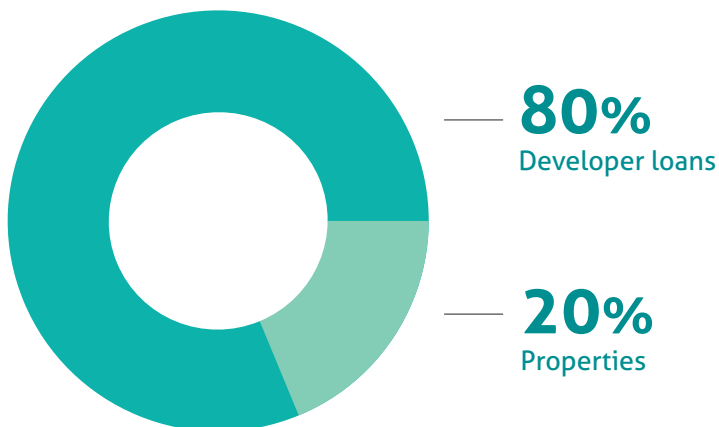
Sareb received

200,000 ASSETS

valued at

€50,781 M

of which...



Mission

Divesting assets optimising their value. Sareb has to guarantee its viability as a company in order to meet the commitments assumed with shareholders, investors and society as a whole.



Vision

Sareb is a private undertaking committed to fulfilling the public mandate that it has been entrusted with, contributing to the recovery of the financial sector and the Spanish economy. In this process the professional qualifications and ethics of its employees are crucial.



Values

Integrity: This means assuming that actions and attitudes will preserve the ethical standards of Sareb's corporate culture.

Transparency: Sareb assumes the commitment to openness in communicating its policies and procedures, aware that it acts under the watchful eye of society as a whole.

Civic engagement: The company operates under ethical standards and with socially responsible criteria.



More information on [What is Sareb?](https://www.sareb.es/es_ES/conoce-sareb/quienes-somos/que-es-sareb)

https://www.sareb.es/es_ES/conoce-sareb/quienes-somos/que-es-sareb

Business model

Long-term focus to maximise the value of the assets in our portfolio, to undertake the divestment mission efficiently, and to fulfil the commitment to repay senior debt

The effects of the systemic international financial crisis, which began in 2007, quickly became apparent in the Spanish economy, as most of the representative indicators show.

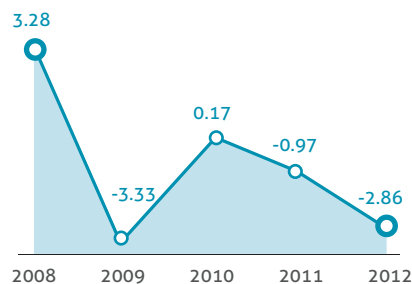


DIVESTMENT MODEL

STRATEGIC GUIDELINES TO THE 2019-2027 BUSINESS PLAN

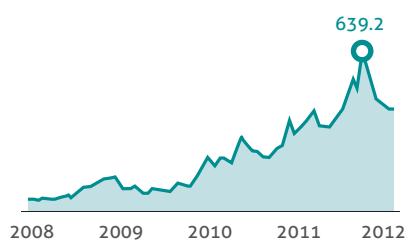
REDUCTION IN VOLUME OF THE PORTFOLIO

Year-on-year growth of GDP (%)



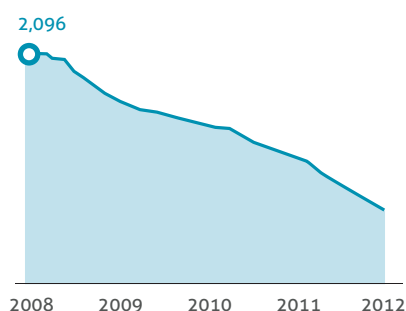
Source: National Institute of Statistics (INE)

Risk premium (basis points)

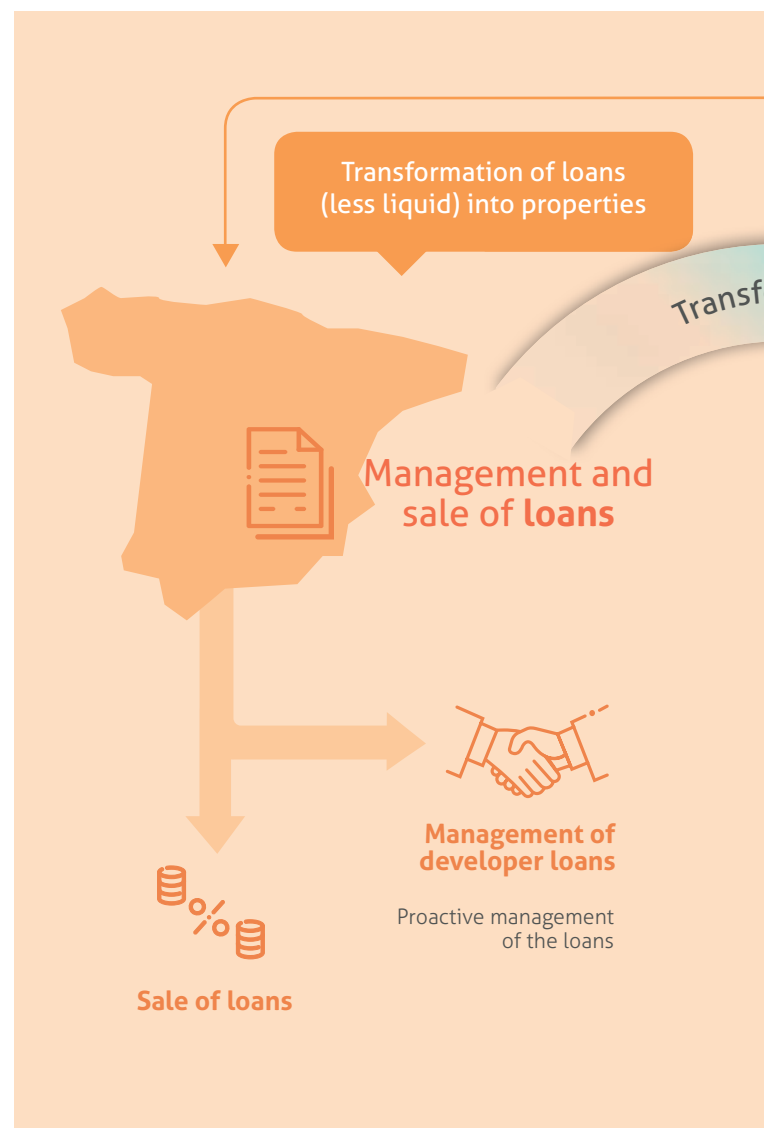
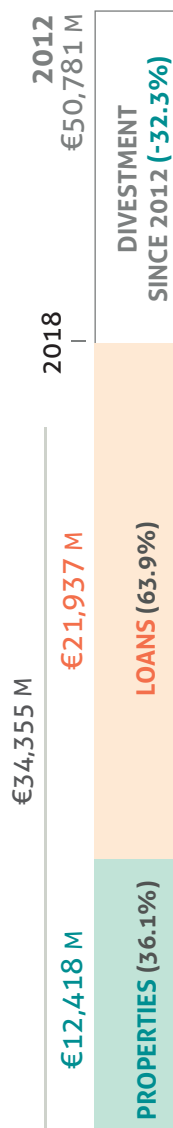


Source: Bloomberg.

Free-market housing price (€/m²)



Source: National Institute of Statistics (INE)



394
EMPLOYEES



4 SERVICERS



716
SUPPLIERS



32
SHAREHOLDERS



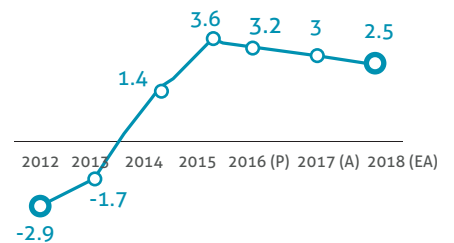
Following the creation of Sareb, and other the measures applied, the representative economic indicators have shown positive growth in the construction and real estate sectors.

INTENSIFICATION OF THE TRANSFORMATION OF THE BALANCE SHEET

INVESTMENT AND SPECIALISED MANAGEMENT FOR THE CREATION OF VALUE

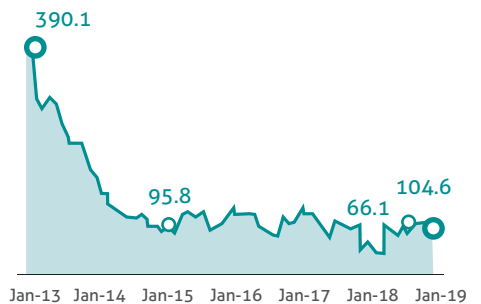
REPAYMENT OF SENIOR DEBT

Year-on-year growth of GDP (%)



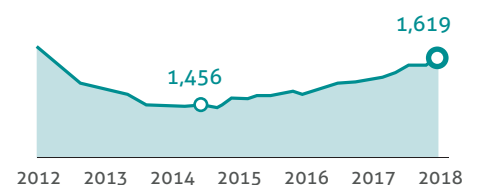
Source: National Institute of Statistics (INE).
Forecasts: Bank of Spain.

Risk premium (basis points)



Source: Bloomberg.

Free-market housing price (€/m²)



Source: National Institute of Statistics (INE).

Territorial branch offices to give an impetus to divestment

Retail property sales

Management and sale of properties



Stock of homes for renting

Creation of the REIT Tempore Properties

Sareb handles the management and maintenance of the properties making up its portfolio until the moment of sale.

Property development and promotion

- Construction of new developments
- Completion of unfinished construction work

REDUCTION SINCE 2012
€15,020 M (-29.6%)

2012
€50,781 M

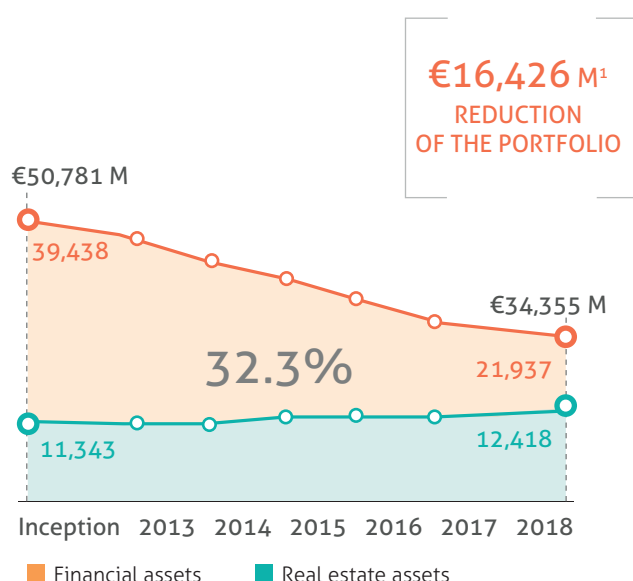
2018

€35,761 M

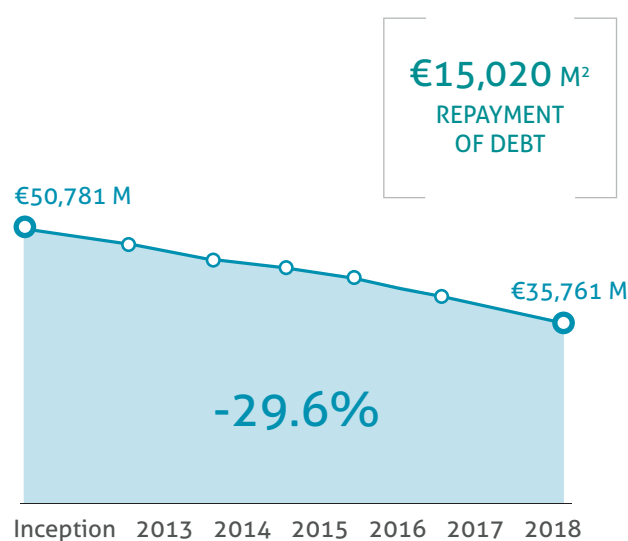
Our milestones during this time

Balance 2012-2018

1. Reduction of the portfolio



2. Reduction of debt



2012

- Incorporation of Sareb.
- First subordinated debt subscribed.
- Assets received from BFA-Bankia, Catalunya Banc (CX), Banco de Valencia, Novagalicia Banco and Banco Gallego.

2013

- Second subordinated debt subscribed.
- Assets received from Liberbank, Caja 3, CEISS and BMN.
- Approval of the Sareb Code of Conduct.
- Closing the first institutional operation with the allocation of the 'Bull' portfolio.
- Creation of a pool of 2,000 properties for social purposes which subsequently would be increased to 4,000.

2014

- It was announced that €259 M had been written-off from the loan portfolio.
- Signing of the first agreement for assignment of social housing.
- Management of the assets was assigned to four real-estate management companies or *servicers*: Altamira, Haya Real Estate, Servihabitato and Solvia.

2015

- Further write-off of €719 M from the loans portfolio.
- Launch of the new Sareb website, which shows all the properties being marketed by the company.
- The Bank of Spain Circular was published which establishes the criteria for valuing Sareb's assets.
- For the first time, Sareb announced the development of land it owns.

¹ Not including accumulated amortisation/depreciation or impairment.

² Includes amortisation of €169 M of the *escrow account* charged to 2018 and repayment of €504.9 M in 2019 charged against the cash generated in 2018.

Key figures



€24,343 M

INCOME³



€2,784.6 M

INTEREST PAID TO THE
ASSIGNING BANKS



89,430

PROPERTIES
SOLD



63,437

PROPOSALS FROM
DEVELOPERS
MANAGED



6,958

PROPERTIES
APPROVED FOR
CONSTRUCTION



4,000

HOMES
FOR SOCIAL
PURPOSES

2016

2017

2018

- A further recovery to the Sareb portfolio with €2,044 M in provisions⁴.
- The company approved the capitalising of €2,170 M of subordinated debt to cover write-offs in the portfolio.
- Closing the largest institutional transaction, the sale of the 'Eloise' portfolio, for a nominal value of €553 M.
- Creation of the area for Development, Promotion and Investment to enhance the value of its portfolio.
- Launching of the online channel for the sale of loans.
- Creation of the REIT, Témopre Properties, with a portfolio of 1,554 assets transferred by Sareb for the value of €175 M.
- Témopre Properties makes its debut on the Alternative Stock Market (MAB).
- Collaboration agreement signed with the Government of Murcia to promote the economic and social development of the region.
- The company advances toward a territorial structure by setting up five branch offices.
- Sareb inaugurated the Sheraton hotel Hacienda del Álamo Golf & Spa Resort, in Murcia.
- Sareb launches a competitive process to sell its stake in Témopre Properties.
- Sareb and the Spanish Federation of Municipalities and Provinces (FEMP) sign a collaboration agreement that will simplify and streamline the payment of Property Tax (IBI) and local taxes for the company's properties.

³ Includes the transfer of €145 M of assets to Témopre Properties at the end of 2018, within the framework of a ROFO agreement signed between Sareb and the REIT.

⁴ From application of the 2015 Bank of Spain Circular which establishes the criteria for valuing Sareb's assets and requires it to capitalise €2,171 M of the company's subordinated debt.

Beyond our mandate: a vision for the future

The long term as a fundamental variable in the company's decision-making process

Sareb's decision-making is based on a long-term vision that allows the company to maximise the value of its assets and efficiently fulfil its mandate. To this end, Sareb has launched initiatives that will allow the company to increase margins in the future, even though this involves current investment and containment of income, with their consequent impact on present results.

Beyond fulfilling its liquidating mission, the company aspires to transcend its useful life by contributing to the development of the sector and growth of the market through innovative initiatives.

Revitalisation of the real estate market and innovation in loan management



Témpore Properties

Sareb has promoted the creation of a REIT specialising in the rental of residential properties, in order to accelerate the divestment rate of its property portfolio. By the end of 2018, the company had already transferred 2,249 homes to Témpore Properties, and was working on a competitive process to sell its stake in the REIT.

Témpore Properties commenced operations in 2017, with a portfolio valued at €175 M. This total reached €339 M by the end of 2018, following a new transfer of assets from Sareb to the REIT. It is expected that improvements in the management of its stock of homes will allow Témpore Properties to achieve a gross return of 5.5% by 2020.



Picture: Apartment building in Arganda del Rey (Madrid).



Online channel for the sale of loans

The company has also launched a pioneering online channel for the sale of loans, which brings greater visibility, dynamism and transparency to the market for sales of non-performing loans (NPL⁵).

The objective is to provide maximum information to potential buyers who have already been referred to financing or servicing providers.



Sales Growth Plans (SGP)

The Sales Growth Plans are initiatives with Sareb debtors for them to sell properties which are set up as collateral for their loans and in this way obtain the liquidity necessary to reduce their debt to the company.



Visita.Me

In its pilot phase, Visita.me is a mobile application that enables anyone interested in Sareb properties to organise their visit independently and easily via the app.

Value-adding projects, focussed on specialisation, to optimise the divestment of the asset portfolio



Esparta Project

In 2014, Sareb launched the Ibero Project, which concluded with the hiring of Haya Real Estate, Solvia, Altamira Asset Management and Servihabitat as *servicers* responsible for the management and marketing of a large part of Sareb's portfolio. In the intervening period, the *servicing* market has evolved. Operators have undergone significant changes and new players have appeared. At the same time, Sareb has gained experience and knowledge in the efficient management of its assets.

In this context, and before the expiry of the current contract with Haya Real Estate in 2019, Sareb is already studying alternatives to strengthen the

efficiency and agility of its portfolio management. This analysis has allowed the company to determine three fundamental pillars on which to base its future *servicing* model:

- Manager specialisation in certain activities (such as maintenance) and the development of certain specific activities from Sareb.
- Centralised information about Sareb assets to enable any operator to manage this information with greater flexibility.
- Territorial management of the complementary portfolio, with the creation of five branch offices in 2018.

⁵ NPL - Non-performing loans.



Specialised property development management

2018 saw Sareb working on the selection of a specialised partner for the management of its property development business. In 2019, the company plans to create a vehicle for transferring land, works in progress and unfinished projects, which will result in thousands of homes being put on the market.

Management of these assets, which will be undertaken by Aelca, will allow us to optimise the costs associated with project development and increase margins deriving from the marketing and sale of the properties.

Contribution to economic and social development of the geographical areas in which Sareb operates

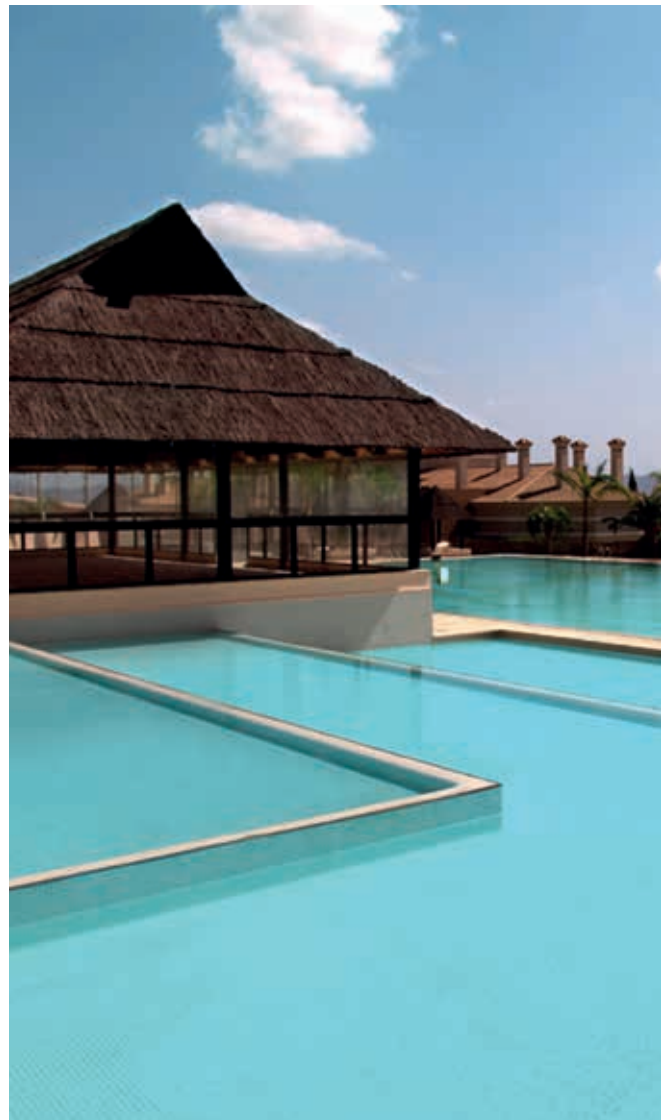


Hacienda del Álamo Golf & Spa Resort

In 2018, Sareb opened the Sheraton Hacienda del Álamo Golf & Spa Resort, leased to the ADH Hoteles Group, along with the operation of the apartments on the complex. Since Sareb took over its management in 2013, the company has been committed to modernising and reopening the the property, and has invested a total of €8.6 M in the completion and refurbishing of the resort, as well as an additional €10 M for maintenance.

As well as breathing new life into the real estate sector in the Region of Murcia, in which Sareb has an important portfolio of assets, the resort has also contributed to boosting local tourism and economic development, with the direct creation of 120 jobs.

This contribution to the development of this autonomous region is reflected in the signing of a collaboration agreement between Sareb and the Government of Murcia to promote economic and social development in the region. Measures designed to attract new investment to the Region include Sareb's commitment to facilitating the locating of real estate for the development of industrial and business projects of common interest, and the provision of promotion and presence at trade fairs and events in the real estate sector.



Picture: Hotel Sheraton Hacienda del Álamo Golf & Spa Resort, in Fuente Álamo (Murcia).



Sareb in the world

The role played by Sareb in the financial restructuring has become an example to be followed in other countries which are currently looking for formulas similar to the one applied in Spain for restoring the health of their financial systems.

Since its creation, Sareb has held meetings with international authorities interested in learning about the company's experience. These include Slovenia, through the BAMC⁶, and Vietnam, through its State Bank. In 2018, Sareb continued to exchange knowledge and experiences with other agencies and met with delegations from Mongolia and Kazakhstan. Sareb has also participated in a series of meetings promoted by the World Bank to highlight the Spanish experience of managing non-performing loans.



More information on [International reference](https://www.sareb.es/es_ES/conoce-sareb/referencia-internacional)

https://www.sareb.es/es_ES/conoce-sareb/referencia-internacional

⁶ Slovenia's Bank Asset Management Company (BAMC).

Social footprint

Committed to improving access to housing in partnership with public administrations

Sareb's social vocation forms an integral part of its mission, which establishes the company's commitment to paying off the debt underwritten by the Spanish Treasury. This commitment to responsible and efficient portfolio management is complemented by its contribution to alleviating the housing shortage for groups at risk of exclusion.

To this end, the company has promoted the creation of a pool of 4,000 social housing properties, and has signed agreements for the assignment of these homes to regional governments and local councils. 2018 saw the signing of an agreement with the Elche Town Council, which is added to those agreements reached with other administrations, which already benefit almost 6,000 people

Social housing initiatives and their main results

Affordable homes aid

Temporary assignment of properties to groups at risk of social exclusion.

Aid to groups in a situation of social emergency

Temporary assignment of properties to groups who are in exceptional circumstances.

Alternative affordable rentals

In collaboration with the social services, it is proposed as an alternative housing solution for families who are socially vulnerable.



4,000

Pool of properties intended for social purposes



2,367

Properties committed for rented social housing with autonomous regions and town councils



5,893⁷

People who have benefited from the social housing programmes with autonomous regions and town councils



764⁸

People benefiting from agreements with Sareb itself for assignment of properties


⁷ Estimate based on the average size of homes according to the National Institute of Statistics (INE) (2.49 people in 2017) (considering committed properties).

⁸ Estimate calculated for an average of 4 people per unit in properties assigned through agreements signed with Sareb itself.

**10****Agreements with autonomous regions**
(Number of homes)

	
Andalusia	400
Aragón	80
Balearic Islands	75
Canary Islands	50
Cantabria	40
Castile and Leon	100
Catalonia	930
Extremadura	45
Galicia	50
Basque Country	10

**7****Agreements with town councils**
(Number of homes)

	
Barcelona	200
Madrid	300
San Sebastián de los Reyes	9
Malaga	6
Seville	15
L'Hospitalet de Llobregat	50
Elche	7



Picture: Apartments in the Hacienda del Alamo Golf & Resort complex, in Fuente Álamo (Murcia).

Jobs with social value

The company also demonstrates its commitment to residents of its rented social housing through the development of initiatives aimed at improving their employability and integration into society.

In 2018, Sareb launched the programme 'Building future: jobs with social value', which it implements in collaboration with the Integra Foundation. This initiative was set up to help people at risk of social exclusion holding a social rental contract in a Sareb

property.

The programme makes available to people in a vulnerable situation the social and employment tools that they need for being able to enter the employment market. In 2018, training workshops were given by 24 volunteers -employees of Sareb- and took place in the Strengthening Schools of the Integra Foundation.

**30**
participants
in vulnerable
circumstances**2**
training
workshops
in the Integra
Strengthening
School**10**
participants in the
programme
have found a job

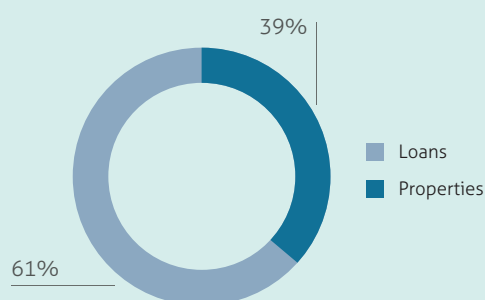
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Main figures in 2018

Advances for the fulfilment of our mandate

INCOME FROM MANAGEMENT AND SALE OF PROPERTIES AND LOANS (% of €M)



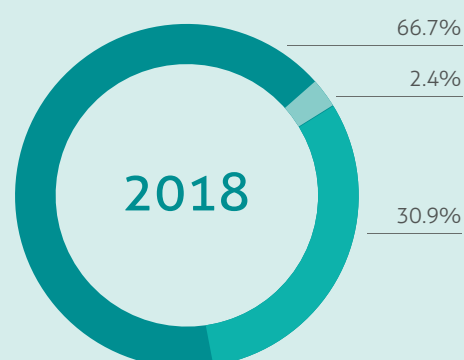
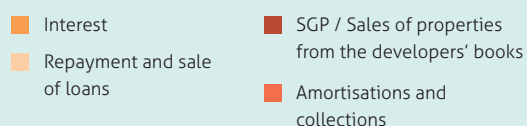
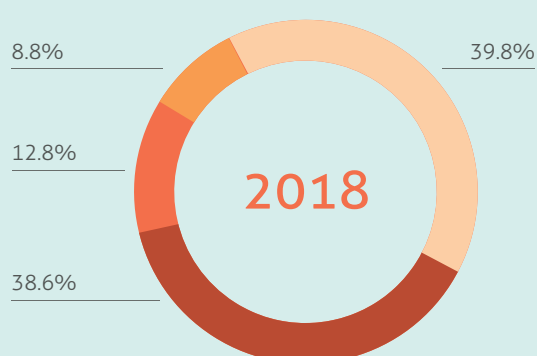
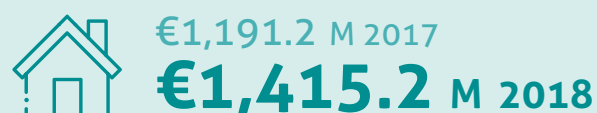
TOTAL INCOME



LOANS

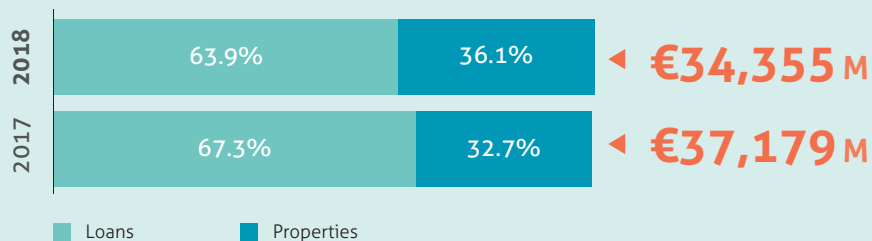


PROPERTIES



⁹Includes the transfer of €145 M of assets to Tempore Properties at the end of 2018, and other income totalling €22.8 M.

PORTFOLIO OF ASSETS



-7.6%
vs 2017

MANAGEMENT AND SALE OF LOANS



12,076

Proposals managed

-8.0% vs 2017



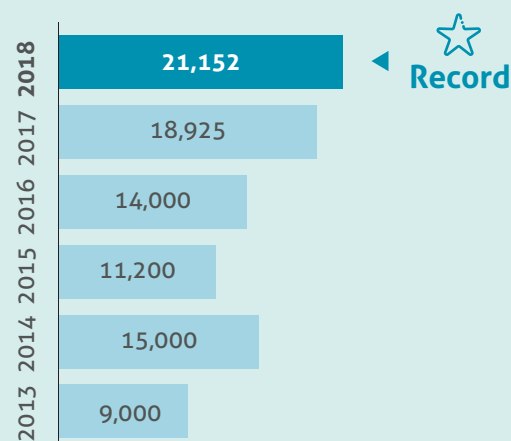
13,239

Number of debtors

9.2%
less than at the end of 2017

MANAGEMENT AND SALE OF PROPERTIES

Number of units



PROPERTY DEVELOPMENT



1,636

New properties approved in 2018

981
Sold

585
Delivered

331
Completed



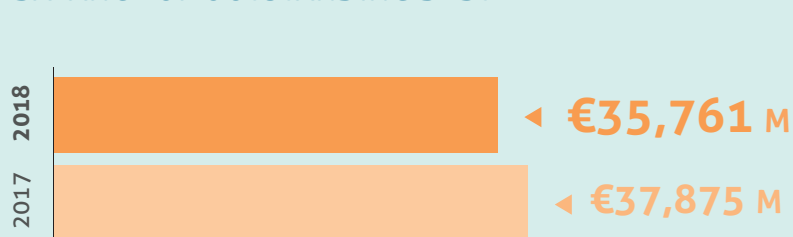
21,152

Properties¹⁰ sold in 2018

Own units
13,329

Agreements with developers
7,823

BALANCE OF OUTSTANDING DEBT



-5.6%
vs 2017

¹⁰ Residential, commercial property and land

Evolution of the Business Plan

Sareb remains committed to its obligation to submit the objectives and strategy of the Business Plan for annual review

Significant changes in the real estate market in 2018 have had an impact on the implementation of the strategy contained in the 2018-2027 Business Plan.

As a result, the review, which was approved in the first months of 2019, reflects a substantial change in strategy, in line with the changes that occurred in the sector and medium-term projections for the real estate market.

This new update of the Plan puts the preservation of the economic value of its assets at the centre of the company's vision, and envisages more moderate growth than the forecasts made in previous years, in line with the growth forecasts for the Spanish economy indicated by international organisations.



Picture: Sareb apartment building development in the centre of Madrid.

Fulfilment of the Business Plan in 2018

At the close of December of 2018 the degree of compliance with the objectives of the Sareb Business Plan stood at 82% from the perspective of revenue, and at 80% in respect of margins.

Levels of progress during the year have varied between business lines, with the most positive results achieved in the areas of real estate asset management and sales, with target fulfilment at 80% and 100%, respectively.

The geographical distribution of company sales is in line with Business Plan projections, with a lower concentration of Sareb assets in market areas showing growth. This can be put down to the nature and location of the portfolio the company is working to divest, rather than the slowness of the market, which continues to evolve in an uneven way.

The management and sale of financial assets has recorded more moderate growth, due to the emergence of new market competitors and the amount of discount demanded in portfolio sales transactions. As a result, target fulfilment levels are 83% for revenue and 72% in terms of net margin.

However, it should be remembered that the maturity and expiry dates of the loans in the portfolio will result in an ever-increasing reduction of revenue in business lines relating to repayment and cancellation or interest. This decrease will also result from the process of converting loans into real estate as a means of divestment. Consequently, reductions in revenue and margins for these items in 2018, compared to 2017, stand at €83 M for revenue and €43 M for net margin.

Keys to the 2019-2027 Business Plan

The Sareb 2019-2027 Business Plan is based around a mechanism that allows the company to address the challenges posed by the current context, while maintaining a balance between disinvestment rate agility and the maintenance of the value of its assets.



Reduction in volume of the portfolio

Search for alternatives and new formulas that contribute to operational efficiency and divestment

Implementation of a new relationship model with its *servicers* that seeks to improve the efficiency of the company through tighter control of information on the part of Sareb, greater proximity to the territory and the specialisation of certain services.

This new approach to the way we operate will also contribute to the achievement of substantial savings in the cost of servicing.

Regional sales growth plans will be maintained in order to ensure adequate rotation of the portfolio and to counteract downward pressure on the price of other properties.

Sareb is committed to the generation of value for its rental real estate assets, whether residential or commercial, through the REIT *Témpore Properties* or other types of structures.



Picture: Hacienda del Álamo Golf & Resort, in Fuente Álamo (Murcia).



Intensification of the transformation of the balance sheet

Greater liquidity: acceleration of the process of converting of loans into properties

In the light of current conditions in the loan market, and in line with the maximisation of the recovery value of assets, the company has opted to avoid the divestment of NPL loans in the form of financial assets.

This decision allows the company to protect the current value of assets and optimise future value through sales in the retail channel.

In the case of loans, where recovery capacity is focussed on taking possession of collateral, the company carries out a process of reorganisation, publication and sale in the retail market.

Sareb is also working hard to recover value, over and above the value of collateral of the financial assets, which requires management over a period of time for achieving a flow of properties unencumbered by the borrowers or their guarantors or bondsmen, or that are not pledged in guarantee of other assets.



Investment and specialised management for the creation of value

Optimisation of the value of the portfolio through the reserving of assets for property development and sale in the medium term

Greater amount of resources assigned to assets with potential for maximising value in the medium term:

- Promotion of new developments on Sareb-owned land, completion of work in progress and investment in land obtained from the management and foreclosing of collateral properties for urban development.
- Partnership with a manager specialised in residential property development, which will allow activity to respond more dynamically to the characteristics of each area and potential customers, and adjust to supply and demand more effectively.
- Further progress on land, with a view to converting such real estate assets into development land with greater market value.
- Application of the repositioning strategy employed with the Sheraton Hacienda del Alamo Golf & Spa Resort to other single assets with similar characteristics.

The market and trends for the sector

A favourable economic context...

2018 saw average GDP growth in Spain of 2.5%, mainly due to improvements in the economic situation of the population and better access to financing.

... accompanied by the recovery of the real estate market...

Residential property market

Housing

- The number of homes sold has grown by 9% compared to 2017, with similar forecasts for the coming years.
- Second-hand properties represent 90.9% of total sales.
- House prices have risen by an average of 3%, with slight spikes driven by the increase in prices in major cities and some coastal towns, given that growth is uneven by region.

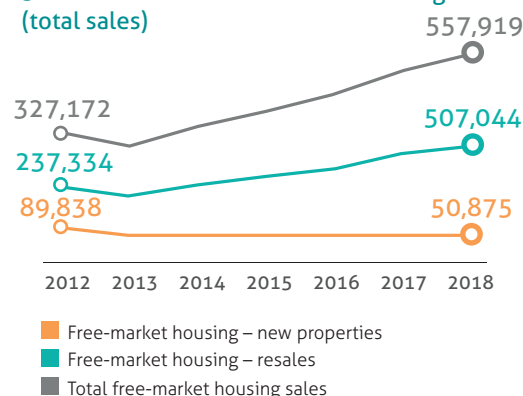
580,000
homes¹¹ sold
in 2018

1,619 €/m²
at close of 2018

Major and minor variations in average price

- | | | | |
|-----------|-------------|---------------|----------|
| ▲ Melilla | ▲ Madrid | ▼ Ciudad Real | ▼ Teruel |
| ▲ Malaga | ▲ Barcelona | ▼ Zamora | ▼ Ceuta |

3. Transactions for free-market housing (total sales)



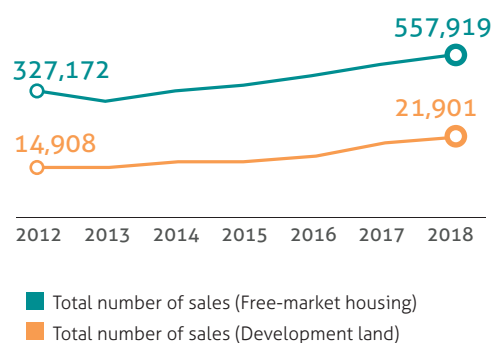
Land

- Investment in land for housing development continues to grow. In 2018, land transactions increased by 5.3% to 21,901 units.
- The price of land varies by region, with the highest values concentrated in Madrid, Guipúzcoa and the Balearic Islands and the lowest prices found in Palencia, León and Zamora.
- The outlook for 2019 is positive, due to an upturn in new construction projects.

21,901
units
sold in 2018

159.7 €/m²
(average in 2018)

4. Transactions for free-market housing and land (total sales)



¹¹ Includes free-market housing and subsidised housing.

Non-residential property market



Offices

- The sector is going through a period of expansion. Current average rent for office space is above eight euros per square metre per month.
- The largest volume of investment and rentals is concentrated in Madrid and Barcelona.



Commercial premises and shopping centres

There is a growing investor appetite for retail. High street investment exceeds €1,200 M in 2018, although shopping centres and flagship stores maintain their upward trend.



Industrial and logistics-related properties

Demand is increasing in the major cities, but availability is decreasing. This shortage of available space attracts demand for logistics space in secondary markets. Electronic commerce, and its potential in this sector, are attractive to investors.

Loans

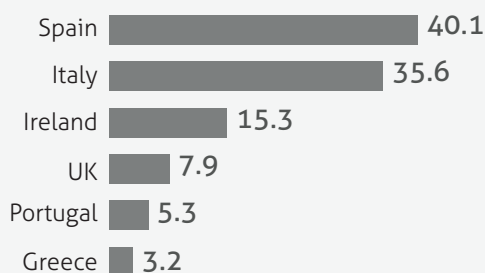
The year has been marked by intense divestment activity by Spanish banks in order to reduce their exposure to real estate risk. This has generated very strong competition in the market for the sale of loans and assets linked to real estate.



€40,100 M¹²
in 2018

Transactions involving allocated assets and NPL linked to the real estate sector of Spanish banks.

5. Spain: European leader by volume of transactions in 2018 (billion euros)



¹² Source: Evercore (2019)

... and new challenges on the horizon.



Demographic and social change

By 2027, Spain will have a population of over 48 million. More than a quarter will be over the age of 65 (INE, 2018). There is also a trend towards smaller families and households, single-parent families, singles, people living alone...



Energy efficiency in buildings

Buildings consume 40% of the energy used in the European Union (EU). In line with the Paris Agreement, the EU has established an indicative target for improving energy efficiency by at least 27% for 2030.



Innovation applied to real estate business

The use of technology such as virtual reality, artificial intelligence, internet of things and big data, is transforming how the sector operates.



Resilient infrastructures to climate change

Investment in low-carbon infrastructure, combined with structural improvements, could increase the world GDP by up to 5% by 2050, while at the same time reducing CO₂ emissions and mitigating the risks associated to extreme weather events (OECD, 2017).



Smart, interconnected cities

The market for smart cities will increase to 1.29 billion in 2020 (Bank of America Merrill Lynch, 2017). The incorporation of technology seeks to improve the efficiency and conditions for city living.



New models of residential properties

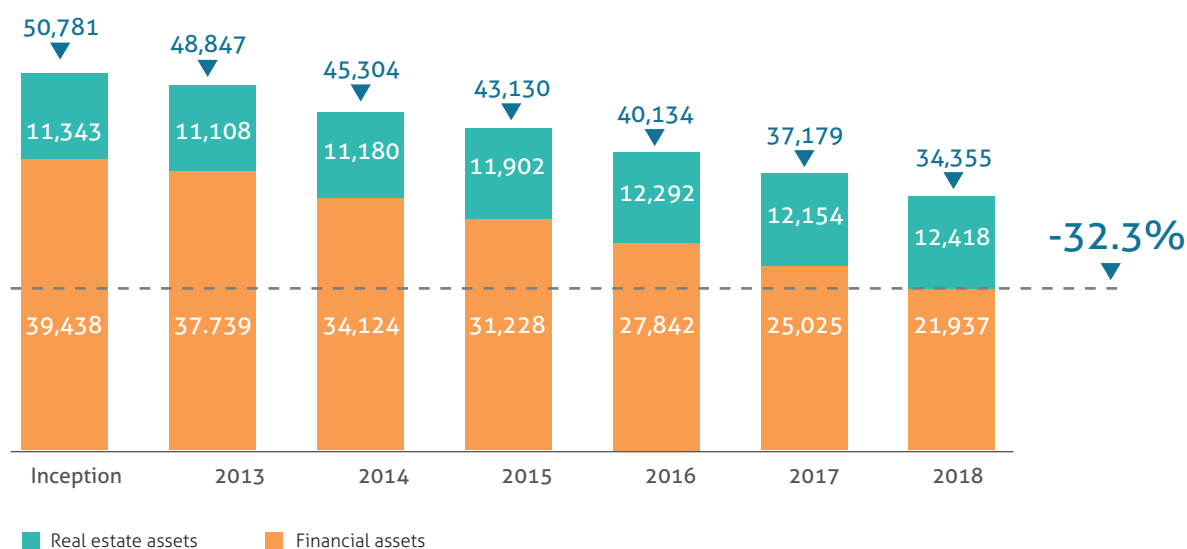
The emergence of new models for living together, such as co-living –shared living spaces– becomes more relevant and is a boost for the market for these properties.

Divestment of the portfolio

Sareb's asset portfolio has decreased by 32.3% since its inception

At the close of 2018 the asset portfolio went down to €34,355 M – a 7.6% decrease compared to December 2017. Compared to the original starting portfolio of €50,781 M, this figure represents a reduction of 32.3%.

6. Evolution of the portfolio (€M)¹³

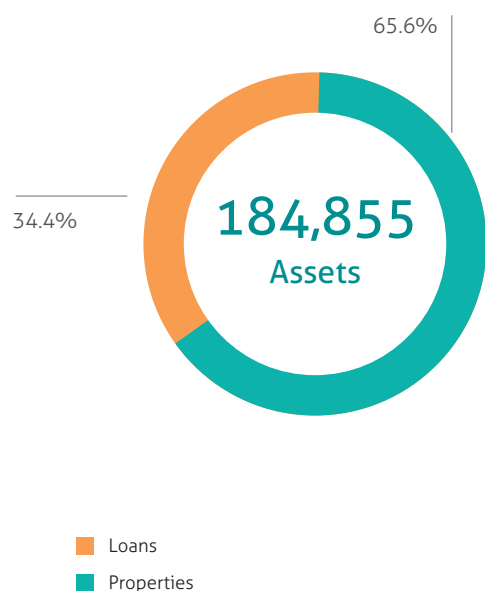


7. Composition of the portfolio (% of €M)

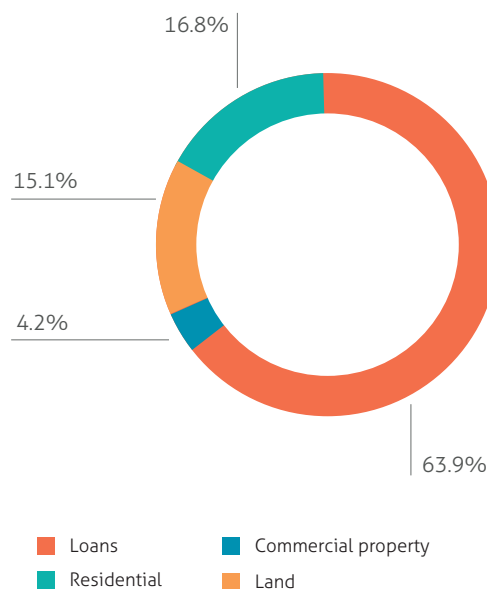


¹³ Not taking into account amortisation/depreciation or impairment.

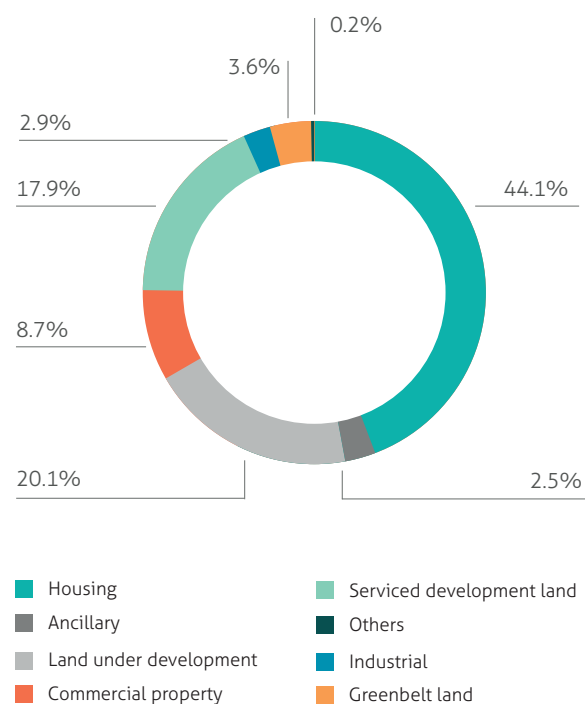
8. Composition of the portfolio (number of assets)



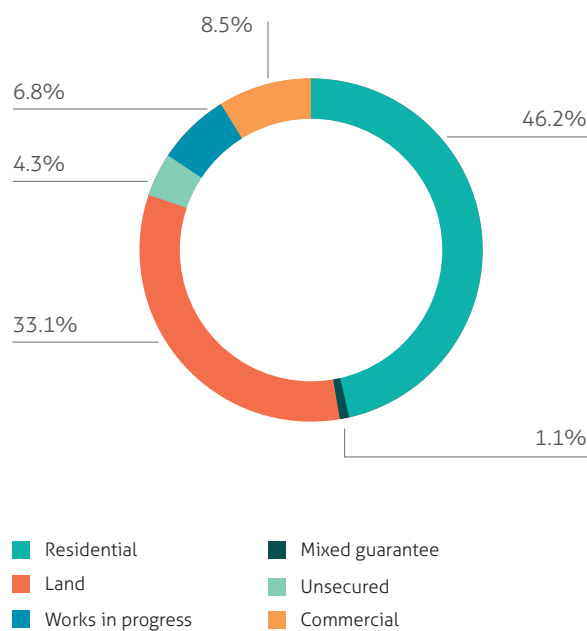
9. Breakdown per type of asset (% of €M)



10. Breakdown of real estate assets per type (% of €M - NBV¹⁴)



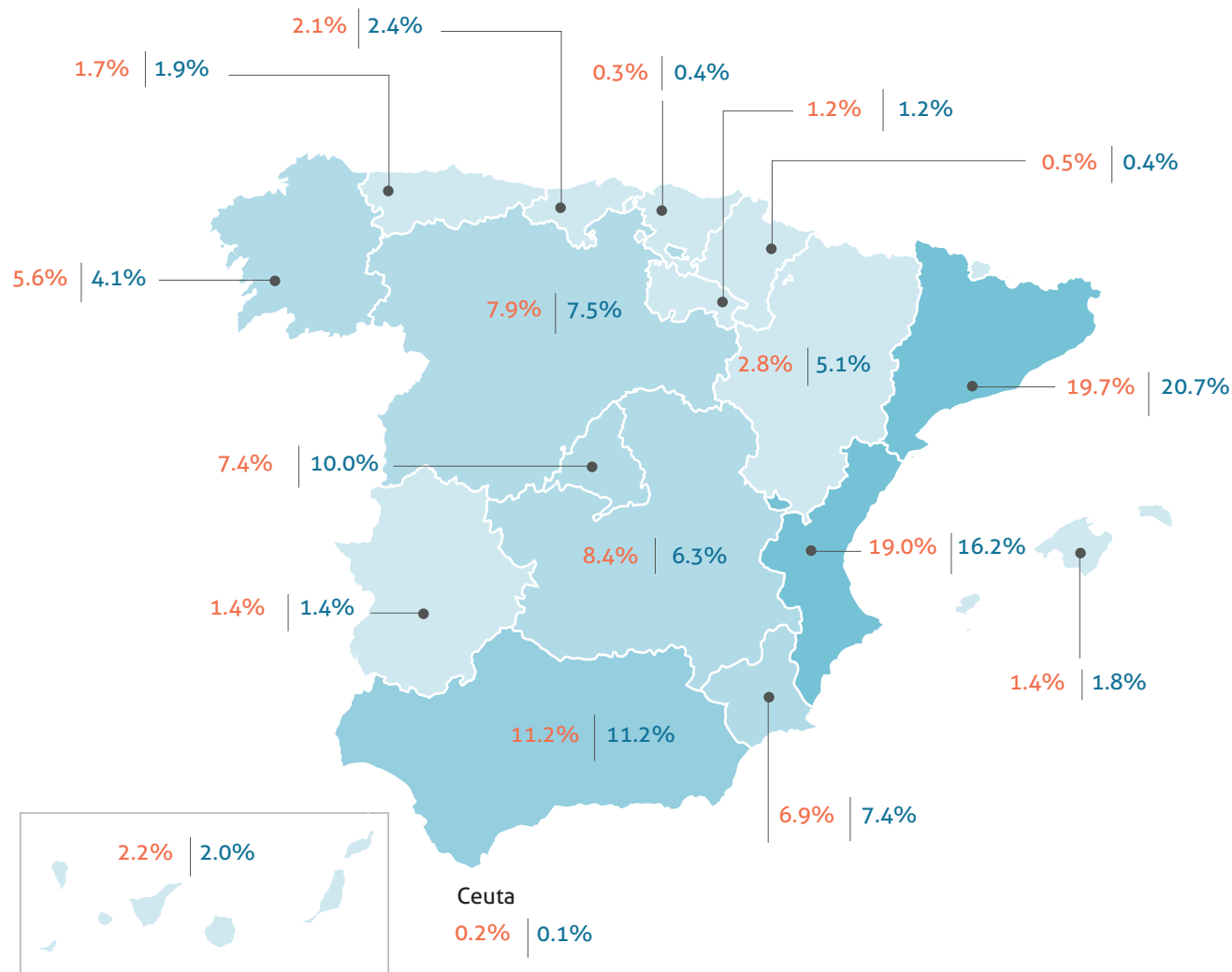
11. Breakdown of financial assets per type of guarantee (% of €M - NBV¹⁴)



¹⁴ Net Book Value



12. Geographical breakdown of the portfolio of real estate assets (% of units¹⁵ and of NBV¹⁶)



■ % of units

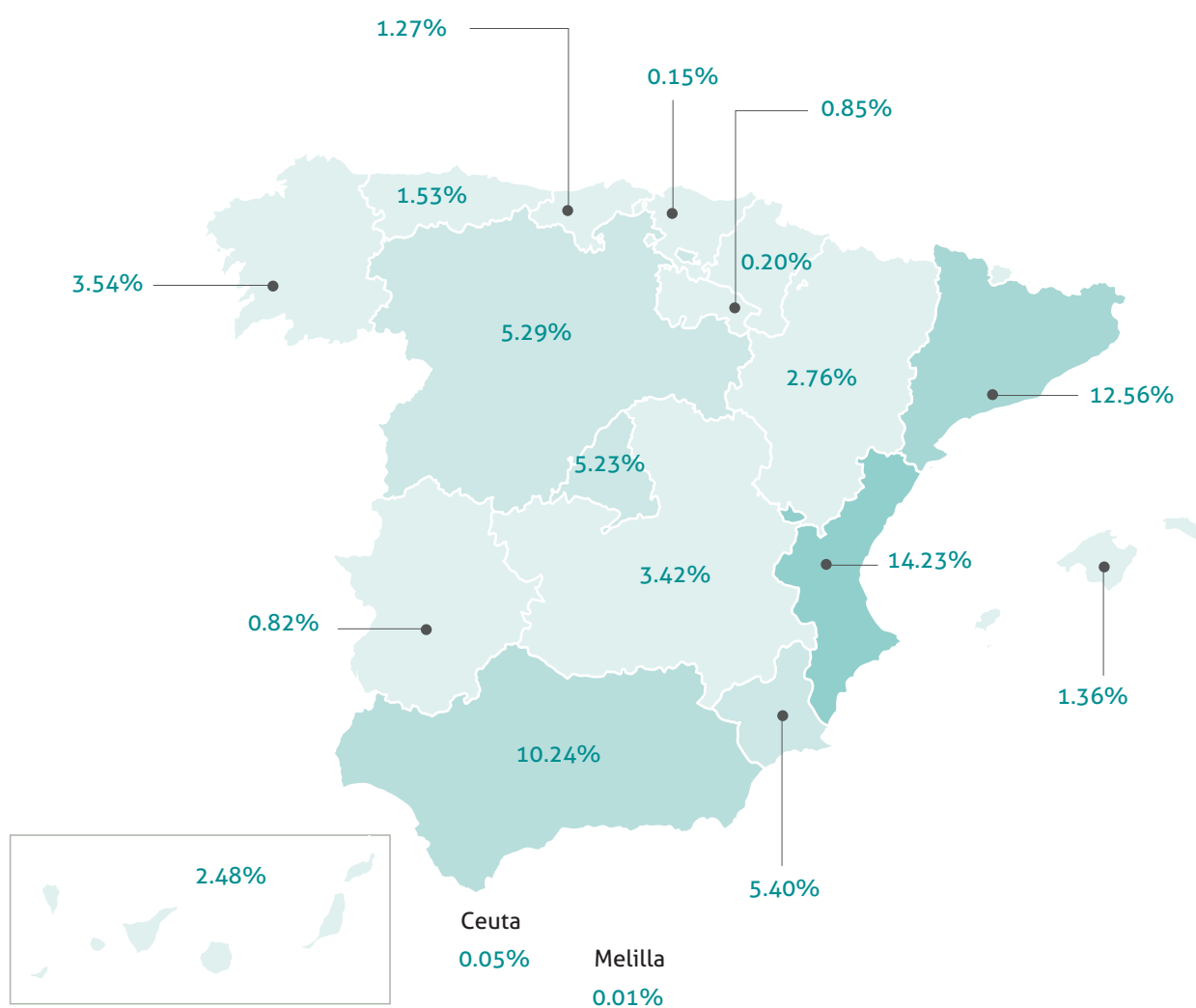
■ % of NBV

¹⁵ Not reported: 0.1%.

¹⁶ Net Book Value.



13. Geographical breakdown of the portfolio of loans¹⁷ (% of €M based on debt)



¹⁷ 28.61% of the debt is not assigned to a specific autonomous region.

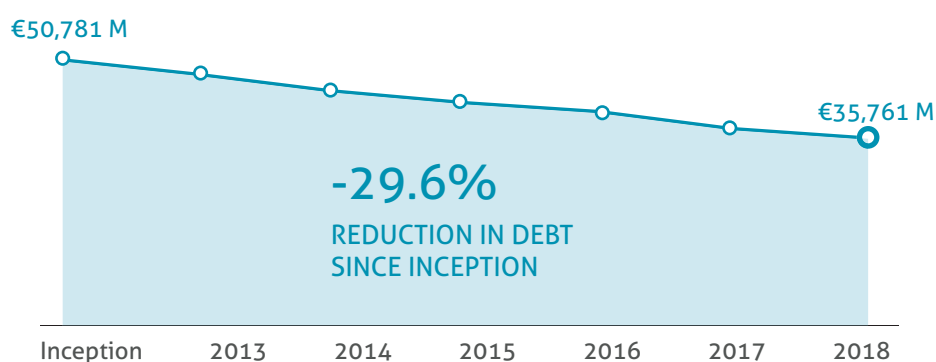
Senior debt

In 2018 the company repaid 5.6% of the issued debt underwritten by the Spanish government

Sareb's activity focusses on generating revenue through the management and sale of loans and properties to pay off the senior debt issued when the company was set up and to pay the associated interest on it.

Since its creation, the company has reduced the amount of senior debt by €15,020 M, 29.6% of the total. Of that total, €2,114 M were repaid and charged against 2018¹⁸.

14. Evolution of senior debt since the inception of Sareb (€M)



€2,114 M
repaid in 2018



Picture: Homes in Daganzo (Madrid).

¹⁸ Includes €169 M of the escrow account and repayment of €504.9 M in 2019 charged against the cash generated in 2018.



How is the repayment of debt?

The repayment mechanism is based on applying the cash surplus following the cash protocol defined in Sareb's senior debt contract. Under that mechanism, 92% of the cash generated is used entirely for the regular or early cancellation of the debt on the corresponding amortisation date.

During the first five years of Sareb's life, the remaining 8% had been reserved in a deposit account as a guarantee or escrow account against possible management contingencies. At the end of that period, and after complying with

one of the financial ratios established for its release, €1,058 M accumulated in that account were amortised and charged against 2017 and 2018. Of that amount, €889 M related to 2017 and €169 M to 2018.

From now on, Sareb will use 100% of the cash surplus for the repayment of the debt, provided that the financial ratios defined in the company's senior debt contract have been met.

Amortisation of Group 1 and Group 2 bonds

In 2018, Sareb amortised a total of €1,945 M for the repayment of Group 1 bonds –maturing during the year– and Group 2 bonds –maturing in February and are charged against the previous year.

15. Amortisation of bonds in 2018 (€M)

	Maturity	Total
GROUP 1¹⁹	31/12/2018	1,440.1
GROUP 2²⁰	28/02/2019	504.9 ²¹

Interest paid, associated to Sareb's debt since its inception, stood at €4,841.7 M, of which €2,784.6 M went directly to the banks assigning the assets to Sareb.

¹⁹ Group 1: BFA-Bankia, Catalunya Banc, NCG Banco-Banco Gallego and Banco de Valencia.

²⁰ Group 2: Liberbank, BMN, CEISS and Caja 3.

²¹ Amortisation made in February 2019 charged against 2018.

Management and sale of loans

The financial asset portfolio has decreased by 44% since its inception

Sareb's loans portfolio has been reduced by 12.3% in the year, to €21,937 M, which represents 64% of its total asset value. Since its inception, in 2012, this type of asset has been reduced by over 44%.

Income from the management and sale of those loans has gone down by 16% compared to 2017, to €2,208 M, due to the decision adopted by Sareb to reduce its activity in this segment in order to not assume the large discounts being imposed in the institutional market –as can be seen from the major sales transactions taking place in Spain in recent months.

Throughout the year, Sareb has looked into the possibility of selling off a large loan portfolio, but in the end it was considered to be unfeasible due to the high discount demanded by the investors and the impact this would have on the company's own resources.

Another aspect that has influenced the results is the drop in the lines for repayments and interest, something that will continue to be seen in the future as a result of the reduction in the portfolio up-to-date with payments and the greater difficulties in reaching agreements with the debtors after six years of activity.



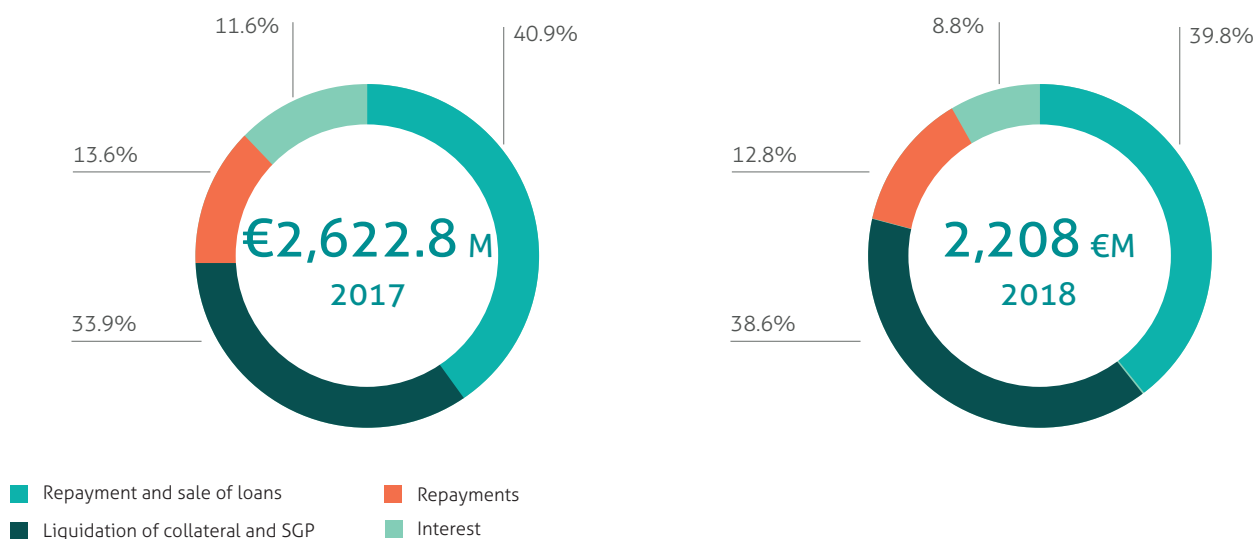
Picture: Marketing of a residential development under construction in Ponent, Badalona (Barcelona).

16. Strategy for the management and sale of loans

Debt recovery	Repayment of loan	Liquidation of collateral and SGP	Dation in payment	Sale of debt
Continued collection of non-performing loans within the deadlines established.	Paying off debt positions by the agents involved in the loan.	Sale of real estate collateral from the developers' books for repayment of the debt.	Paying off debt through dation of the property held as collateral.	Sale of debt positions to third parties.

In this context, while Sareb advances in the achievement of its mandate, the composition of the income per business line will continue to evolve in favour of a greater volume coming from the management and sale of properties.

17. Breakdown of income from managing and selling financial assets per business line (% of €M)



In 2018, Sales Growth Plans (SGP) and the repayment and sale of loans accounted for 78.4% of the total income, as opposed to 74.8% in 2017, and have established themselves as the principal strategies for this period.



Sales Growth Plans and liquidation of property given as collateral

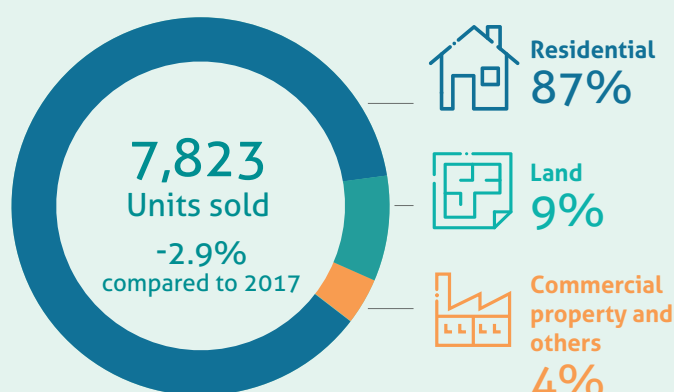
These operations allow Sareb to recover part of the debt without being involved in the costs and deadlines associated to mortgage foreclosure procedures.

Following an agreement with the developers, the SGP and liquidation of property given as collateral facilitate the sale of properties -residential promotions, single buildings or land- which appear as collateral for the loans directly on the debtor balance sheets, thus enabling them to reduce their debts with Sareb.

In 2018, property sales under the Sales Growth Plans and liquidation of property given as collateral stood at 7,823 properties, 2.9% less than in 2017.

In line with the the previous year, most sales corresponded to collateral in the form of residential properties, accounting for 87% of the total properties sold through these channels.

18. Liquidation of collateral and SGP per type (total units sold and % of units)



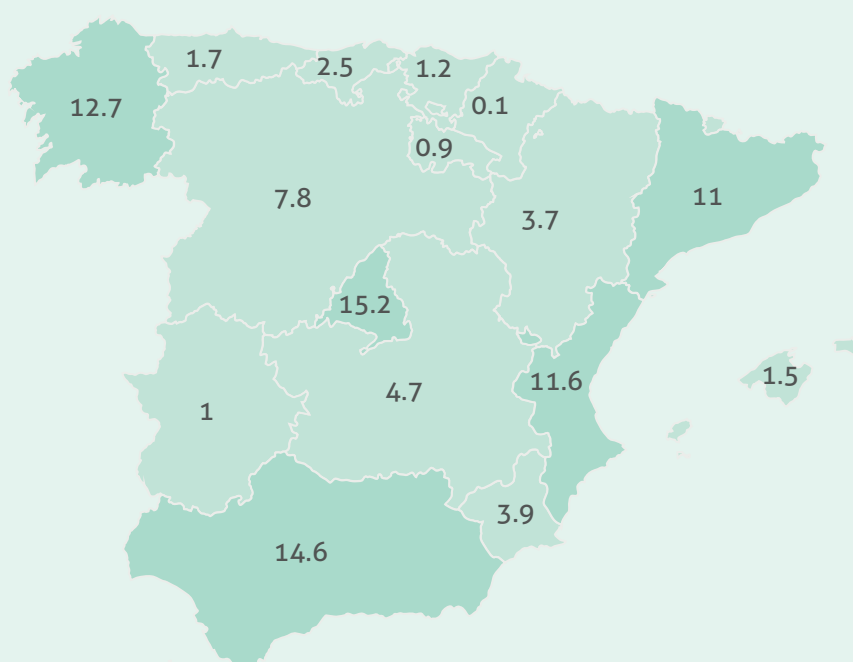
19. Geographical breakdown²³ of sales under SGP and liquidation of security properties (% of units)

Leaders in units sold 2018 SGP

- Madrid Region
- Region of Valencia
- Andalusia
- Catalonia
- Galicia

Variation in units sold under SGP per autonomous region vs 2017

- ▲ Cantabria
- ▼ La Rioja
- ▲ Aragón
- ▼ Balearic Islands
- ▲ Andalusia
- ▼ Canary Islands



²³ 3.5% of sales under SGP and liquidation of security properties is not associated to any autonomous region.

Active management of the loans portfolio

The company assigns strategies for recovery adapted to the characteristics of each asset

The high number of debtors, the volume of debt and the level of risk concentration require proactive and systematised management of the processes.

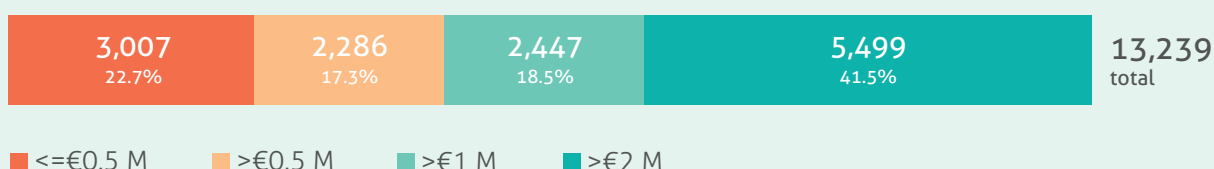


Type of debtors

58 % of borrowers are subject to exposure of less than two million euros and 40% to exposure of less than one million, in line with the previous year.

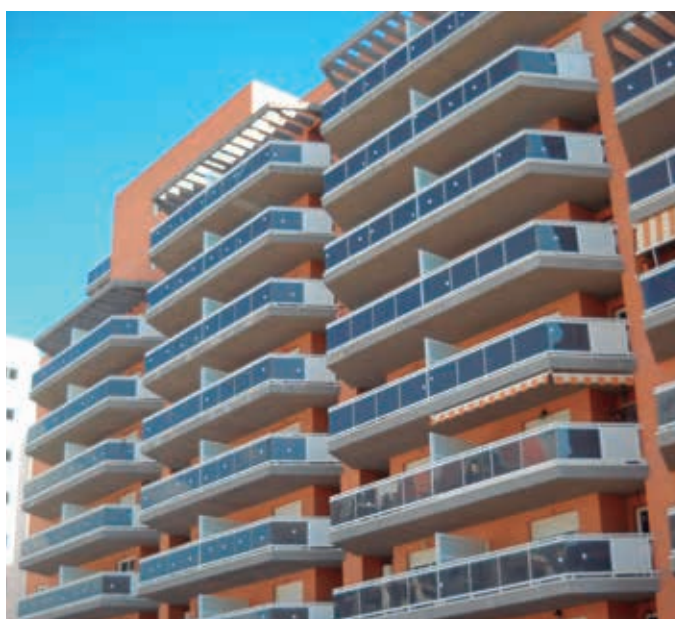
At the close of 2018, Sareb's financial asset portfolio was composed of 13,239 debtors, 9% less than the figure at the close of the previous year. The distribution of borrowers per volume of debt is similar to that at the close of 2018, as 80% of the debt is concentrated in 23% of borrowers.

20. Number of borrowers per ranking of debt (% of the total in 2018)



One of the most important variables used by Sareb for establishing and segmenting its loan management strategies is the expectation that the debtor will cooperate. The objective is to accelerate the collection of outstanding debt, mainly through arranging agreements or by taking over the properties given as collateral for the loans, in order to then sell them on the retail market.

The company has a roadmap for dynamically and uniformly divesting financial assets in a way that allows for monitoring the operations and ensuring the overall, effective management of the portfolio assigned to each servicer. From the risk aspect, this model makes it possible to prevent and analyse the cause of possible deviations in order to act accordingly well in advance.



Picture: Marketing of a residential development in Puebla de Farnals (Valencia).

Pillars of the management model



Establishing strategies for segmenting the portfolio.



Monitoring management by controlling the evolution of the strategies.



Tactical and operational planning that guarantees flexibility in implementing strategies.

Acceleration of the process of transformation of loans into properties.

Proposals managed

Since it was created, Sareb has managed 63,437 proposals, of which 12,076 were handled in 2018.

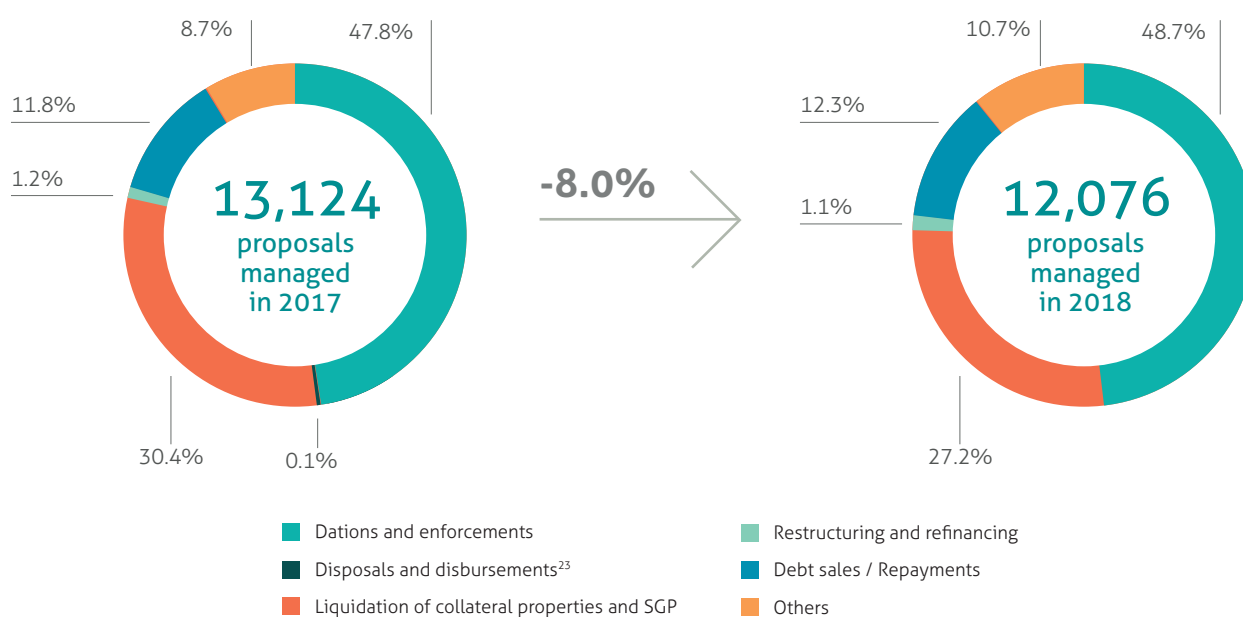
In line with the strategic priority of intensifying the transformation of its financial assets into properties in order to bring greater liquidity to its balance sheet, most of the financial proposals managed in 2018 relate to transactions of dation and foreclosure.

The foreclosure procedures, through which Sareb is able to take possession of the properties appearing as collateral for the loans, usually take place when there is no possibility of reaching an agreement with the debtors. But the fact of starting this process does not limit the search for other alternatives for collaboration that will enable Sareb to recover the debt.



Picture: Building under construction in Astillero (Cantabria).

21. Breakdown of proposals managed per type (%)



Sale of loans

Greater competition in the institutional market for buying and selling NPL and the demand from investors for significant discounts have conditioned the company's operations in respect of loans in 2018.

In this context, operations with institutional investors in 2018 entailed sales of debt for a nominal value of €511.7 M²⁴, as opposed to €1,089 M in 2017.

For its part, Sareb's loans sale channel –targeting a professional retail market– has enabled Sareb to sell debt for a nominal value of €102.7 M in 2018.



Picture: Marketing of a residential development in the Vallecas district (Madrid).

 **More information on** [Market and trends for the sector](#)

²³ During 2018 only five proposals were handled related to disposals and disbursements.

²⁴ This figure does not include the sale to Axactor of a portfolio of loans without mortgage guarantee which included financial assets for a nominal value of €2,335 M.

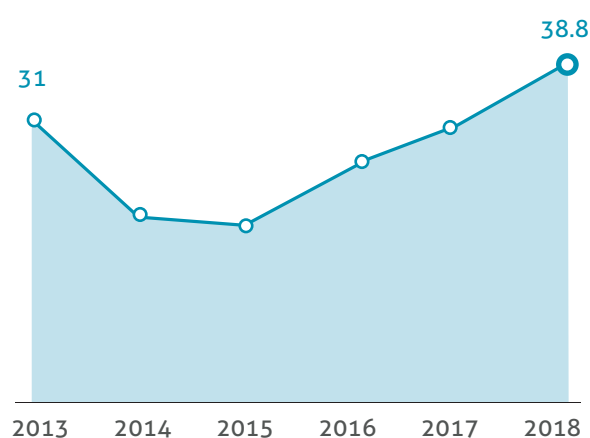
Management and sale of properties

In 2018, Sareb obtained record property sales, a total of 21,152 units

As Sareb advances in the performance of its mandate, property management and sales take on greater relevance as a result of the company's strategic decision to further the process of transforming its loans into real estate assets, which have greater liquidity in the divestment market.

In 2018, income associated to property management and sales stood at €1,415.2 M, 18.8% more than in the previous year, and represented 38.8% of the total sales volume of the company²⁵. That income includes the transfer of assets to Témopore Properties for the amount of €145 M at the end of 2018, within the framework of the *right of first offer* (ROFO) agreement between Sareb and the REIT.

22. Income from the sale of properties (% of the total)



Promotion on transforming loans into properties

Although the portfolio was closed in 2013, following the transfer from the banks that received public aid, the nature of the assets acquired changes as Sareb sells off the loans or gains access to the properties that secure them. In 2018 alone, the value of the real estate collateral allocated to Sareb amounted to €1,402.5 M²⁶, 39.2% more than in 2017.

Behind this transformation, in many cases there is a process of collaboration with the debtors, which makes it possible to reach agreements for repaying their debt through donations. In other cases it is achieved by claiming the debt through court.

In any case, the inclusion of these properties in the balance sheet makes it possible to diversify Sareb's real estate offer and increase the number of assets being marketed.

²⁵ 0.6% of the total sales figure for 2018 relates to other income

²⁶ Gross Book Value (GBV).

Property sales

The real estate market evolves and stimulates the divestment of real estate assets

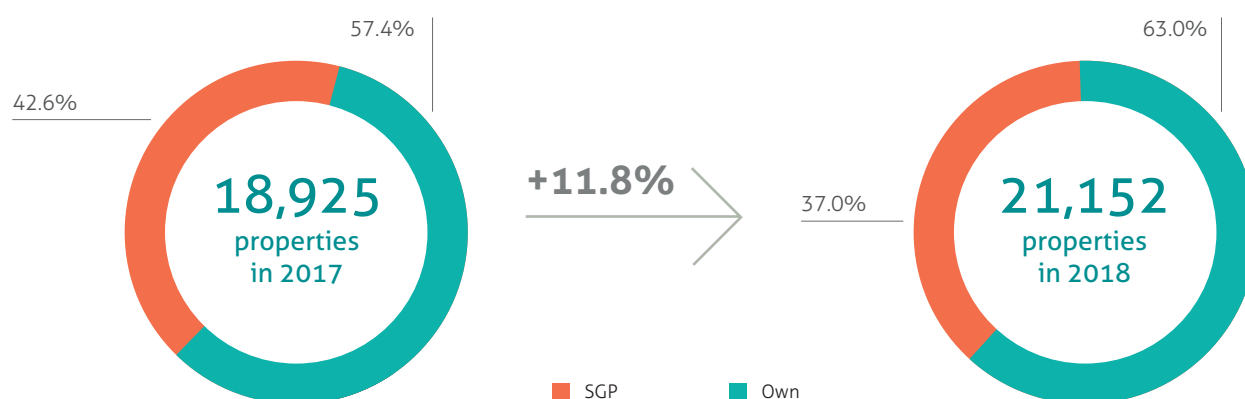
In 2018, Sareb reached a record number of sales, with the sale of 21,152 units, which is 11.8% more than in 2017. Of this, 13,329 relate to Sareb's own properties, while 7,823 were real estate assets associated to loans sold from the developers' books.

The evolution of the real estate sector and the perspectives for growth and expansion in the short and medium term have stimulated the market in Spain, although there are significant differences from one region to another. Progress in the sector was influenced by improvements in the economic situation of the population and better access to financing.

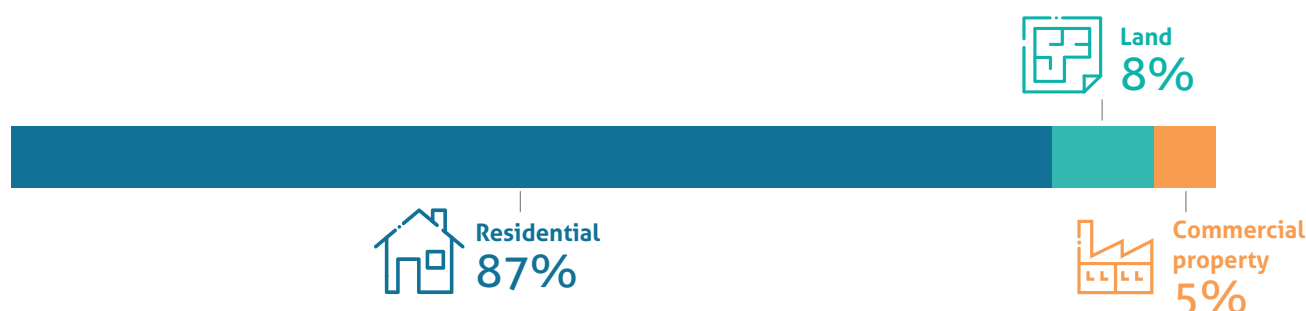
In terms of declared price, income from sales of its own properties reached €1,235.3 M this year, 9.3% more than in 2017.

Per autonomous region, the highest volume for property sales was concentrated in the Region of Valencia, Catalonia and the Region of Madrid.

23. Property sale (% of the total of units sold)



24. Sale of real estate assets per type in 2018 (% of the total of units sold)





Residential

In 2018, Sareb sold 18,391 residential units, of which 11,594 corresponded to its own properties, 27.9% more than in the previous year.

In the domestic market, the appraisal value of free-market properties per square metre stood at €1,619²⁷ at year end, 3.9% more than in 2017. The average price of own properties sold by Sareb was €108,245, which is 0.8% lower than that for 2017.

In terms of declared price, sales of Sareb's own residential properties went up by 32.2% compared to the previous year, reaching €797.4 M.

Per geographical area, the highest volume for residential real estate asset sales was concentrated in Catalonia, the Region of Valencia and the Region of Madrid, which accounted for 51.1% of the residential business in 2018.

Profile of the buyer of an own residential property



Individuals

Spanish

73%

Foreign

9%



Companies

18%



Land

Land sales stood at a total of 1,695 units during this year, of which 998 are Sareb-owned land, 0.8% less than in the previous year.

In terms of declared price, the volume of income was €241 M, 38.2% less than in 2017. This result is explained by Sareb's marketing strategy for this type of assets, focussed on the reservation and future development of land with greater potential -rather than selling it now- to maximise its value at the time of divestment.

Castile-La Mancha, Catalonia and the Region of Valencia are the autonomous regions that concentrate the highest volume of Sareb-owned units sold in 2018, with a total of 633.



Commercial property

The recovery of the productive fabric has been positive for the sale of Sareb's commercial properties, which in 2018 stood at 1,066 units in 2018, a 3.1% increase on the previous year.

This year, for the first time since the company was incorporated, sales of commercial properties were higher than entries in the asset portfolio as loan collateral.

The declared value of own tertiary assets sold amounted to €197 M, an increase of 52.5% over 2017.

The contribution made by commercial premises accounts for more than half of Sareb-owned units sold during the period.

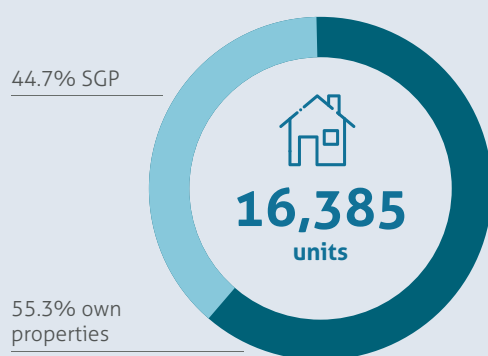
Per geographical area, the Region of Madrid, Catalonia, Region of Valencia and Andalusia –with a total of 529 units sold– account for the highest volume of sales of own commercial properties in the period.

²⁷ Source: Ministry of Public Works.

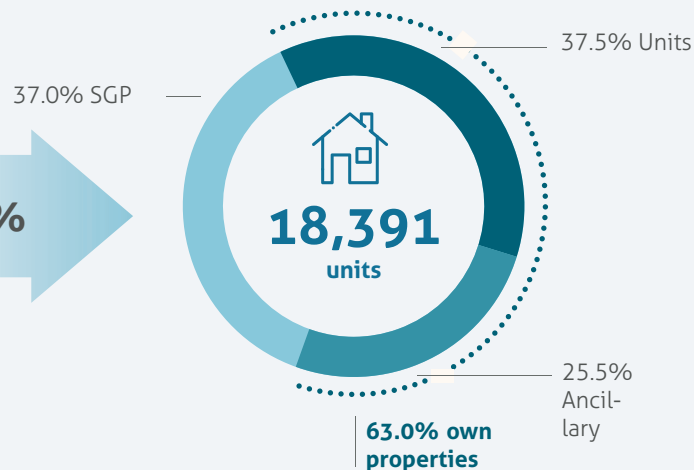
2017

2018

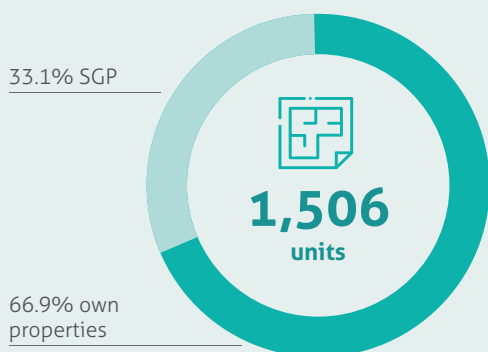
25. Sales of residential properties (% of units)



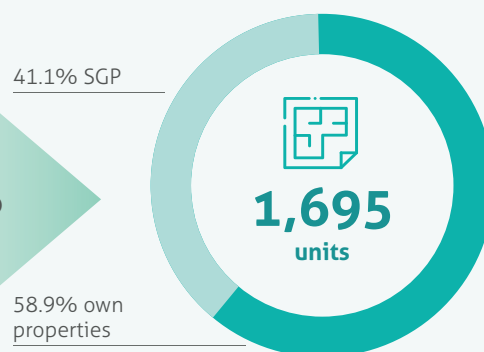
+12.2%



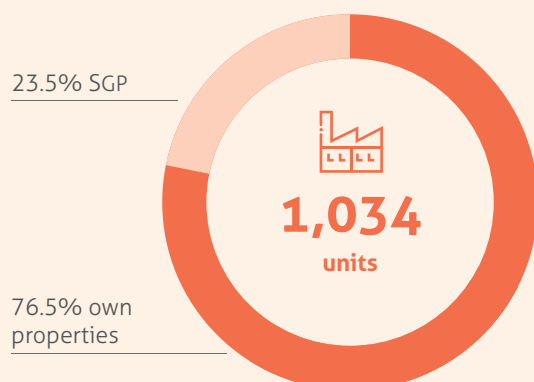
26. Land sales (% of units)



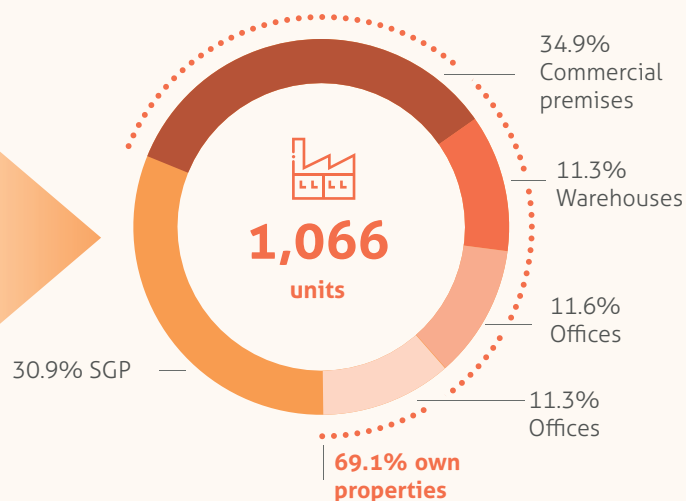
+12.5%



27. Sales of commercial properties (% of units)



+3.1%

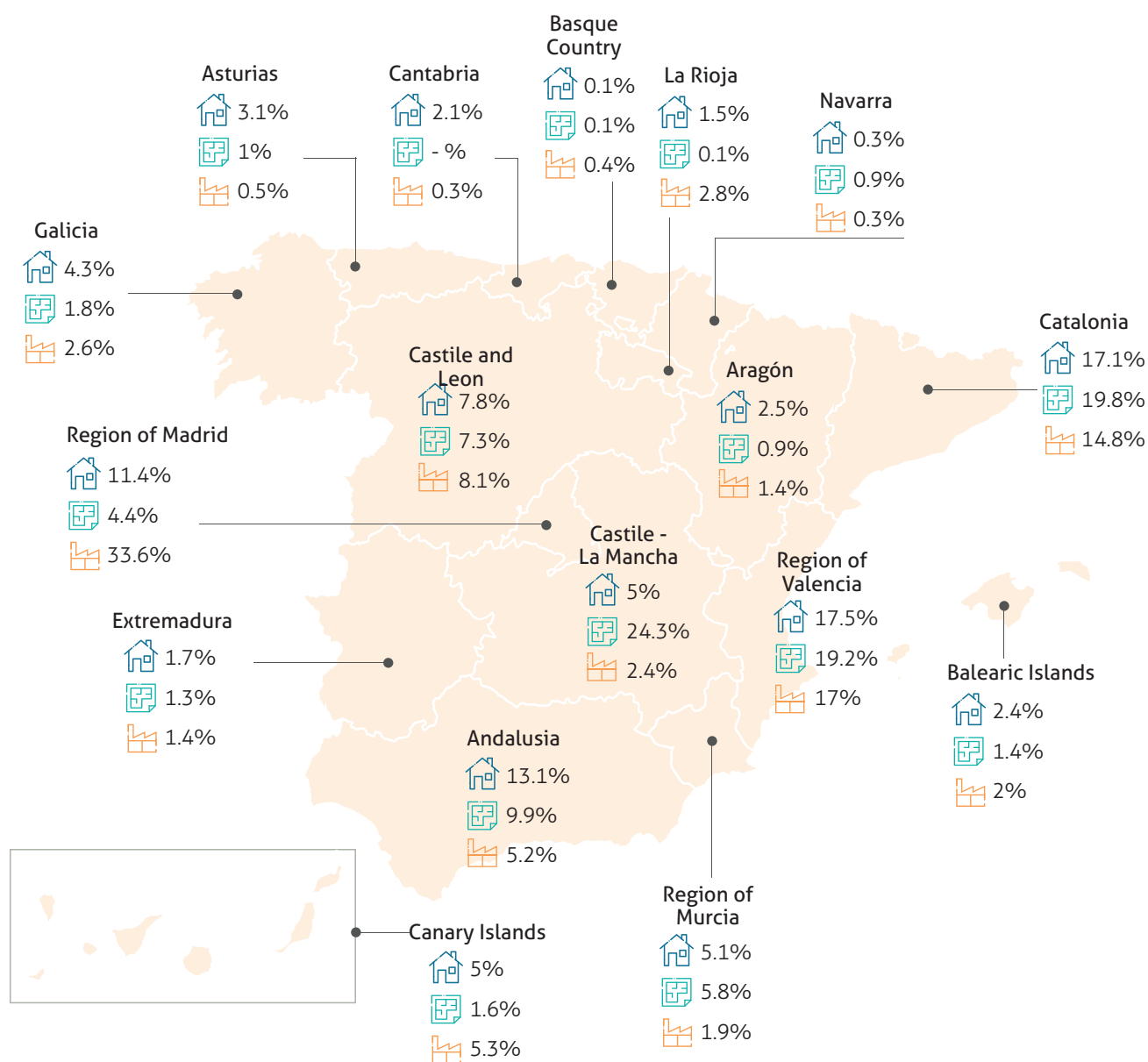


28. Geographical breakdown of sales of own properties (% of units sold)²⁸Residential²⁹

Land



Commercial property



Leading autonomous regions in units sold in 2018

- Region of Madrid
- Andalusia
- Castile and Leon
- Region of Valencia
- Catalonia

Variation in Units sold per autonomous region vs 2017

- ▲ La Rioja
- ▲ Castile and Leon
- ▲ Castile-La Mancha
- ▼ Basque Country
- ▼ Navarra
- ▼ Andalusia

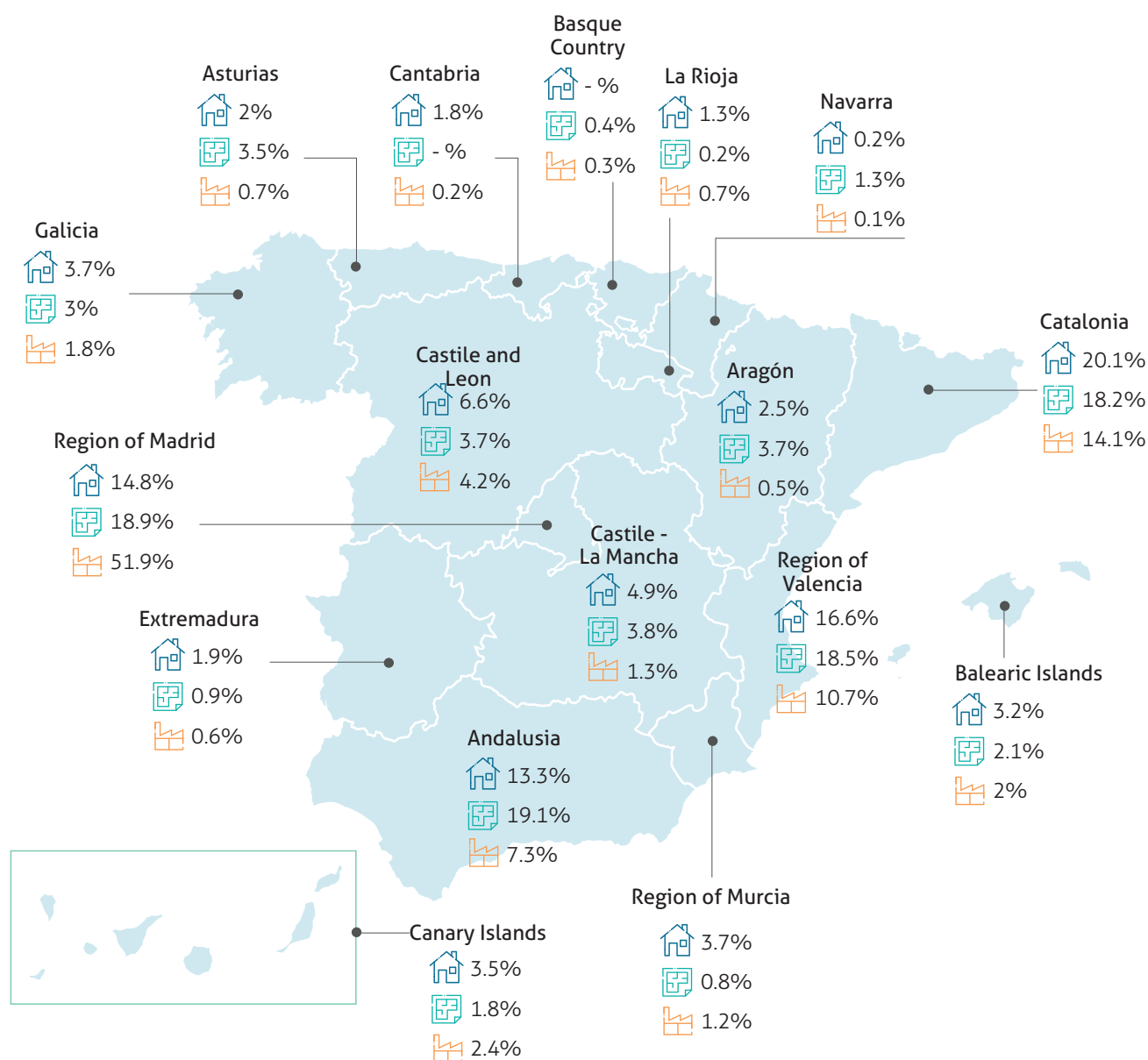
²⁸ Includes works in progress.²⁹ Residential includes homes and ancillary

29. Geographical breakdown of sales of own properties (% of sales volume)

 Residential

 Land

 Commercial property





Specific plans for provinces with less real estate activity

In 2018, Sareb has launched specific initiatives to stimulate its sales activity in regions in which the real estate market develops less rapidly but in which the company has to advance with its divestment. Its activity also contributes to the growth of these areas.

To this end, Sareb has launched marketing campaigns for a defined perimeter of 1,375 properties distributed over 60 municipalities in Castellón, Huelva, Murcia, Tarragona and Zaragoza.

At year end, the number of units sold in these municipalities went up to 68% compared to the previous year, exceeding the targets established for the year.

+ 68%
units sold
compared to 2017



Picture: Marketing of a residential development in Yebes (Guadalajara).

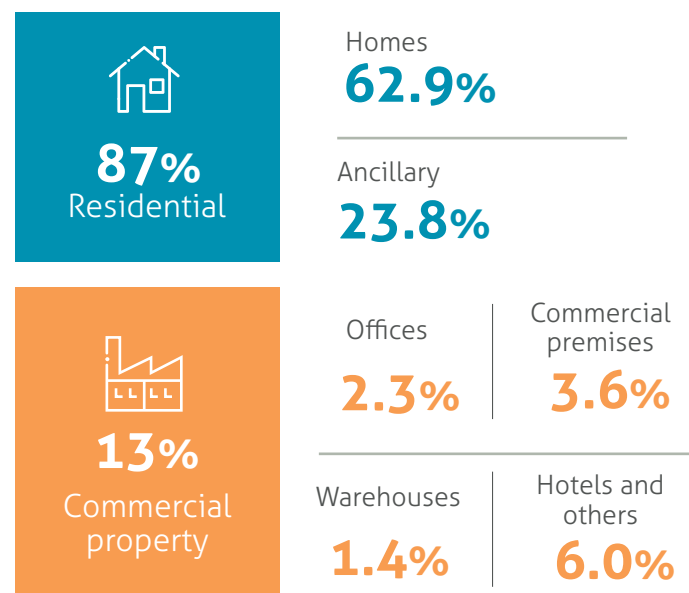
Rentals

At the close of 2018, Sareb's rental portfolio amounted to a total of 7,552 properties³⁰, of which 87% are residential properties and the rest are commercial.

The rental channel enables Sareb to optimise the value of the properties making up its real estate pool. The income generated during the lease period is used to recover part of the maintenance costs for those properties that take longer to sell. This is especially relevant in the case of commercial premises and offices.

In 2018, the volume of income associated to Sareb's rentals portfolio went down by 41% as a result of the sale of leased assets –residential and commercial– and due to the transfer of properties to the REIT T  mpore Properties.

30. Portfolio of properties for renting per asset type at close of 2018 (% of units)

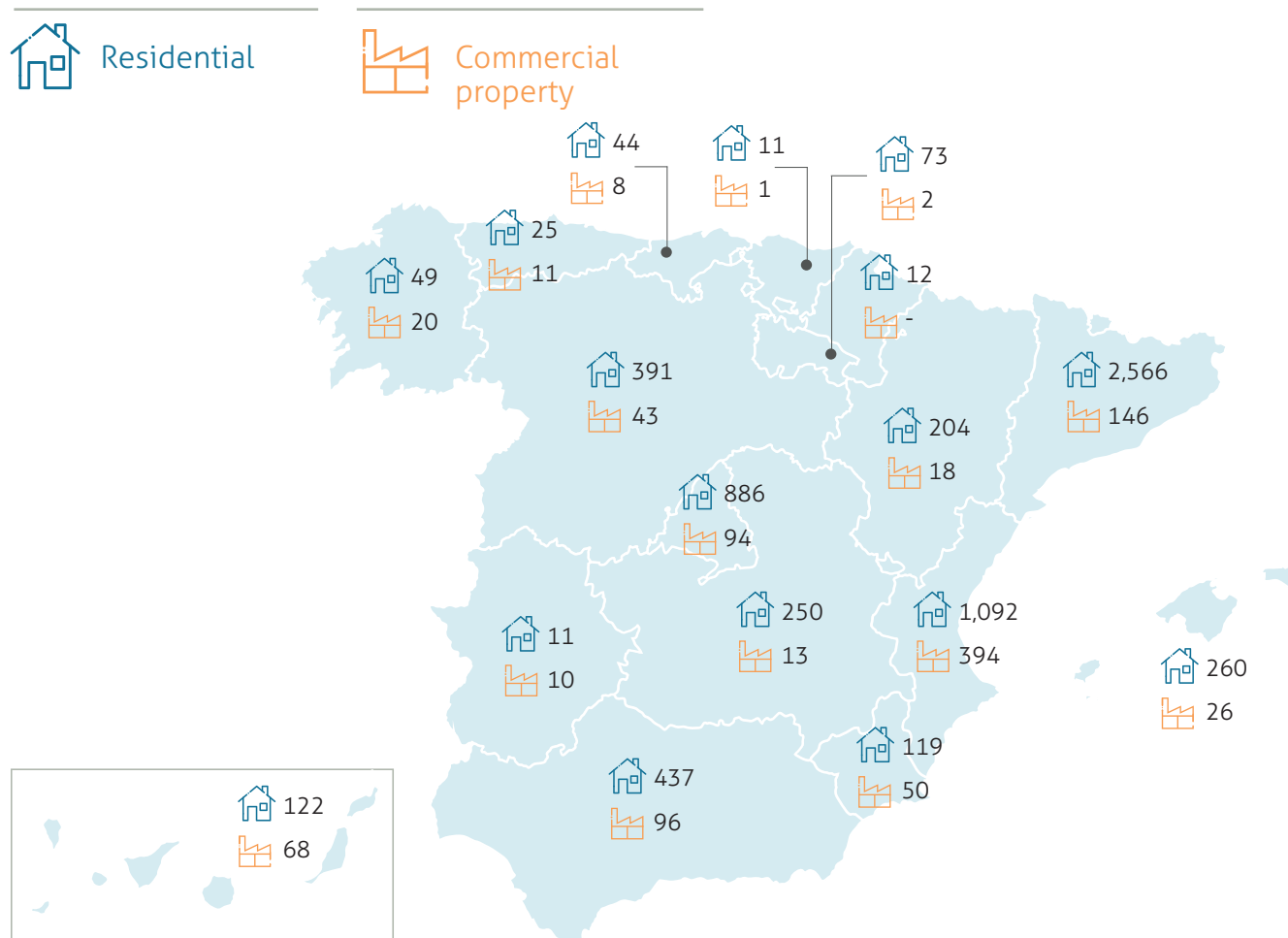


Picture: Sareb apartment building development in the centre of Madrid.

 **More information on T  mpore Properties at [Get to know Sareb](#)**

³⁰ Not including assets transferred to the REIT T  mpore Properties.

31. Geographical breakdown of the number of properties for rental (units)

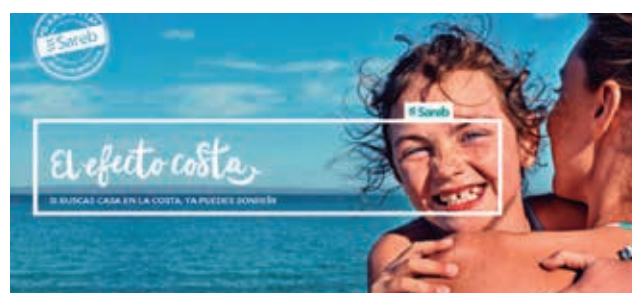
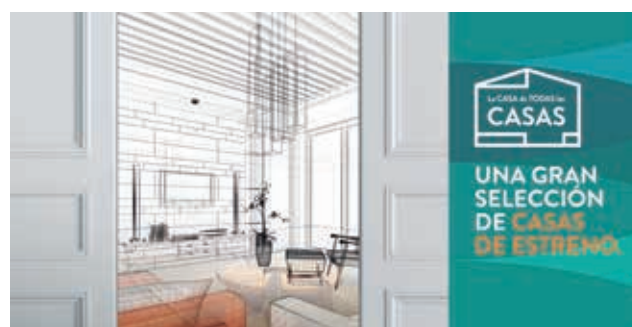


Commercial activity

Sales associated to marketing campaigns increased by 15.8% in 2018, to €388 M

In 2018, 10 new marketing campaigns were launched, through which Sareb has given visibility to a total of 21,771 assets, mainly residential. The income figure associated to these campaigns is €388 M, 15.8% more than in 2017.

In 2019, the company will move forward in the shaping of an individualised roadmap that will make it possible to study new marketing opportunities for each asset and prioritise them according to each one.



Clients' experience and communication

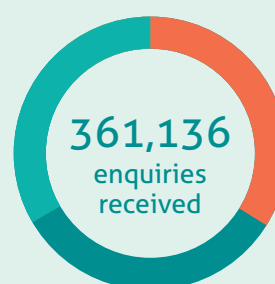
Sareb works on broadening and deepening the knowledge and profiles of the potential buyer base through processes of participation and active listening. The ultimate aim is to detect areas for improvement from when the opportunity is identified until the sale is made.



Sareb Responde

Sareb's Customer Service Centre attends to queries, requests and complaints related to the company's assets. In 2018, it received a total of 361,136 queries, 100.5% more than in 2017.

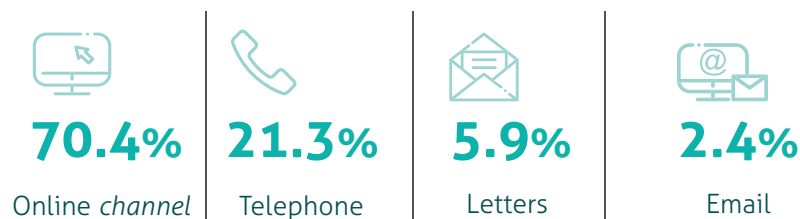
32. Enquiries received at Sareb Responde



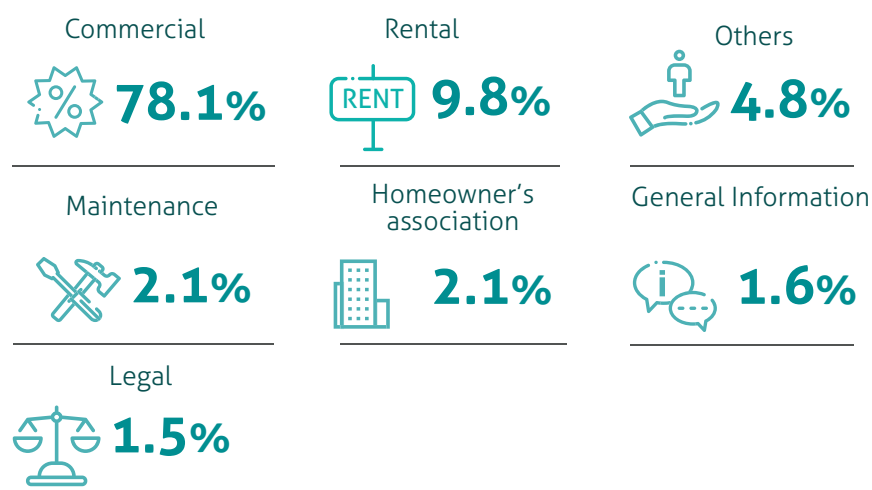
Per type of client



Per input channel



Per type of enquiry



Satisfaction surveys

Sareb makes a quarterly follow-up to assess the satisfaction of anyone interested in buying its properties.

In addition to making a general assessment of customer satisfaction –which at the close of 2018 stood at 75%– other issues related to the purchasing process are also analysed. Specifically, an analysis is made from the moment of contact with the real estate agents until the sale of the property is closed; at the same time other aspects such as delays or notarisation times are evaluated, amongst others.

75%
General customer satisfaction

Property development and promotion

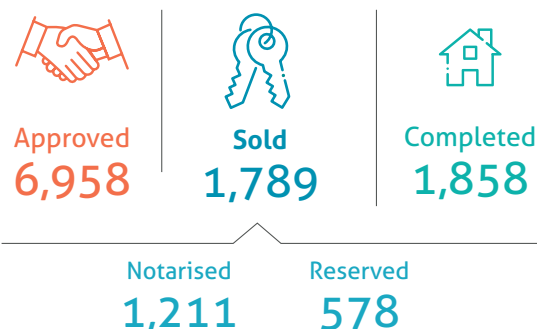
Actions for real estate development involve wagering on creating value on the land and unfinished construction work held in the portfolio

Development and delivery of new promotions

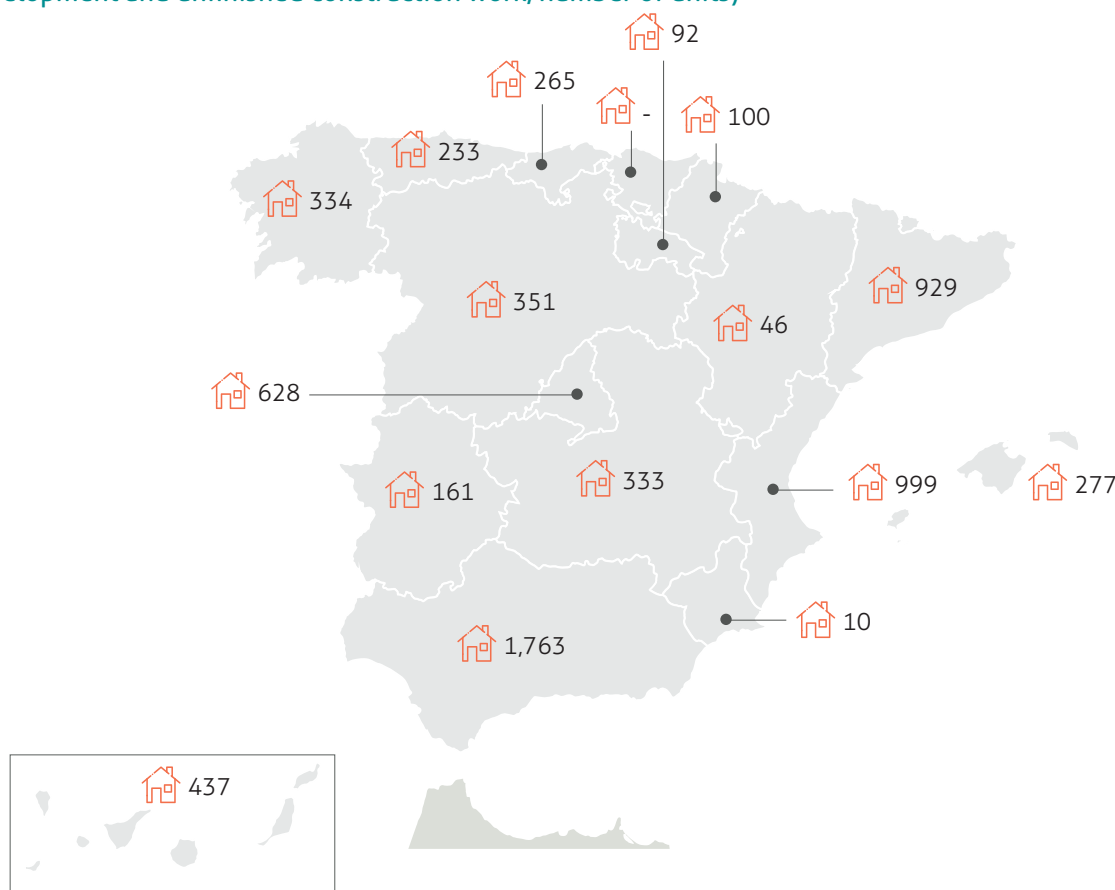
In 2018, construction concluded for 331 properties for which work had commenced in previous years. During the year the company also sold 981 homes and a further 585 were delivered.

Since its creation, Sareb has already approved the construction of 6,958 homes by developing projects on land in its portfolio and finishing construction works that had been left unfinished. In 2018 alone, 1,636 homes were approved.

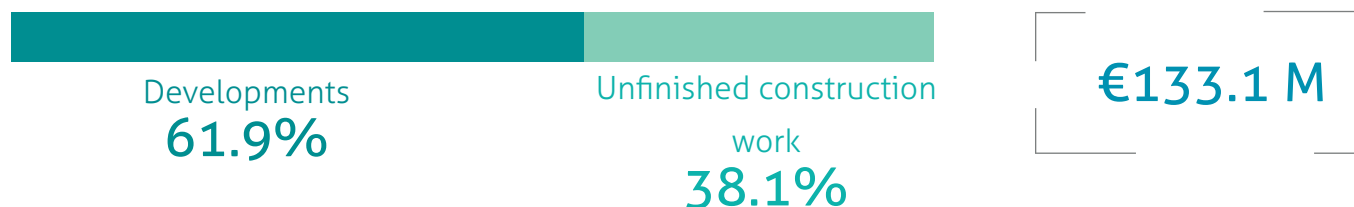
33. Actions for property development since its creation (number of units)



34. Geographical breakdown of planned promotion and development of housing (Development and unfinished construction work, number of units)



35. Breakdown of the total investment in the development of promotions on Sareb land and completion of unfinished construction works (% of €M)



Specialised property development management

In line with the search for specialisation in the management of its different assets, in 2018 the company worked on formalising a partnership with Värde Partners for creating a vehicle that will centralise the management and promotion of part of its portfolio of residential projects. This vehicle will be set up in 2019 under the legal format of a Banking Assets Fund (FAB).

This vehicle will contain a selection of land, buildings under construction and residential projects halted and awaiting development, which are valued at more than €800 M. Värde Partners will have a minority interest of 10% in the FAB and the asset management will be handled by Aelca –100% owned by it–, a developer of reference in the real estate sector.

 [More information on this partnership in Get to know Sareb](#)

Urban land management

Sareb's portfolio of land encompasses 83.8 million square metres of land under development and serviced development land, and 6,400 hectares of greenbelt land

The company has put different initiatives into operation for enhancing the value of these assets before they are sold, amongst which drawing up individualised strategies for sale or lease.

Furthermore, during 2018 land that could have been contaminated by activities carried out before being transferred to Sareb was inspected, in order to address these risks before being developed or marketed.



Real estate development in Seville

In 2018, building began on the development of La Florida (Seville), an historical asset that had been halted since before the creation of Sareb.

The company has carried out the preliminary work before the lifting of the archaeological precautionary order on the land, to then continue with the rest of the development, which will conserve the historic façade of the building.

The project will also stand out for the quality of the materials employed, and for its sophisticated interior design.

36. Breakdown of the Sareb land portfolio



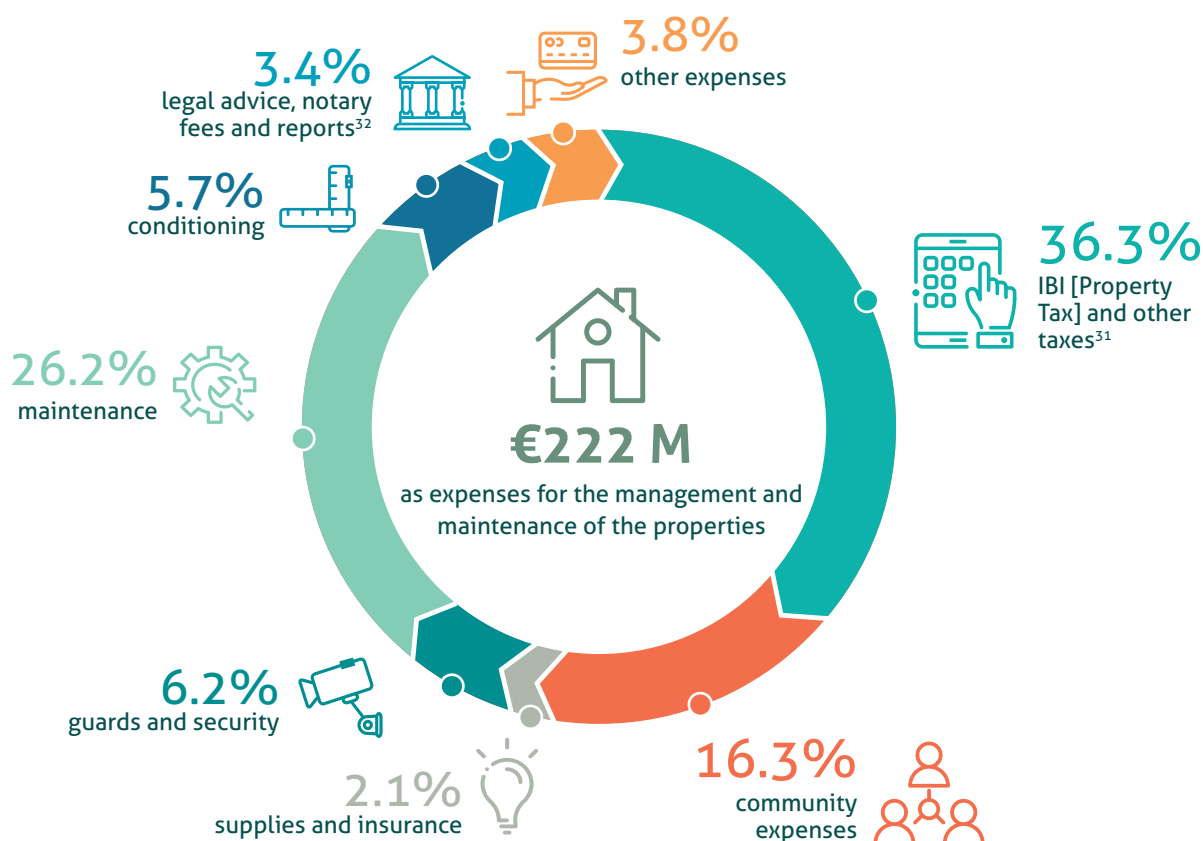
Property management and maintenance

The costs associated to the management and maintenance of the properties amount to €222 M in 2018

Sareb bears the costs of management and maintenance of its properties until they are sold. In 2018, those expenses amounted to €222 M, of which 52.6% corresponds to the payment of taxes and community expenses. Maintenance also requires carrying out comprehensive conservation work which entails an additional cost for the company. During 2018, Sareb has defined a new Technical Real Estate Management system with ISO 9001 standard certification.

The company has also continued to carry out important work for identifying and keeping up to date with the payments for all of the real estate assets that were transferred to it when it was incorporated. At the close of the year, almost 9 out of every 10 assets were up to date with the payment of their community fees.

37. Expenses for the management and maintenance of the properties (% of €M)



To gain in efficiency and to minimise risks, Sareb has continued working on the automation of managing and maintenance of its properties. After implementing this system in its portfolio of halted building sites, in 2018 it has also been extended to all the assets of one of the servicers and it is expected to be applied to all of the rest during the course of the next year.

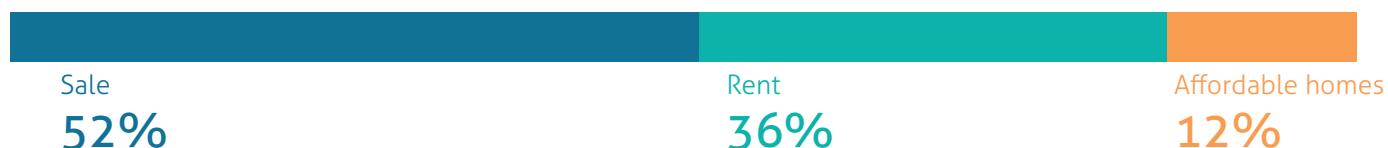
³¹ IBI [Property Tax] and other taxes and fees; also includes licence/permit costs.

³² Legal advice and technical reports comprises expenses for lawyers, court representatives and the fees for preparing technical reports.

Property conditioning

In 2018, 2,925 properties had been reconditioned. This includes minor repairs but which are necessary for marketing –whether for sale or rental– or for use as social housing.

38. Conditioning in properties for marketing and transfer (% of the number of assets conditioned)



Insurance cover and claims management

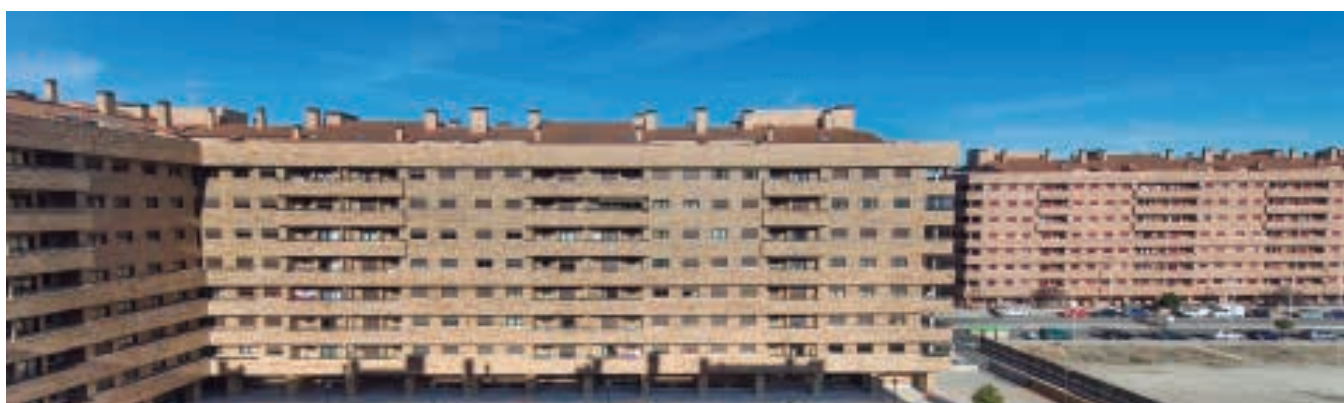
Every year Sareb reviews the assets that need to be insured and analyses whether the cover taken out is suitable.

The risk coverage policy requires Sareb to take out ample cover with reduced excesses and to sign policies with companies of recognised capacity and maximum solvency.

To cover the entire potential damage to which its real estate assets are exposed, Sareb takes out various insurance policies to cover those risks.

These policies also include civil liability for damage of any nature caused by third parties as a result of the company's activity, including any arising from decisions made by directors and senior management.

In 2018, the company renewed its programme of insurance for damage to property, civil liability and directors and senior management liability, as well as comprehensive construction cover and ten year building insurance. During the year, Sareb has broadened the analysis of the risk map to include events not included until now –data protection, guarantees amounts paid on account by home buyers and cybersecurity, amongst others.



Picture: Marketing of a residential development in Seseña (Toledo).

Financial information

The income for the year has enabled the company to repay a total of €2,114 M of senior debt



Accounting legislation and implicit losses

Sareb's activity is governed by the accounting framework for the valuation of assets established by the Bank of Spain in its Circular 5/2015 of 30 September, subsequently complemented by Royal Decree-Law 4/2016.

That Circular establishes that the company has to value its portfolio and consider any possible unrealised gains or losses in its assets, consequently recognising any impairment in a Value change adjustments account forming part of the company's equity and which is not taken into consideration as grounds for a capital reduction or dissolution of the company.

In 2018, the valuation of the entire portfolio using the method implemented by the Circular revealed the need for an impairment fund to be created by the end of the year in respect of €5,092 M of financial assets (€4,229 M in the previous year), around 19% of their carrying amount and 7.5% of the contractual debt.

Impairment established in the financial asset portfolio

Type	Debt	Guarantee	Vacbe ³³	NBV	Profit/ (Loss)	2017
Secured by property guarantee	49,730	19,177	16,777	19,262	-2,485	-2,009
Without first charges and participating	17,370	553	264	2,586	-2,322	-2,620
Awarded/dations			4,889	5,163	-274	400
Total	67,100	19,730	21,930	27,011	-5,081	-4,229
Other adjustments					-11	
IMPAIRMENT OF FINANCIAL ASSETS					-5,092	

Growth at the close of the year is due more to changes in the parameters for estimating the future value of properties serving as loan collateral than to changes in their appraisal value which, although not having followed the same evolution in the general market, have shown an increase.

Unrealised capital gains in the real estate asset portfolio

The real estate portfolio shows a gain of €260 M, 4% of its net book value. However, this portfolio was affected by the above-mentioned adjustments for the assets allocated.

³³ Value updated according to the Bank of Spain Circular.

Evolution of turnover

The Income Statement shown below follows the guidelines of the General Chart of Accounts (PGC) which, for the purposes of turnover does not take into consideration the amount received, but instead the margin generated in transactions under the Sales Growth Plans (SGP), reductions and repayments of principal.

Income statement (€M)		
	2018	2017
Turnover	1,938	2,144
Real estate assets	1,267	1,188
Sales of real estate assets	1,226	1,132
Income from leases	35	49
Bank Asset Funds (FAB) and others	6	7
Financial assets	671	955
Sales of financial assets	377	452
Financial income from loans (margin)	294	503
Sales costs	-1,411	-1,394
from financial assets	-351	-413
from real estate assets	-1,059	-981
Gross accounting margin	527	750
Other operating income	23	17
Management, marketing and maintenance expenses	-697	-683
Amortisations and others	-74	-77
Operating income/(loss)	-221	7
Net financial income/(loss)	-658	-541
Profit/(Loss) before taxes	-879	-534
Corporate Income Tax	1	-31
Net profit/(loss)	-878	-565

If all collections and accruals are taken into consideration, the income from Sareb transactions with financial and real estate assets stood at €3,478 M. For its part, gross margin stood at €527 M.

An additional amount of €23 M is to be added to those figures, both in income and in margin, which corresponds to the activity of the company (value adjustments, income from contract termination, receipts from assets under servicing).



Breakdown of turnover for the year

Most of the revenue, €2,207.8 M, was obtained from the management and sale of financial assets, while €1,270.2 M corresponds to the property activity.

In €M	Income	Gross margin
Retail financial assets	2,207.8	319.8
Retail real estate assets	1,270.2	207.6
Total regular business activities	3,478.0	527.4
Others	22.8	22.8
Total amount management business	3,500.8	550.2

Although loans still account for the major part of Sareb's income and gross margins, the reduction was greater compared to the previous year due to less activity in the sale of loans and the negative contribution of the SGP, which in previous years had a neutral effect on the margins. It has also had a significant impact on the reduction under the heading of interest.

From the perspective of real estate assets, income and margins went up compared to 2017, in a market that is increasingly more competitive in which major funds have come into play, having acquired significant quantities of assets at reduced prices. The positive evolution in the line of real estate assets supports Sareb's strategy of pushing forward with the transformation of loans into properties, which are more liquid when it comes to divestment.

In €M	Income	Gross margin
Retail real estate assets	1,270.2	207.6
Residential	797.4	110.0
Land and Commercial property	437.9	62.7
Rents	34.9	34.9

The operating expenses are similar, with a slight increase, to the figures for the previous year, although with some differences in their breakdown. This all leads to a business loss of €221 M –as opposed to the €7 M of profit in 2017– which is insufficient for meeting the financial costs of the senior debt which, furthermore, have been affected by the unfavourable outcome of the arbitration regarding negative coupons.

Losses before taxes stand at €879 M –as opposed to the €534 M of the previous year–, and are marginally reduced by the tax deduction of €1 M for innovation and development (I+D).



Operating expenses

The company's non-financial expenses amounted to €696.9 M, which is a 2% increase on 2017.

Nearly on third, 29%, relates to fees established under contracts with the servicers for management, administration and marketing.

Expenses arising from owning real estate assets –conservation and maintenance, community fees, security, Property Tax (IBI) – account for a third of the expenses and have increasingly more impact as a result of Sareb's commitment to reconditioning homes with the aim of maintaining a larger and better pool of properties for sale.

Nevertheless, it is the tax bill for Value Added Tax (VAT) which has increased more, due to the double effect of the higher cost of the foreclosures (considered as the first transfer) and the adjustment for the deductible percentages of what is known as apportionment.

With regard to structure expenses, which go down, consideration should be given to the important economic effort made in improving the information on Sareb assets –both from the aspect of updating appraisals and of the development of projects of a technological nature which make it possible to centralise all the information in its systems and the associated transactions. Thus, in addition to complying with the regulatory requirements for valuing the portfolio, work is also being carried out for more efficient management of the assets which, ultimately, will make it possible to obtain better prices in the transactions.

Structure expenses (€M)

	2018	2017
Fees for management and marketing	203.8	242.9
Management	95.8	120.8
Marketing	108	122.1
Taxes (IBI, VAT, Capital gains and others)	217.5	177.8
IBI, capital gains and others	93.8	89.2
VAT (expenses and foreclosures)	123.6	88.6
Expenses arising from foreclosure procedures and dation	27.2	28.5
Technical reports - Registration expenses and other	12.2	12.2
Homeowner's associations and maintenance	134.3	114.3
Homeowner's associations	68.7	63.2
Maintenance	58.0	49.8
Other operating expenses	7.6	1.3
Structure expenses	101.9	107.5
General expenses	65.1	66.7
Staff expenses	36.8	40.8
Total expenses	696.9	683.2

Evolution of equity

At the close of 2018, Sareb's capital and subordinated debt amounted to €2,607 M, less than the €4,800 M with which it was incorporated. This reduction is due to the accounting losses recorded by the company since it was incorporated.

4. OUR WAY OF WORKING

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Sareb people

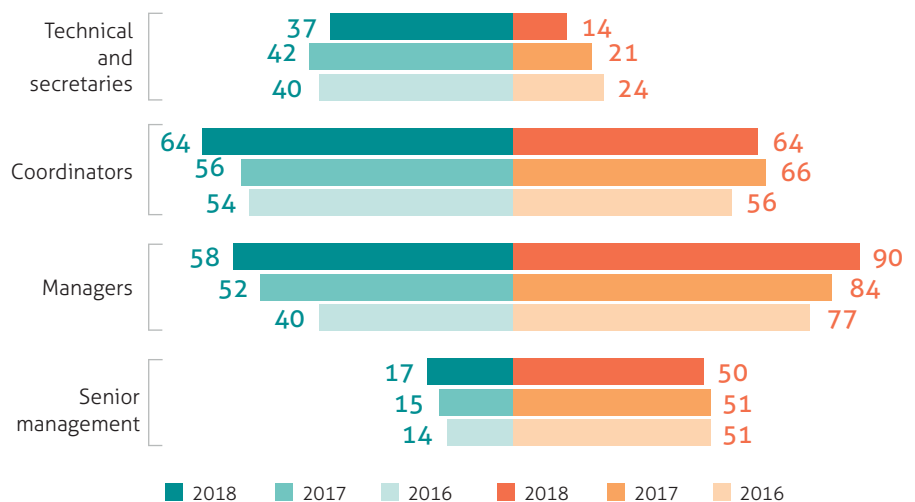
The mandate is fulfilled on the basis of added value and by having distinctive employees

By the end of 2018, the number of Sareb employees totalled 394, an increase of 1.8% over the previous year. The slight upturn is explained by new hirings during the year (40 people), which offset the slight increase in the turnover of employees in the year due to a more dynamic employment market in Spain.

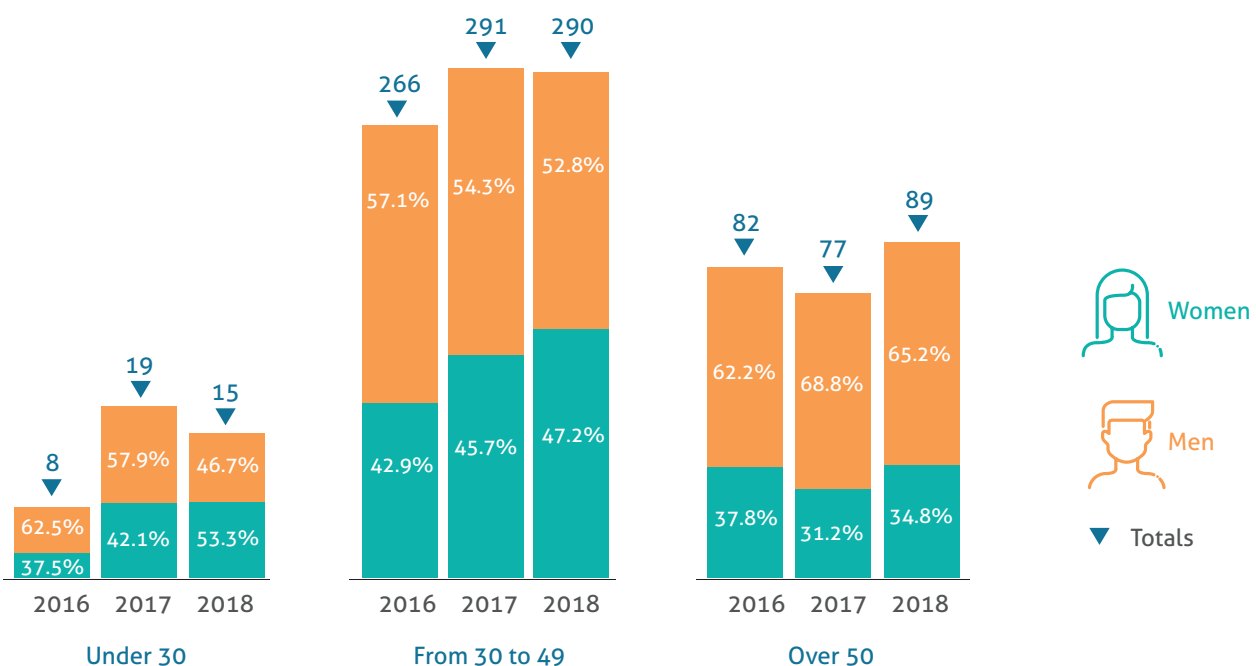
394 Professionals
+1.8% compared to 2017

39. Profile of employees (number and %)

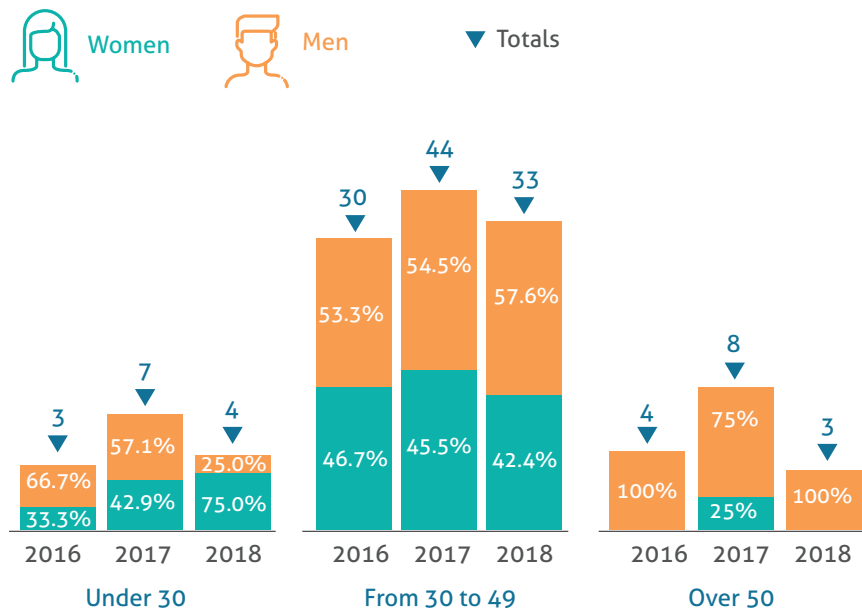
44.7% Women   **55.3%** Men 



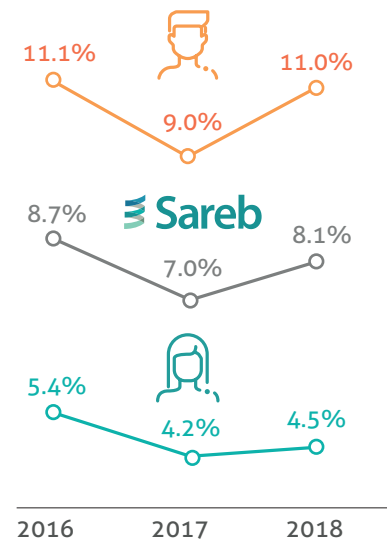
40. Breakdown of Sareb staff by age and gender (%)



41. New staff recruitments by age and gender (%)



42. Employee turnover (total)



Sareb's employees are a reflection of the company's commitment to diversity, understood in its broadest sense. The Plan for reconciliation, equality and diversity (CID), which was implemented in 2018, consolidates Sareb's commitment to a more inclusive and flexible workplace environment that guarantees equal opportunities for all those who form a part of the company.

In this respect, the plan covers a wide range of measures for achieving effective diversity, not only between men and women, but also between the different generations that live together in the

organisation –in 2018 the average job experience of the workforce is 19 years.

In the framework of this plan, in 2018 Sareb developed new measures enabling the consolidation of a flexible work culture which facilitates conciliation. Among these initiatives special mention is made of training employees in corporate tools for remote working, the implantation of flexible timetables, the option of teleworking on certain days and the provision of portable work devices and mobile phones to the whole workforce.



Female talent

For the past 3 years Sareb has been promoting the visibility of its female talent through the Promociona project.

The company participates in the project Promociona –Programme for Promoting Women in Senior Management– promoted by the Spanish Confederation of Employers and Industries of Spain (CEOE) and the Institute of Women. This project was launched in 2013 thanks to the EEA and Norway Grants and since 2016 it is co-financed by the European Social Fund. The programme includes academic training in collaboration with ESADE Business & Law School, individual mentoring with high-level executives, coaching sessions and networking activities. The object is to develop and strengthen the professional capacities and leadership skills of women so they can reach executive positions.

A seal of professional guarantee for the future

Sareb is a unique business project with a limited lifespan that requires a differentiated approach to attract and retain the best talent. Its strategy is based on a strong commitment to the development of its employees beyond Sareb's useful life, and prepares them for taking on new challenges in future working environments.

The people management plan reflects this philosophy, which is based on four pillars that contribute to fulfilling the company's commitments and objectives with regard to its employees.

Sareb and me: People Management Plan

Attracting, selecting and introduction of employees

For Sareb to comply with its mandate, it needs employees with high professional added value who have the skills necessary at each moment of the useful life of the project.

A new model of corporate culture

Leadership and organisational structure are based on Sareb values and on the commitment to employees' flexibility and autonomy with regard to choosing their own professional development.

Learning and training: the driving force for talent

Staff development is the main transmitter of Sareb culture and contributes to heightening the commitment levels of the staff with the company. Employees have various tools available to them for fostering their development, amongst which the possibility of living meaningful experiences -such as joining another department for a period of time to have first-hand experience of its day-to-day functions- or the promoting of self-learning activities using information and materials provided by the company. All of this in addition to the possibility of following training courses offered by the company in its annual programmes.

Satisfied, motivated employees

The measurement and follow-up of employee satisfaction and motivation makes it possible to develop and implement initiatives for ongoing improvement based on the results.



Sareb Escucha: establishing action plans

In 2018 different working groups were held with employees to establish action plans covering the areas for improvement identified in the last edition of Sareb Escucha, held in 2017.

The action plans implemented mainly focussed on the areas of conciliation and job flexibility. In 2019 a new edition of this survey will take place.

Further training

Sareb offers its employees specific practical training adapted to the needs of the company, based on the philosophy of learning by doing.



Sareb, gold medal for its method of learning by playing

The company has obtained world-wide recognition from the *Brandon Hall Awards*.

In 2017, Sareb implemented a method of learning based on videogames (game-based learning). As a result of this initiative, in 2018 the company was awarded the gold medal in the *Brandon Hall Awards* in the category of *Best Use of Games and Simulations for Learning* for the use of videogames for consolidating corporate culture and developing soft skills of its employees.

Sareb's professional training and development programmes combine technical knowledge with other necessary skills for management and leadership. Furthermore, employees regularly attend courses on company integrity.

The concept of in-house training staff has also been kept, so that employees with specific technical knowledge can share it with the rest of the company. This initiative, known as 'Trainer Training', also serves as an acknowledgement to the employees who hold the courses.

Training in figures



19,768 h.

total of training hours

+53.4%

compared to 2017



400³⁴

participants in training courses



9/10

results of satisfaction surveys regarding training



€995

Investment in training per employee



49 h.

training hours per participant

+53.1%

compared to 2017



26 technical training courses and

26 sessions for developing skills

34. Average workforce



Real Estate Expert Scheme: a qualification for encouraging the transformation of the balance sheet

The company places special emphasis on adapting its employees' skills at all times, in line with the transformation of the balance sheet and of the business.

Sareb's Real Estate Expert Scheme has been implemented in collaboration with the Official Association of Architects of Madrid (COAM). This came about with the object of helping the company to adapt the profiles of its professionals to the transformation of its balance sheet and business: less financial and more property-based. In 2018, the first edition of this initiative was held with the participation of 30 professionals.

Sareb Ambassadors

Sareb professionals exemplify the values of the company and its social commitment to fulfilling its missions. Within the framework of the corporate social responsibility programmes, 2018 saw further development of the Sareb Ambassadors initiative, in which volunteer employees share and disseminate Sareb's values and activities with the educational community.



169 sessions
42 centres

since its
implementation in
2016

Boost to innovation

Sareb's novel ecosystem is the backbone of the company's business model and way of working

Sareb performs its activity with an innovative approach that aims to develop disruptive projects that contribute not only to the company's fulfilment of its mandate, but also serve to transform and energise the sector.



Culture of internal innovation

In 2018 the company has carried out training, internal communication campaigns and the launching of disruption projects aimed at its employees in order to create new business models.

An example of this is the ExO Innovation Programme through which Sareb selected 24 individuals from throughout the company who, by enhancing their disruptive thinking skills, can introduce innovative initiatives in their working time and promote innovation in their respective fields. Under this project more than 50 business support ideas have been put forward.

Responsible management of suppliers

Transparency, competition and no supplier concentration govern how Sareb purchases assets and services

The purchase of goods and services of Sareb is based on attaining the best value-for-money, in accordance with the principles of transparency, competition and non-concentration of suppliers.

Among the criteria for choosing many of its suppliers, the company evaluates the degree to which these suppliers have progressed in terms of corporate social responsibility and their willingness to collaborate with Sareb in this field.

The search for efficiency in Sareb's management model has permeated through to its chain of supply in 2018. During the year, the contract for the centralisation of the maintenance of most of the applications used by the company was put up for tender. The concentration of this task in a single provider will make it possible to optimise processes and will lead to savings.

Main figures for the supply chain³⁵



More information on the process for the contracting and standardisation of suppliers on corporate social responsibility issues

https://www.sareb.es/file_source/web/contentInstances/documents/files/Homologacion%20proveedores.PDF

³⁵ The data provided corresponds to Sareb suppliers. That is, servicers' providers are excluded from the scope of the information.

Impact on the environment

The efficiency measures implemented in 2018 have enabled a reduction in electricity consumption

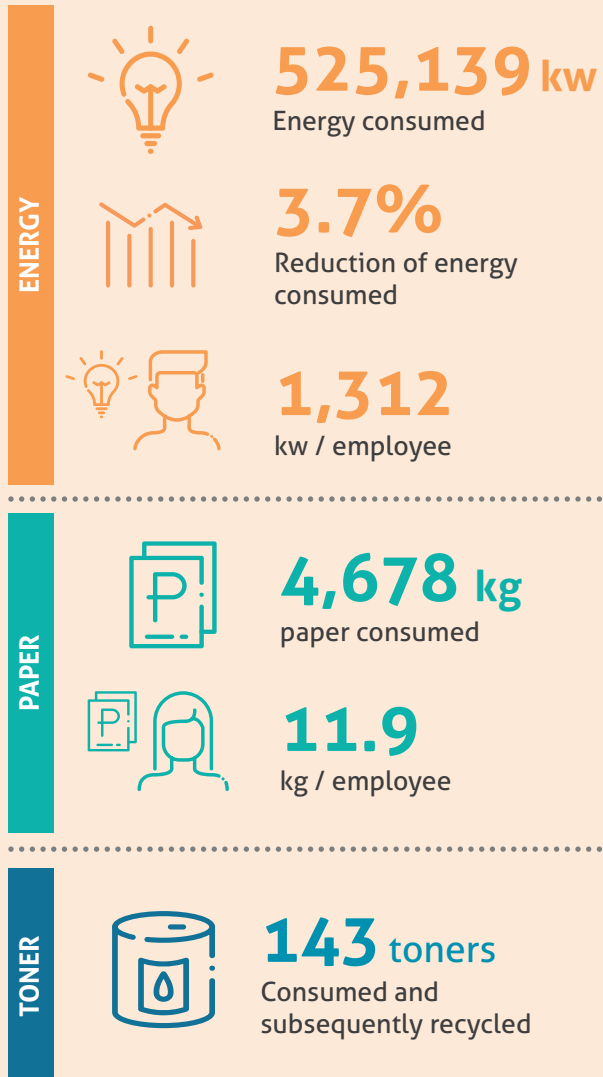
Sareb has an integrated management policy³⁶ –approved by the Board of Directors– which brings together the principles and key aspects to be implemented by the company for the respect and protection of the environment.

This year the company introduced the integrated management system in accordance with the international standard ISO 14001 on environmental management, in order to improve compliance with environmental regulations, while also gaining a deeper understanding and furthering progress in the identification, prevention and control of the environmental impact of activities carried out by Sareb.

One of the aspects in which the company can have some influence is in the promotion of efficient use of resources through awareness campaigns and the introduction of new efficiency measures. Noteworthy initiatives include the replacement of equipment with low-consumption technologies, promoting recycling and the provision of containers for batteries. In addition, and to reduce CO₂ emissions related to employees' transportation, the company has implemented initiatives that encourage remote meetings.

As a result of these measures, electricity consumption has been reduced and all paper used is recycled.

43. Principal figures on environmental impact



More information on Environmental Management, Quality and Occupational Hazard Prevention Policy
https://www.sareb.es/file_source/web/contentinstances/documents/files/politica-de-gestion-medioambiental-calidad-prl.pdf

³⁶ The policy includes Environment, Quality and Occupational Hazard Prevention and takes the ISO standards applicable to each scope as a reference.

5. CORPORATE GOVERNANCE

Composition and functioning of the Board of Directors	69
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Composition and functioning of the Board of Directors

The Board of Directors of Sareb stands out for the balance in its composition and the experience of its members

The Sareb Board of Directors is currently composed of 15 members, of which one third are independent, in compliance with the provisions of Royal Decree 1559/2012, which establishes the legal system governing asset management companies.

Following the resignation of Lucía Calvo on 1 January 2018, the Shareholders General Meeting held in May 2018 approved the appointment of Juan Ignacio Ruiz de Alda as a new Sareb proprietary director, representing the Fund for the Orderly Bank Restructuring (FROB). In June Ruiz de Alda was appointed as member of the Remuneration and

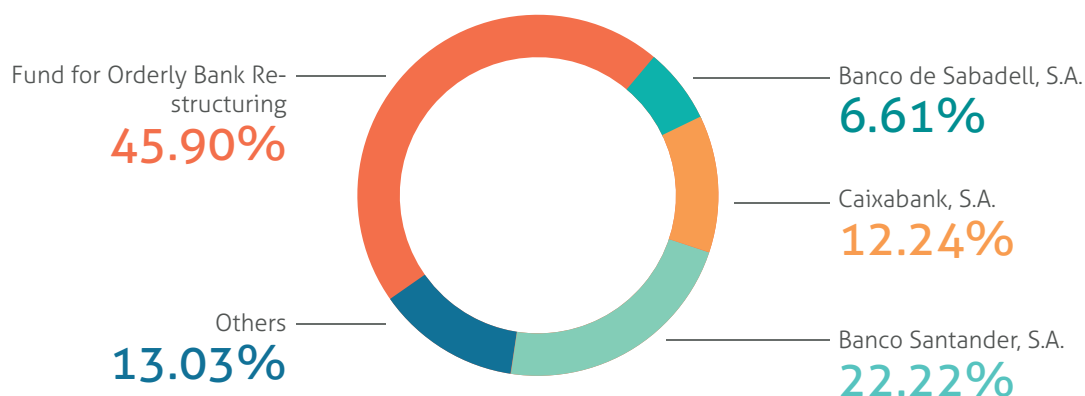
Appointments Committee to replace Eduardo Aguilar Fernández-Hontoria, following the favourable report from that Committee.

His appointment followed the principles established to that effect in the applicable provisions in the Articles of Association and in the Board Regulations. In that respect, an assessment was made of the skills, knowledge and experience required for being a member of the Board and the Remuneration and Appointments Committee, as well as the dedication necessary for performing his duties and the availability and existence of any possible incompatibility of the candidate.

Shareholder structure of Sareb

Sareb was incorporated in November 2012, with 55% of the capital coming from private entities, while the Fund for Orderly Bank Restructuring contributed 45% of the capital. At 31 December 2018, the distribution of capital and subordinated debt was as follows:

44. Shareholder structure of Sareb³⁷



More information on [What is Sareb?](https://www.sareb.es/es_ES/conoce-sareb/quienes-somos/que-es-sareb)

https://www.sareb.es/es_ES/conoce-sareb/quienes-somos/que-es-sareb

³⁷ Banco Santander, S.A. Includes Banco Popular Español, S.A.

Governance model

Sareb develops its activity while meeting the specific requirements for governance required under applicable legislation and acts under strict rules of ethics that safeguard its integrity at all times as well as its transparency, commercial reputation and professionalism.



A clear and specific legislative framework

The incorporation and development of Sareb is defined under the following legislative framework:

- Act 8/2012, of 30 October, on the write-off and sale of real estate assets in the financial sector.
- Act 9/2012, of 14 November, on the restructuring and winding-up of credit institutions.
- Royal Decree 1559/2012, of 15 November, which establishes the legal system governing asset management companies.
- Circular 5/2015, of 30 September, on the accounting particularities of Sareb.
- Royal Decree-Law 4/2016, of 2 December, on urgent financial measures.



Supervision

The singularity of its corporate purpose and the public interest associated to Sareb's activity mean it is also subject to supervision by the Bank of Spain, the Spanish National Securities Market Commission (CNMV) and the Monitoring Committee.

Supervisory bodies



Bank of Spain

- Sole objective
- Specific requirements
- Standards of transparency
- Constitution and composition of the governing bodies



Spanish National Securities Market Commission (CNMV)

Issue of fixed income and registration authority for Banking Asset Funds (FAB)



Monitoring Committee

This reviews the compliance of the general objectives.

It is formed by:

- Bank of Spain
- Ministry of Economy and Business
- Ministry of Finance
- Spanish National Securities Market Commission (CNMV)



Governance

Monitoring of the best governance practices applicable to listed companies.



Compliance and regulation

Strict regulatory regime: which helps to ensure that the business is carried out according to legislation, with integrity and ethics, in order to uphold its reputation.

Composition of capital

54.1%

Private Capital

45.9%

Public capital through the FROB [Fund for Orderly Bank Restructuring]

Board of Directors

15 directors



20 meetings in 2018

Executive Committee

6 members



6 meetings in 2018

Auditing Committee

8 members



12 meetings in 2018

Remuneration and Appointments Committee

8 members



9 meetings in 2018

Support committees

- Management Committee
- Risks Committee
- Investments Committee
- Assets and Liabilities Committee



10 meetings in 2018

● Independent Director

Internal control system

Internal control system on governance and strategic processes (SCEG)

Governance and strategic processes:

- Strategy and reputation

Internal control system on Processes for Managing Business Risks (SCIR)

Risk management:

- Credit
- Property price
- Liquidity
- Operational
- Interest rate

Internal control system on Ethical Standards (SCISNE)

Ethical standards:








































































































































- Integrity
- Criminal liability
- Money laundering and the financing of terrorism
- Reputation contagion risk (servicers)

Internal control system on Financial Information (SCIIF)

Financial Information:

- Risk of reliability of financial reporting

Profile of Sareb directors

First appointment	Director	Nature	Committees to which they belong	Profile and competences
05/03/2014	Jaime Echegoyen Enríquez de la Orden	Executive	  	     
27/11/2013	José Poveda Díaz	Independent	  	     
27/11/2013	Isidoro Lora-Tamayo Rodríguez	Independent	  	     
14/04/2015	FROB (represented by Jaime Ponce Huerta)	(D) FROB	  	     
10/06/2015	Francisca Ortega Hernández-Agero	(D) Banco Santander	  	     
10/06/2015	Pedro Antonio Merino García	Independent	  	     
25/11/2015	Enric Rovira Masachs	(D) Banco Sabadell	  	     
05/05/2016	Javier García-Carranza Benjumea	(D) Banco Santander	  	     
28/11/2016	Iñaki Goikoetxea González	Independent	  	     
28/11/2016	Javier Bartolomé Delicado	Independent	  	     
13/12/2017	Jaime Rodríguez Andrade	(D) Banco Santander	  	     
13/12/2017	Jorge Mondéjar López	(D) Caixabank	  	     
13/12/2017	Eduardo Aguilar Fernández-Hontoria	(D) FROB	  	     
13/12/2017	Antonio Cayuela Gil	(D) Caixabank	  	     
17/05/2018	Juan Ignacio Ruiz de Alda	(D) FROB	  	     



Executive committee



Remuneration and Appointments Committee



Finance



Legal



Auditing Committee



Chairman of the committee



Real Estate Sector



Public Administrations

(D) Proprietary



Business management



International



More information on Board of Directors

https://www.sareb.es/es_ES/conoce-sareb/gobierno-corporativo/consejo-de-administracion

Bodies and responsibilities

The governance of Sareb takes place through two main bodies: the Shareholders General Meeting and the Board of Directors, whose functioning is backed up by the Auditing Committee, the Remuneration and Appointments Committee, and the Executive Committee –the first two in place since Sareb was incorporated, and the third since 2017.

Responsibilities and functions of the governing bodies and their committees

SHAREHOLDERS GENERAL MEETING	Composed of Sareb shareholders. It discusses and makes decisions on matters within its competence, according to the articles of association and the Capital Companies Act	
BOARD OF DIRECTORS The body holding the representation, administration, management and control of the company.	Auditing Committee	Responsibility for internal control systems, requisite financial information, and associated non-financial information, auditors or auditing firm, and conflict of interests and related transactions.
	Remuneration and Appointments Committee	Amongst its functions are the duty to inform, propose and assess the suitability of the Sareb Directors, and to inform on the general policy on remunerations and incentives.
	Executive Committee	Its activity focusses on the approval of business transactions and other powers delegated by the Board of Directors.
	Support committees	Formed by representatives of the management team and representatives of the shareholders of the Company. Its functions are based on support and assistance to the Board.



More on the nature, functions and scope of action of the governing bodies:
Board of Directors

https://www.sareb.es/es_ES/conoce-sareb/gobierno-corporativo/consejo-de-administracion

Remuneration and Appointments Committee and Auditing Committee

https://www.sareb.es/es_ES/conoce-sareb/gobierno-corporativo/comites

The effectiveness of the Board of Directors

The Board diligently handles the powers of management and supervision attributed to it, encouraging participation and debate in each session, on company strategy and the topics studied within the committees.

The members of the Sareb Board of Directors perform their duties in strict compliance with ethical and behavioural standards relating to possible conflicts of interest and related operations.

The Conflicts of Interests and Related Operations Policy, approved by the Board of Directors in 2013, with its procedures for identifying such situations, applies more restrictive criteria than those required

by applicable legislation. With this, not only are the affected directors prohibited from deliberating and voting on resolutions and decisions relating to transactions in which there is a potential conflict³⁸, but they are also denied information on these matters, and must be absent from the Board or Executive Committee while the matter is being discussed.

This policy was applied on 41 occasions during 2018, with three of those applying to members of the Executive Committee.



More information on [the Conflicts of Interests and Related Operations Policy](https://www.sareb.es/file_source/web/contentInstances/documents/files/Politica_conflictos_intereses.pdf)

https://www.sareb.es/file_source/web/contentInstances/documents/files/Politica_conflictos_intereses.pdf

Evaluation of the performance of the Board of Directors

Article 6 of the Regulations of the Sareb Board of Directors establishes the obligation to prepare and approve an annual report on the performance of the members while carrying out their duties.

The assessment made in 2018 results in a positive evaluation of the composition of the Board and its organisation, and also the diversity of the profiles of its members, which allows it to function as efficiently as possible.

Nevertheless, the Board of Directors will continue contributing to improve its effectiveness by introducing measures for the ongoing updating and training of its members, and with greater dialogue with the management team.

Remuneration for members of the Board of Directors

Sareb's remunerations framework is defined in accordance with the terms of the General Policy on Remunerations for members of the Board of Directors.

Each year sees the publication of a report on the manner in which the company has applied the policy in the last closed financial year. This is available for consultation at www.sareb.es



More information on [the Remunerations Policy Report](https://www.sareb.es/es_ES/conoce-sareb/gobierno-corporativo)

https://www.sareb.es/es_ES/conoce-sareb/gobierno-corporativo

³⁸ According to the provisions of the Capital Companies Act.

Internal control system

The principles of integrity, transparency and civic engagement mark Sareb's guidelines for behaviour

The Internal Control System on Ethical Standards³⁹ includes all policies, manuals and procedures that contribute to the performance of the organisation's activity, not only in accordance with current legislation, but also in a full and integrated manner so as to protect its reputation and consolidate a corporate culture based on ethics.

The Compliance, Internal Control and Institutional Relations department is in charge of monitoring compliance with ethical standards aimed at crime prevention, data protection and the detection of other risks, amongst other issues.

Central to this model is the Code of Conduct, which is complemented by a broad set of policies that cover areas that include, among others, criminal liability,

the prevention of money laundering and financing of terrorism, data protection and relations with third parties. These also apply to servicers.

With regard to data protection, in 2018 the company adapted to the General Regulations on Data Protection (GRDP), which unify the regulations applicable in the European Union on this subject.

Furthermore, in 2018, Sareb renewed the AENOR certifications that accredit and validate that the organisation has the mechanisms in place for preventing, detecting and managing both criminal risks and possible bribery behaviour, in accordance with UNE 19601/2017 and UNE-ISO 37001/2017, respectively.



Internal control mechanisms that guarantee efficiency and rigour in the processes

Sareb directs the efforts in its operations toward the search for efficiency, without compromising the rigour required in its business.

In 2018 it implemented a specific cost-saving scheme intended to achieve improvements in efficiency of around 25% in some programmes. This initiative is based on the simplification and industrialisation of internal processes to avoid duplication and inefficiency and includes measures such as centralisation of suppliers or optimisation of activities related to the management of assets (security, utility supplies, homeowner's associations, insurance, appraisals, amongst others).

In addition, there has been a reorganisation of the regulatory framework of Sareb, which has enabled the company to simplify the whole set of regulations and reduce the number of internal and external documents by almost 40%. After this review, there was a total of 105 policies, manuals and procedures published, between the new documents and the modifications of those already in existence.

Sareb also has an internal document management tool that improves the handling of information and its distribution to employees and servicers. The company intends to continue this process in the coming year, with a view to ensuring the availability -in due time and form- of key documentation for decision-making and business operations.

³⁹ SCISNE

The Code of Conduct

Inspired by the 10 principles contained in the United Nations Global Compact, the Code of Conduct is the ultimate expression of Sareb's corporate culture and determines the framework to which policies and procedures must adhere.

The Code –approved by the Board of Directors in 2013 and last updated on 21 December 2017– expressly includes the commitments and behaviour guidelines that must be observed and followed by the people included in its scope of application.

This framework should form the basis for the behaviour of employees from the moment they start working for Sareb. For this reason, new employees receive a copy of the Code of Conduct along with their employment contract, and express and signed acceptance of the Code of Conduct is requested as a contractual obligation. In addition, a training plan is approved every year, relating to the internal regulations -the Code of Conduct and the rest of the policies- and the external legislation that is applicable at all times. All Sareb professionals must complete this training. In 2018, 100% of the company employees took the courses on ethical regulations and compliance.

Beyond the employees themselves, compliance with the Code also extends to the servicers -all of them must adhere to the Sareb Code of Conduct- and the main suppliers, through the inclusion of a specific clause in contracts that requires express acceptance of the Code prior to the provision of services.

The Whistleblowing Channel, an effective way for reporting possible irregularities

Sareb provides its employees and third parties related to the company –specifically servicers and suppliers– with a channel to facilitate the communication of irregularities and other ethically questionable behaviour.

This channel is outsourced to an expert in complaints management, with the aim of protecting the confidentiality of the complainant and thus avoiding fear of possible reprisals when it comes to reporting these issues.

Sareb is constantly implementing different initiatives for the dissemination of the channel amongst employees and servicers. These include on-site and online information sessions, informative posters in areas where Sareb's asset management is performed, and the publication of news on the intranet.

In 2018, a survey took place on this channel in which 100% of the participants stated they were aware of the situations in which this medium is to be used. Furthermore, the employees have suggested new ways for spreading it, and were anxious to have more knowledge on how it works. This will be worked on in 2019.

Although during the year no complaints were received through the Channel, a previous complaint related to a property being conveyed is currently undergoing analysis and follow-up.



Identification and management of risk

The identification and evaluation of the risks as key to proactive management

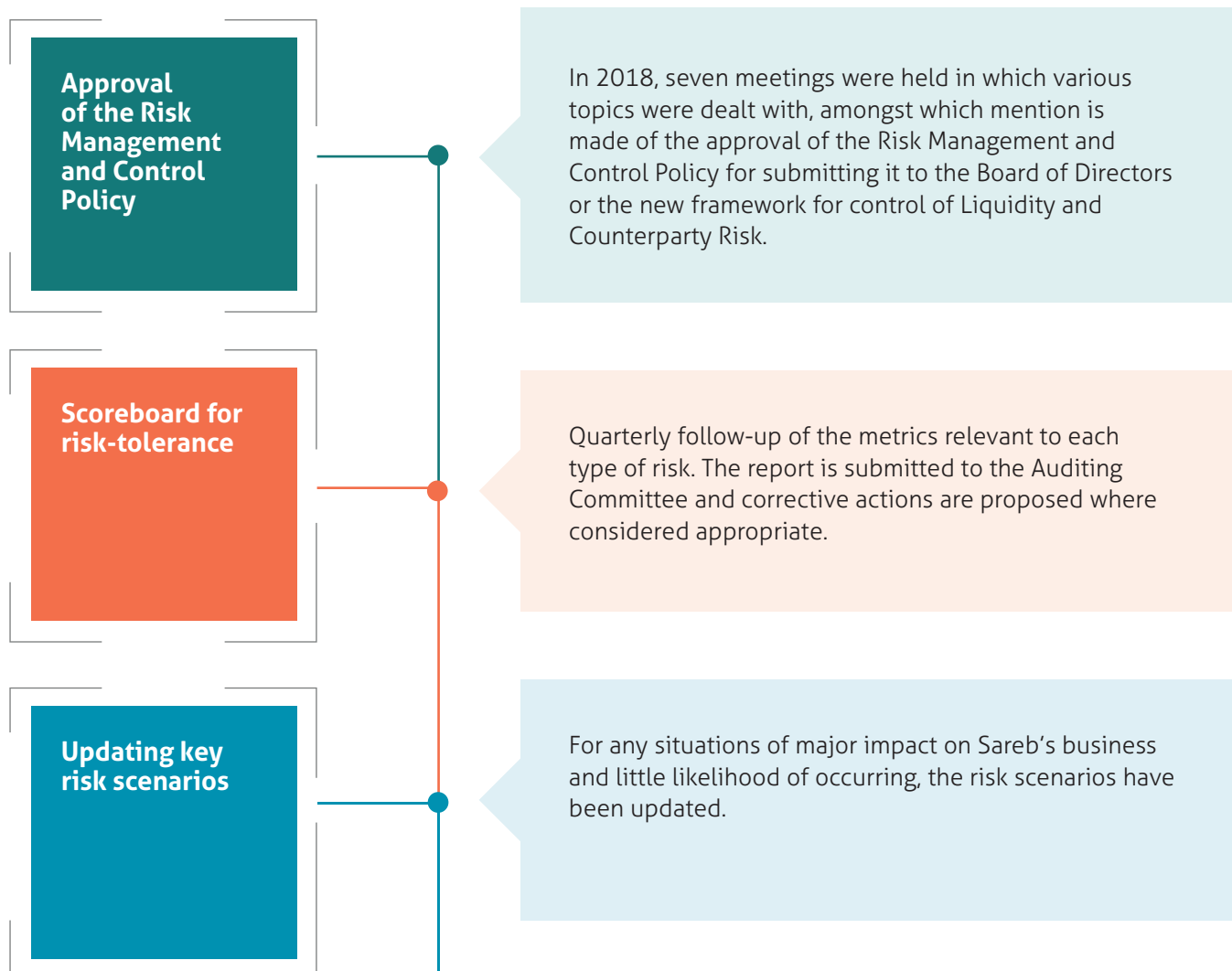
The risk management and control model allows the company to further improve the identification of potential situations that could lead to the materialisation of risks, as well as the associated procedures that must be carried out to mitigate them. Its definition is based on the recommendations given by an independent expert.

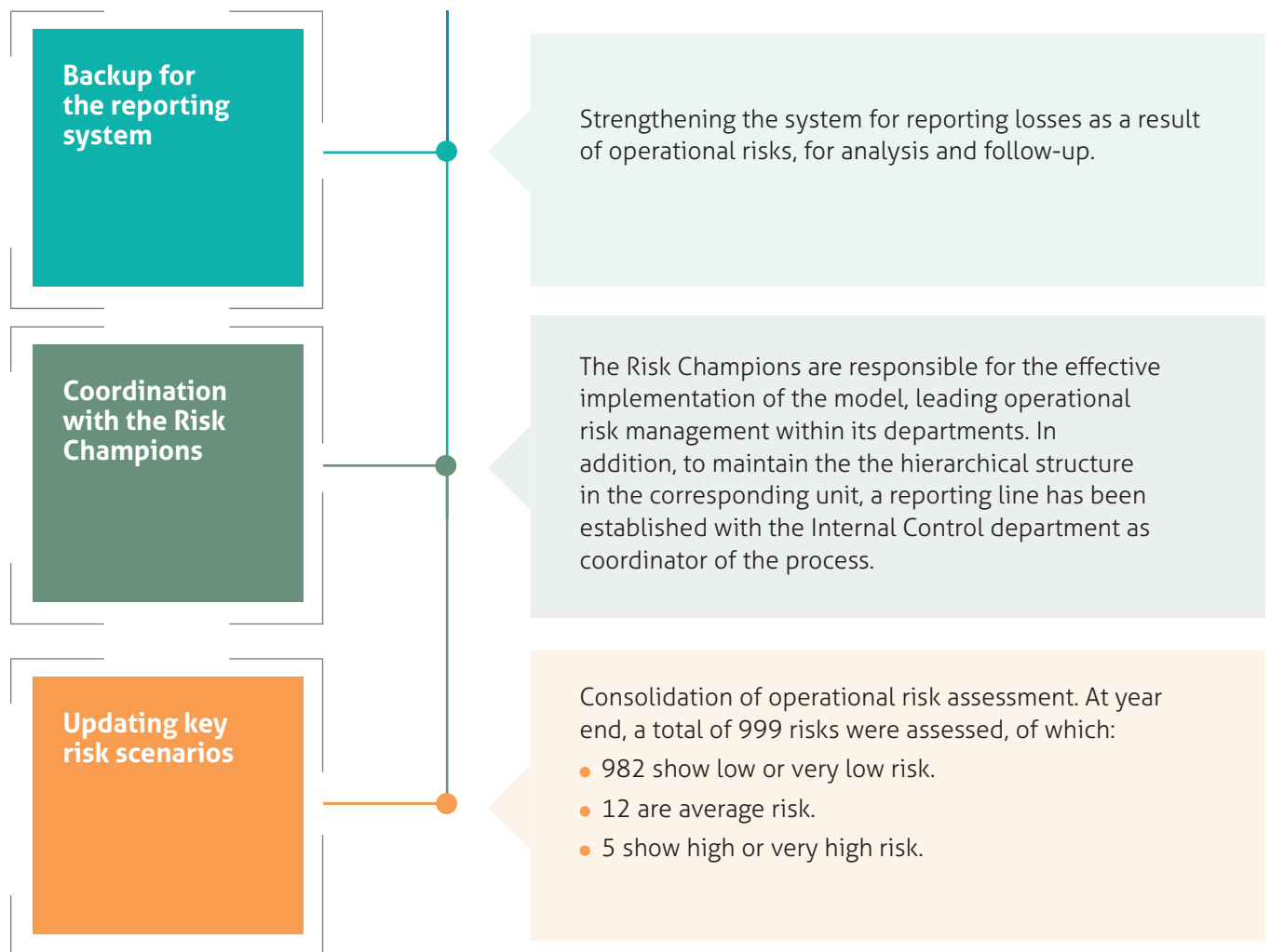
Sareb has carried out a risk assessment throughout the entire organisation, incorporating a risk tolerance framework –financial and non-financial– which

includes specific metrics for each type of identified risk and minimum thresholds that trigger the action plans.

In 2018, functions and data were consolidated and introduced into the company's risk management. In this respect, special mention is made of the role of the Risk Management Team (GGCR) -made up by different areas of the company-, which is responsible for approving the methodological approaches for all risks, in order to then refer them to the Board of Directors.

Within the scope of the GGCR's activity in 2018, the following are highlighted:





Emerging risks for Sareb





One of the challenges the company faces in the short term is explained by the pressure exerted on prices by the large investment funds.





If the large investment funds are looking for short-term return –due to the heavy discounts with which they have bought their portfolios–, they could enter the retail property market with significant price reductions compared to the appraisal values. If this happens, Sareb would be affected to the extent that both parties hold assets in overlapping territories.

Other risks facing Sareb involve the expectation of a slight deceleration shown by most of the financial forecasts by official institutions or potentially disrupting events such as Brexit or the hardening of trade tensions with the USA.

The Sareb map of risks

In line with the above, the company undertook a review of risk taxonomy and evolution from the inception of Sareb in 2012 to the current state of identified risks, approved in 2017.

	 Integrity	 Financial information
DEFINITION OF RISK	Non-compliance with ethical standards or generally accepted principles that result from deficiencies in the standards of conduct established by the Company or the procedures associated with them or improper personal behaviour. This includes risks deriving from legal, criminal and fiscal issues when due to wilful intent.	The consequences of errors in financial information attributable to inadequate accounting policies or failures in the establishment of accounting treatment criteria for transactions or deficiencies in how they are implemented.
HOW IS IT MANAGED?	The Code of Conduct and its developments ensure the safekeeping of the company's integrity and its proper management.	Management comprises a set of controls that provide reasonable assurance about the reliability of the financial information included in the financial statements.
	 Operational	 Credit
DEFINITION OF RISK	Failures in the processing of transactions attributable to unintentional human error or inadequate or defective processes or system failures, or as a consequence of external events.	<p>Breach by third parties of the contractual terms agreed with the company for fulfilling their debt payments.</p> <p>This includes counterparty risk, which arises from the possibility of insolvency of any of the banks where Sareb has deposited its liquid assets or with which it has derivative contracts.</p>
HOW IS IT MANAGED?	Management encompasses an exhaustive and complete set of policies, manuals and procedures that ensure the minimisation of operational errors. As far as possible, Sareb automates those risks that are considered critical.	Management establishes specific procedures based on the different characteristics of the financial asset units and operations.

	 Real Estate	 Interest rate
DEFINITION OF RISK	Caused by variations in market prices which could have an adverse effect on the value of the company's assets.	Changes in interest rates affect both the variable rates for the assets and liabilities and the financial value of the assets
HOW IS IT MANAGED?	Active risk management covers the analysis of all the variables that affect the evolution of the real estate market, in order to optimise valuation and implement palliative strategies.	Management is carried out through the daily monitoring of the evolution of interest rate curves and monthly monitoring of the impact on Sareb's financial costs, raising awareness of extreme scenarios.
	 Liquidity	 Reputational
DEFINITION OF RISK	Inability to meet payment obligations in the terms established in the contracts with third parties as a result of not having the necessary resources.	<p>This is derived from the set of perceptions that the stakeholders have about Sareb as a result of its behaviour and actions over time.</p> <p>There is reputational risk when Sareb projects a message/image to its internal and external stakeholders that does not conform to its values.</p> <p>This could be attributed to events of any nature different from those directly related to the integrity of the company or with the reliability of its financial information.</p>
HOW IS IT MANAGED?	<p>Management includes continuous analysis and definition of contingency plans, as well as the management of surpluses in accordance with the prudence principle, and an investment policy under the framework defined by the method of establishing counterparty risk limits, approved by the Board of Directors.</p> <p>The liquidity horizon is also calculated every quarter, that is, Sareb's ability to meet its average payment commitments with the cash available.</p>	<p>Sareb has a Policy on Reputation Risk "by contagion", which allows the ordering of different risk situations the company may face and those derived from the parties involvement in criminal procedures related to assets received by Sareb.</p> <p>The company also has Communication and Institutional Relations Policies, which ensure transparency, and a Corporate Social Responsibility Policy which details the company's commitments to carry out its mandate in a sustainable manner.</p>

	✓ Strategic
DEFINITION OF RISK	<p>As a result of policies, targets or strategies inconsistent with company mission or the context in which its business and activities would have to be developed. This includes the risk for decisions incorrectly executed or inadequately implemented.</p> <p>This applies to all areas of Sareb, including those directly involved in the activity of divestment of company assets and those involved in activities of internal organisation, given their capacity to influence compliance with the company mandate.</p>
HOW IS IT MANAGED?	<p>Management is carried out through the monitoring and annual update of the Sareb Business Plan.</p>



6. APPENDICES

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About this report

For the second consecutive year, Sareb has prepared and presented its Annual Activity Report in accordance with the guidelines of the International Integrated Reporting Framework (IIRC) and in line with the reporting principles of the Global Reporting Initiative

The company complies with its duty to report annually on the evolution of its activity, and is working towards the implementation of the provisions of Act 11/2018⁴⁰, which extends the obligation to present a non-financial information statement to companies with more than 250 employees within a maximum period of three years, which will apply to Sareb from 2021.

This report has also been prepared in accordance with the Essential option of the GRI Standards.

The content of this report is also supplemented with the other publications and information available on Sareb's corporate website, which can be accessed following the links placed throughout the report for expanding on the information.

Scope of the information

The information and quantitative data in this report correspond to 2018. However, and with the aim of making it easier for the reader to understand the evolution of the business from the outset, the figures and facts relating to previous years are also included.

Similarly, throughout the report prospective information is provided, based on the analysis of the current context and its expected evolution, without compromising those objectives for achieving it.



⁴⁰ Arising from RD-Law 18/2017 and which transposes the 2014/95/EU directive into Spanish Law.

Sareb stakeholders

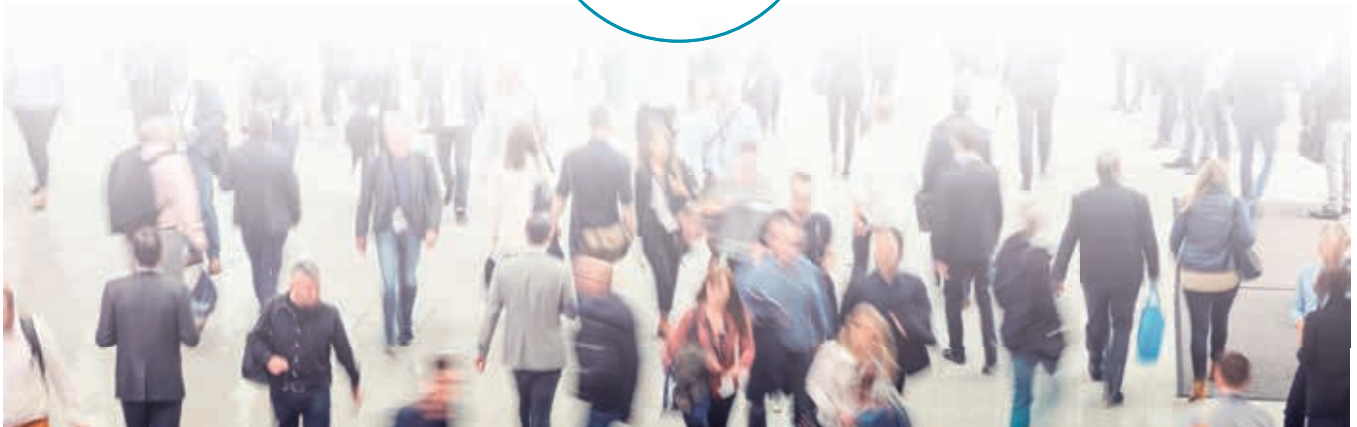
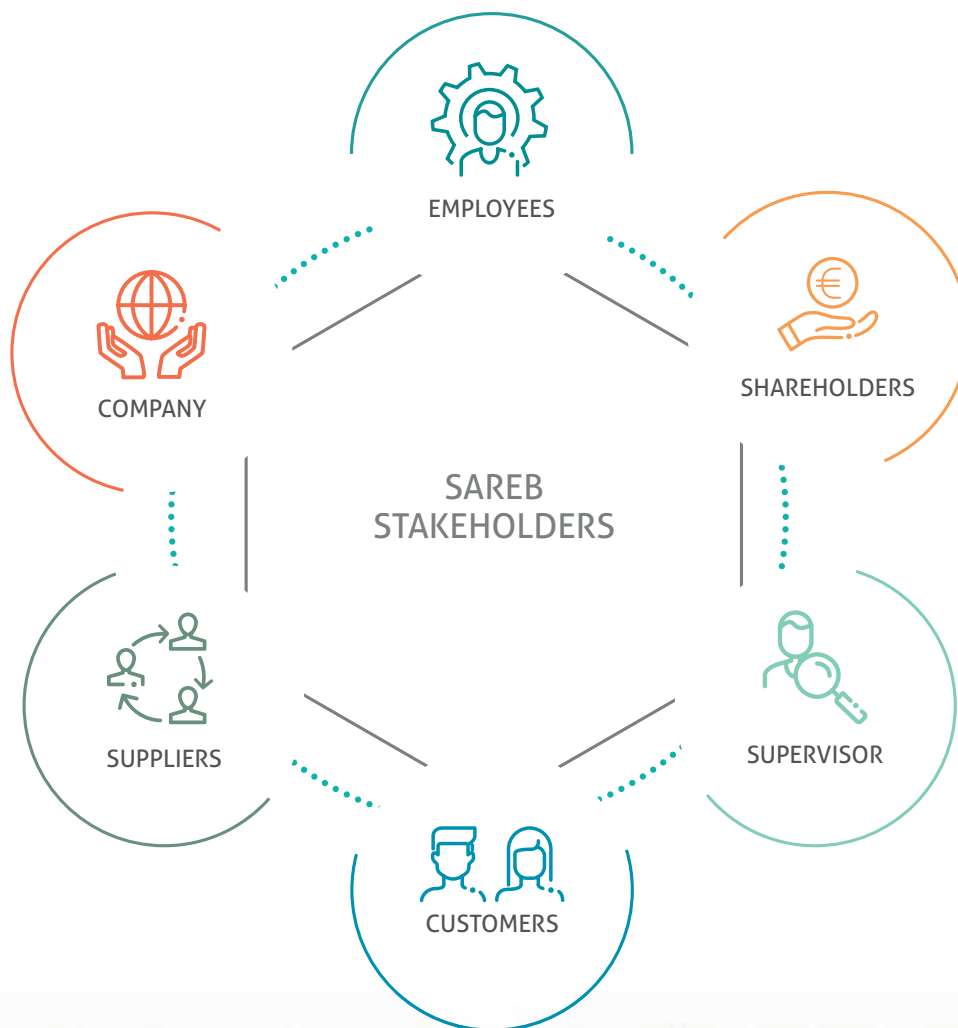
102-40

102-42

102-44

Sareb identifies stakeholders on the basis of their influence and impact on the activity of the company

Taking these criteria into account, and bearing in mind the assumption that the identification of stakeholders is an ongoing process, Sareb's main stakeholders are the following:





Mechanisms for closeness and communication with stakeholders

102-43

Since its creation, Sareb has maintained a firm commitment to transparency and the ready availability of information to its stakeholders. With this in mind, the company has designed various online and face-to-face mechanisms for each of its major stakeholders, in order to manage the relationship between the parties and provide useful information when taking decisions relating to the organisation.

Sareb has also created bidirectional listening and dialogue channels, designed to promote a deeper understanding and awareness of the perceptions and expectations of the most important stakeholder groups.

Channels worthy of mention

Employees 	<p>Sareb conducts staff surveys to identify employees' concerns and possible improvements. The company then develops action plans to respond to the issues raised.</p> <p>The Sareb intranet functions as an interactive platform where employees receive information about company initiatives and achievements, and share their own thoughts on the subject.</p>
Shareholders 	<p>Shareholders receive invitations to participate in meetings and video conferences on the evolution of the company.</p> <p>The company is currently working on developing a space on its website with specific information of interest to shareholders. This will provide improved communication and a more dynamic relationship with them.</p>
Supervisor and public authorities 	<p>Sareb maintains fluid and transparent communication with supervisors and public administrations, meeting on a regular basis to share information about the evolution of the company and the fulfilment of its objectives.</p> <p>Sareb also works closely with the autonomous regions and local councils with which it has agreements for the assignment of housing for social purposes, and promotes dialogue with other organisations that are interested in entering into similar agreements with the company.</p>
Customers 	<p>The Sareb Responde channel allows the company to address any questions or concerns that may arise from potential clients and buyers.</p>
Suppliers 	<p>Sareb establishes stable relationships with suppliers, based on proactive communication designed to ensure continuous improvement and mutual benefit.</p>
Company 	<p>In addition to the Sareb Responde channel, the company conducts regular surveys to gain a deeper understanding and awareness of the general public's perceptions and expectations in relation to the organisation. Sareb also maintains bidirectional communication with the media, in order to provide society with useful and reliable information about the evolution of the company.</p>

The Sareb website (www.sareb.es) is the main portal for obtaining information about the company. 2018 has seen the addition of a new Twitter profile (@Sareb) and Facebook profile (@Sareb_Oficial) to complement Sareb's activity on its LinkedIn account. The company has also created its own 'Huellas' blog, which aims to report on social changes and the company's relationship with the real estate sector.



More information on **Huellas**

<https://www.huellasbysareb.es/>

Review of the materiality analysis

102-46

The orientation and focus of the contents of this new report have been determined by the review of the materiality analysis carried out by Sareb in 2017. The conclusions obtained in the previous study have undergone deeper analysis to ensure continued compliance with the guidelines of the International Integrated Reporting Framework and the provisions of the GRI Standards for the preparation of sustainability reports.

Methodological development

The identification of issues and their prioritisation was addressed from two perspectives: internal, as a starting point to define and prioritise those issues relevant to the business; and external, which allows Sareb to know which of these issues concern its stakeholders or that could have an impact on them, considering the context and trends for the sector.

In 2018 the company has taken into account new aspects to enhance both perspectives:

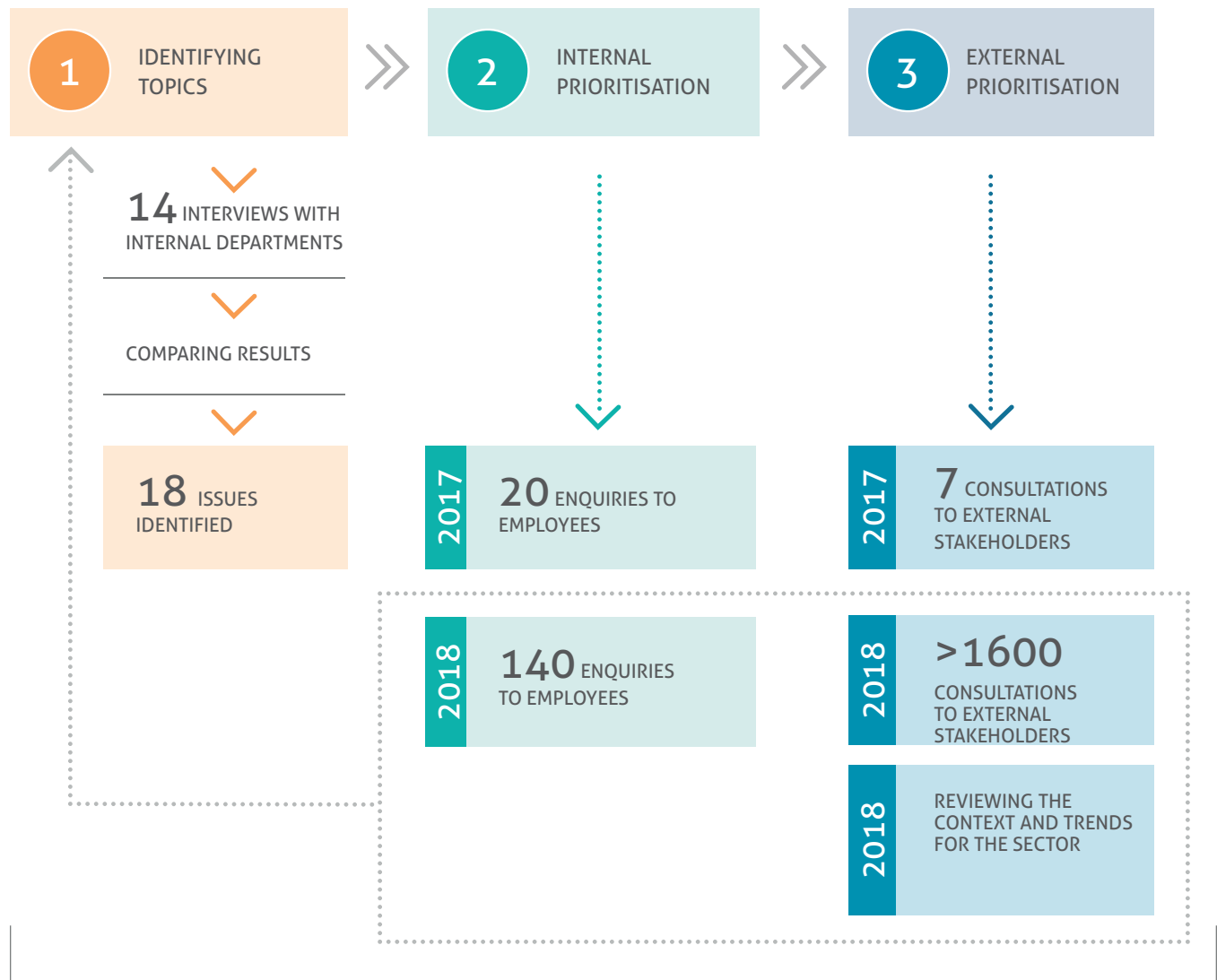
INTERNAL PRIORITISATION	A survey was carried out with 140 employees to reflect on, review and update the results obtained in the previous materiality assessment.
EXTERNAL PRIORITISATION	<p>In addition to the interviews carried out in 2017 with the various external stakeholders, this year's report also takes into account the reputation survey that Sareb conducted during the year. This quantitative and qualitative analysis, which was based on over 1,600 surveys of company stakeholders⁴¹, gathered information about stakeholder concerns and priorities in relation to Sareb.</p> <p>The company has also carried out a review of the sector context and trends that affect Sareb and potentially influence stakeholder assessments and decisions.</p>



⁴¹ The reputation survey includes consultations with experts from the real estate, financial and public administration sectors, clients, opinion leaders, employees and society in general. Consultations with opinion leaders do not have quantitative assessments. Employees are not taken into account for the external perspective, as they are part of the internal dimension, where ad hoc consultation has been conducted with 140 people.

Assessment methodology

102-46



List of issues

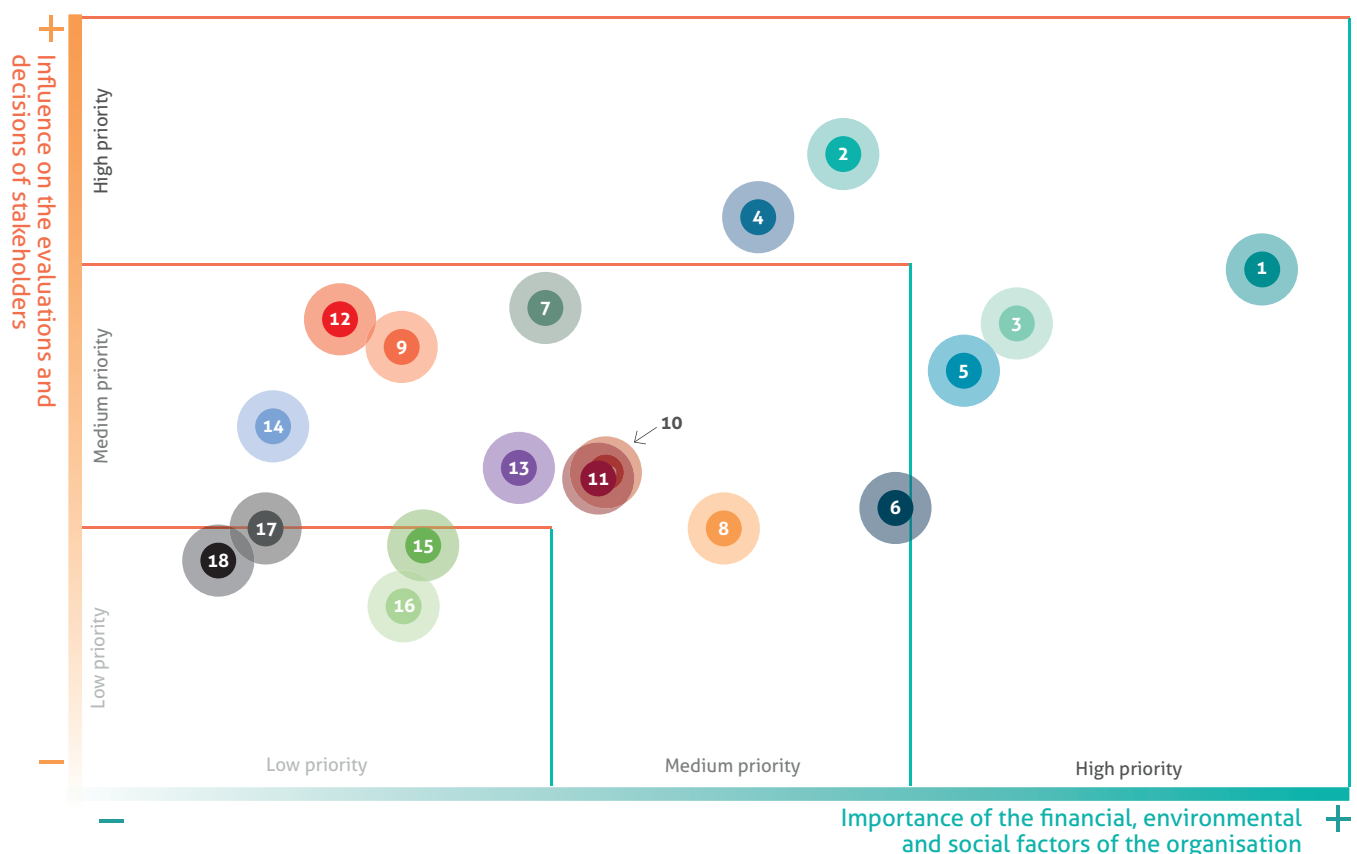
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102-47

HIGH PRIORITY	MEDIUM PRIORITY	LOW PRIORITY
<ol style="list-style-type: none"> 1 Efficient and responsible management of the asset portfolio received 2 Transparency in the activity carried out 3 Payment of the debt without cost to the taxpayer 4 Integrity, prevention of corruption and conflicts of interest 5 Creation of value to improve the commercial viability of the portfolio 	<ol style="list-style-type: none"> 6 Commercial viability of real estate assets 7 Systems for the control, supervision and monitoring of activity 8 Flexibility to adapt to the market 9 Relationship with counterparties: public authorities, suppliers, etc. 10 Expected return for shareholders 11 Talent management and the professional development of employees 12 Respect for free competition and the free market 13 The company's role in providing impetus to the real estate sector 14 Closeness and communication with stakeholders 	<ol style="list-style-type: none"> 15 Respect for equality, diversity and non-discrimination 16 Applied innovation: efficiencies and development of new products and services 17 Impact of construction work on the environment 18 Social action initiatives related to housing

Materiality matrix

Prioritisation of issues on the basis of internal and external assessments.



GRI content index



For the Materiality Disclosures Service, GRI Services have checked that the list of GRI contents is clear, and that the references for Contents 102-40 to 102-49 correspond with the indicated sections of the report.

This service was performed on the Spanish version of the report.

GRI Code	Description of the indicator	Reference / Response
GRI 101: Foundation 2016		
GRI 102: General Disclosures 2016		
Profile of the organisation		
102-1	Name of the organisation	Sareb, Sociedad de Gestión de Activos Procedentes de la Reestructuración Bancaria, S.A.
102-2	Activities, brands, products and services	12-15
102-3	Location of headquarters	Paseo de la Castellana, 89, Madrid 28046
102-4	Location of operations	Spain
102-5	Ownership and legal form	Public Limited Company
102-6	Markets served	Spain
102-7	Scale of the organisation	13, 23, 24
102-8	Information on employees and other workers	61, 62 and 66
102-9	Supply chain	66
102-10	Significant changes to the organisation and its supply chain	66
102-11	Precautionary Principle or approach	Not applicable
102-12	External initiatives	United Nations Global Compact
102-13	Membership of Associations	Association of Professionals in Regulatory Compliance
Strategy		
102-14	Statement from senior decision-maker	7-9
102-15	Key impacts, risks and opportunities	25-27, 29, 77-81
Ethics and integrity		
102-16	Values, principles, standards and norms of behaviour	11, 75-76
102-17	Mechanisms for advice and concerns about ethics	76
Governance		
102-18	Structure of governance	The Board of Directors is responsible for approving the Corporate Liability Policy –as part of its function of drawing up the strategy and policy guidelines of the Company–, drafting programmes and setting targets for the performance of all the activities included in the corporate objects, as well as the Medium-Term Social Housing Programme, for providing rental properties at affordable prices through the autonomous regions and other public institutions.
102-21	Consulting stakeholders on economic, environmental, and social topics	85-87

GRI Code	Description of the indicator	Reference / Response
102-22	Composition of the highest governance body and its committees	69, 70-74
102-23	Chair of the highest governance body	72
102-24	Nominating and selecting the highest governance body	73
102-25	Conflict of interest	74
102-26	Function of the highest governance body in setting purpose, values, and strategy	73
102-27	Collective knowledge of the highest governance body	72
102-28	Evaluating the highest governance body's performance	73
102-35	Remuneration policies	73
Stakeholder engagement		
102-40	List of stakeholder groups	84
102-41	Collective bargaining agreements	All employees are covered by collective bargaining agreements.
102-42	Identifying and selecting stakeholders	84
102-43	Approach to stakeholder engagement	85
102-44	Key topics and concerns raised	84, 88
102-45	Entities included in the consolidated financial statements	At 31 December 2018, Sareb had a 99.12% interest in Tempore Properties Socimi, S.A. and a 49% interest in the '2013 Bull' Banking Assets Fund (FAB) (the only FAB set up that has not been deconsolidated).
Reporting practice		
102-46	Defining report content and topic boundaries	86, 87
102-47	List of material topics	88
102-48	Restatement of information	During 2018 there was a change of criterion for calculating the number of debtors per ranking of debt.
102-49	Changes in reporting	The list of material issues is kept in respect of 2017 but the order of priority does vary between items.
102-50	Reporting period	2018
102-51	Date of most recent report	2018
102-52	Reporting cycle	Annual
102-53	Contact point for questions regarding the report	Tel.: (+34) 915 563 700 www.sareb.es
102-54	Claims of reporting in accordance with the GRI standards	83
102-55	GRI content index	89
102-56	External assurance	Not applicable
MATERIAL TOPICS		
Efficient and responsible management of the asset portfolio received		
GRI 103: Management Approach 2016		

GRI Code	Description of the indicator	Reference / Response
103-1	Explanation of the material topic and its boundary	12-13, 26-27
103-2	The management approach and its components	12-13, 26-27
103-3	Evaluation of the management approach	12-13, 26-27
GRI 201: Economic performance 2016		
201-1	Direct economic value generated and distributed	14-15
Transparency in the activity carried out		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	11, 83
103-2	The management approach and its components	11, 83
103-3	Evaluation of the management approach	11, 83
Payment of the debt without cost to the taxpayer		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	13, 34, 35
103-2	The management approach and its components	13, 34, 35
103-3	Evaluation of the management approach	13, 34, 35
GRI 203: Indirect economic impacts 2016		
203-2	Significant indirect economic impacts	13, 18, 20.21
Integrity, prevention of corruption and conflicts of interest		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	71, 75, 76, 79
103-2	The management approach and its components	71, 75, 76, 79
103-3	Evaluation of the management approach	71, 75, 76, 79
GRI 205: Anti-corruption 2016		
205-2	Communication and training about anti-corruption policies and procedures	76
Creation of value to improve the viability of the portfolio		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	16, 17, 26, 27
103-2	The management approach and its components	16, 17, 26, 27
103-3	Evaluation of the management approach	16, 17, 26, 27
Commercial viability of real estate assets		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	26, 27
103-2	The management approach and its components	26, 27
103-3	Evaluation of the management approach	26, 27
Systems for the control, supervision and monitoring of activity		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	70, 71, 75, 76

GRI Code	Description of the indicator	Reference / Response
103-2	The management approach and its components	70, 71, 75, 76
103-3	Evaluation of the management approach	70, 71, 75, 76
Flexibility to adapt to the market		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	12, 13, 16, 17
103-2	The management approach and its components	12, 13, 16, 17
103-3	Evaluation of the management approach	12, 13, 16, 17
Relationship with counterparties: public authorities, suppliers, etc.		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	21, 66, 85
103-2	The management approach and its components	21, 66, 85
103-3	Evaluation of the management approach	21, 66, 85
GRI 204: Procurement practices 2016		
204-1	Proportion of spending on local suppliers	66
GRI 308: Supplier Environmental Assessment 2016		
308-1	New suppliers that were screened using environmental criteria	Of the suppliers assessed in accordance with environmental criteria in 2018, 65% are new and the rest correspond to the reviews of suppliers already approved.
GRI 414: Supplier Social Assessment 2016		
414-1	New suppliers that were screened using social criteria	Of the suppliers assessed in accordance with social criteria in 2018, 65% are new and the rest correspond to the reviews of suppliers already approved.
Expected return for shareholders		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	11, 13
103-2	The management approach and its components	11, 13
103-3	Evaluation of the management approach	11, 13
GRI 201: Economic performance 2016		
201-1	Direct economic value generated and distributed	23-27
Talent management and the professional development of employees		
GRI 103: Management Approach		
103-1	Explanation of the material topic and its boundary	61-65
103-2	The management approach and its components	61-65
103-3	Evaluation of the management approach	61-65
GRI 401: Employment 2016		
401-1	New employee hires and employee turnover	62
GRI 404: Training and education 2016		
404-1	Average hours of training per year per employee	64
404-2	Programmes for upgrading employee skills and transition assistance programmes	64

GRI Code	Description of the indicator	Reference / Response
404-3	Percentage of employees receiving regular performance and career development reviews	64
Respect for free competition and market		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	61-65
103-2	The management approach and its components	61-65
103-3	Evaluation of the management approach	61-65
GRI 206: Anti-competitive behaviour 2016		
206-1	Legal action related to unfair competition and monopolistic practices and against free competition.	No cases have been notified of non-compliance related to unfair competition and other similar practices in the reporting period.
The company's role in providing impetus to the real estate sector		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	13, 15, 16
103-2	The management approach and its components	13, 15, 16
103-3	Evaluation of the management approach	13, 15, 16
GRI 203: Indirect economic impacts 2016		
203-2	Significant indirect economic impacts	13
Closeness and communication with stakeholders		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	84, 85
103-2	The management approach and its components	84, 85
103-3	Evaluation of the management approach	84, 85
Respect for equality, diversity and non-discrimination		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	61, 62, 71-73
103-2	The management approach and its components	61, 62, 71-73
103-3	Evaluation of the management approach	61, 62, 71-73
GRI 405: Diversity and equal opportunity 2016		
405-1	Diversity of governance bodies and employees	61, 62, 71, 72
GRI 406: Non-discrimination 2016		
406-1	Incidents of discrimination and corrective actions taken	No incidents of discrimination have been identified during the reporting period.
Applied innovation: efficiencies and development of new products and services		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	65
103-2	The management approach and its components	65

GRI Code	Description of the indicator	Reference / Response
103-3	Evaluation of the management approach	65
Impact of construction work on the environment		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	67
103-2	The management approach and its components	67
103-3	Evaluation of the management approach	67
GRI 302: Energy 2016		
302-1	Energy consumption within the organisation	67
302-3	Energy intensity	67
GRI 307: Environmental compliance 2016		
307-1	Non-compliance with environmental laws and regulations	No cases have been notified of non-compliance of environmental legislation during the reporting period.
Social action initiatives related to housing		
GRI 103: Management Approach 2016		
103-1	Explanation of the material topic and its boundary	20
103-2	The management approach and its components	20
103-3	Evaluation of the management approach	20
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7. FINANCIAL STATEMENTS

Sociedad de Gestión de Activos
Procedentes de la Reestructuración
Bancaria, S.A.

Annual accounts and Directors' report at
31 December 2018



This version of our report is a free translation of the original, which was prepared in Spanish. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views and opinions, the original language version of our report takes precedence over this translation.

Independent auditor's report on the annual accounts

To the Shareholders of Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.:

Report on the annual accounts

Opinion

We have audited the annual accounts of Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A. (the Company), which comprise the balance sheet as at December 31, 2018, the income statement, the statement of changes in equity, the cash flow statement and the related notes for the year then ended.

In our opinion, the accompanying annual accounts present fairly, in all material respects, the equity and financial position of the Company as at December 31, 2018, as well as its financial performance and cash flows for the year then ended, in accordance with the applicable financial reporting framework (as identified in Note 2 of the notes to the annual accounts), and, in particular, with the accounting principles and criteria included therein.

Basis for opinion

We conducted our audit in accordance with legislation governing the audit practice in Spain. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the annual accounts* section of our report.

We are independent of the Company in accordance with the ethical requirements, including those relating to independence, that are relevant to our audit of the annual accounts in Spain, in accordance with legislation governing the audit practice. In this regard, we have not rendered services other than those relating to the audit of the accounts, and situations or circumstances have not arisen that, in accordance with the provisions of the aforementioned legislation, have affected our necessary independence such that it has been compromised.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the annual accounts of the current period. These matters were addressed in the context of our audit of the annual accounts as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

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Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Key audit matters	How our audit addressed the key audit matter
<p><i>Going concern assessment</i></p> <p>As disclosed in note 2.4 of the accompanying annual accounts, the Company recognised negative equity in the amount of 5,135,891 thousand euros at 31 December 2018. However, the Company is not affected by any of the grounds for dissolution stipulated in article 363 of Spain's Capital Companies Act (LSC) because, under the regulations applicable to the Company, the following items do not compute for such purposes: (i) the changes in the measurement of derivatives - a negative balance of 1,221,223 thousand euros - which is recognised under "Value change adjustments for cash flow hedges"; and (ii) the balance of impairment allowances against the financial asset unit - in the amount of 5,091,686 thousand euros - which is recognised under "Valuation adjustment for the impairment of financial assets". As a result, at 31 December 2018, the Company's equity, for corporate law purposes, stood at 1,177,018 thousand euros.</p> <p>In addition, the Directors believe, as set down in the assessment outlined in note 2.4, that there are other factors that mitigate any doubts about the Company's ability to continue as a going concern, including the existence at 31 December 2018 of positive working capital in the amount of 2,938,348 thousand euros and of cash and cash equivalents in the amount of 2,827,392 thousand euros. The Company also has the unilateral option to roll over senior debt issues with a face value of 36,434,600 thousand euros at year-end 2018 (refer to note 13.2). As disclosed in note 13, those issues are unconditionally and irrevocably guaranteed by the Spanish Administration, which has moreover waived its right to require the creditor to exhaust all remedies before executing the guarantee.</p> <p>In addition, it had subordinated debt that is convertible into equity in the amount of 1,429,560 thousand euros at year-end (note 13).</p>	<p>Within the scope of our audit, we analysed the going concern assessment performed by the Company's Directors. The main audit procedures conducted in this respect as follows:</p> <ul style="list-style-type: none"> • We met with the Company's management to obtain an adequate understanding of the considerations made in conducting the going concern assessment. • We read the minutes of the meetings of the Board of Directors and of the Audit Committee. • We obtained and analysed the information used by the Company to prepare its going concern assessment. <p>Specifically, the most relevant information obtained for the analysis is business plan prepared by the Company and approved by the Board of Directors. We have assessed for reasonableness the hypothesis and significant assumptions used in the Business Plan by means of the following audit procedures, among others:</p> <ul style="list-style-type: none"> • We tested the business plan's hypothesis for consistency with the Company's annual budgets for the future exercises. • We assessed the reasonableness of the underline assumptions and hypothesis of the business plan in the context of the uncertainty implicit in those estimates. • We conducted sensitivity analysis for certain of the most significant assumptions used in the projections prepared by the Company, focusing particularly on the next 12 months. • We also obtained and evaluated the legal analysis conducted by the Company and its legal advisors, in collaboration with our own legal experts, regarding the legal consequences of a potential shortfall of equity at the Company and the potential consequences for its business activities.



Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Key audit matters	How our audit addressed the key audit matter
<p>As disclosed in note 2.4, the Company is required to update its business plan annually. That plan is prepared under currently prevailing accounting standards and measurement rules, summarised in note 4, in keeping with the applicable financial reporting framework (note 2.1). It is worth noting in this respect that the most recently updated Board-approved business plan evidences a change in the Company's strategy towards preservation of the economic value of its assets. As indicated by the Directors in that note, although the Company is pursuing full disposal of its assets, in so doing it needs to adapt to unfolding market circumstances as well as the circumstances affecting the assets themselves in order to protect their value, which is implying the accumulation of its inventory of assets on its balance sheet towards the end of the projection period contemplated in its business plan.</p> <p>Given that realization of the business plan in accordance with current estimates is subject to a high degree of uncertainty, depending on the actual performance of the markets and the Company's ability to divest, the Company could experience a deficit of its own funds consumed in the medium term, however, under no circumstances during the next 12 months.</p> <p>If the above mentioned situation occurs, the Company and its shareholders would have to take, within the periods of time prescribed in the Capital Companies Act (LSC), the measures necessary to replenish its equity for corporate law purposes. One of those measures, during an initial phase, would be to convert the above-mentioned debt into equity (note 13). In addition, depending on the needs that emerge, the Directors state in note 2.4 of its annual accounts that they would weigh up complementary or alternative measures for replenishing the Company's equity, including any of the measures contemplated in commercial legislation.</p> <p>As a result, based on the above assessment and as indicated in note 2.4, the Company's Directors have prepared the accompanying annual accounts on a going concern basis.</p> <p>Against this backdrop, our analysis of the adequate application of the going concern principal and of the related disclosures provided in the note of the annual accounts forms the basis for a key audit matter.</p>	<p>As a result of the above procedures, we obtained sufficient and adequate audit evidence regarding the judgements used by the Company's Directors in the preparation of their going concern assessment and the related disclosures made in the 2018 annual accounts.</p>



Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Key audit matters	How our audit addressed the key audit matter
<p><i>Valuation of the units of financial assets and real estate assets</i></p> <p>At the year end, the Company assesses the need to execute valuation adjustments relating to financial and property assets impairment. This evaluation was carried out on individual basis, offsetting gains against losses for assets within the same “assets unit”, in accordance with the Bank of Spain Circular 5/2015, of September 30.</p> <p>The valuation adjustments relating to financial assets and real estate assets impairment, is one of the most significant and complex estimation for the accompanying annual accounts, therefore was consider a key audit matter.</p> <p>According to the Bank of Spain Circular 5/2015, the Company has classified its assets in two different assets units as follows:</p> <ul style="list-style-type: none"> Financial assets unit: credit rights transferred to the Company, mortgage foreclosures and acquired in payment after the transfer date. Real estate asset unit: properties with that nature at the transfer date. <p>In accordance with the regulation set by the Circular as well as based on the criteria established in it, the Company has developed a assets’ methodology for estimating the impairment adjustments.</p> <p>The process to estimate the possible impairment adjustments of the assets carried out by the Company is as follows:</p> <ul style="list-style-type: none"> As regards to the property assets unit, the evaluation was carried out individually, according to the Bank of Spain Circular 5/2015, taking into account the following criteria: <ul style="list-style-type: none"> Generally, the Company estimates the value of property assets based on their mortgage value, calculated from valuation reports (full individual appraisals) made in accordance with the criteria set out in Order ECO/805/2013, of 27 March. Appraisal companies registered in the Official Registry of Appraisal Companies of the Bank of Spain made these valuation reports. 	<p>Our audit work regarding the estimation of the impairment adjustments to financial assets and real estate assets value has focused, among others, on the analysis, evaluation and verification of the internal control system, as well as the performance of detailed tests on the estimates made by the Company.</p> <p>With respect to the internal control environment, we have evaluated the design and tested the controls operational effectiveness in the following areas:</p> <ul style="list-style-type: none"> Verifying the IT general controls of the systems used to produce the financial information. Verification of the main aspects of the security environment of the information systems that include the calculation of impairment adjustments. Verifying the adequacy of the policies and procedures, internal methodology approval to the relevant regulatory requirements applied, as well as obtaining, understanding and analyzing the interpretations of the Company in relation to the specific applicable rules. Understanding of the internal control environment regarding the internal valuation methodology, identifying and validating the main key controls. <p>In addition, we have carried out, among others, the following substantive procedures:</p> <ul style="list-style-type: none"> Reviewing the sample of the operations for the data quality testing purposes of the information contained in the systems, which was used as a basis for the assets’ value estimation as well as for the calculation of possible impairment adjustment of the asset units’ value. We evaluated the competence, independence and integrity of the appraisal companies whose reports had been used for the valuation of the financial and property assets of the Company.



Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Key audit matters	How our audit addressed the key audit matter
<ul style="list-style-type: none"> The company has the possibility to choose to perform full individual valuations, valuations based on sampling statistical procedures or making valuation by using automatic valuations, with the objective to estimate the value of finished houses and annexes to them as well as commercial premises located in towns where there is a representative market for comparable properties, and if exists a valuation report prepared in accordance with regulation mentioned above and which seniority is less than three years. Appraisal companies registered in the Official Registry of Appraisal Companies of the Bank of Spain made these valuation reports. For those assets of the property assets unit, different from categories mentioned in the previous paragraph, the Company uses its best estimate based on an internal valuation model evaluated by an independent expert. 	<ul style="list-style-type: none"> For a selected sample of valuation reports, we have verified, in collaboration with our experts in this matter, the assumptions used by the appraisal companies in the realization of their valuations in order to evaluate the reasonableness of them, as well as comparing with market data relevant and attending to the current situation of the buildings. In cases of use of automatic valuation models, we have verified, in collaboration with our experts in this matter, the adequacy of the valuation methodologies applied by the appraisal companies and communicated to the Company. We have carried out verifications regarding to the adjustments applied by the Company on the values of the appraisals received from third parties in relation to: i) the reflection of the evolution of market prices and the horizons of the Company's business plan; ii) the estimated maintenance and marketing costs and iii) the update to present value of the values obtained after applying the above mentioned adjustments. The above mentioned adjustments made to appraisals should be treated as a change in the Business Plan during a complex exercise and it requires a high degree of judgment and estimation based on the circumstances, applicable regulations, the information that is available at the moment and that should be updated as well as should be approved by the Board of Directors of the Company on the annual basis.
<p>Additionally to the valuation obtained according to the criteria described in the previous paragraphs, the methodology developed by the Company mainly considers the following aspects in the final valuation of the assets:</p>	<ul style="list-style-type: none"> We have obtained and analyzed the assessment made by the Company regarding the contrast between the evolution of the appraisals (revaluations made in the year) and the evolution of the price curves used by type of assets (land, residential, other assets) and respective analysis of the sales during the period. We have Re-performance of the impairment adjustments calculation of each assets unit basing on the estimation of assets' value. We have verified the sensitivity analysis and assumptions verifications used in the valuation of the asset units.
<ul style="list-style-type: none"> Adjustments to reflect the evolution of market prices and the horizons of the Company's business plan. Estimation of maintenance and marketing costs, which were deducted from the result applying the criteria described above. 	



Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Key audit matters	How our audit addressed the key audit matter
<ul style="list-style-type: none"> - Discount or update rate. The valuation obtained after the application of the above adjustments was update to present value by applying an estimated discount rate taking into account the cost of financing the Company and the inherent risks in the assets. • Regarding to the financial assets, the evaluation was carried out on individual basis, according to the capacity of payment of theirs debtors, taking into account the existence of guarantors with demonstrated payment capacity. 	<ul style="list-style-type: none"> • We have verified the correct accounting registration of the impairment adjustments estimated by the Company in accordance with the Bank of Spain Circular 5/2015. <p>Based on the procedures described above, we consider that the methodology used by the Company, as well as the impairment estimation of its asset units, are within a reasonable range in the context of the applicable accounting framework and the circumstances that were considered in the process of preparation of accompanying annual accounts.</p>

For those financial assets for which it was estimated that the recovery of the amounts owed would be make through the foreclosure of the guarantees, the valuation of the financial assets are made by taking into account the property valuation of the guarantees. The evaluation was carried out in a similar way as the real estate assets described above, including in the estimation of costs not only those of maintenance and commercialization until the subsequent sale of the collateral, but also those necessary for the execution of the guarantees (procedural, legal and fiscal).

Financial assets without property asset collateral that presents delays in contractual obligations exceeding eighteen months from the date of transfer of the assets to the Company, or from the date of the first default if this is later, are considered, except for evidence against, with null value.

According to the criteria described above and the value of each asset calculated, the Company estimates the value of each asset, compensating for losses and gains of assets within the same assets unit.

As indicated in notes 4.7, 4.7.1 and 4.7.2., in estimating the value of the assets, a series of assumptions based on the business plan of the Company had been apply. Therefore, the evolution of the valuation was linked to compliance with the key assumptions of the business plan. In notes 4.7.1 and 4.7.2, the Company had included a sensitivity analysis on the key assumptions considered more volatile.



Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Key audit matters	How our audit addressed the key audit matter
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In accordance with the RD 4/2016, of December 2, on urgent financial measures, which modifies Act 9/2012, of November 14, on restructuring and resolution of credit institutions, the Company recognizes the valuation adjustments of the unit asset in the balance sheet, net of their tax effect, charged to "Value Change Adjustments - Impairment of financial assets", within equity. As established in the aforementioned RD 4/2016, the aforementioned adjustments would not be consider equity for the purposes of the distribution of profits, the mandatory reduction of share capital and the mandatory dissolution for losses established in the Capital Companies Act (LSC).

See notes 2.4. Critical aspects of the valuation and estimation of the uncertainty, 4.7 Impairment of financial assets, property investments and other accounts receivable, 4.7.1. Impairment of the property assets unit, 4.7.2. Impairment of loans and credits receivable and property assets received in payment of debts, 5. 5. Property Investments, 7.1.1. Long and short term third party loans, 8. Inventories, 11.4. Value change adjustments and 11.5 Equity Situation of the Company.

Aspects associated with the generation of financial information

The Company has four external managing companies (hereinafter, servicers) who manage the portfolios of financial and property assets assigned to them. Within its functions, each servicer registers and prepares the financial and accounting information of their own portfolios, reporting this information to the Company on a monthly basis. Based on this information, the Company carries out a process of accounting aggregation and generation of the financial information as a whole.

Among the accounting entries that are recorded by each servicer as part of the Company's accounting records, the most important are those that originate in the operation of sales of financial and property assets, mortgage foreclosures and dations in payment, leases of real estate, maintenance expenses of real estate and ordinary management of loans, among others.

The following describes the main procedures carried out at the headquarters of each servicer, regarding the generation of the Company's financial and accounting information:

- Verifying the IT general controls of the applications where the information on the managed financial and real estate assets is gathered.

In the framework of our work, certain aspects of improvement were detect in relation to access controls in some applications. This aspect has led to an increase in the work to be done by our side over the mitigating controls identified by the Company and an increase in the work done regarding certain substantive testing.



Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Key audit matters	How our audit addressed the key audit matter
<p>For an adequate control of the operations managed in each servicer, the Company has a communication platform. This platform was use in order to gather information and documentation about the operations and verify that they are within the framework of functions delegated to each servicer or, in its case, to be able to authorize the transaction before its formalization and its subsequent accounting registration.</p> <p>Consequently, the financial and accounting information associated with the operations managed at the headquarters of each servicer, resides in the computer systems of each of them, this way each and one of them is responsible for monthly and year end information submission to the Company. Therefore, an adequate control over the information systems in the main offices of each servicer is fundamental to guarantee the correct processing of the accounting information.</p> <p>In this context, the knowledge, evaluation and verification of controls established by the Company to ensure the integrity of financial information, as well as the execution of certain substantive verification tests at the servicers' headquarters, were consider a key audit matter.</p> <p>See note 1 Company Activity of the report of the attached annual accounts.</p>	<ul style="list-style-type: none"> Identifying automatic controls and key manual controls established by each servicer, on the financial and accounting information sent to the Company, and verification. Reviewing the sample of the operations, executed by each servicer with supporting documentation, verifying the proper accounting treatment and classification. Likewise, we have verified whether the framework of delegated functions was fulfill or, where appropriate, the existence of authorization of the operation by the Company when it is required. Reviewing the sample of the operations for the data quality testing purposes, verifying the information accounted in the servicers' systems with the supporting documentation, this way verifying the coherence between the information reflected in the servicers' systems and the systems of the Company. Verifying the reconciliation of accounting inventories generated by each servicer with the financial information sent to the Company. Understanding and analysis, on a sample basis, of entries introduced manually in the financial information systems. <p>Additionally, we have identified the automatic controls and key manual controls established by the Company, regarding the integrity of the financial and accounting data submitted by the servicers and we have evaluated their effectiveness.</p> <p>Our procedures allow us to obtain sufficient and adequate audit evidence in relation to the accounting aggregation process and the generation of financial information by the Company, without having identified relevant aspects that could significantly affect the financial information included in the financial statements in the accompanying annual accounts.</p>

Other information: Management report

Other information comprises only the management report for the 2018 financial year, the formulation of which is the responsibility of the Company's Directors, and does not form an integral part of the annual accounts.



Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Our audit opinion on the consolidated annual accounts does not cover the consolidated management report. Our responsibility regarding the information contained in the consolidated management report is defined in the legislation governing the audit practice, which establishes two distinct levels in this regard:

- a) A specific level applicable to certain information included in the Annual Corporate Governance Report, as defined in article 35.2 b) of Audit Act 22/2015, that consists of verifying solely that the aforementioned information has been provided in the management report and in opposite case, to inform regarding inconsistencies.
- b) A general level applicable to the rest of the information included in the consolidated management report that consists of evaluating and reporting on the consistency between that information and the consolidated annual accounts as a result of our knowledge of the Group obtained during the audit of the aforementioned financial statements and does not include information different to that obtained as evidence during our audit, as well as evaluating and reporting on whether the content and presentation of that part of the consolidated management report is in accordance with applicable regulations. If, based on the work we have performed, we conclude that material misstatements exist, we are required to report that fact.

On the basis of the work performed, as described above, we have ascertained that the information mentioned in paragraph a) above has been provided in the consolidated management report and that the rest of the information contained in the consolidated management report is consistent with that contained in the consolidated annual accounts for the 2018 financial year, and its content and presentation are in accordance with the applicable regulations.

Responsibility of the Directors and the Audit Committee for the annual accounts

The Company's Directors are responsible for the preparation of the accompanying annual accounts, such that they fairly present the equity, financial position and financial performance of the Company, in accordance with the financial reporting framework applicable to the entity in Spain, and for such internal control as the Directors determine is necessary to enable the preparation of annual accounts that are free from material misstatement, whether due to fraud or error.

In preparing the annual accounts, the Company's Directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The Audit Committee is responsible for overseeing the process of preparation and presentation of the annual accounts.

Auditor's responsibilities for the audit of the annual accounts

Our objectives are to obtain reasonable assurance about whether the annual accounts as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with legislation governing the audit practice in Spain will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these annual accounts.



Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

As part of an audit in accordance with legislation governing the audit practice in Spain, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the annual accounts, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Company's Directors.
- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the annual accounts or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the annual accounts, including the disclosures, and whether the annual accounts represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Company's Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Company's Audit Committee with a statement that we have complied with relevant ethical requirements, including those relating to independence, and we communicate with the Audit Committee those matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Company's Audit Committee, we determine those matters that were of most significance in the audit of the annual accounts of the current period and are therefore the key audit matters.

We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.



Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Report on other legal and regulatory requirements

Additional report to the Audit Committee

The opinion expressed in this report is consistent with the content of our additional report to the Company's Audit Committee dated on March 28 2019.

Appointment period

The General Ordinary Shareholders' Meeting held on May 9, 2017 appointed us as auditors for a period of two years, as from the year ended on December 31, 2017.

Previously, we were appointed by resolution of the General Shareholders' Meeting for a period of three years and we have audited the annual accounts continuously since the year ended on December 31, 2012.

Services provided

Services, other than the audit of the accounts, provided to the Company are disclosed in the note 16.4 of the accompanying annual accounts.

PricewaterhouseCoopers Auditores, S.L. (S0242)

Original in Spanish signed by:

Amagoia Delgado Rodríguez (22009)

March 28, 2019

SOCIEDAD DE GESTIÓN DE ACTIVOS PROCEDENTES DE LA REESTRUCTURACIÓN BANCARIA, S.A. (SAREB)

BALANCE SHEETS AT 31 DECEMBER 2018 AND 31 DECEMBER 2017

(Thousands of Euros)

ASSETS	Notes in Report	31/12/18	31/12/17
NON-CURRENT ASSETS		30,385,201	31,934,374
Intangible assets	Note 4.1	18,610	17,982
Administrative concessions		453	
Industrial property		39	46
Computer software		18,117	17,936
Property, plant and equipment	Note 4.2	12,409	5,081
Fixtures		181	212
Technical installations and other property, plant and equipment		12,135	4,695
IT equipment		94	174
Property investments	Note 5	11,893,908	11,699,278
Land		5,461,173	5,072,450
Completed properties		6,121,713	6,486,782
Advances on property investments		311,022	140,046
Long-term investments in group companies and associates		324,588	186,034
Equity instruments	Note 7.2.1	324,244	182,867
Loans to companies	Note 7.2.2	344	3,167
Long-term financial investments	Note 7.1	1,628,535	19,414,953
Loans to third and related parties		15,257,553	17,207,323
Other financial assets		2,370,982	2,207,630
Deferred tax assets	Note 15.3	507,152	611,046
CURRENT ASSETS		4,938,644	8,210,490
Inventories	Note 8	308,570	268,359
Products in progress		269,052	217,790
Finished products		19,387	17,327
Advances to suppliers		20,131	33,242
Trade and other accounts receivable	Note 9	208,703	196,236
Customer receivables from sales and services rendered		186,861	180,970
Sundry debtors		14,721	7,938
Staff		2	8
Current tax assets	Note 15.1	2,832	1,949
Other receivables from the Public Administrations	Note 15.1	4,287	5,371
Short-term financial investments	Note 7.1	1,592,072	3,608,270
Loans to companies		1,587,479	3,600,337
Other financial assets		4,593	7,933
Short-term accrual accounts		1,907	-
Cash and other cash equivalents	Note 10	2,827,392	4,137,625
Cash		2,692,538	2,751,862
Other cash equivalents		134,854	1,385,763
TOTAL ASSETS		35,323,846	40,144,864

Notes 1 to 19 described in the attached report form an integral part of the Balance Sheet at 31 December 2018.

SOCIEDAD DE GESTIÓN DE ACTIVOS PROCEDENTES DE LA REESTRUCTURACIÓN BANCARIA, S.A. (SAREB)

BALANCE SHEETS AT 31 DECEMBER 2018 AND 31 DECEMBER 2017

(Thousands of Euros)

LIABILITIES	Notes in Report	31/12/18	31/12/17
EQUITY	Note 11	(5,135,891)	(3,707,230)
SHAREHOLDERS' EQUITY-		1,177,018	2,055,367
Capital			
Subscribed capital		30,862	303,862
Issue premium		-	-
Legal reserve		19,174	19,174
Other reserves		1,732,331	2,296,907
Profit/(Loss) for the year		(878,348)	(564,576)
VALUE CHANGE ADJUSTMENTS-	Note 13.3	(6,312,909)	(5,762,597)
- Hedging operations		(1,221,223)	(1,533,045)
- Impairment of financial assets		(5,091,686)	(4,229,552)
NON-CURRENT LIABILITIES		38,459,441	39,383,208
Long-term provisions	Note 12	7,862	9,530
Long-term debts	Note 13	38,451,579	39,373,678
Debentures and other negotiable securities		36,403,198	36,891,090
Derivatives		1,710,260	2,057,320
Other financial liabilities		338,121	425,268
CURRENT LIABILITIES		2,000,296	4,468,886
Short-term provisions		3,930	2,397
Short-term debts	Note 13	1,477,649	3,968,991
Amounts owed to credit institutions		15,963	22,947
Debentures and other negotiable securities		1,461,245	3,907,378
Other financial liabilities		441	38,666
Trade and other accounts payable	Note 14	518,086	490,511
Suppliers		409,374	380,069
Staff		7,728	8,545
Current tax liabilities		-	-
Other payables to the Public Administrations	Note 15.1	72,095	50,586
Customer advances		28,889	51,311
Income collected in advance		631	6,987
TOTAL EQUITY AND LIABILITIES		35,323,846	40,144,864

Notes 1 to 19 described in the attached report form an integral part of the Balance Sheet at 31 December 2018.

SOCIEDAD DE GESTIÓN DE ACTIVOS PROCEDENTES DE LA REESTRUCTURACIÓN BANCARIA, S.A. (SAREB)

INCOME STATEMENT FOR THE YEARS 2018 AND 2017

(Thousands of Euros)

	Notes in Report	2018	2017
ONGOING OPERATIONS			
Turnover	Note 16.1	1,937,584	2,143,800
Sales of inventories		70,872	22,769
Income from sales of property investments		1,154,950	1,109,609
Income from leases		34,831	49,443
Income from sales of loans and credits		376,569	452,427
Financial income from loans and credits		532,685	723,818
Margin of recovery of loans and credits		(238,296)	(220,844)
Income from remuneration of FABs		3,506	1,778
Income from sale and liquidation of FABs and other group companies	Note 7.2.1	2,467	4,800
Changes in inventories of finished products and work in progress	Note 16.2	(4,571)	(15,841)
Sales costs	Note 16.2	(1,363,940)	(1,378,013)
Cost of property investments		(1,009,977)	(962,234)
Sales costs of financial assets		(351,164)	(413,165)
Sales costs of FABs and other group companies		(2,799)	(2,614)
Other operating income		23,164	17,058
Non-core and other current operating income		23,164	17,058
Staff expense	Note 16.3	(36,793)	(40,787)
Wages, salaries and similar		(30,504)	(34,890)
Social Security		(6,289)	(5,897)
Other operating expense		(669,657)	(659,617)
External services	Note 16.4	(435,582)	(460,564)
Taxes	Note 16.4	(217,511)	(177,766)
Losses, impairment and variation in provisions for trade transactions	Notes 9 and 12	(9,629)	(17,331)
Other current operating expense		(6,935)	(3,956)
Amortisation/Depreciation of fixed assets	Notes 4.1, 4.2 and 4.3	(59,846)	(61,444)
Overprovisions	Note 12	2,615	3,053
Impairment and profit/(loss) from sales of property, plant and equipment		-	(94)
- Profit/(Loss) from sales and others		-	(94)
Impairment and profit/(loss) from sales of financial instruments		(7,522)	(1,169)
Impairment and losses		(7,522)	(1,047)
Profit/(Loss) from sales and others		-	(122)
OPERATING INCOME/(LOSS)		(220,968)	6,946

Continue

Notes 1 to 19 described in the attached report form an integral part of the Income Statement for 2018.

Financial income	Note 16.6	3,751	7,640
From negotiable securities and other financial instruments			
- In third parties		3,751	7,640
Financial expense	Note 16.5	(661,775)	(548,494)
For debts with third parties		(644,926)	(530,894)
Other financial expense		(16,849)	(17,600)
Exchange rate differences	Note 4.12	(10)	3
FINANCIAL INCOME/(EXPENSE)		(658,034)	(540,851)
PROFIT/(LOSS) BEFORE TAXES		(879,002)	(533,905)
Income tax	Note 15	654	(30,671)
PROFIT/(LOSS) FOR THE YEAR FROM ONGOING OPERATIONS		(878,348)	(564,576)
PROFIT/(LOSS) FOR THE YEAR		(878,348)	(564,576)

SOCIEDAD DE GESTIÓN DE ACTIVOS PROCEDENTES DE LA REESTRUCTURACIÓN BANCARIA, S.A. (SAREB)

STATEMENT OF CHANGES IN EQUITY FOR THE YEARS 2018 AND 2017

TOTAL STATEMENT OF CHANGES IN EQUITY

(Thousands of Euros)

	Capital	Legal reserve	Restricted reserve
OPENING BALANCE 2017	303,862	19,174	629,428
Total recognised income and expense	-	-	-
Transactions with shareholders			
Other changes in equity (Note 2.5)	-	-	-
CLOSING BALANCE 2017 (Note 11)	303,862	19,174	629,428
Total recognised income and expense	-	-	-
Transactions with shareholders			
Other changes in equity - Distribution of profit/(loss)	-	-	-
CLOSING BALANCE 2018 (Note 11)	303,862	19,174	629,428

Voluntary reserves for application RD 4/2016	Accumulated loss from previous years	Profit/(Loss) for the year	Value change adjustments - Financial derivatives	Value change adjustments - Impairment financial assets	TOTAL
2,330,270	-	(662,791)	(1,987,672)	(3,289,542)	(2,657,272)
-	-	(564,576)	454,627	(940,010)	(1,049,958)
-	(662,791)	662,791	-	-	-
2,330,270	(662,791)	(564,576)	(1,533,045)	(4,229,552)	(3,707,230)
-	-	(878,348)	311,822	(862,134)	(1,428,661)
-	(564,576)	564,576	-	-	-
2,330,270	(1,227,367)	(878,348)	(1,221,223)	(5,091,686)	(5,135,891)

Notes 1 to 19 of the attached report form an integral part of the statement of total changes in equity for 2018.

SOCIEDAD DE GESTIÓN DE ACTIVOS PROCEDENTES DE LA REESTRUCTURACIÓN BANCARIA, S.A. (SAREB)
STATEMENT OF CHANGES IN EQUITY FOR THE YEARS 2018 AND 2017
STATEMENT OF RECOGNISED INCOME AND EXPENSE
 (Thousands of Euros)

	Notes in Report	2018	2017
BALANCE OF THE INCOME STATEMENT (I)	Note 3	(878,348)	(564,576)
Income and expense recognised directly in equity			
- For cash flow hedges	Note 15.2	(224,401)	80,746
- For impairment of financial assets	Note 7.1	(862,134)	(840,196)
- Tax effect	Note 15.2	56,100	(20,186)
TOTAL INCOME AND EXPENSE RECOGNISED DIRECTLY IN EQUITY (II)		(1,030,434)	(779,637)
Income and expense recognised in the income statement			
- For cash flow hedges	Note 13.3	640,162	525,424
- Tax effect		(160,041)	(231,170)
TOTAL TRANSFERS TO THE INCOME STATEMENT (III)		480,122	294,254
TOTAL RECOGNISED INCOME AND EXPENSE (I+II+III)		(1,428,661)	(1,049,959)

Notes 1 to 19 of the attached report form an integral part of the statement of total changes in equity for 2018.

SOCIEDAD DE GESTIÓN DE ACTIVOS PROCEDENTES DE LA REESTRUCTURACIÓN BANCARIA, S.A. (SAREB)**CASH FLOW STATEMENTS FOR THE YEARS 2018 AND 2017**

(Thousands of Euros)

	2018	2017
A) CASH FLOWS FROM/(USED IN) OPERATING ACTIVITIES (1 + 2 + 3 + 4)	1,922,071	2,327,498
1. Profit/(Loss) before tax	(879,002)	(533,905)
2. Adjustments to profit/(loss):	199,722	(106,195)
(+/-) Amortisation/Depreciation of fixed assets	59,846	61,444
(+/-) Financial expense	661,775	548,494
(+/-) Financial income	(3,751)	(7,640)
(+/-) Financial income from interest on loans and credits	(532,685)	(723,818)
(+/-) Other adjustments to profit/(loss)	(2,615)	(3,053)
(+/-) Loss, impairment and variation in provisions for trade operations	9,629	17,331
(+/-) Impairment of financial instruments	7,522	1,047
2.a Tax payments (-)	(2,832)	(1,949)
3. Increase / (Decrease) of assets and liabilities	2,845,247	3,095,218
Increase / (Decrease) of inventories (+/-)	9,350	(15,659)
Increase / (Decrease) of accounts receivable (+/-)	(32,813)	34,568
Increase / (Decrease) of other current financial assets (+/-)	3,340	17,402
Increase / (Decrease) of accounts payable (+/-)	27,790	32,954
Increase / (Decrease) of other current financial liabilities (+/-)	(461)	(461)
Increase / (Decrease) of loans and credits to third parties	1,875,816	2,076,708
Increase / (Decrease) of property investments	962,225	949,706
4. Other cash flows from/(used in) operating activities:	(241,065)	(125,671)
(-) Interest payable	(595,961)	(574,803)
(+) Dividends receivable	-	-
(+) Interest receivable	3,51	3,751
(+/-) Interest receivable from loans and credits	350,401	445,381
(+/-) Other receivables/(payables) from operating activities	744	-

Continue

Notes 1 to 19 described in the attached report form an integral part of the cash flow statement for 2018.

	2018	2017
B) CASH FLOWS FROM/(USED IN) INVESTMENT ACTIVITIES (1 + 2)	(166,047)	577,693
1. Payments on investments:	(532,411)	(8,898)
(-) Intangible assets	(4,837)	(8,074)
(-) Credit and holdings in associates	(325)	(824)
(-) Other financial assets	(527,249)	-
2. Receivables from divestments:	366,364	586,591
(+) Credit and holdings in associates	2,467	17,532
(+) Other financial assets	363,897	569,059
C) CASH FLOWS FROM/(USED IN) FINANCING ACTIVITIES (1 + 2 + 3)	(3,066,256)	(2,260,651)
1. Receivables from/(Payables for) equity instruments:	-	-
(+) Issue	-	-
(-) Amortisation/Depreciation	-	-
(-) Acquisition	-	-
(+) Sale of own shares	-	-
2. Net obtained from new financing with third parties	(3,066,256)	(2,260,651)
(+) Other current and non-current financial liabilities	(125,372)	(71,288)
(-) Drawdowns / (Amortisations) credit accounts	(6,984)	8,737
(-) Repayment and amortisation	(2,933,900)	(2,198,100)
3. Net receivables for issue own securities	-	-
D) EFFECT OF FLUCTUATIONS IN EXCHANGE RATES	-	-
E) INCREASE/(DECREASE) NET OF CASH AND CASH EQUIVALENTS (A + B + C + D)	(1,310,233)	644,540
F) CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR	4,137,625	3,493,085
G) CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR (E + F)	2,827,392	4,137,625
COMPONENTS OF CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR		
(+) Cash and banks	2,692,538	2,751,862
(+) Other financial assets	134,854	1,385,763
(-) Less: Bank overdrafts repayable on demand		
TOTAL CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	2,827,392	4,137,625

Notes 1 to 19 described in the attached report form an integral part of the cash flow statement for 2018.

Notes to the annual accounts for the year ended 31 December 2018

31 December 2018

1. Company Activity

The company Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A. (hereinafter, the "Company" or "Sareb") was incorporated for an indefinite term in Madrid, on 28 November 2012, in accordance with the provisions of Act 9/2012, of 14 November, on the restructuring and winding-up of credit institutions, with the name Sociedad Promotora de la Sociedad de Gestión de Activos Procedentes de la Reestructuración Bancaria, S.A., as a single-member public limited company; its purpose is to carry out all the preparatory measures necessary for putting Sareb into operation. It is registered in the Companies Registry of Madrid in volume 30,521, Sheet 1, Section 8, Page M-549,293, 1st entry.

On 12 December 2012 it changed its term and name under the deed which places on public record the company resolutions adopted on that date in the presence of the Madrid Notary Mr José María García Collantes under number 1624 of his official record, limiting its duration until 28 November 2027 and assuming its current name.

At 31 December 2018 the Company has its registered and tax address in Paseo de la Castellana number 89, in Madrid.

The Company is governed by its Articles of Association and by legislation in force that is applicable to it, i.e. the current Capital Companies Act, except for the provisions of articles 537 and 348 bis thereof,

in accordance with the terms of Act 9/2012, of 14 November, on the restructuring and winding-up of credit institutions, with the specific terms necessary for ensuring that the accounting principles applicable to it are consistent with the mandate and general objectives of the company as established in the Act of reference and which are set out by law (see Note 2.1).

Its corporate purpose consists of holding, managing and directly or indirectly administering, buying and selling the assets and, where appropriate, liabilities, transferred to it by the credit institutions referred to in the Ninth Additional Provision of the Act 9/2012, (or any legislation that replaces, implements or supplements it) which appear in their balance sheets or in those of any company over which it exercises control in the sense of article 42 of the Code of Commerce (and also any others that it might acquire in the future as a result of the mentioned activity involving the management and administration of such assets).

Notwithstanding the above-described corporate purpose, in accordance with the legislation regulating it, the Company has to contribute to the correct implementation of the processes for the restructuring or winding-up of credit institutions, making it possible to meet the objectives set out in article 3 of Royal Decree 1559/2012 in accordance with the general principles of transparency and professional management, namely:

- a) Contribute to the clean-up of the financial sector by acquiring the related assets in such a manner that the risk associated with these assets are effectively transferred from the time of their transfer.
- b) Minimise public funding.
- c) Settle debts and meet obligations it assumes in the course of its operations.
- d) Minimise any possible distortions in the markets that might arise from its actions.
- e) Sell the assets received, enhancing their value within the time period established and for which the company was incorporated.

Background to the incorporation of the Company and transfer of assets

In 2012: Acquisition of assets from banks in Group 1

On 21 December 2012, Sareb and the banks making up the mentioned Group 1 concluded the corresponding asset transfer contracts which, in accordance with the terms thereof, did not come into full effect until 31 December 2012. Those assets were transferred free of any charges by the assigning banks as a whole and at a fixed price which was for the amount of 36,695,308 thousand euros, and were acquired by Sareb through the issue of senior bonds for a total of 36,694,100 thousand euros, which were subscribed by the assigning banks, deferring the payment of the difference between the transfer price and the value of the bonds issued for a period of 36 months, which may be offset by the Company with any amount owed to it by the assigning banks under the terms set out in the asset transfer contracts. Those amounts were paid in full in 2013.

Below is the breakdown of the assets that were transferred by the banks in Group 1 according to their nature on that date:

Thousands of euros	
Financial assets	28,298,902
Real estate assets	8,396,406
Total	36,695,308

The breakdown of the financial assets that were transferred by the Group 1 banks, according to the type of guarantee on each, was as follows:

Amounts in Thousands of euros	Nº of assets	Total transfer price
Loans	62,435	26,493,181
Normal	28,047	8,368,902
Sub-standard	11,877	6,646,904
Doubtful	22,511	11,477,375
Créditos	5,714	1,805,721
Normal	1,810	537,427
Sub-standard	870	495,392
Doubtful	3,029	557,025
Others	5	215,877
Total	68,149	28,298,902

For its part, the breakdown of the real estate assets that were transferred by the banks in Group 1 was as follows:

Amounts in Thousands of euros	Nº of assets	Total transfer price
Land	10,322	2,812,430
Completed properties for sale	30,158	2,426,138
Properties for rental	5,822	927,620
Total property investments	46,302	6,166,188
Works in progress	3,050	470,124
Completed properties	27,682	1,760,094
Total inventories	30,732	2,230,218
Total	77,034	8,396,406

Below is a summary of the main features of the senior bonds issued by the Company and subscribed by the Group 1 banks on 21 December 2012 in payment of the mentioned assets:

ISIN Code	Description	Issue date	Maturity date (**)	Applicable rate in force	Nominal (Thousands of euros) (*)
ES0352506002	SAREB/VAR BO 20131231 2012-1	31/12/2012	31/12/2013	2.374%	11,008,100
ES0352506010	SAREB/VAR BO 20141231 2012-2	31/12/2012	31/12/2014	2.747%	16,512,500
ES0352506028	SAREB/VAR BO 20151231 2012-3	31/12/2012	31/12/2015	3.149%	9,173,500
					36,694,100

(*) Those bonds carry an irrevocable guarantee from the Kingdom of Spain (see Note 13.2).

(**) There is an option to renew at the Company's discretion, as described in Note 13.

Those bonds were subscribed by the assigning banks in accordance with the following distribution:

	Thousands of euros
Bankia, S.A./Banco Financiero y de Ahorros, S.A.	22,317,600
Catalunya Banc, S.A.	6,708,300
Banco Gallego, S.A.	609,700
NovaGalicia Banco, S.A.	5,096,800
Banco de Valencia, S.A.	1,961,700
Total	36,694,100

In 2013: Acquisition of assets from banks in Group 2

On 20 December 2012, the European Commission approved the plans for the restructuring of the financial institutions falling under Group 2 (Banco Grupo Cajates, S.A., Banco Mare Nostrum, S.A., Banco Caja España de Inversiones, Salamanca y Soria, S.A. -CEISS- and Liberbank, S.A.) after they had been approved by the Bank of Spain.

On 28 February 2013 Sareb and the banks making up Group 2 concluded the corresponding asset transfer contracts; the assets were transferred free of charges by the assigning banks of Group 2 to Sareb as a whole and at a fixed price for the amount of 14,087,157 thousand euros, and were acquired by Sareb through the issue of senior bonds at a nominal value of 100 thousand euros, for a total of 14,086,700 thousand euros, that were subscribed by the assigning banks, deferring the payment of the difference between the transfer price and the value of the bonds issued for a period of 36 months, which may be offset by the Company for any amount owed to it by the assigning banks under the terms set out in the asset transfer contracts. At 31 December 2013 that amount had been settled, with no amounts appearing for that item on the accompanying balance sheet at that date.

The breakdown of those assets that were transferred by the Group 2 banks, according to their nature, was as follows on that date:

	Thousands of euros
Financial assets	11,139,891
Real estate assets	2,947,266
Total	14,087,157

The breakdown of the financial assets that were transferred by the Group 2 banks, according to the type of guarantee on each, was as follows:

Amounts in Thousands of euros	Nº of assets	Total transfer price
Loans	21,889	10,855,331
Normal	9,337	4,642,163
Sub-standard	1,800	1,872,775
Doubtful	10,752	4,340,393
Credits	727	284.560
Normal	270	125.758
Sub-standard	137	44.161
Doubtful	230	110.643
Others	90	3.998
Total	22,616	11,139,891

For its part, the breakdown of the real estate assets that were transferred by the Group 2 banks was as follows on that date:

Amounts in Thousands of euros	Nº of assets	Total transfer price
Land	4,630	1,062,531
Halted building sites	1,445	163,505
Completed properties for sale	23,404	1,619,800
Properties for rental	906	98,140
Total property investments	30,385	2,943,976
Works in progress	27	3,290
Total inventories	27	3,290
Total	30,412	2,947,266

Below is a summary of the main features of the senior bonds subscribed on 28 February 2013 in payment of the mentioned assets:

ISIN Code	Description	Issue date	Maturity date (**)	Applicable rate in force	Nominal (Thousands of euros) (*)
ES0352506036	SAREB/VAR BO 20140228 2013-1	28/02/2013	28/02/2014	1.451%	4,225,900
ES0352506044	SAREB/VAR BO 20150228 2013-2	28/02/2013	28/02/2015	2.233%	6,339,200
ES0352506051	SAREB/VAR BO 20160228 2013-3	28/02/2013	28/02/2016	2.674%	3,521,600
					14,086,700

(*) Those bonds carry an irrevocable guarantee from the Kingdom of Spain (see Note 13.2).

(**) There is an option to renew at the Company's discretion, as described in Note 13.

Those bonds were subscribed by the assigning banks in accordance with the following distribution:

	Thousands of euros
Banco Mare Nostrum, S.A.	5,819,600
Banco Caja España de Inversiones, Salamanca y Soria, S.A.	3,137,300
Liberbank, S.A.	2,917,800
Banco Grupo Cajates, S.A.	2,212,000
Total	14,086,700

Rectification of the deeds for asset purchases concluded in 2018 and 2017

Subsequent to the transfer, and in application of the provisions of the mentioned Royal Decree 1559/2012 and in the asset transfer contracts themselves, the loan and credit portfolios and the portfolios of real estate assets acquired from the banks in Groups 1 and 2 were reviewed in order to identify any inappropriate classification of assets, changes in perimeter and errors or variations in the valuation estimated on the date of transfer.

In 2018 no rectifications were made to the original deeds for transferring assets, and the deeds were concluded during the year. The overall amount for rectifications in 2017 was 44 million euros, through the return of assets to the assigning banks of Group 1 and 2 for the amount of 5 million euros and by making price adjustments of 17 million euros, respectively, reducing the amount of the real estate assets initially transferred by 10 million euros and the amount of loans and credits by 12 million euros, respectively. Furthermore, in 2017 a rectification of 22 million euros was made corresponding to amounts pending offsetting arising from changes in the portfolio transferred, between the signing and the transfer.

In return, the assigning banks handed Sareb part of the above-mentioned bonds issued in payment of the portfolios for an amount equivalent to the assets returned, and also the cash equivalent of the coupons received by the banks corresponding to the bonds handed over. Furthermore, according to the transfer contract, the banks applied a compensatory interest rate of 1% per year on the total amount of coupons paid by the Company, which were for 44 thousand euros in 2017, in relation to the bonds returned.

The summary of the rectifications made in 2017 was as follows:

Amounts in Thousands of euros	Real estate assets rectified (Note 5) **	Financial assets rectified (Note 7) **	Differences between signing and transfer (***)	Total rectifications	Amounts pending offsetting (****)	Amounts after offsetting	Bonds returned (Note 13.2) (*****)	Cash adjustment (*)
Banco Mare Nostrum, S.A. (****)	9,558	12,101	22,270	43,929	(36,290)	7,639	(30,500)	315
Total	9,558	12,101	22,270	43,929	(36,290)	7,639	(30,500)	315

(*) Corresponds to the difference, paid in cash, between the total amount of the rectification and the amount of the bonds returned.

(**) Out of the amount of real estate assets rectified, 865 thousand euros corresponded to properties sold by the Company prior to rectification and 2,906 thousand euros to loans sold prior to rectification.

(***) Referring to changes produced in the assets transferred since the close of the perimeter until the transfer deeds from Banco Mare Nostrum, S.A. were placed on public record.

(****) That amount includes the price of a number of assets which, by error, were included in the perimeter but not in the calculation of the transfer price.

(***** This figure includes the return of 23,177 thousand euros in bonds corresponding to rectifications concluded in 2016 which were pending return.

Furthermore, during the years 2017 to 2014 the Company concluded different settlement agreements with all of the assigning banks under which the parties have agreed to waive demanding further price adjustments and also the 36-month period granted in the asset transfer contract for making claims. The Company may exercise any rights and take any actions to which it is entitled by law or under contract, whether for latent defects, damages or losses. That agreement does not prevent making future perimeter adjustments with those banks for assets incorrectly transferred due to not meeting the specifications of art. 48 of RD 1559/2012 or of the Fund for Orderly Bank Restructuring (FROB) Resolution on transfer conditions dated 14 December 2012 as it has done during the past years.

Íbero Project

In 2014 the Company launched what was known as the “Íbero” project. That project consisted of substituting the management and administration contracts concluded on the date of transferring the assets, by way of a bidding process in which it sought:

- To group together the management of the nine portfolios initially provided by the banks in Group 1 and 2 into new managers, in order to simplify and facilitate the management of the assets transferred.
- To achieve professionalisation and improvement in the quality of the service at market prices which would enable the Company to fulfil its commitments and the tasks with which it is entrusted, that is, to be able to achieve the divestment of the assets acquired within the period established and maximise their value.

During the months of November and December of 2014 the new administration and management contracts were formally awarded and signed, with the following new managers being appointed:

- Solvia Servicios Inmobiliarios, S.L. was awarded the real-estate portfolio of Bankia, S.A. and the entire portfolios of Banco Gallego, S.A. and Banco Caja España de Inversiones Salamanca y Soria, S.A.
- Altamira Asset Management, S.L. was awarded all of the portfolios up until then managed by

Catalunya Caixa, S.A., Banco Mare Nostrum, S.A. and Banco Caja 3, S.A.

- Haya Real Estate, S.L.U. was awarded the loan portfolio originally transferred by Bankia, S.A. and Banco Financiero de Ahorros, S.A.
- Lastly, Servihabitat Servicios Inmobiliarios, S.L. was awarded the portfolios initially transferred by NovaGalicia Banco, S.A. (Abanca, S.A.), Liberbank, S.A. and Banco de Valencia, S.A.

The term established under the contracts ranges from 5 to 7 years from when each one comes into force, and can be automatically renewed for a further year unless any of the parties informs the other giving 6 months advance notice that it does not wish to renew. Furthermore, the contract provides for the possibility of early cancellation by SAREB at any time by giving a minimum of 3 months advance notice and paying compensation to the managers calculated in accordance with the terms of the contract. At 31 December 2019 one of the above-mentioned contracts will expire. The Company is studying possible options, amongst which either to renew the contract (completely or partially) or to offer the management of that portfolio again for tender, if with this it would be possible to streamline the costs or improve the quality of the service.

In any case, the contracts for the services to be provided by the managers include:

- Migration: services necessary for developing, implementing and concluding the migration of the asset management and administration. The last portfolio to migrate was the portfolio of financial assets originally transferred by Bankia, S.A. which migrated in 2017.
- Administration and management of the portfolios awarded. Management is performed by the four managers listed above, who handle and manage the portfolios of financial assets and real estate assets assigned to them. As part of their functions, each Servicer records and prepares the financial and accounting information for their portfolios, reporting to the Company.
- Legal advice in relation to the administration and management of the assets migrated.

In consideration for the above services the contract establishes fees for management and administration and sale, which are calculated on the basis of the volume of assets held for management by each of the managers, and for sales, which are calculated on the basis of the revenue and cash generated in the divestment of the assets managed. In 2018 and 2017 management fees were accrued for the amount of 84,810 and 96,171 thousand euros, and sales fees for the amount of 119,015 and 146,755 thousand euros, respectively (see Note 16.4).

Furthermore, and with the aim of guaranteeing a certain level of service and performance in the tasks entrusted, and also to bring their objectives in line with those of the Company, in 2014 the awardees set up performance guarantees for an initial amount of 588,600 thousand euros, of which 331,108 thousand euros of nominal value are currently pending return, this being recorded under the heading "Other financial liabilities" in non-current liabilities on the accompanying balance sheet (see Note 13.4).

Regarding the above guarantees, it is worth pointing out that they were calculated based on an estimation of the assets that will be managed, adjusted to the final figure once the various migrations of the portfolios have been completed.

The return of those guarantees is considered a contingent item and is associated to the adequate trading performance of the new managers. The Company considers it likely that, according to current estimations, those guarantees will be returned and that the return will take place as the fees arranged between the Company and its new managers become due and are paid. This contract provides for measuring the degree of the managers' fulfilment of the various performance indicators applicable to the services agreed upon, establishing a scale of penalties to be applied on the invoiced amounts and also the circumstances for early termination (for example if the managers' failure to fulfil extends over a period of 12 months with the highest level of materiality and degree of divergence from the target value established in the contract). On the basis of the fees accrued in 2018 and 2017, the Company has returned 83,241 and 71,178 thousand euros of guarantees provided by the new managers, respectively (see Note 13.4).

Other information

At 31 December 2018, the Company's annual accounts were not included in the consolidated financial statements of any Shareholder using the full consolidation method as none held more than 50% of the Company's share capital and none were considered to control the Company or to have the power to govern its financial and operating policies so as to obtain benefits from its activities, or to hold a majority of voting rights or to have the power to appoint or remove the majority of members of its Board of Directors (see Note 11).

In turn, at 31 December 2018 the Company had no majority holdings in the capital of any subsidiaries with the exception of the interest in T  mpore Properties Socimi, S.A. However, the Directors consider that, given the figures for assets, equity and turnover of that subsidiary, it is not of any relevant size in terms of the Group and therefore it is released from filing consolidated accounts under the terms of article 43 of the Code of Commerce (see Note 7.2.1).

Furthermore, the participation in Bank Assets Funds ("FABs") (Note 4.6.1) which does not require the deconsolidation of the assets and liabilities involved, does not have any significant effect on the true and fair view of the equity, the financial position and the profit/(loss) of the Company. Consequently, in accordance with article 43 of the Code of Commerce, the Company is not required to draw up consolidated financial statements.

2. Bases for the presentation of the Annual accounts

2.1 Regulatory framework for financial information applicable to the Company

These Annual accounts have been drawn up by the Directors in accordance with regulatory framework for financial information applicable to the Company which is that set out in:

- a) Code of Commerce and other commercial legislation, with the specific aspects set out in sub-section 10 of the Seventh Additional Provision of Act 9/2012 which, where appropriate, were implemented in 2015 through a Bank of Spain Circular and amended under article 2 of RD 4/2016 (see point c).
- b) The Spanish General Chart of Accounts approved by Royal Decree 1514/2007 and its subsequent amendments, except for the specific aspects included under Act 9/2012 and amendments thereto included in article 2 of RD 4/2016.

Similarly, due to the nature of its business, in the preparation of these annual accounts, the Ministry of Economy and Finance Order of 28 December 1994 which approved the adaptation of the 1990 General Chart of Accounts to Real Estate Companies was taken into consideration, and applicable in all issues not contrary to the provisions of the Code of Commerce, the Capital Companies Act, Act 9/2012 and the General Chart of Accounts approved under Royal Decree 1514/2007.

In addition, the Company has to comply with the general requirements for transparency, and for the preparation of annual accounts as established in RD 1559/2012.

- c) In accordance with the provisions of sub-section 10 of the Seventh Additional Provision

of the mentioned Act 9/2012, in 2015 the Bank of Spain issued Circular 5/2015, of 30 September, under which it implemented the specific accounting aspects for Sareb (hereinafter, "Circular 5/2015"). Subsequently, on 3 December 2016 an amendment was made to letter c) of sub-section 10 of that Seventh Additional Provision by way of article 2 of RD 4/2016 of 2 December, on urgent financial measures, later included in the Circular 5/2015 by publication of Circular 2/2017.

- d) The mandatory rules approved by the Institute of Accounting and Account Audits in order to implement the General Chart of Accounts and relevant secondary legislation.
- e) All other Spanish accounting legislation that is applicable.

2.2 True and fair view

The accompanying annual accounts have been obtained from the Company's accounting records and are presented in accordance with the regulatory framework for financial information applicable to the Company and in particular with the principles and criteria contained therein, in such a way as to show the true and fair view of the equity, the financial position of the Company at 31 December 2018, the profit/(loss) of the Company and the cash flows during the year ended on that date.

The annual accounts of Sareb for 2017 were approved by its Shareholders General Meeting on 17 May 2018 and those for 2018, which were drawn up by the Board of Directors of Sareb in its meeting on 27 March 2019, will be submitted for the approval of the Shareholders General Meeting, and are expected to be approved without amendments.

2.3 Non-mandatory accounting principles applied

No non-mandatory accounting principles were applied in the preparation of these annual accounts. In addition, the Directors have drawn up these annual accounts taking into consideration the whole set of accounting principles and standards of mandatory application that have any significant effect on said annual accounts (see Note 4). There is no accounting principle that is mandatory and has a significant effect on these annual accounts which has not been applied.

2.4 Critical aspects of the assessment and estimation of uncertainty

In the preparation of the accompanying annual accounts, estimates were made by the Directors of the Company in order to measure certain of the assets, liabilities, income, expense and obligations reported therein. Basically these estimates refer to:

- The assessment of impairment of certain assets (see Notes 4.7, 5, 7, 8).
- The useful life of intangible assets, property, plant and equipment and property investments (see Notes 4.1, 4.2, 4.3 and 5).
- The market value of certain financial instruments (see Note 7).
- The recoverability of prepaid tax and tax credits and the deductibility of impairment losses on the Financial assets unit (see Note 15).
- The calculation of provisions (see Note 12).
- The estimation of the bonds and other short-term negotiable securities (see Note 13.2).
- The classification of the balance sheet amounts between the long term and the short term based on the estimated future cash flows (see Note 7 and 13).

In 2014 the Company ended reviewing the assets transferred (*Due Diligence*). That analysis was intended to establish that the estimations and the mechanism

for calculating prices (correct application of the transfer pricing, confirmation of the features of the assets acquired and the accuracy of the information provided by the assigning banks) are reasonable.

Based on the outcome obtained from that analysis, in 2017 the Company formalised the rectifications specified in Note 1. Except for those rectifications, with the current information, the estimation of any possible differences that might come to light regarding the transfer pricing are not relevant for the purposes of these annual accounts.

Although, in accordance with applicable legislation, these estimations have been made on the basis of the best information available at the end of the year 2018 and at the date of preparing these annual accounts, it is possible that events that might take place in the future could mean modifying them (increasing or decreasing) in the coming years, which would, if the case arises, be carried out prospectively, with a balancing entry in the income statement of the year affected in the future.

Going concern principle

At 31 December 2018 the situation of the equity of the Company is as follows:

Thousands of euros	
Equity in the annual accounts of Sareb, S.A. at 31/12/2018	(5,135,891)
Less:	
Value change adjustments for cash flow hedges	1,221,223
Value change adjustments for impairment of financial assets	5,091,686
Equity for the purposes of reduction and dissolution 31/12/2018	1,177,018

It should be mentioned that under prevailing accounting legislation, any changes in the value of derivative hedging instruments are recognised in equity until they are allocated to profit or loss in the corresponding year. The total fair value of this interest

rate risk derivative, net of its tax effect, is recognised under the heading “Value change adjustments – Hedging operations”. However, from a business perspective and according to the provisions of article 36 of the Code of Commerce, these value changes in the hedging derivative yet to be allocated to the income statement are not considered as equity for the purposes of profit distribution, mandatory reduction of share capital and mandatory dissolution for losses.

In turn, as established by article 2 of RD 4/2016, the Company has recorded the value adjustments of the units of assets established in Circular 5/2015 allocating them to the heading “Value change adjustments – Impairment of financial assets” net of taxes. As established in that RD the adjustments referred to above will not be considered as equity for the purposes of profit distribution, mandatory reduction of share capital and mandatory dissolution for losses (see Note 11.5).

The Company has sustained significant losses during this year, and also in preceding years, which has resulted in a reduction of its equity. Nonetheless, as mentioned before, at 31 December 2018 the Company is not in the process of dissolution established in article 363 of the Capital Companies Act. It should also be pointed out that the Company has various measures available to it to mitigate any concerns as to its ability to continue as a going concern, namely:

1. At 31 December 2018, the Company shows positive working capital for the amount of 2,938,348 thousand euros as a result of classifying the senior debt as long term, because although 21,010,100 thousand euros of senior debt contractually matures in 2019, the Company has the option of unilaterally novating the maturity term of those bonds, meaning that a good part of the debt has been classified as long term taking the current estimates of the Company into consideration.
2. At 31 December 2018 the amount of cash and other cash equivalents was 2,827,392 thousand euros.

It is worth pointing out that, apart from having

considerable working capital permanently available until the end of its mandate, which would enable it to cover its financial commitments, the company could in the future be affected by the legal effects arising from its equity figure each year, considered for the purposes of art. 363 of the Capital Companies Act.

In this respect, Sareb is required to update its Business Plan every year for all of its remaining life and to apply the accounting principles and standards in force in its financial reporting. The most recent updating of the Business Plan reflects a change that emphasises the company’s strategy regarding the preservation of the financial value of its assets, in accordance with its mandate. Even though the Company’s goal is the total divestment of the assets, it has to adapt to the circumstances of the market and to those of the assets themselves in order to protect that value, which, according to the current Business Plan, involves accumulating the stock of assets on the Company’s balance sheet toward the end of the period considered in that Plan. It must be considered that the assumptions used and the long-term nature of the projections involve a high degree of uncertainty in the scenario of the Business Plan approved. Based on the actual evolution of the market and of the Company’s own ability to divest in accordance with that forecasting, the Company could see its shareholders’ equity used up in the medium term, although in any case this would not occur during the coming twelve months. In any event, this possible situation would not imply the Company’s inability to fulfil its financial and payment commitments.

If that situation arises, within the deadlines established in the Capital Companies Act, the Company and its shareholders should adopt the measures necessary for restoring the balance of equity, one of which, and at an early stage, being converting the Company’s subordinated debt (see Note 13). In addition, and on the basis of the necessities that might become evident, the directors will evaluate additional or alternative measures that will enable it to restore that balance, as well as any others available under commercial legislation.

In consequence, based on the above, the Directors of the Company have drawn up these annual accounts based on the going concern principle.

2.5 Changes in accounting policies

In 2018 there have been no significant additional changes in accounting policies with regard to the policies applied in 2017.

2.6 Comparison of the information

The information contained in this report referring to 2017 is presented solely for comparison with the information for 2018, in accordance with the provisions of current legislation.

2.7 Grouping of items

To enhance comprehension of the balance sheet, income statement, statement of changes in equity and cash flow statement, certain items are presented in grouped form, and the necessary breakdown is given in the corresponding notes, wherever it is relevant.

2.8 Correction of errors and changes in estimations

No significant errors have been detected in the preparation of the accompanying annual accounts that would involve the restatement of the amounts included in the 2017 annual accounts.

2.9 Environmental Impact

Given the business in which the Sareb is engaged, it has no responsibilities, expenses, assets, provisions or contingencies of an environmental nature which could be significant in respect of its equity, financial position and profit or loss.

For this reason, in the Company's annual accounts for 2018 no information is given relating to this issue.

2.10 Presentation of the annual accounts

Unless indicated otherwise, the figures reflected in these annual accounts are stated in thousands of euros.

3. Distribution of profit or loss

The proposals put forward by the Board of Directors for the distribution of the profit/(loss) obtained in 2018, to be submitted for the approval of the Shareholders General Meeting and the proposal for 2017 which was approved by the Shareholders General Meeting held on 9 May 2017 are as shown below:

Amounts in Thousands of euros	2018	2017
Balance of the Income Statement:	(878,348)	(564,576)
Distribution:		
To legal reserves	-	-
To voluntary reserves	-	-
To accumulated loss from previous years	(878,348)	(564,576)

4. Principles for accounting and measurement

The main principles for accounting and measurement used by the Company in the preparation of the annual accounts for 2018, in accordance with the regulatory framework applicable were as follows:

4.1 Intangible assets

Intangible assets are initially valued for their acquisition price or production cost. Subsequently, they are valued at cost decreased by the relevant accumulated amortisation and, where appropriate, by any impairment losses they may have undergone. These assets are amortised over their useful life.

Industrial property

The amounts recognised by the Company under the heading Industrial property correspond to the expenses capitalised by obtaining the corresponding patents, or similar, including costs for registering and formalising the industrial property, notwithstanding any amounts that can also be included in the accounts for purchasing the corresponding rights from third parties. The Company amortises the amounts capitalised under the heading of "Industrial property" on a straight line basis over 10 years.

Administrative concession

Under the heading of Administrative concessions, the Company records the rights of use it has on several berths in the port of Santa Pola (Alicante). The useful life of those berths is 17 years from when they were acquired by the Company, and they are depreciated on a straight-line basis over that useful life.

Computer software

Computer software acquired or designed by the Company is recognised at acquisition or production cost, as the case may be, amortised on a straight line basis over 5 years. The costs for maintaining computer software are recognised in the income statement in the income incurred. At 31 December 2018 and 2017 that heading mainly includes the gross cost of the computer software acquired by the Company, for the amount of 35,734 and 29,137 thousand euros, respectively.

The provision for the amortisation of the intangible assets in 2018 and 2017 was 6,447 and 5,100 thousand euros, respectively, having been recognised with a charge to the heading "Amortisation/ Depreciation" on the accompanying income statement. The balance of the cumulative amortisation at 31 December 2018 and 2017 was 17,648 and 11,201 thousand euros, respectively.

The work the Company performs on its own fixed assets is reflected at the accumulated cost resulting from adding the internal costs determined according to the actual consumption of materials and manufacturing expenses to the external costs, applied using the same principles as those used for measuring inventories. In 2018 and 2017 the Company has not capitalised any cost for these items in its intangible assets.

Impairment of intangible assets

Whenever there are indications of impairment of intangible assets with a finite useful life, that classification being applicable to all of the Company's intangible assets, it performs "impairment testing" to assess whether there is any indication of impairment that reduces the recoverable amount of such assets to below their carrying amount.

When an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised in prior years. That reversal of an impairment loss is recognised as income.

In 2018 and 2017 the Company has not recognised impairment for its intangible assets.

Furthermore, at the close of 2018 and 2017 the Company has no firm commitments for the purchase and/or sale of any items of intangible assets for any significant amount.

4.2 Property, plant and equipment

Initial measurement

Property, plant and equipment is initially measured at acquisition or production cost, to which are added the amounts of additional or complementary investments made, and subsequently reduced by the relevant accumulated depreciation and the impairment losses if any, pursuant to the criteria mentioned in this Note.

Costs of expanding, upgrading or improving property, plant and equipment that increase its productivity, capacity or efficiency, or prolong its useful life are capitalised as an increase in the cost of the asset.

Repair and maintenance costs for the year are recognised as "External services" in the accompanying Income Statements.

In 2018 and 2017 the Company has not capitalised any financial interest as an increase in the value of its property, plant and equipment.

The work the Company performs on its own fixed assets is reflected at the accumulated cost resulting from adding the internal costs determined according to the actual consumption of materials and manufacturing expenses to the external costs, applied using the same principles as those used for measuring inventories. In 2018 and 2017 the Company has not capitalised any cost for these items in its property, plant and equipment.

Depreciation

The depreciation of property, plant and equipment is calculated on a straight-line basis over the estimated useful life of the assets. The annual depreciation percentages for the respective current cost value, where relevant, and the estimated years of useful life are the following:

Heading	Annual percentage	Years of estimated useful life
Straight-line depreciation method:		
Other facilities	10	10
Fixtures	10	10
Data processing equipment	20	5
Other property, plant and equipment	12.5	8

The provision for the depreciation of property, plant and equipment at 31 December 2018 and 2017 was 296 and 328 thousand euros, respectively, having been recognised with a charge to the heading "Amortisation/Depreciation" on the accompanying income statement. The balance of the cumulative depreciation at 31 December 2018 and 2017 was 1,291 and 995 thousand euros, respectively.

The assets in progress do not begin to depreciate until they are fully operational, which is when they are transferred to their corresponding account in property, plant and equipment, depending on their nature.

Impairment of property, plant and equipment

Whenever there are indications of impairment of property, plant and equipment, that classification being applicable to all of the Company's property, plant and equipment, it performs "impairment testing" to assess whether there is any indication of impairment that reduces the recoverable amount of such assets to below their carrying amount.

When an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined

had no impairment loss been recognised in prior years. That reversal of an impairment loss is recognised as income.

In 2018 and 2017 the Company has not recognised impairment for its property, plant and equipment.

Furthermore, at the close of 2018 and 2017 the Company has no firm commitments for the purchase and/or sale of any items of property, plant and equipment for any significant amount.

4.3 Property investments

The heading property investments on the balance sheet includes the values for land, buildings and other constructions that are held, either to earn rentals or for capital gains when sold as a result of future increases on the respective market prices.

Initial measurement

Property investments are initially measured at acquisition or production cost, to which are added the amounts of additional or complementary investments made, and subsequently reduced by the relevant accumulated depreciation and the impairment losses if any, pursuant to the criteria mentioned in this Note.

According to the provisions of letter a) of sub-section 10 of the Seventh Additional Provision of Act 9/2012, the acquisition cost of the assets received from the assigning banks in Group 1 and Group 2 was established applying the transfer prices for each type of assets that were fixed by resolution of the Bank of Spain according to the principles established in RD 1559/2012.

Under the provisions of Rule 3 of Circular 5/2015, in the case of real estate assets allocated or acquired in payment of debts, the amount for which they are initially recognised is the carrying amount of the financial assets cancelled on the date of foreclosure or dation in payment. The legal and registry expenses, and taxes paid are added to the initial value provided that by doing

so the estimated fair value of that initial value is not exceeded.

Costs of expanding, upgrading or improving these assets that increase their productivity, capacity or efficiency, or prolong their useful life are capitalised as an increase in the cost of the assets.

The Company recognises any properties acquired under mortgage foreclosure procedures having a court ruling under the heading "Advances on property investments". Those properties are transferred to the heading of "Land" or "Completed properties" once that ruling becomes final.

Repair and maintenance costs for the year are recognised as "External services" in the accompanying Income Statement.

The work the Company performs on its own fixed assets is reflected at the accumulated cost resulting from adding the internal costs determined according to the actual consumption of materials and manufacturing expenses to the external costs, applied using the same principles as those used for measuring inventories. In 2018 and 2017 the Company has not capitalised any cost for these items in its property investments.

In 2018 and 2017 the Company has not capitalised any financial interest or charges as an increase in the cost of property investments.

Subsequent measurement and evaluation of impairment

The impairment of those assets is assessed as described in Note 4.7.

Depreciation

The depreciation of property investments is calculated on a straight-line basis over the estimated useful life of the assets. The annual depreciation percentages for the respective cost values, where relevant, and the estimated years of useful life are the following:

	Annual percentage	Years of estimated useful life
Straight-line depreciation method:		
Constructions	2	50
Other facilities	10	10
Fixtures	10	10
Data processing equipment	20	5
Other property, plant and equipment	12.5	8

The provision for the depreciation of property investments in 2018 and 2017 was 53,103 and 56,016 thousand euros (see Note 5) having been recognised with a charge to the heading "Amortisation/Depreciation" on the accompanying income statement.

4.4 Asset exchanges and awards

"Asset exchanges" are taken to be the acquisition of property, plant and equipment or intangible assets in exchange for other non-monetary assets or for a combination of these and monetary assets.

As a general rule, the asset received in an asset exchange transaction with commercial substance is recognised at the fair value of the asset given up, plus, where appropriate, any monetary consideration paid. The valuation differences that arise on derecognition of the asset given up in the exchange are recognised in the income statement

Assets received in an exchange that lacks commercial substance are measured at the carrying amount of the asset given up plus, where appropriate, any monetary consideration paid, up to the limit of the fair value of the asset received if this is lower.

In the specific case of assets allocated as payment of debt, depending on their nature and the purpose for which they are to be used, they are classified as property investments and inventories and recognised in accordance with the terms of Notes 4.3. and 4.11, respectively.

4.5 Leases

The Company considers as operating leases those originating from an agreement under which the lessor arranges with the lessee the right to use an asset for a certain period of time, in return for a one-off payment or a series of payments, without involving a lease which, under the provisions of current legislation, could be considered as a financial lease.

The Company charges to the income statement the income and expense arising from the operating leases agreements in which it acts as lessor in the year to which they relate. Likewise, the acquisition cost of the asset is presented on the balance sheet according to its nature, increased by the amount of the costs of the contract directly attributable, which are recognised as an expense during the term of the contract, applying the same method used to report income from the lease.

For its part, the Company treats any amount collected or paid that could be made through an operational lease agreement as an advance collection or payment and takes it to the income statement throughout the term of the lease as the profits from the leased assets are transferred or received.

In 2018 and 2017, the Company has not entered into any financial lease agreement.

4.6 Investments In group companies and associates - Categories of financial assets

4.6.1 Investments in group companies and associates

Associates are entities over which significant influence can be exercised. Significant influence is understood to be when the Company has a holding in another company and has the power to participate in the financial and operating policy decisions of the investee, but without having control or joint control over them. Usually, this influence is evidenced by a direct or indirect holding of 20% or more of the investee's voting rights.

They are valued for their cost less, if the case, the accumulated amount for adjustments related to

impairment. However, if there is an investment prior to its status as a group company, jointly controlled entity or associate, its book value before acquiring that status is considered as the cost of the investment. Any prior adjustments in value recorded directly against equity are maintained there until they are derecognised.

If there is objective evidence that the book value is not recoverable, the appropriate value adjustments are made for the difference between the book value and the recoverable amount, this being understood as the higher amount between the fair value less the sales value and the present value of future cash flows derived from the investment. Unless there is better evidence of the recoverable amount, the impairment of these investments is estimated based on the value of the equity of the investee, adjusted by the amount of the unrealised gains existing at the date of measurement. Value adjustments and, where applicable, their reversal, are recognised in the income statement in the year they arise.

Holdings in associates are entered under the heading "Long-term investments in associates – Equity instruments" on the balance sheet and measured for their acquisition cost, net of any impairments that might have been sustained by those holdings (see Note 4.7.3).

When the remuneration arising from these holdings does not originate unequivocally from earnings generated before the acquisition date, they are recognised under the caption "Turnover" on the income statement (see Note 16.1).

Bank Assets Funds (FABs)

Article 20 of Royal Decree 1559/2012, of 15 November, authorises the Company to create separate equity compartments in what are known as "Bank Assets Funds" (hereinafter, FABs).

The corporate purpose of the FABs, fund-based entities without legal personality, will be to liquidate the portfolio of assets and liabilities provided by Sareb, for which their duration will be the term for which they were created.

In its accounting of the investments in FABs the Company distinguishes between:

- FABs whose creation does not transfer substantially all the risks and rewards incidental to ownership of the assets and liabilities transferred to third party investors. As a general rule, such funds are those in which the Company has control and holds over 50% of the sum of the liabilities and equity of the Fund. In those cases, the Company does not derecognise the assets and liabilities (that is, it does not recognise any sales income nor the corresponding costs) and it measures them using the same criteria applicable before the transfer; it does however recognise a liability for an amount equal to the consideration received which it measures at amortised cost, where appropriate netting and recognising both the income from the assets transferred and not derecognised as costs of the new financial liability when it is effectively sold to third parties. At 31 December 2018, the only FAB set up that has not been deconsolidated is the FAB 2013 Bull. Those FABs have their own accounting and taxation rules.
- FABs whose creation does transfer substantially all the risks and rewards incidental to ownership of the assets and liabilities transferred to third party investors. As a general rule, such funds are those in which the Company does not hold more than 50% of the total liabilities and equity of the Fund. In these cases, and given that control of the assets sold has usually been transferred to the investor, the Company records the cost of the amounts equivalent to the share capital subscribed by the Company under the caption "Long-term investments in associates – Equity instruments". Those equity instruments are measured in accordance with the terms of Note 4.7.3 (Impairment of equity instruments issued by FABs). Furthermore, if any financing has been granted by the Company, it is recognised under the heading of "Long-term investments in associates - Loans to companies". At 31 December 2018, the only FAB set up that has been deconsolidated is the FAB Teide 2013.

In 2018 the Company had carried out no transactions with FABs for any significant amount nor had it set up

any new funds. Meanwhile, in 2017, an agreement was reached with the investment partner of the FAB May in order to liquidate that fund. The agreement reached provided for assigning 5% of the equity corresponding to Sareb to the investment partner in exchange for monetary compensation of 4,800 thousand euros. That amount was recorded under "Turnover" of the accompanying income statement.

4.6.2 Loans and receivables

This category of financial instruments includes debt instruments originating in the services provided by the Company and those which, while not originating in those services, represent fixed or determinable collection rights and are not traded in an active market.

Loans and receivables are recognised on the balance sheet at 31 December 2018 under the captions "Long-term investments in group companies and associates - Loans to companies", Long-term and short-term financial investments corresponding to "Loans to third and related parties", "Loans to companies" and "Other financial assets" and the captions "Trade and other accounts receivable" and "Cash and other cash equivalents" on the asset side of the balance sheet on those dates.

The Company follows the policy of transferring to the caption of doubtful assets any loans and credits having interest and/or capital payments due and outstanding for more than 90 days.

Initial measurement

In general, loans and receivables are initially measured at fair value, which is the transaction/ acquisition price, which is equivalent to the fair value of the consideration paid plus the transaction costs directly attributable to them. In 2013 the Company capitalised those costs necessary for taking control of the assets as their increased value, which amounted to 17,561 thousand euros. At 31 December 2018 and 2017, the amount capitalised for the expense amounted to 11,376 and 12,417 thousand euros, respectively (Note 7.1.1.).

According to the provisions of letter a) of sub-section 10 of the Seventh Additional Provision of Act 9/2012, the acquisition cost of the assets received from the assigning banks in Group 1 and Group 2 was established applying the transfer prices for each type of assets that were fixed by resolution of the Bank of Spain according to the principles established in RD 1559/2012.

Subsequent measurement

The assets included in this category are measured at their amortised cost, net of any impairment. The interest generated by these assets is recorded in the income statement, applying the effective interest rate method. According to the reply to the consultation made to the Bank of Spain and to the earlier pronouncements from the Institute of Accounting and Account Audits (ICAC), the estimation of the future cash flows for the purposes of establishing the effective interest rate takes into account, where appropriate, the value of the collateral on transactions.

Notwithstanding the above, certain items established in applicable legislation, maturing in less than one year, are booked initially at their nominal value if the effect of not discounting their cash flows is insignificant, and are later measured for the same amount.

Any impairment losses existing on these assets are booked in accordance with the terms of Note 4.7.2.

At 31 December 2018 and 2017, Sareb did not hold or have any financial assets of the type provided for in applicable legislation, other than those outlined in this note.

4.7 Impairment of financial assets, property investments and other accounts receivable

As stated in Note 2.1, pursuant to the provisions set out in sub-section 10 of the Seventh Additional Provision of Act 9/2012, in 2015 the Bank of Spain published Accounting Circular 5/2015 which implemented the specific accounting aspects of the Company.

The publication of that Circular 5/2015 regulated the principles which were to be the basis of the method that the Company was to use for estimating the value of the assets transferred by the banks in Group 1 and 2. According to the terms set out in the Circular, the calculation of that value has to be carried out in a way that is consistent with the one originally used for establishing the transfer pricing to the Company taking into account the evolution of market prices and the time horizons forecast in the Company's business plan.

To comply with the provisions of the Circular, the Company has implemented and approved the method for estimating the adjustments related to impairment based on the criteria established in the Circular.

The recognition of the impairment arising as a result of measuring the assets should be made per asset unit. The Circular establishes the offsetting of losses with capital gains on assets within the same «asset unit». The asset units set forth in the Circular are as follows:

- a. Properties foreclosed or acquired in payment of debt, regardless of their origin, provided that they appear on the individual balance sheets of the assigning banks or in their consolidated balance sheets at the time of the transfer.
- b. The following credit rights:
 - i. Loans or credits for financing land for development in Spain or for financing property construction or promotion in Spain, whether in progress or completed, regardless of their age and accounting classification.
 - ii. Participating loans granted to companies in the property sector or to companies related to them, regardless of their age and accounting classification.
 - iii. Other loans or credits granted to the holders of credits or loans included in sub-section 1 above, if the Fund for Orderly Bank Restructuring (FROB) considers the transfer to be suitable, so that the Sareb can properly manage the assets transferred.
- c. The properties and credit rights that meet the requirements set out in the foregoing letter coming from companies in the property sector, or from companies related to them, over which the bank exercises control as set forth in article 42 of the Code of Commerce.
- d. Instruments representing the capital of companies in the property sector or of companies related to them which directly or indirectly enable the bank or any other company in its group to exercise joint control or significant influence over them, if the Fund for Orderly Bank Restructuring (FROB) considers the transfer to be suitable as they hold a considerable volume of assets referred to under letter a), or serve as an effective channel for the company to engage in **property construction or promotion in Spain**.
- e. Consumer loans or credits or loans to small and medium businesses, loans or credits guaranteed by mortgage or by any other assets not included in those sub-sections, whenever those assets are especially impaired or if their continuation on the balance sheet would be considered detrimental to the viability of the company. The consideration of the presence of these circumstances will require a prior report from the Bank of Spain.

Notwithstanding the definition given in Circular 5/2015 for 5 asset units, only the first two are applicable to Sareb: the one relating to the properties allocated originally transferred to Sareb; and the one created by the original credit rights.

It is worth mentioning that the Circular establishes that the assets allocated or received in payment of debts subsequent to the transfer dates will remain in the asset unit in which they were initially included.

At year-end, or whenever the Company publicly provides information on its financial position, it should assess the need to make adjustments related to impairment of each of the asset units. To this end, with the best information available at all times, it will assess whether the carrying amount of the asset unit is higher than the value estimated for the asset unit as a whole using the method implemented by the Company, according to the criteria established in Rule 4 of Circular 5/2015. If that is so, an impairment will be recognised net of taxes, with a charge to the caption "Value change adjustments" within the Company Equity, in compliance with the provisions of article 2 of RD 4/2016 (see Note 2.1).

The debit balance of that account will be taken to the income statement only in those years in which the Company shows a profit. For this purpose the profit before taxes will be taken into account without considering any possible accrual of interest on the subordinated debt.

Impairment of each «asset unit» can be reversed when there is evidence that the value of the assets in the «asset unit» has been recovered using the method implemented by the Company and regulated under Circular 5/2015, with the limit being the value that the «asset unit» would have had if no impairment had been recognised.

In each «asset unit», the amount of the losses in the impaired assets can be offset against the capital gains on the unimpaired assets included in the same «asset unit», estimated according to the criteria of Rule 4 four of Circular 5/2015.

Assets shall remain in their corresponding «asset unit» as long as they meet the requirements set out in letter a) of sub-section 1 of article 36 of the Code of Commerce, namely that there are sufficient objective factors confirming that the likelihood of recovering the value of the asset recognised is not remote.

In compliance with the Bank of Spain Circular 5/2015, the Company has measured its entire portfolio of Financial and Real Estate Assets. However, considering the large volume of assets and collateral subject to being measured, and the complexity of that process,

there is a small percentage of the portfolio that has not obtained a qualifying appraisal in accordance with Rule 4 of the Circular.

In relation to 3.5% of the portfolio, 3.6% in terms of the carrying amount (1.8% and 0.7% respectively in 2017) of the assets recognised under the captions "Financial investments - Loans to third and related parties", "Property investments" and "Inventories"- (on which there are no qualifying appraisals in accordance with Rule 4 of the Circular), the Company, the same as in 2017, has updated the latest appraisals available using correction indices calculated on the basis of information obtained from the updating carried out on the 96.4% of the portfolio (98.2% in 2017) that does meet the qualifying requirements described in the mentioned Rule 4. At 31 December 2018, this block includes 2.9% of appraisals (3.1% in respect of the carrying amount) which, having been eligible in the measurement process for the previous year and fulfilling the technical requirements of the Circular, exceeded the 3-year period for updating. The calculation of this estimation takes into consideration the type of asset, its location and the age of the appraisals available. According to the Directors, the criteria followed provide the best estimation of the value of the assets in this portfolio, and will not differ significantly from the values that would result from an updated appraisal that is eligible under Rule 4 of the Circular.

Furthermore, it is worth mentioning that for the case of appraisals in which the appraiser has indicated conditioning factors, the Company has applied correction indices according to each type, whether due to being unable to have access to the property, due to checking the urban land development, or checking with registries. Those correction indices range from 7% to 30% and have been drawn up internally on the basis of the best understanding and professional judgement of the Company.

Assets will be derecognised from the balance sheet for their carrying amount, without taking into consideration any adjustments related to impairment estimated per «asset unit» as a result of applying the provisions of Rule 4.

Below are the principles applied by the Company for establishing the existence of impairment losses in each of the different asset units identified, and also the method employed for calculating the hedges accounted and recognised for that impairment.

4.7.1. Impairment of the property assets unit

This asset unit includes the amounts booked under the captions "Property investments" and "Inventories" except for 5,163 and 4,228 million euros in 2018 and 2017 respectively of real estate assets received by the Company in payment of debts subsequent to the date of transferring the financial assets and which have been measured within the asset unit itemised in Note 4.7.2.

To determine the value of its real estate assets the Company takes into account the features that a properly informed buyer would use for deciding to buy it, such as its geographical location, available infrastructure, legal status, terms of sale or operation, demand and offer for similar properties, its most likely use, as well as aspects related to urban development, demographical evolution and prices of utility supplies. For the purposes of considering the legal status of the property and its urban development issues, for the measurement of the land the Company has used the development levels defined in article 4 of Order ECO/805/2003, of 27 March on the rules for measuring real estate assets and defining the fees for certain financial purposes.

Estimation of the value of Property investments for rental

In those property investments that the Company keeps for rental, the value has been calculated on the basis of discounting future cash flows, considering the level of occupation corresponding to the date when measured, the likelihood of future occupation of the properties and current market rents.

Estimation of the value by making individual appraisals

The Company has estimated the individual value of its real estate assets according to measurement reports from independent experts with proven experience in the area and type of properties being appraised. The valuation of the assets has been specifically carried out by appraisal companies registered in the Registry of Licensed Appraisal Companies held by the Bank of Spain, in accordance with the criteria established in Order ECO/805/2003, of 27 March, on the rules for property valuation. In accordance with the provisions

of Rule 4 of the Bank of Spain Circular 5/2015, those valuations were performed by independent experts who took into account the following methods depending on the type of assets:

- Residual dynamic method for land.
- Discounting future cash flows for assets used for obtaining income, considering the expected occupation levels and current market rents.

At least every three years, the Company shall review the mortgage appraisals made on its real estate assets by changing the independent expert. If the market conditions and circumstances demonstrate the need to perform appraisals more frequently, the Company will reduce that period.

Estimation of the value of completed properties, annexes and commercial premises

In the case of completed properties, annexes (such as garages or storerooms) as set out in Rule 4 of Bank of Spain Circular 5/2015, they may be measured using automated valuation methods by independent experts (appraisal companies registered in the Registry of Licensed Appraisal Companies held by the Bank of Spain). Those methods can be used to determine the value of commercial premises in towns where there is a market that is representative of comparable properties in the sense that, at almost any time, it is possible to find operators willing to negotiate a sale or rental. However, it is Company policy to have an ECO appraisal carried out, as it considers that with this, the situation of the asset and its market value can be more accurately represented. Assets measured using those statistics-based methods account for 1.2% (1.8% in terms of carrying amount) for mortgage guarantees, and 4.8% (3.8% in terms of carrying amount) for real estate assets (2.8% of the carrying amount of mortgage guarantees and 9% of the carrying amount of the real estate assets at 31 December 2017).

Those measurements using statistics-based or automated valuation methods are recalculated every year and are performed taking into account the statistics from the National Institute of Statistics in respect of the evolution of prices for new and resale property.

Estimation of value of other assets using internal estimations or methods

In the case of real estate assets other than those described in the previous sub-sections and with a combined carrying amount per batch of less than one million euros, the company has used its best estimate to establish their current value, at least once a year. Those estimates were made using measurement models for which an external independent expert has recognised the method, and solely for those assets for which sufficiently tested data was available. Otherwise, those assets would be measured using the ECO appraisals.

In addition to the measurements carried out according to the above methods, the method developed by Sareb, based on the criteria established in Circular 5/2015 applicable to both property and financial assets, includes a number of assumptions, of which the following are worthy of special mention:

- Adjustments for reflecting the evolution of market prices and the horizons of the Company's business plan. In order to apply those adjustments, the Directors have employed their best estimate depending on the type and location of the different properties, as well as the estimated sales for the different years contained in the business plan. To this end, and on the basis of the provisions of Circular 5/2015, they have considered an estimated evolution of average market prices ranging from between 3.1% and 4.92% in 2018 (2.1% and 6.3% in 2017), and an average time horizon, depending on the different types of assets, ranging from between 4.3 and 7 years in 2018 (4 and 6.5 years in 2017).
- Estimation of the costs for maintenance and marketing, which are deducted from the estimated measurements. In order to calculate that cost estimate, the average estimate of the asset's permanency has been taken into consideration, taken from the Business Plan as reflected in the previous paragraph. To this end, according to the different types of asset, the average costs associated to them range between 1.3% and 8.9% in 2018, respectively (1.1% and 9.0% in 2017).

- Discount rate. The measurement obtained after applying the above adjustments is updated to the current value using an estimated discount rate taking into consideration the Company's financing costs and the risks inherent to the assets. Average rates have been considered ranging between 1.4% and 1.75% in 2018 (1.4% and 3.0% in 2017), which include an aggregate figure for the financial costs estimated for the Company according to the Business Plan. Moreover, the financial assets measurement model includes a measure that is in addition to the financial costs related to the Business Plan and the property risk contained in the methods under the ECO Order, which varies between 8% and 30%.
- Also, and in application of the Circular, any measurement that is seen to be 15% higher than the mortgage value or the value obtained using sample statistical procedures or automated valuation models must be evidenced with more than one market transaction involving similar assets. However, the Company has made no adjustments higher than 15% above the mortgage value or the measurements obtained using sample statistical procedures or automated valuation models.

At 31 December 2018 and 2017, the Company shows no net losses in this asset unit.

The Company has carried out a sensitivity analysis on the key assumptions considered to be more volatile in the real estate assets measurement model. The results obtained are summarised below:

Figures in millions of euros	+ 100 b.p. / + 1 year	- 100 b.p. / - 1 year
Appraisal values	65	(67)
Sales prices of real estate assets	335	(320)
Time horizon of the business plan	106	(126)
Total	506	(513)

The only sensitivity that would give rise to the need for the Company to make a provision is a reduction of 100 b.p. in the sales prices of real estate assets, which would result in the need to make a provision of 60 million euros.

In 2017 those sensitivities brought about effects ranging between 651 thousand euros of capital gains and 624 thousand euros of lower capital gains.

4.7.2 Impairment of loans and credits receivable and property assets received in payment of debts

Trade receivables

At least at year end, the Company carries out impairment testing to bring the trade receivables into line with their recoverable value. Objective evidence of impairment is considered to exist if the recoverable value of the financial asset is lower than its book value. If this happens, this impairment is recognised in the income statement. At 31 December 2018 and 2017, the Company has a provision for impairment of trade receivables for the amount of 63,047 and 54,981 thousand euros, respectively (see Note 9).

Loans and credits and other real estate assets received in payment of debts

The value of financial assets representing debt transferred to the Company is estimated on an individual basis according to the payment capacity of the main debtors liable for payment, where appropriate,

considering the possible existence of guarantors or surety with proven payment capacity.

Estimating the payment capacity of debtors takes place either individually depending on the payment capacity of the debtor if this can be verified and evidenced with documents in respect of fulfilment of contractual obligations with no significant delays or hold-ups in payments. In the case of loans without collateral, the valuation is made collectively, considering that the expected loss of the portfolio in question is reflected, except for financial assets without collateral not paid or whose payment has been delayed for over 18 months and which are considered to be of zero value, unless demonstrated otherwise. That principle is applied to the residual value of assets with collateral other than a first-ranking guarantee, after deducting all of the liability insured with the first-ranking guarantees, including interest on arrears. Only when the Company is the sole best-ranking creditor, the current value of the debt is used when this is less than the mortgage liability and the value of the guarantee could cover both senior-ranking and junior-ranking loans, whether fully or partially.

For any financial assets (or real estate assets received by the Company in payment of debts) in respect of which it is estimated that the amounts owed will be recovered by foreclosing the guarantees and those guarantees represent a first-ranking collateral to the assets, or a lesser-ranking right if the requirements set out in the previous paragraph are met, the measurement of the financial asset will be made taking into consideration the property measurement of the guarantees. That measurement is made according to the terms set out in Note 4.7.1 on real estate assets (including in the estimation of costs not only those for maintenance and marketing up until the subsequent sale of the collateral, but also those necessary for the foreclosure of the guarantees (court costs, legal costs and taxes).

In the case where the loans and receivables with collateral other than properties, such as pledging debt securities or capital, the Company calculates their market value on the measurement date if it is a financial instrument traded on an active market or, where appropriate, it uses generally accepted measurement methods.

For the estimation of the value of these assets a number of assumptions have been applied, based on the Company's Business Plan, which are listed in Note 4.7.1. With regard to the costs and deadlines for foreclosure and dation in payment of collaterals, these have been

estimated on the basis of the type of assets and the Company's Business Plan, fluctuating between 1% and 21% of the debt (1%-18% for 2017).

Following the impairment testing carried out, in 2018 and 2017 the Company has provisions which have been funded with a charge to the caption "Value change adjustments – Impairment of financial assets" for the amount of 5,091,686 and 4,229,552 thousand euros, respectively, for the impairment of debt instruments classified as loans and receivables and assets received in payment of debt (see Note 7.1.1.). That provision is recognised under the caption "Long-term financial investments – Loans to third and related parties".

The same as for the unit of real estate assets, the Company has carried out a sensitivity analysis on the key assumptions considered to be more volatile in the measurement model, obtaining the following results:

Figures in millions of euros	Effect on equity	
	+ 100 b.p. / + 1 year	- 100 b.p. / - 1 year
Appraisal values	192	(193)
Sales prices of real estate assets	1.019	(977)
Time horizon of the business plan	536	(587)
Total	1,747	1,757

4.7.3 Investments in group companies and associates

Impairment losses on the investments in group companies and associates are estimated and booked by the Company whenever, according to the provisions of applicable legislation, there is objective evidence that the book value of an investment in those companies may not be recovered.

When estimating the existence of evidence of the impairment of those holdings, amongst other factors, the Company considers any drop in its underlying book value adjusted for any non-recorded unrealised gains of the companies or the evolution of its share price (in the case of those that are publicly traded), inactivity of the investee, its financial position, etc.

The amount of the impairment loss to be recognised is estimated as the difference between the carrying value of the holdings and their recoverable amount, this being understood as the higher amount between the fair value less the sales costs and the present value of future cash flows arising from the investment.

In any cases in which it is not possible to estimate the recoverable amount of an investment as described in the previous paragraph or in any insignificant investments, the estimation of their impairment is based on the equity of the investee company, adjusted by the amount of the unrealised gains existing at the date of impairment measurement.

In application of the 2nd consultation of the Official Bulletin of the Institute for Accounting and Auditing (BOICAC) 79, adjustments related to impairment and, where applicable, their reversal, are recognised as income or expense, respectively, under the caption "Impairment and profit/(loss) from sales of financial instruments – Impairment and losses" forming part operating profit/(loss) on the income statement. The reversal of a previously recorded impairment is limited to the book value of the investment that would have been recorded on the date of reversal if the value impairment had not been recorded.

In 2018 and 2017 the impairment recorded by the Company for this item was 4,698 and a reversal amounting to 218 thousand euros, respectively (see Note 7.2).

4.8 Categories for classification of financial liabilities

This category includes the classification of trade payables originating in the purchase of assets and services under the Company's trade transactions, the funding received (see Note 1) and any non-trade payables which are not derivatives and have no trade origin.

Debits and items payable are initially valued at the fair value of the consideration received, adjusted by the transaction costs directly attributable to them. Subsequently those liabilities are valued for their amortised cost.

Notwithstanding the above, certain items established in applicable legislation, maturing in less than one year, are

booked initially at their nominal value if the effect of not discounting their cash flows is insignificant, and are later measured for the same amount.

Derivative financial instruments are measured at fair value.

The interest accruing on those liabilities, calculated using the effective interest rate method, is recorded under the caption "Financial expense" on the income statement.

4.9 Hedging derivatives

The Company uses financial derivatives to hedge its equity positions as part of its strategy for reducing its exposure to interest rate risks.

When the Group designates a transaction as a hedge it does so from the inception of the transactions or instruments included in the hedge, and the hedging transaction is documented appropriately. The hedging operation documentation identifies the hedged instrument or instruments and the hedging instrument or instruments, the nature of the risk to be hedged, and the criteria or methods used by Sareb to assess the effectiveness of the hedge over its entire life, taking into account the risk intended to be hedged.

Sareb only classifies as hedging operations those considered to be highly effective during their expected life. A hedge is considered to be highly effective if, during its expected life, the changes in fair value or in the cash flows that are attributed to the risk hedged under the hedging operation for the financial instrument or instruments hedged are almost entirely offset by changes in the fair value or in the cash flows, as appropriate, of the hedging instrument or instruments.

To measure the effectiveness of hedging operations defined as such, the Company analyses whether, from the beginning to the end of the term defined for the hedge, it may be expected, prospectively, that the changes in fair value or in the cash flows of the hedged item that are attributable to the hedged risk will be almost entirely offset by changes in the fair value or in the cash flows, as appropriate, of the hedging instrument or instruments and, retrospectively, that the results of the hedge will vary within a range of 80% to 125% of the results of the hedged item.

In order to establish that fair value, the Company takes into account its credit risk in the event of the measurement being negative, or the counterparty risk in the event of the measurement being positive.

The hedge accounting ceases to take place when the hedging instrument matures or is sold, expires or is exercised, or if it no longer meets the criteria for hedge accounting. At that time any cumulative gain or loss corresponding to the hedge instrument that has been recorded in equity is held there until the anticipated transaction has occurred. If the hedging operation is no longer expected to occur, any cumulative gains or losses recognised in Equity are transferred to the income statement.

Cash flow hedges

The hedging operations held by the Company at 31 December 2018 are in line with the definition of "Cash flow hedges", that is, hedges to cover exposure to cash flow fluctuations associated to the interest rate risk for a highly probable forecast transaction and for the financing received at a floating interest rate, respectively, which affect the Company's income statement. The portion of the gain or loss on the hedging instruments qualifying as effective hedges is recognised temporarily in equity, net of tax, under the caption "Value change adjustments - Hedging operations", and the corresponding portion is taken to the income statement in the year or years in which the planned hedged operation affects profit/(loss).

In 2018, the derivatives hedging the 1-year bonds and part of the 2-year bonds have conserved their effectiveness within the thresholds required under the International Standards of Accounting but, due to the downward trend in the interest rates to which the hedged risks are indexed and to Sareb's application of a "floor" by which the interest rate may in no case be lower than 0%, they have lost part of that effectiveness. At 31 December 2018 and 2017, the measurement of the ineffective portion of the derivatives was 81,962 and 13,260 thousand euros, respectively. The Company has recorded the change in the ineffectiveness as a "Financial expense" (see Note 16.5).

Certain information is provided in Note 13.3 on the cash flow hedging operations carried out by the Company.

4.10 Derecognition of financial instruments

Financial assets are derecognised when any of the following circumstances arises:

1. The contractual rights on the cash flows generated by the asset have expired; or
2. The contractual rights to the cash flows from the financial asset are assigned and substantially all its risks and rewards are transferred or, although these are not substantially transferred or retained, control over the financial asset is transferred.

Also, a financial liability is derecognised when the obligations it generates have been extinguished or when it is repurchased by the Company, with the intention either to resell or to cancel it.

4.11 Inventories

These mainly correspond to property developments in progress and to the value of the associated land intended for sale in the normal course of the Company's business. Sareb recognises under the caption "Inventories" all assets on which it is going to take any kind of action, construction and/or development for subsequent sale through marketing.

The costs incurred in property development still to be completed are considered as works in progress. Those costs include any corresponding to the land, urbanising and construction, as well as the capitalisation of the financial expense incurred during the construction stage and any other direct and indirect costs attributable to them. Moreover, the Company does not capitalise marketing costs, which are taken directly to the income statement.

All real estate assets for which the Company's governing bodies have approved an investment and development plan for their subsequent retail sale are transferred from "Property investments" to the caption "Inventories".

The expense corresponding to any property developments for which construction has concluded during the year and are still to be sold is transferred from "Works in progress" to "Completed buildings".

The principles applicable to the impairment testing of inventories are similar to those applicable to Property investments (see Note 4.7.1.).

4.12 Foreign currency transactions

The functional currency used by the Company is the Euro. Therefore, transactions in currencies other than the Euro are considered to be denominated in foreign currency and are recorded according to the exchange rates in force at the transaction dates.

At the close of the year, the Company had no balances nor had it carried out transactions in foreign currencies for any significant amount. The amount recognised in 2018 and 2017 for this item was 10 and 3 thousand euros, respectively.

4.13 Income and expense

Income and expense are recorded according to the principle of accrual, that is, at the moment when the goods or services represented by them are provided, regardless of when actual payment or collection occurs. This income is measured at the fair value of the consideration received, after deducting discounts and taxes.

Reporting in the income statement:

In line with the provisions set out in sub-section 10 of the Seventh Additional Provision of Act 9/2012, of 14 December, and its amendment included in the Ninth Additional Provision of Act 26/2013, of 27 December, and also the provisions of Bank of Spain Circular 5/2015, the Company has recognised the income generated as a result of the process for orderly management and liquidation of all the transferred assets in the income statement forming part of its "Turnover" (see Notes 2.1 and 16.1).

Income from interest

Notwithstanding the principles provided in the Accounting and Measurement Rule 9 of the General Chart of Accounts (PGC), under which the subsequent measurement of the financial assets should follow the amortised cost principle and also that “interest accrued is recorded in the income statement, applying the effective interest rate method”, the general application of the accrual principle and the amortised cost principle can have specific practical applications depending on the type of asset to which they are to be applied, the terms under which they were acquired and even the sector applying that principle, to the extent that it responds to the true and fair view of the annual accounts.

Considering the characteristics of the assets received and the high degree of uncertainty in their recovery through regular channels as already described in Note 4.6.2, the accrual model applied by Sareb provides that interest will only accrue on transactions in which they are estimated to be effectively recovered, backed up by the recoverable value of the guarantees for those transactions. That recoverable value is estimated on the basis of the principles set out in Note 4.7.2.

As part of the effective interest rate, the Company records under the heading “Turnover – Margin of recovery of loans and credits”, the difference between the recovered value and the net carrying value of the loans and credits that have been cancelled or partially repaid.

Income from sales of loans and credits

Income from sales of loans are recognised under the heading of “Turnover – Sales of loans and credits”. That sale takes place once all the risks and benefits related to the financial assets transferred have been passed on to the buyer, which usually coincides with signing the sales deeds and collecting payment on the sale.

Income from property sales (Property investments and inventories)

Income from property sales (both for Property investments and Inventories) is recognised when the significant risks and rewards of ownership of the goods sold have been transferred to the buyer, and the Company neither continues to manage the goods nor retains effective control over them. That moment usually coincides with signing the sales deeds for the property being sold. The amount of property sales is recorded under the heading “Turnover” on the accompanying income statement.

The Company includes in the accompanying Income Statement the charge for the amounts corresponding to the expense yet to be incurred for liquidating the promotion, as a provision for finishing building work.

Amounts paid in advance in the form of cash or notes receivable corresponding to reservations and sales contracts for promotions when they have not yet been handed over to the buyer and therefore the sale has not been recognised, are booked under the caption “Customer advances” on the liability side of the accompanying Balance Sheet, and are classified as current regardless of the date planned for recognition of the sale of the developments.

The Company recognises sales of land and sites when the risks and benefits inherent to them are transferred, which normally takes place when the sales deeds are signed.

Income from leases

Rental income is recognised on an accrual basis, and incentive-related income and the initial costs of lease agreements are allocated on a straight-line basis.

4.14 Income Tax

The expense or income from Income Tax includes the portion relative to the current tax expense or income and the portion corresponding to the deferred tax expense or income. Corporate Income Tax for the year is calculated based on the economic or accounting profit or loss determined by applying generally accepted accounting principles, which does not necessarily coincide with taxable profit or loss, this being taken as the tax base for this tax.

Current tax is the amount that the Company pays as a result of paying Income Tax relating to one year. Any deductions and other tax benefits in the tax charge, excluding any withholdings and payments made on account, and the tax losses that can be offset from previous years and applied effectively in this year, give rise to a lower amount of current tax.

Any deferred tax expense or income corresponds to the recognition and derecognition of the deferred tax assets and liabilities. These include any temporary differences which are identified as those amounts that are foreseen to be payable or recoverable, arising from the differences between the book values of the assets and liabilities and the tax base value, and the tax loss carryforwards and unused tax credits. Those amounts are recorded by applying to the corresponding temporary difference or credit the charge at the rate at which it is expected to be recovered or paid.

Deferred tax assets are only recognised to the extent that it is considered probable that the Company will have future taxable profits available against which they can be offset. In this case, the deferred taxes are measured on the basis of the current tax rate expected at the time of recovery.

Deferred tax liabilities are recognised for all taxable temporary differences, except those arising from the initial recognition of the goodwill or other assets and liabilities in a transaction that has no effect on the taxable profit or loss or on the accounting profit or loss, and is not a business combination, and also those associated to investments in subsidiaries, associates and joint ventures in which the Company is able to control the timing of the reversal of the temporary difference and it is probable that they will not reverse in the foreseeable future.

Deferred tax assets and liabilities originating in transactions with charges or payments directly made in equity accounts are also entered with a balancing entry in equity.

At each year-end the recorded deferred tax assets are reviewed, and appropriate adjustments are made to the extent that there are doubts as to their future recovery. Also, at each year-end, the deferred tax assets not recorded on the balance sheet are assessed and recognised to the extent that it has become probable that future taxable profit will enable them to be recovered.

4.15 Provisions and contingencies

In the preparation of these annual accounts the Directors differentiate between:

- a. Provisions: credit balances that cover current obligations arising from past events, the cancellation of which is likely to originate an outgoing of resources, but that is undefined as to the amount and/or moment of cancellation.
- b. Contingent liabilities: possible obligations arising as a consequence of past events, the materialisation of which is conditioned to one or several future events occurring beyond the control of the Company.

The annual accounts contain all the provisions with respect of which it is anticipated that the probability of having to attend to the obligation is greater than not having to. Contingent liabilities are not recognised in the annual accounts, but information is provided on them in the notes in the report, to the extent that they are not considered to be remote.

Provisions are measured at the current value of the best calculation possible of the amount necessary for cancelling or transferring the obligation taking into account the information available on the event and its consequences, and recording the adjustments that arise from updating those provisions as a financial expense as they become due.

The compensation to be received from a third party at the moment of liquidating the obligation, as long as there are no doubts that said reimbursement will be received, is recorded as an asset, except in the case of there being a legal relation through which part of the risk has been externalised, and by virtue of which the Company is not bound to respond; in that circumstance, the compensation shall be taken into account to estimate the amount for which, if appropriate, the relevant provision shall be recorded.

At 31 December 2018 and 2017, the Company had set up the provisions for risks and expenses described in Note 12.

4.16 Transactions with related parties

A related party is deemed to be any individual or legal entity having control or significant influence over a company, or who is a key member of its Management. According to the Directors, no other company exercises sole or joint control of the Company and there is no association with key members of Management, other than their employment relationship.

Significant influence is understood to be the power to participate in the financial and operating policy decisions of the Company, but without having control over them. In this respect, the Company considers that the FROB is the only shareholder having any significant influence on the Company.

In general, transactions with related parties are recognised according to the general rules for measurement contained in the General Chart of Accounts, namely that the items involved in the transaction are initially recorded for their fair value and subsequently according to the relevant accounting standards.

Note 17 gives information on transactions with related parties concluded in 2018 and 2017 and on the balances held at 31 December of those years with related parties.

4.17 Termination indemnities

In accordance with current legislation, the Company is required to pay indemnities to any employees who, in certain conditions, have had their employment relationships terminated. Therefore, termination indemnities that can be reasonably quantified are recorded as an expense in the financial year in which the decision to dismiss them is taken. At 31 December 2018, the Company had no liabilities for this item, however in 2018 and 2017, the Company recognised termination indemnities for the amount of 161 and 216 thousand euros, respectively, which were recorded under the caption "Staff expense – Salaries, wages and similar" on the accompanying income statement.

4.18 Cash flow statements

In the cash flow statements, prepared using the indirect method, the following expressions are used with the following meanings:

1. Cash flows: inflows and outflows of cash and cash equivalents, which are short-term, highly liquid investments that are subject to an immaterial risk of changes in value.
2. Operating activities: the principal activities of the Company and other activities that are not classified as investment or financing activities. The Company classifies these activities as described in Note 4.13.3.
3. Investing activities: the acquisition and disposal of non-current assets and other investments not included in cash and cash equivalents.
4. Financing activities: activities that result in changes in the size and composition of equity and liabilities that are not amongst the Company's operating activities, as well as any others which cannot be classified as for investment or operating.

5. Property investments

The composition of this caption at 31 December 2018 and 2017, is as follows:

	Thousands of euros	
Land and sites	5,461,173	5,072,450
Completed buildings		
Residences- Main residence	4,545,675	4,766,283
Offices, commercial premises and multi-purpose facilities	1,156,227	1,212,669
Other properties	411,689	457,135
Residences - Other than main residence	8,122	50,695
Total completed buildings	6,121,713	6,486,782
Of which: Buildings rented (Note 6)	760,705	763,954
Of which: Land	3,688,926	3,852,914
Advances on property investments	311,022	140,046
Total property investments	11,893,908	11,699,278

For its part, the changes under the caption Property investments in 2018 and 2017 are as follows:

2018

	Thousands of euros			
	Completed buildings	Land and sites	Advances	Total
Cost:				
Balance at 01 January 2018	6,706,618	5,072,450	140,046	11,919,114
Additions from awards and donations	564,514	389,087	453,361	1,406,962
Other additions	10,392	15,361	3,906	29,658
Sales and derecognition	(980,054)	(195,442)	(520)	(1,176,016)
Transfers	47,785	237,986	(285,771)	-
Transfers to inventories (Note 8)	8,708	(58,269)	-	(49,561)
Withdrawals due to rectifications (Note 1)	-	-	-	-
Balance at 31 December 2018	6,357,963	5,461,173	311,022	12,130,158
Depreciation				
Balance at 01 January 2018	(219,836)	-	-	(219,836)
Provisions charged against profit or loss	(53,103)	-	-	(53,103)
Sales, derecognition and other changes	36,689	-	-	36,689
Balance at 31 December 2018	(236,250)	-	-	(236,250)
Net balances at 31 December 2018	6,121,713	5,461,173	311,022	11,893,908

2017

	Thousands of euros			
	Completed buildings	Land and sites	Advances	Total
Cost:				
Balance at 01 January 2017	7,155,094	5,019,864	-	12,174,958
Additions from awards and dations	485,487	379,746	137,888	1,003,121
Other additions	7,490	10,245	8	17,743
Sales and derecognition	(824,387)	(340,739)	-	(1,165,126)
Transfers	(15,386)	13,236	2,150	-
Transfers to inventories (Note 8)	(102,404)	469	-	(101,935)
Withdrawals due to rectifications (Note 1)	724	(10,371)	-	(9,647)
Balance at 31 December 2017	6,706,618	5,072,450	140,046	11,919,114
Depreciation				
Balance at 01 January 2017	(188,227)	-	-	(188,227)
Provisions charged against profit or loss	(56,014)	-	-	(56,014)
Sales, derecognition and other changes	24,405	-	-	24,405
Balance at 31 December 2017	(219,836)	-	-	(219,836)
Net balances at 31 December 2017	6,486,782	5,072,450	140,046	11,699,278

The most relevant changes produced in 2018 and 2017 under this caption are itemised as follows:

Other additions

In 2018 and 2017 the Company capitalised 29,658 and 17,743 thousand euros, respectively, as the higher cost of property investments corresponding to improvements and developments it carried out on the items of its Property investments. Those improvements were mainly related to urban development works carried out on land and sites.

Transfers between items

In 2018 and 2017 the Company reclassified 49,561 and 101,935 thousand euros from the caption Property investments to Inventories corresponding to various plots of land and construction work in progress that had been halted and regarding which the Company has decided to begin or resume the construction and promotion of properties (see Note 8).

Advances on property investments

The Company recognises under the caption "Advances on property investments" all properties acquired through mortgage foreclosure proceedings which have an enforcement order but are still pending a final ruling. The Company adopted that principle in 2017 in order to standardise the accounting and tax treatment of the operation.

Mortgage foreclosures and dations in payment

2018

On 19 February and 26 June 2018, the Company formalised the foreclosures on various lands and finished products that the borrower "Epaat, S.L." had mortgaged in guarantee of various loans held by the Company. The acquisition cost of land and finished products acquired was 34,983 thousand euros, this

being the net carrying amount of the loans and credits cancelled in lieu of payment.

On 23 February 2018, the Company formalised the foreclosures on 45 sites that the borrower "Greenpar Proyectos Inmobiliarios, S.L." had mortgaged in guarantee of various loans held by the Company. The acquisition cost of the land acquired was 19,504 thousand euros.

On 18 December 2018, the Company formalised the foreclosures on 8 sites that the borrower "Gediaz Suelo, S.A." had mortgaged in guarantee of various bilateral loans held by the Company. The acquisition cost of the land acquired was 20,288 thousand euros.

In December of 2018 various mortgage foreclosure procedures were concluded in respect of various loans secured by mortgage guarantee on finished product and land belonging to the agency "Inmobelsa, S.A.". The acquisition cost of the land and finished product acquired was 25,769 thousand euros.

2017

On 19 July of 2017, the Company formalised the foreclosures on various sites and finished products that the borrower "Liderazgo Inmobiliario de Aragón, S.L." had mortgaged in guarantee of various loans held by the Company. The acquisition cost of the land and finished product acquired was 43,677 thousand euros, this being the net carrying amount of the loans and credits cancelled following dation in payment.

In August of 2017 various mortgage foreclosure procedures were concluded in respect of various loans secured by mortgage guarantee on finished product and land belonging to the agency "Martinsa-Fadesa S.A.". The acquisition cost of the land and finished product acquired was 18,235 thousand euros.

On 29 September 2017, the Company formalised the dation in payment of 6 sites that the borrower "Promociones Montegancedo 2013" had mortgaged in guarantee of various bilateral loans held by the Company. The acquisition cost of the land acquired was 22,760 thousand euros.

Sales and derecognition

2018

On 1 February 2018, the sale took place of various commercial premises located in the shopping centre "Parque Corredor" in Torrejón de Ardoz (Madrid) for the price of 75,000 thousand euros, of which 29,998 thousand euros were received by year-end, and the rest was deferred. That deferral was guaranteed by the buyer and accrues interest for the Company at market rate.

On 31 October 2018, the deeds were signed for the sale of 180 assets of different types included in the "TER" portfolio for a total price of 18,953 thousand euros, of which 10,386 thousand euros were received by year-end, and the rest was deferred. Also, in the same portfolio, on 29 December 2018, deeds were signed for the sale of another package of 63 assets for a total amount of 8,823 thousand euros, of which 4,853 thousand euros were received, and the rest was deferred. That portfolio also contains various properties yet to be notarised, waiting for the Regional Government of Catalonia to exercise its right of first refusal on them, or not.

On 28 December 2018, the Company sold various residences belonging to the portfolio known as "Garona". The sales price assigned to said portfolio was 20,831 thousand euros, of which 9,374 thousand euros are still to be received. That portfolio also contains various properties yet to be notarised, waiting for the Regional Government of Catalonia to exercise its right of first refusal on them, or not.

On 4 December 2018, the company Témpe Properties, S.A. increased its capital, which was taken up entirely by the Company through the contribution of a package of completed properties to be used for rental. The net carrying amount of said assets was 144,977 thousand euros (see Note 7.2.1).

2017

On 25 May 2017, the deeds were signed for the sale of a serviced development land located in Sotogrande, in the municipality of San Roque (Cadiz), for a total

price of 8,000 thousand euros, which was received in full upon notarising the deed.

On 19 July 2017, the deeds were signed for the sale of the Hotel Senator Parque Central and the garages located on the basement floor, located in Valencia, for a total price of 16,462 thousand euros, which was received in full upon notarising the deed.

On 5 December 2017, the sale took place of a plot of land located in the municipality of Rivas-Vaciamadrid (Madrid) for the price of 15,100 thousand euros, of which 8,325 were received by year-end, and the rest was deferred.

On 14 December 2017, the deeds were signed for the sale of a site in Benahavis (Malaga) for the price of 10,500 thousand euros, of which 5,775 thousand euros were received by year-end, and the rest was deferred.

On 7 July, the Company incorporated T  mpore Properties Socimi, S.A. through a non-monetary contribution of a complex of residential buildings and residences for rental located in the main urban centres in Spain. The net carrying amount of those assets transferred was 172,055 thousand euros (see Note 7.2.1).

On 29 December 2017, the deeds were signed for the sale of a site on Plot D Son Ferragut (Palma de Mallorca), for the price of 8,353 thousand euros which was received in full at the close of 2017.

Sales commitments:

At 31 December 2018 and 2017, the Company had the following sales commitments regarding items of its Property investments:

- FAB Bull: In 2013 the Company transferred the amount of 100,000 thousand euros to the FAB 2013 Bull for a package of Property investments whose net cost at 31 December 2013 was 97,896 thousand euros. The Company did not record the corresponding sale as it considered that the risks and benefits inherent to those assets had not been transferred. At 31 December 2018 and 2017, the amount of outstanding real estate assets belonging to the FAB Bull, was 1,637 and 13,686 thousand euros, respectively.
- TER and Garona portfolios: In December 2018 the Company sold those portfolios, which included various residences located in Catalonia, on which it has a right of first refusal, for which reason the deeds were not signed at the close of 2018. The committed price of those residences, awaiting notarisation, is 57,302 thousand euros, of which 5,733 thousand euros have been advanced, recorded under the caption "Customer advances" of the accompanying balance sheet.

At 31 December 2018 and 2017, the Company signed sales commitments on various residences and plots of land whose carrying amount is 37,940 and 62,915 thousand euros, to which a sales price of 43,847 and 85,767 thousand euros has been assigned, respectively; of this amount, 6,464 and 4,666 thousand euros was advanced and has been recognised under the caption "Customer advances" on the accompanying balance sheet.

Other information

At the end of 2018 and 2017:

- All the Company's property investments are unencumbered and free from security rights.
- The Company has no fully depreciated items of property investments on its balance sheet.
- There are no dismantling or withdrawal costs capitalised as a higher cost of the property investments for any significant amount.
- The assets allocated by Sareb forming part of the Financial Assets Unit have not generated any profit/(loss) upon being entered on the balance sheet of real estate assets.
- In this respect, the application of the rules for measurement established by Circular 5/2015 for the Real Estate Assets Unit, consisting of the assets transferred by the assigning banks when Sareb was set up, which are classified under the caption Property investments and Inventories (see Note 8), at the end of 2018 and 2017 showed a capital gain on the net carrying value of 260 and 689 million euros, respectively.
- For its part, the measurement of assets allocated or received in payment of debt subsequent to the date of transfer, carried out according to the principles of Bank of Spain Circular 5/2015, has brought to the financial assets unit (see Note 7.1) a loss of 275 million euros in 2018 and a capital gain of 400 million euros in 2017, respectively, which reduces the need for write-off of the credit transactions of that Unit.
- The Company had no impairment provisions for its portfolio of property investments.

The Company's policy is to take out all insurance policies deemed necessary to cover the risks that could affect the property investments. The insurance cover taken out by the Company in respect of its property investments is higher than the net carrying amount of the investments, and is updated annually.

6. Operating leases

At the close of 2018 and 2017, the Company acts as the lessor in certain operating lease agreements whose minimum lease payments, according to the contracts currently in force, without taking into account the repercussion of common expense, future increases in the Consumer Price Index, nor future contractually agreed rent updates, are as follows:

Minimum rents	Thousands of euros	
	2018	2017
Less than one year	29,153	45,652
From one to five years	53,529	72,831
Over five years	45,077	46,780
Total	127,759	165,263

Also, the amount of rent from the operating leases and sub-leases corresponding to 2018 and 2017 were recorded under the heading "Turnover" with the following breakdown:

	Thousands of euros	
	2018	2017
Minimum payments per lease (Note 16.1)	34,831	49,443
Repercussion on general expense	1,793	2,627
Total	36,624	52,070

The most significant lease agreements are those itemised below:

Location	Contract date	Type of property	Gross annual amounts (thousands of euros)	Expiry date
Various	27/06/2014	Apartamentos Turísticos	1,681	30/09/2024
c/ Cronos (Madrid)	26/06/2006	Edificio de Oficinas	761	30/06/2021
c/ Italia (Franqueses del Vallés)	01/01/2013	Nave Industrial	732	01/01/2023
c/ Doctor Trueta (Sant Celoni)	01/11/2016	Local Comercial	531	03/12/2034
c/ Gaiteira (La Coruña)	04/10/2013	Edificio de Oficinas	411	03/10/2019
c/ Amplaries (Oropesa del Mar)	13/07/2017	Apartamentos Turísticos	371	12/07/2022
c/ Manfredonia	01/03/2009	Nave Industrial	338	27/04/2024

The net cost of the Company properties being rented at 31 December 2018 and 2017 was 760,705 and 763,954 thousand euros, respectively (see Note 5).

Also, the amount of contingent rents, i.e. variable lease payments, corresponding to those leases recorded in 2018 and 2017 under the caption "Turnover" are insignificant.

Lastly, the lease agreements in which the Company acts as lessee mainly refer to the lease for the offices where it has its head office, and to the leasing of various items of computer software. The lease payments to which the Company is committed for these items are insignificant at the close of 2018 and 2017.

7. Long-term and Short-term financial assets

The book value of each category of financial asset held by the Company at 31 December 2018 and 2017 is shown below.

7.1 Breakdown of long-term and short-term financial investments

Below is the breakdown of financial assets belonging to Sareb at 31 December 2018 and 2017, classified according to the breakdown required under applicable legislation:

2018

Categories	Classes	Thousands of euros			
		Long-term financial instruments		Short-term financial instruments	
		Equity instruments	Credits, derivatives and others	Debt securities	Credits, derivatives and others
Other financial assets		-	2,370,982	-	4,593
Loans and receivables - Loans to third parties		-	15,257,553	-	1,587,479
Assets available for sale		-	-	-	-
Total		-	17,628,535	-	1,592,072

2017

Categories	Classes	Thousands of euros			
		Long-term financial instruments		Short-term financial instruments	
		Equity instruments	Credits, derivatives and others	Debt securities	Credits, derivatives and others
Other financial assets		-	2,207,630	-	7,933
Loans and receivables - Loans to third parties		-	17,207,323	-	3,600,337
Assets available for sale		-	-	-	-
Total		-	19,414,953	-	3,608,270

7.1.1 Long-term and short-term loans to third parties

The breakdown of the financial instruments - long-term and short-term loans to parties, per counterparty and per instrument type, at 31 December 2018 and 2017, is as follows:

	Thousands of euros	
	31/12/2018	31/12/2017
Public Administrations	17,085	12,962
Other resident sectors	1,149,498	1,285,374
Trade credit	-	-
Borrowing with collateral	1,112,022	1,228,989
with mortgage	1,069,421	1,228,989
with other securities	42,601	-
Other term receivables	27,408	30,453
Overdrafts and others	10,068	25,932
Non-resident private sector	-	-
Doubtful loans and credits	19,584,580	22,628,585
Valuation adjustments	(3,906,131)	(3,119,261)
Impairment losses on assets	(5,091,686)	(4,229,552)
Other valuation adjustments - accrued interest pending collection	1,174,179	1,097,874
Others- Capitalised expense - (Note 4.6.2)	11,376	12,417
Total	16.845.032	20.807.660

In 2018 and 2017 the Company has granted no new loans or credit to third parties for any significant amount, except for the drawdowns that the beneficiaries have made on the unused funds available to them, which were also not significant.

Rectifications formalised

As stated in Note 1, in 2017 the Company formalised the rectifications made on financial assets for the amount of 12,101 thousand euros, following the process of reviewing the portfolio of loans and credits transferred by the banks in Group 1 and 2. In 2018 the Company has not made any rectifications affecting its financial asset portfolio.

Financial income

At 31 December 2018, 88.32% of the loan and credit portfolio is indexed to Euribor plus a market spread (88.70% of the total loans and credits at 31 December 2017). Conversely, 11.68% is indexed to fixed interest rates (11.30% at 31 December 2017) - see Note 7.3.3.

In 2018 and 2017, the Company recognised interest arising from its loan and credit portfolio for the amount of 532.685 and 723,818 thousand euros under the heading "Turnover" on the accompanying income statement (see Notes 4.13 and 16.1). That amount includes 350,401 thousand euros (384,089 thousand euros in 2017) corresponding to amounts received in operations offset or partially repaid which were applied to interest following the company's order of priority according to which it gives priority to the cancellation of interest and then to capital; and also 52,793 thousand euros (61,292 thousand euros in 2017) for receiving contractual interest.

Sales of loans and credits

In 2018 the Company has carried out wholesale lending sales for the amount of 376,569 thousand euros, recording a gross positive margin of 25,405 thousand euros (452,427 thousand euros of income and a gross positive margin of 39,262 thousand euros in 2017) (see Note 16.1).

The most significant sales transactions of portfolios in 2018 and 2017 are described below:

2018

Operation "Arco y Argón II": On 27 July 2018, the Company concluded the transfer of 148 loans with first-ranking mortgage. The price established for this portfolio was 25,396 thousand euros, which have been received in full and are recorded under the caption "Turnover" on the accompanying income statement.

Operation "Bidasoá": On 10 October 2018, the sale was concluded for a portfolio of mortgage loans for various properties for the total price of 44,809 thousand euros which is recorded under the caption "Turnover". At 31 December 2018, 3,888 thousand euros are still to be received and recorded under the caption "Trade and other accounts receivable". This portfolio includes a package of properties recorded under the caption "Investment properties" having been assigned a sales price of 1,662 thousand euros (see Note 5).

Operation "Adra": On 5 December 2018, the sale was concluded for a portfolio of 166 mortgage loans on various properties for the total price of 115,217 thousand euros which is recorded under the caption "Turnover". At 31 December 2018, the price was received in full.

On 28 December 2018, the Company sold the portfolio known as "Candanchú", comprising 350 mortgage loans. The sales price for this portfolio was 42,648 thousand euros, which has been received in full and is recorded under the caption "Turnover" on the accompanying income statement.

2017

Operation "Amanda": On 28 June 2017, the Company concluded the transfer of 49 loans with first-ranking mortgage. The price fixed for this portfolio was 63,035 thousand euros, which was received in full and recorded under the caption "Turnover" on the attached income statement.

Operation "Inés": On 19 December 2017, the sale was concluded for a portfolio of mortgage loans on various properties for the total price of 140,125 thousand euros which was recorded under the caption "Turnover". At 31 December 2017, the price was received in full. This portfolio included a package of "Property investments" at a sales price of 2,988 thousand euros.

Operation "Tambo": On 29 December 2017, the sale was concluded for a portfolio of 109 mortgage loans on various properties for the total price of 62,770 thousand euros which is recorded under the caption "Turnover". At 31 December 2017, the price was received in full.

On 29 December 2017, the Company sold 321 mortgage loans. The sales price for this portfolio was 50,192 thousand euros, which was received in full and recorded under the caption "Turnover" on the accompanying income statement.

Margin of recovery of loans and credits

Under this heading the Company records the difference between the amount recovered from loans that have been repaid and/or fully or partially cancelled, and their carrying amount (see Notes 4.13 and 16.1). The order of priority adopted by the Company means that the amounts received are firstly applied to the cancellation of interest and then to capital. The amount of interest received during 2018 and 2017 was 350,401 and 384,089 thousand euros. This has resulted in the recovery of loans and credits in 2018 being a negative figure of 238,296 thousand euros (a negative figure of 220,844 thousand euros in 2017).

Adjustments related to impairment of credit risk

Changes in adjustments related to impairment recorded by the Company in 2018 and 2017 were as follows:

2018

	Thousands of euros			
	Opening balance	Charge	Application	Closing balance
Provision for depreciation of loans and credits	(4,229,552)	(862,134)	-	(5,091,686)
Total	(4,229,552)	(862,134)	-	(5,091,686)

2017

	Thousands of euros			
	Opening balance	Charge	Application	Closing balance
Provision for depreciation of loans and credits	(3,389,356)	(840,196)	-	(4,229,552)
Total	(3,389,356)	(840,196)	-	(4,229,552)

In application of the rules for measurement established by the Bank of Spain Circular 5/2015 for what is known as Financial Assets Unit, in 2018 and 2017, the Company recognised charges for the impairment of its loan and credit portfolio for the

amount of 862,134 and 840,196 thousand euros, respectively, for adjustments related to impairment of credit risk (see Note 4.7.2).

The provision for depreciation of loans and credits for the years 2018 and 2017 is composed of the following:

Type of operation	31/12/2018		31/12/2017	
	Carrying amount (million euros)	Loss / (Gain) (million euros)	Carrying amount (million euros)	Loss / (Gain) (million euros)
With collateral	19,262	2,495	22,126	2,009
Personal guarantee or without	2,586	2,322	2,911	2,620
Allocated to Sareb	5,163	275	4,228	(400)
Totals	27,011	5,092	29,265	4,229

For its part, Note 7.3.1 includes the necessary information on the nature and degree of the credit risk of the portfolio of loans and receivables at 31 December 2018 and 2017 (see Note 4.7.2).

Other information

At 31 December 2018 and 2017:

- The nominal amount of unused credit associated to loan and credit transactions is 1,126,610 and 1,343,553 thousand euros, respectively. Nonetheless, practically all of that unused credit relates to loans that are overdue.
- There are no sales commitments for any significant amount regarding the financial assets appearing under the caption "Loans and credits to third parties".
- There are no lawsuits or seizure proceedings having any significant effect on the figure for long-term and short-term financial investments.

Taking into additional consideration what is described in Note 4.7, the Directors of the Company consider that the book value of the aggregate balances included in this caption of the balance sheet approximates to the fair value.

According to the analysis and updating of the estimates made by the Company, any financial assets classified as doubtful are classified under the caption of non-current financial assets as they are estimated to be recovered within a time horizon longer than twelve months (Note 2.4).

7.1.2 Long-term and short-term financial investments - Other financial assets

The breakdown of the caption "Other financial assets" -both long-term and short-term- on the balance at 31 December 2018 and 2017 is as follows:

Thousands of euros	31/12/2018		31/12/2017	
	Non-current	Current	Non-current	Current
Monetary guarantees from derivative contracts subscribed (Note 13.3)	1,814,900	-	2,186,100	-
Guarantees for leases (Note 6)	4,135	-	4,656	-
Deposits and judicial consignments	17,873	-	15,630	-
Fixed-term deposits	527,249	-	-	-
Other financial assets	6,825	4,593	1,244	7,933
Total	2,370,982	4,593	2,207,630	7,933

Guarantees for leases

Non-current guarantees and deposits mainly correspond to the amounts paid by the lessees which the Company deposits with the Institute of Housing or Chamber of Property pertaining to each Autonomous Region.

Monetary guarantees from derivative contracts subscribed

At 31 December 2018 and 2017, the Company held guarantees for an amount of 1,814,900 and 2,186,100 thousand euros, respectively, from the counterparties with which it has entered into financial derivative contracts (see Note 13.3). Those guarantees will have an interest rate indexed to the Eonia and to 3-month Euribor plus a market spread. Financial income accrued in 2018 and 2017 was insignificant.

The Directors of the Company consider that the book value of the balances included in this caption of the balance sheet approximates to the fair value.

Fixed-term deposits

With the aim of optimising liquidity, at 31 December 2018, the Company has 527,249 thousand euros on deposits and fixed-term deposits in various banks, with maturity at more than 12 months.

Deposits and judicial consignments

At 31 December 2018 and 2017, the Company held deposits and judicial consignments for the amount of 17,873 and 15,630 thousand euros, respectively, mainly as a result of the mortgage foreclosure procedures in which it is involved.

7.2 Breakdown of financial investments with associates

The balance of the accounts under the caption "Long-term investments in associates" at the close of 2018 and 2017 is as follows:

2018

Thousands of euros	31/12/2017	Additions	Amortisations and derecognition	31/12/2018
Financial investments in group companies and associates	18,076	149,096	(3,021)	331,151
Impairment financial investments in associates	(2,209)	(4,698)	-	(6,907)
Total equity instruments	182,867	144,398	(3,021)	324,244
Loans to associates	13,171	-	-	13,171
Impairment loans to associates	(10,004)	(2,823)	-	(12,827)
Total loans to associates	3,167	(2,823)	-	344
Total	186,034	141,575	(3,021)	324,587

2017

Thousands of euros	31/12/2016	Additions	Amortisations and derecognition	31/12/2017
Financial investments in group companies and associates	12,129	173,272	(325)	18,076
Impairment financial investments in associates	(2,427)	-	218	(2,209)
Total equity instruments	9,702	173,272	(107)	182,867
Loans to associates	30,704	-	(17,533)	13,171
Impairment loans to associates	(8,739)	(1,265)	-	(10,004)
Total loans to associates	21,965	(1,265)	(17,533)	3,167
Total	31,667	172,007	(17,640)	186,034

7.2.1. Financial investments in group companies and associates

Group companies

2018

On 4 December 2018, Témopore Properties Socimi, S.A. increased its capital; that increase was fully taken up by the Company through the non-monetary contribution of a portfolio of completed residences rented or available for renting for the amount of 148,834 thousand euros. The carrying amount of the residences transferred was 144,977 thousand euros (see Note 5); that value was increased by a commitment acquired by the Company with that REIT, under which it undertook to assume other refurbishment work on various residences up to a maximum of 2,477 thousand euros.

In addition, the Company made a monetary contribution of 325 thousand euros.

In 2018 the Company sold 237,167 shares in Témopore Properties Socimi, S.A., which represent 0.88% of the share capital of that Company. The total sales price was 2,467 thousand euros, having generated a negative gross margin of 333 thousand euros. Those sales were made to minority shareholders to comply with the requirements established by the Alternative Stock Market (MAB) for that Company to be admitted for listing, which took place on 3 April 2018.

2017

On 7 July 2017, Témopore Properties Socimi, S.A. was incorporated, in which the Company has a 100% interest, through the issue of 60,000 shares each with a nominal value of 1 Euro, all of the same class, fully subscribed and paid up by the Company.

Subsequently, on 24 November 2017, Témopore Properties Socimi, S.A. increased its capital; that increase was fully taken up by the Company through the non-monetary contribution of a portfolio of completed residences available for renting for the amount of 175,458 thousand euros. The carrying amount of that portfolio of residences was 172,055 thousand euros, this being the carrying amount assigned to the 100% holding in the capital of Témopore Properties Socimi, S.A.

In addition to the properties described above, the outstanding lease agreements associated with them were transferred and so were guarantees received for the amount of 644 thousand euros, additional guarantees for the amount of 1,119 thousand euros, deposits with the different official institutions for the amount of 538 thousand euros and the rents received in advance for the amount of 39 thousand euros.

On 1 March 2018, the Board of Directors of Témopore Properties Socimi, S.A. decided to make the application to place the shares of that Company on the Alternative Stock Market (MAB).

Lastly, the debt of lessees associated to the transferred lease agreements was also assigned at no charge for the amount of 380 thousand euros.

Details for Témopore Properties Socimi at 31 December 2018 and 2017 are as follows:

31 December 2018:

Company	Holding	Address	Main activity	Thousands of euros				
				Shares (*)	Issue premium	Other shareholders' contributions	Operating profit/(loss) (*)	Profit / (Loss) after taxes
Témopore Properties Socimi, S.A.	99.12%	Paseo de la Castellana 89, Madrid	Lease of properties	27,073	297,278	1,153	(377)	(384)

(*) Data extracted from the audited annual accounts at 31 December 2018, prepared in accordance with the regulations applicable to each company.

31 December 2017:

Company	Holding	Address	Main activity	Thousands of euros				
				Shares (*)	Issue premium	Other shareholders' contributions	Operating profit/(loss) (*)	Profit / (Loss) after taxes
Témopore Properties Socimi, S.A.	100%	Paseo de la Castellana 89, Madrid	Lease of properties	14,681	160,836	824	(719)	(719)

(*) Data extracted from the audited annual accounts at 31 December 2017, prepared in accordance with the regulations applicable to each company.

Associates

2018

On 3 May 2018, the company sold 4,267,740 preferential subscription rights in the company Quabit Inmobiliaria, S.A., reducing the value of the holding by 222 thousand euros. The registered address of that company is calle Poeta Joan Maragall 1 (Madrid) and its corporate purpose is property development. The share capital of that company is 74,381 thousand euros, with an issue premium of 179,717 thousand euros and other reserves amounting to 40,416 thousand euros. The operating profit/(loss) for 2018 was 29,049 thousand euros of losses and, after tax, the result was a positive figure of 20,338 thousand euros.

At 2018 year-end, the shares of that company were measured on the basis of their quoted price, recording a charge for impairment in the year for the

amount of 2,475 thousand euros taken to the caption "Impairment and profit/(loss) from sales of financial instruments" on the accompanying income statement.

On 20 June 2018, the company acquired a total of 938,226 shares by way of dation from the company Reyat Urbis, S.A., for the amount of 2,223 thousand euros. At 31 December 2018, the value of that holding was fully impaired. The registered address of that company is calle Ayala 3 (Madrid) and its corporate purpose is property development. The main figures have not undergone any relevant changes in 2018.

Also, at 31 December 2018, the Company had a 6.94% holding in the capital of the company Hecesa Internacional, S.L. (whose registered address is in Plaza de Europa 3, Guadalajara and whose corporate purpose is property development). The main figures have not undergone any relevant changes in 2018.

2017

On 15 February 2017, the company sold 4,064,515 preferential subscription rights in the company Quabit Inmobiliaria, S.A., reducing the value of the holding by 325 thousand euros. That sale gave rise to a loss of 122 thousand euros. The registered address of that company is calle Poeta Joan Maragall 1 (Madrid) and its corporate purpose is property development. The share capital of that company is 55,317 thousand euros, with an issue premium of 129,522 thousand euros and other reserves amounting to 27,571 thousand euros. The operating profit/(loss) for 2017 was 14,149 thousand euros of losses and, after tax, the result was a positive figure of 17,487 thousand euros.

At 2017 year-end, the shares of that company were measured on the basis of their quoted price, recording a reversal of the impairment loss of the previous year for the amount of 218 thousand euros taken to the caption "Impairment and profit/(loss) from sales of financial instruments" on the accompanying income statement.

Also, at 31 December 2016, the Company had a 6.94% holding in the capital of the company Hercesa Internacional, S.L. (whose registered address is in Plaza de Europa 3, Guadalajara and whose corporate purpose is property development). The main figures have not undergone any relevant changes in 2017.

Deconsolidated Bank Assets Funds

In 2018 no transactions have been concluded for any significant amount with the FABS, nor were any new vehicles set up.

On 19 September 2017, an agreement was reached with the investment partner of the FAB May in order to liquidate that fund. The agreement reached provided for assigning 5% of the equity corresponding to Sareb to the investment partner in exchange for monetary compensation of 4,800 thousand euros. That amount was recorded under "Turnover" on the accompanying income statement (see Note 4.6.1.)

2018

Company	Holding	Address	Main activity	Thousands of euros			
				Values (*)	Reserves and other equity items	Gross margin (*)	Profit / (Loss) after taxes
1. Unlisted.-							
FAB 2013 Teide	15%	C/ Principe de Vergara 131, Madrid	Property sales and management	87,815	-	1,705	-

(*) Data extracted from the last annual accounts available at 31 December 2018, prepared in accordance with the regulations applicable to each company. At the date of preparation of these annual accounts the annual accounts of that fund were yet to be audited.

2017

Company	Holding	Address	Main activity	Thousands of euros			
				Values (*)	Reserves and other equity items	Gross margin (*)	Profit / (Loss) after taxes
1. Unlisted.-							
FAB 2013 Teide	15%	Pza. Pablo Ruiz Picasso 1, Madrid	Property sales and management	87,815	-	4,164	-
FAB May(**)	-	-	-	-	-	-	-

(*) Data extracted from the audited annual accounts at 31 December 2017, prepared in accordance with the regulations applicable to each company.

In 2015, at the request of the CNMV (Spanish National Securities Market Commission), the FAB Teide and FAB May made a change to their accounting principles consisting of offsetting the profit/(loss) for the year by recording a balancing entry, i.e. an allowance account that reduces the amount of the debt securities issued. That change in the accounting principles had no impact on the annual accounts of the Company.

Non-Deconsolidated Bank Assets Funds

In 2018 and 2017 there were no significant changes nor were any new non-deconsolidated funds set up other than those mentioned above. The most relevant information on those funds is provided below:

2018

Company	Holding	Address	Main activity	Thousands of euros			
				Values (*)	Reserves and other equity items	Gross margin (*)	Profit / (Loss) after taxes
1. Unlisted.-							
FAB 2013 Bull	49%	C/ Principe de Vergara 131, Madrid	Property sales and management	50,364	-	2,459	-

(*) Data extracted from the last annual accounts available at 31 December 2018, prepared in accordance with the regulations applicable to each company. At the date of preparation of these annual accounts the annual accounts of that fund were yet to be audited.

2017

Company	Holding	Address	Main activity	Thousands of euros			
				Values (*)	Reserves and other equity items	Gross margin (*)	Profit / (Loss) after taxes
1. Unlisted.-							
FAB 2013 Bull	49%	Pza. Pablo Ruiz Picasso 1, Madrid	Property sales and management	50,364	-	771	-

(*) Data extracted from the audited annual accounts at 31 December 2017, prepared in accordance with the regulations applicable to each company.

7.2.2. Loans to associates

The changes under that caption in 2018 and 2017 are as follows:

2018

	31/12/2017	Drawdowns	Amortisations	31/12/2018
FAB 2013 Teide	3,167	(2,824)	-	344
Debt securities	13,172	-	-	13,172
Impairment debt securities	(10,005)	(2,824)	-	(12,828)
Credit facility	-	-	-	-
Total	3.167	(2.824)	-	344

2017

	31/12/2016	Drawdowns	Amortisations	31/12/2017
FAB 2013 Teide	19,023	(1,266)	(14,590)	3,167
Credit facility	13,172	-	-	13,172
Deterioro valores deuda	(8,739)	(1,266)	-	(10,005)
Línea de Crédito	14,590	-	(14,590)	-
FAB May	2,942	-	(2,942)	-
Debt securities (Note 7.2.1)	2,881	-	(2,881)	-
Credit facility	61	-	(61)	-
Total	21,965	(1,266)	(17,532)	3,167

In 2017 Fab 2013 Teide repaid in advance the full amount of the credit line taken, of which the amount drawn down was 14,590 thousand euros.

In 2018 and 2017 the Company obtained yields from the debt securities subscribed to in the FAB Teide

for the amount of 3,423 and 1,534 thousand euros, respectively. The total yields obtained from other FABs in 2018 and 2017 were 3,506 and 1,778 thousand euros, respectively (see Note 16.1).

7.3 Information on the nature and risk degree of the financial assets

Risk management is the key principle for achieving the objectives established for the Company, which consist of contributing to the clean-up of the financial system, minimising public funding, settling debts and meeting obligations it assumes in the course of its operations, minimising any possible distortions in the markets that might arise from its actions and selling the assets received, enhancing their value within the time period established and for which the company was set up, while at all times preserving the Company's financial soundness and equity.

The Board of Directors is the governing body responsible for deciding on and approving the general procedures for internal control, as well as the policies on the assumption, management, control and reduction of the risks to which the Company is exposed. Having been assigned the functions delegated by the Board of Directors, the Risks Team and the departments of Network and Direct Management also act in managing risk.

For its part, the Audit Committee, backed up by the department of Internal Auditing and the department of Internal Control and Compliance, is responsible for supervising the effectiveness of the operating procedures and internal control systems, as well as ensuring compliance with applicable regulations.

The Company manages risk on the basis of the principles of independence, the commitment of Senior Management, delegation of functions, proactive management of lending and property investments in order to minimise default and the decreased value of the investments, by monitoring and controlling the positions and technical specialisation, establishing the most suitable tools and methods of risk management and measurement, and ensuring they are uniformly applied.

As a result of the very structure of the Company's opening balance sheet, the main risks to which it is subject are the following:

- Credit risk and the concentration of credit related to the units of financial assets acquired by the Company, and also to certain investments made in the normal course of its business.
- Liquidity risk associated with financial instruments, arising from the lack of availability of the funds necessary for meeting the commitments acquired by the Company at reasonable prices and for continuing with its credit activity.
- Interest rate risk, linked to the likelihood of losses being generated by an adverse trend in market interest rates.
- Operating risk, brought about by losses due to unsuitable or faulty processes, personnel or internal systems, or due to external events.

Considering the type of assets and liabilities of the Company, the exchange rate risk corresponding to potential losses due to the adverse evolution of the prices of assets and liabilities denominated in foreign currency is not significant.

7.3.1 Credit risk

Credit risk is defined as the possibility of loss arising from the total or partial failure of our customers or counterparties to meet their contractual financial obligations, or a deterioration in their credit-worthiness. At 31 December 2018 and 2017, 96% and 95.8%, respectively, of the loan portfolio as a whole was in default. It is managed by the Risks and Business Group according to the policies, methods and procedures approved by the Board of Directors of the Company.

In line with its corporate purpose, the Company's policy centres on managing the portfolios acquired in order to maximise their recoverability through collection or sale. With this, specific procedures are established for the management of credit risk depending on the different characteristics of the financial assets units, according to the definition included in Note 1 above, and of the operations included in each of those categories, based on the:

- Identification, analysis, monitoring of specific risks during the life of the operation until they disappear.
- Measurement and valuation of those specific risks based on the methods established, which are in line with those used for calculating the transfer price of the financial assets units.
- Recovery management of risk operations.

With regard to the business of assets for rent and property sales, the concentration of customer risk is not relevant and there are no significant deferrals of payment for the purposes of credit risk. Furthermore, in the case of deferred payment, it is Company policy to obtain from the customer the guarantees necessary for ensuring the recoverability of the deferred amounts, either through bank guarantees or conditions precedent or subsequent in the public deeds of transfer.

The Company's exposure to credit risk, at 31 December 2018 and 2017, mainly affects the operations recorded in the category of financial assets under "Loans and receivables" (see Note 7.1); its carrying amount, including the contingent unused amounts available of the loans and credits held to date, is the maximum exposure to the credit risk at that date. In this respect, at 31 December 2018 and

2017, the captions "Long-term financial investments - Loans to third and related parties" and "Short-term financial investments - Loans to companies" account for 86.19% and 89.65%, respectively, of the total financial assets of the Company.

Below is relevant information on the profile of credit risk of the investments included in these captions:

Loans to third parties per segment of activity of the beneficiary

The breakdown, at 31 December 2018 and 2017, of the "Long-term and short-term financial investments - Loans to third parties" based on the beneficiary's activities, is as follows:

Thousands of euros	Total		Of which: property collateral (gross of impairment)		Of which: remaining securities (gross of impairment)	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017	31/12/2018	31/12/2017
Public Administrations	24,673	21,020	7,589	8,058	-	-
Financial institutions		-	-	-	-	-
Non-financial companies and individual businessmen	21,82,833	2,926,322	20,441,398	23,354,344	45,796	23,963
Property construction and promotion	20,566,670	23,467,365	19,621,758	22,317,342	3,485	9,089
Civil engineering work	2,294	2,492	1,782	1,981	-	-
Other purposes	1,255,869	1,456,465	817,858	1,035,021	11,312	1,874
Major companies	24,263	28,166	3,339	3,474	-	-
SMEs and individual businessmens	1,231,606	1,428,299	814,520	1,031,547	11,312	14,874
Other residential properties	75,836	77,453	73,202	7,615	-	49
Capitalised expense (Note 4.6.2)	11,376	12,417	-	-	-	-
Impairment losses on assets	(5,091,686)	(4,229,552)	-	-	-	-
Total	16,845,032	20,807,660	20,522,189	23,436,017	45,796	24,012

Actions for recovery - debt restructuring and refinancing:

Within the scope of measures for recovery carried out by the Company, there were various actions aimed at providing beneficiaries with the conditions necessary for meeting the contractual obligations established on the basis of the continuity of their business as the principal guarantee of compliance.

Those actions comprised, amongst others, operations for allocating property as collateral or as dation in payment of debts (see Note 5), liquidating guarantees and operations for debt restructuring and refinancing.

The actions for recovery and, especially in the case of the operations for debt restructuring and refinancing, were carried out based on objective criteria which took into account both the circumstances common to specific loan and credit portfolios, and the specific circumstances of the beneficiaries, such as their economic and financial situation, and also the viability of their business. The main criteria governing the analysis and implementing of these actions for recovery is to provide a solution to the existing payment problems and to avoid postponing them in time, and also to maximise the recoverable value of the assets received.

The debt restructuring and refinancing tools put into effect include modifying the conditions originally arranged with the debtors in respect of maturity periods, interest rates, collateral provided and, in certain circumstances, writing off or partially reducing the amounts owed. The restructuring or refinancing operations involve bringing the transaction completely or partially up-to-date with the payments of the corresponding debts.

In no case has the refinancing of operations involved any adverse effect on the Company's assets in respect of the status of the restructured or refinanced

operations nor any postponement of the recognition of possible losses due to the impairment of those operations in accordance with the circumstances thereof. Therefore, all operations which, in application of the provisions of the regulatory framework applicable to the Company, should be impaired have been considered as such for the purposes of drawing up these annual accounts.

The number and amount of operations refinanced in 2018 and 2017 is as follows:

2018

	Nº operations	Amount (thousands of euros)
Restructured / Refinanced operations	484	1,002,947
Renegotiated / Renewed operations	-	-
Total	484	1,002,947

2017:

	Nº operations	Amount (thousands of euros)
Restructured / Refinanced operations	543	791,249
Renegotiated / Renewed operations	-	-
Total	543	791,249

Geographical distribution of the balance of loans and credits

The geographical distribution, at 31 December 2018 and 2017, of the “Long-term and short-term financial investments - Loans to third parties”, and also of “Cash and other cash equivalents” is as follows:

Thousands of euros	31/12/2018	31/12/2017
Andalucía	2,276,766	2,574,951
Aragón	937,369	1,134,552
Asturias	349,848	428,750
Baleares	448,097	511,219
Canarias	422,875	515,076
Cantabria	406,703	458,725
Castilla - La Mancha	557,736	701,912
Castilla y León	1,405,686	1,582,051
Cataluña	4,220,124	4,804,340
Extremadura	239,405	258,221
Galicia	1,198,928	1,380,256
Madrid	6,639,979	8,336,267
Murcia	1,061,450	1,205,572
Navarra	27,674	36,779
Comunidad Valenciana	4,006,739	4,516,481
País Vasco	245,193	358,223
La Rioja	286,147	335,548
Ceuta and Melilla	22,014	23,497
Other non-resident sectors	-	-
- Others – Capitalised expense (Note 4.6.2)	11,376	12,417
- Impairment losses on assets	(5,091,686)	(4,229,552)
Total	19,672,423	24,945,285
Of which: Cash and other cash equivalents	2,827,391	4,137,625
Of which: Long-term and short-term loans to third parties	16,845,032	20,807,660

7.3.2 Liquidity risk

Liquidity risk is defined as the risk of Sareb not having the resources available for being able to pay its debts on their maturity dates.

The Company periodically and specifically establishes the cash requirements by means of preparing a treasury budget over a 12-month time horizon, which will be updated on a recurring basis with the aim of identifying those cash requirements or surpluses in the short term. Furthermore, for managing the liquidity risk, the general financing requirements in the medium and long term are identified, and also how to address them in a way that is consistent with the business projections.

In any case, the liquidity risk is also mitigated by the power that the Company has for renewing the bonds issued in consideration of the assets transferred by the assigning banks upon their maturity (see Note 13.2).

During the first years of life of the Company, the criteria for prudence have prevailed in managing liquidity, which is intended to be made more versatile. To this end, a procedure has been established for auctioning liquidity between entities to which limits of counterparty risk have been assigned. The auction takes place following the principles established in Sareb of transparency, competition, and maximisation of profitability.

The Board of Directors has also approved a policy for managing the company's liquidity risk which includes regular measuring and monitoring of a series of short-term and of long-term liquidity ratios, and also, where appropriate, implementing contingent measures designed to preserve the Company's liquidity position.

Breakdown of financial investments according to maturity

Following what is mentioned in Note 2.4, the Company considers its financial assets will be recovered in accordance with the schedule of payments contracted, except for those seen to have difficulties - doubtful - (Note 1) which will be recovered in a period in accordance with the updated estimates made by the Company.

Also, under the unilateral option to renew the maturity of the senior debt (Notes 2.4 and 13.2) the Company classifies the probable maturities of that debt according to updated forecasts. The breakdown of the maturities of the Company's financial assets and liabilities at 31 December 2018, is as follows:

2018:

	Thousands of euros						
	Less than 1 year	From 1 to 2 years	From 2 to 3 years	From 3 to 4 years	From 4 to 5 years	Over 5 years	Total
Assets:							
Cash and other cash equivalents	2,827,391	-	-	-	-	-	2,827,391
Financial investments	1,592,072	3,209,979	3,941,766	2,687,485	2,431,712	5,357,593	19,220,607
Loans and credits to third parties	1,587,479	3,209,979	3,941,766	2,687,485	2,431,712	2,986,611	16,845,032
Other financial assets	4,593	-	-	-	-	2,370,982	2,375,575
Financial investments with associates	-	344	-	-	-	-	344
Loans to companies	-	344	-	-	-	-	344
Total at 31 December 2018	4,419,463	3,210,323	3,941,766	2,687,485	2,431,712	5,357,593	22,048,342
Liabilities:							
Long-term and short-term debts	1,983,083	1,974,912	2,630,501	2,879,165	2,906,581	27,554,986	39,929,228
Debentures and other negotiable securities	1,460,962	1,333,830	2,060,153	2,568,334	2,886,178	27,554,986	37,864,443
Amounts owed to credit institutions	15,963	-	-	-	-	-	15,963
Other financial liabilities	441	163,249	174,872	-	-	-	338,562
Derivatives	505,717	477,833	395,476	310,831	20,403	-	1,710,260
Total at 31 December 2018	1,83,083	1,974,912	2,630,501	2,879,165	2,906,581	27,554,986	39,929,228

2017:

	Thousands of euros						
	Less than 1 year	From 1 to 2 years	From 2 to 3 years	From 3 to 4 years	From 4 to 5 years	Over 5 years	Total
Assets:							
Cash and other cash equivalents	4,137,625	-	-	-	-	-	4,137,625
Financial investments	3,608,270	3,508,700	2,769,347	2,271,462	4,464,093	6,401,351	23,023,223
Loans and credits to third parties	3,600,337	3,508,700	2,769,347	2,271,462	4,464,093	4,193,721	20,807,660
Other financial assets	7,933	-	-	-	-	2,207,630	2,215,563
Financial investments with associates	-	-	-	-	-	3.167	3.167
Loans to companies	-	-	-	-	-	3,167	3,167
Total at 31 December 2017	7,745,895	3,508,700	2,769,347	2,271,462	4,464,093	6,404,518	27,164,015
Liabilities:							
Long-term and short-term debts	4,500,711	4,219,612	4,804,941	4,598,661	4,297,067	20,921,677	43,342,669
Debentures and other negotiable securities	3,907,378	3,632,100	4,094,317	4,221,302	4,038,623	20,904,748	40,798,468
Amounts owed to credit institutions	22,947	-	-	-	-	-	2,947
Other financial liabilities	38,666	76,909	296,678	51,681	-	-	463,934
Derivatives	531,720	510,603	413,946	325,678	258,444	16,929	2,057,320
Total at 31 December 2017	4,500,711	4,219,612	4,804,941	4,598,661	4,297,067	20,921,677	43,342,669

The Company's available cash position, at 31 December 2018 and 2017, was 2,827,392 and 4,137,625 thousand euros. This liquidity, together with the cash generated from amortisations, cancellations and sales of loans and credits, the cash generated from sales of real estate assets and from renting Company equity, lead the Directors to being confident that they will have sufficient resources to meet the cash requirements, mainly motivated by the maturity of the senior bonds and the financial expense

incurred. In this respect, it should be pointed out that the Company has the unilateral right to cancel the senior bonds upon their maturity by delivering new senior bonds of similar characteristics, which very significantly reduce the liquidity risk. Furthermore, and if certain circumstances are fulfilled, Sareb has the option of extending the term of the negotiable securities.

7.3.3. Interest rate risk

Structural interest rate risk is defined as being the exposure of the Company to fluctuations in the market interest rates resulting from the varying maturity and repricing dates of assets and liabilities on the balance sheet. Management of the interest rate risk of the balance sheet seeks to keep the Company's exposure within levels in line with its strategy compatible with the Company's business plan and risk profile in the face of changes in market interest rates.

As regards assets, internal tools have been developed which make it possible to simulate cash flows and loan interest according to the contractual conditions on the basis of the information provided by the servicers. These tools allow for the inclusion of scenarios of interest rate variations and assess the impact on future interest flows, taking into account the likelihood of the borrower's creditworthiness.

Liability modelling also makes it possible to simulate the flows of issued debt with the market conditions or simulated scenarios and make an assessment of that debt. To mitigate the Company's strong exposure to changes in interest rates, arising from the high sensitivity of the company's liability and the strong insensitivity of the assets in the face of those changes, in 2013, the Company decided to use derivative instruments to hedge around 85% of the expected outstanding amount of the senior debt during a 9-year time horizon (4-year time horizon at 31 December 2018) with the object of reducing the risk of any increases in interest rates having a significant negative effect on the future income statement. That decision was taken considering that the rates in force at the time of adopting the hedge were compatible with the Company's Business Plan.

Reference interest rates

With regard to the contractual interest rates to which the portfolio of loans and credits acquired is linked, 88.32% (88.7% at 31 December 2017) of them are linked to floating interest rates, 11.68% (11.3% at 31 December 2017) of them are linked to fixed interest rates. Notwithstanding the above, and given that a large part of the portfolio of loans received has the status of non-performing loans, their actual sensitivity to fluctuations in interest rate is very low.

The floating interest rates applied to the above-mentioned amounts are linked to Euribor at different periods plus the corresponding spread. However, the Company accrues interest income on the basis of the provisions of Note 4.13.

Interest rate hedging derivatives

As stated in Note 13.3, the Company has interest rate hedging contracts in place with various financial institutions which make it possible to fix the interest rate of approximately 85% of the senior bonds that are estimated during the next 5 years, thus eliminating the uncertainty in the income statement and the future cash flows for the coming years that would result from the evolution of the reference rates.

The Directors of the Company have assessed the interest rate risk using a probability-based structure such as VAR with a 95% probability of standard deviation and a time horizon of one year. That analysis has concluded that upward fluctuations of 3-month Euribor by 79 b.p. and of the spread to which the company's senior debt is fixed (see Note 13.2) could have a negative impact of 14 million euros in both cases.

8. Inventories

The composition of this caption at 31 December 2018 and 2017, is as follows:

	Thousands of euros	
	31/12/2018	31/12/2017
Completed buildings	19,387	17,327
Units	19,387	17,327
Offices, commercial premises and multi-purpose facilities	-	-
Other properties	-	-
Residences - Other than the borrower's main residence	-	-
Buildings under construction	269,052	217,790
Units	269,052	217,790
Offices, commercial premises and multi-purpose facilities	-	-
Other properties	-	-
Residences - Other than the borrower's main residence	-	-
Advances to suppliers	20,131	33,242
Total	308,570	268,359

Changes in 2018 and 2017 under the caption "Inventories" were as follows:

	Thousands of euros			
	Completed buildings	Buildings under construction	Advances to suppliers	Total
Balance at 31 December 2016	21,764	95,085	33,916	150,765
Additions	-	32,174	33,242	65,416
Derecognition	(1,841)	-	(33,916)	(49,757)
Transfers to completed buildings	11,404	(11,404)	-	-
Transfers to property investments (Note 5)	-	101,935	-	101,935
Balance at 31 December 2017	17,327	217,790	33,242	268,359
Additions	-	50,490	20,131	70,621
Derecognition	(46,571)	(158)	(33,242)	(79,971)
Transfers to completed buildings	48,631	(48,631)	-	-
Transfers to property investments (Note 5)	-	49,561	-	49,561
Balance at 31 December 2018	19,387	269,052	20,131	308,570

The most relevant changes produced in 2018 and 2017 under this caption are itemised as follows:

Additions

In 2018 and 2017 the Company incurred expense amounting to 50,490 and 32,174 thousand euros in building work and in continuing the work in progress. Those amounts were capitalised as the higher value of the inventories at 31 December 2018 and 2017.

Transfers between items

In 2018 and 2017 the Company carried out a detailed analysis of its works in progress with the object of maximising their value. That analysis mainly sought to differentiate those works in progress on which it expects to obtain a higher degree of profitability through building work, development, completion and offering the properties for sale through the retail channel. That analysis involved the Company making transfers from Property investments to Inventories for the amount of 49,561 and 101,935 thousand euros, respectively, in 2018 and 2017.

Rectifications

In 2018 and 2017 no rectifications were made affecting the caption Inventories.

Other information

At 31 December 2018 and 2017, the entire inventory of the Company is unencumbered and free from security rights.

Furthermore, in 2018 and 2017 no financial expense was capitalised as the higher cost of inventories.

As a standard procedure, practically all the presales are subject to indemnity clauses in the case of delayed delivery as they are formalised in contracts in similar terms. The mentioned clauses on indemnity for delay mainly consist of legal interest on the amounts paid during the period between the delivery date scheduled in the contract and the actual delivery date. The Company does not estimate any impact for this reason mainly due to the fact that the delivery date scheduled in the contracts allows for a safety margin of a certain number of months in respect of the anticipated delivery date. For this reason and due to the low number of operations of this kind in 2018 and 2017, the Company has not considered any impact in the annual accounts of 2018 and 2017 for this item. Generally speaking, presales include indemnities in favour of the Company in the event of cancellation by the buyer, although no amount is recorded for this item until contracts are actually terminated for causes not attributable to the Company.

The procedure followed by the Company in relation to guarantees or bank guarantees covering the advance payments received from clients anticipates that all advance payments received from clients are guaranteed. The total of advance payments received from clients as reservation deposits at 31 December 2018 was 22,426 thousand euros (25,843 thousand euros at 31 December 2017).

The Directors of the Company consider that the book value of the balances included in this caption of the balance sheet approximates at least to the fair value (see Note 5).

9. Trade and other accounts receivable

The breakdown of this caption, at 31 December 2018 and 2017, is as follows:

	31/12/2018	31/12/2017
Customer receivables from sales	186,861	180,970
Sundry debtors	14,721	7,938
Doubtful debts	63,047	54,981
Provision for insolvency	(63,047)	(54,981)
Staff	2	8
Current tax assets (Note 15.1)	2,832	1,949
Other receivables from the Public Administrations (Note 15.1)	4,287	5,371
Total	208.703	196.236

The amount recorded by the Company under the caption "Customer receivables from sales" includes the amount still to be received, mainly from property sales and income from leases handled by the Company in 2018 and 2017. In addition, at 31

December 2018, that caption includes the amount still to be received from the sales of the "Ter" and "Garona" portfolios, for the amount of 12,537 and 9,374 thousand euros, respectively.

Changes in the provision for insolvency in 2017 were as follows:

	31/12/2017	Provisions	Applications	31/12/2018
Provision for insolvency	(54,981)	(8,066)	-	(6,047)

It is Company policy to require guarantees for deferred payments, whether guarantees payable on first demand or guarantors with proven solvency

The Directors of the Company consider that the book value of the accounts of trade and other accounts receivable approximates to its fair value.

10. Cash and other cash equivalents

The caption "Cash and other cash equivalents" includes cash and short-term bank deposits with an initial maturity of three months or less.

The breakdown of those assets, at 31 December 2018 and 2017, is as follows:

	31/12/2018	31/12/2017
Other cash equivalents	134,854	1,385,763
Banks	2,692,538	2,751,862
Total	2,827,392	4,137,625

The amount recorded, at 31 December 2018 and 2017, under the caption "Other cash equivalents" corresponds to various fixed-term deposits taken out by the Company for the amount of 134,854 and 1,385,763 thousand euros, respectively, with different banks. While the initial maturity of those deposits is usually set for more than three months, the Company has decided to classify it under that caption as it can opt to repay them in advance with no cancellation charge.

At 31 December 2018, there are no restrictions on the use of cash and other cash equivalents. At 31 December 2017, there was a restriction for an amount equivalent to 8% of the cash generated by the Company since it was incorporated (889,000 thousand euros). That restriction expired during the first quarter of 2018 and the funds were used for repaying the debt as set out in the financing agreements for the Company's senior loan (see Note 13).

In 2018 and 2017, the Company recorded 419 and 2,341 thousand euros, respectively, as interest from those investments, and also the money deposited in current accounts (see Note 16.6). Furthermore, in 2018 and 2017, the Company obtained negative remuneration on various deposits and current accounts. That negative remuneration amounted to 4,942 and 2,419 thousand euros, recorded under the caption "Other financial expense" on the accompanying income statement (see Note 16.5).

11. Equity

11.1 Share capital

At 31 December 2018 and 2017, the Company's share capital is represented by 2,170,440,000 shares, with a nominal value of euros 0.14 each one, respectively, fully subscribed and paid up. These shares all have the same voting and monetary rights.

Below is a list of shareholders having a shareholding equal or greater than 2.5% of the share capital at 31 December 2018 and 2017:

	Holding %	Share capital	Issue premium
Fund for Orderly Bank Restructuring (FROB)	45.90%	139,472	-
Banco Santander, S.A.	22.21%	67,499	-
Caixabank, S.A.	12.24%	37,181	-
Banco de Sabadell, S.A.	6.61%	20,097	-
Kutxabank, S.A.	2.53%	7,698	-
Other shareholders	10.50%	31,915	-
Total	100%	303,862	-

The Company has no knowledge of any other shareholdings of 3% or more in the Share capital or in the voting rights of the Company, or of any which, while lower than the percentage established, allow it to exercise a notable influence over the Company.

As established under article 326 of the Capital Companies Act, once the share capital has been reduced, the legal reserve will have to be funded so that it is again equivalent to 10% of the new capital.

11.2 Legal reserve

The legal reserve is restricted in its use, which is determined by different legal provisions. According to article 274 of the Capital Companies Act trading companies incorporated under that legal form are obliged, if they make profits, to transfer 10% of those profits to a reserve until such reserve reaches one fifth of the subscribed share capital. The purposes for which the legal reserve may be used are to offset losses, or to increase capital, in respect of the portion of the reserve that exceeds 10% of the increased capital, or to be distributed to shareholders in the event of liquidation.

At 31 December 2018 and 2017, the balance of the legal reserve was 19,174 thousand euros in both years.

11.3 Other reserves

The composition of this caption at 31 December 2018 and 2017 is as follows:

Thousands of euros	31/12/2018	31/12/2017
Loss from previous years	(1,227,367)	(662,791)
Voluntary reserves for application RD 4/2016	2,330,270	2,330,270
Restricted reserve	629,428	629,428
Total	1,732,331	2,296,907

11.4 Value change adjustments

This caption of the accompanying balance sheet includes the amount, net of taxes, of changes in the value of financial derivatives designated as cash flow hedging instruments (see Note 13.3) and the amount, net of taxes, arising from the impairment existing in the financial assets unit, in application of the provisions of RD 4/2016 (see Notes 4.7 and 7.1.1.).

The changes in the balance for this caption in 2018 and 2017 are as follows:

2018

	Thousands of euros				
	Opening balance	Reductions for derecognition of tax credits	Reduction for impairment of FA unit	Increases / Decreases	Closing balance
Measurement of derivatives	(1,533,045)	-	-	211,822	(1,221,223)
Impairment of financial assets unit	(4,229,552)	-	(862,134)	-	(5,091,686)
Balance	(5,762,597)	-	(862,134)	211,822	(6,312,909)

2017

	Thousands of euros				
	Opening balance	Reductions for derecognition of tax credits	Reduction for impairment of FA unit	Increases / Decreases	Closing balance
Measurement of derivatives	(1,987,672)	-	-	454,627	(1,533,045)
Impairment of financial assets unit	(3,289,542)	(99,814)	(840,196)	-	(4,229,552)
Balance	(5,277,214)	(99,814)	(840,196)	454,627	(5,762,597)

The equity value adjustments are as follows:

	Thousands of euros	
	31/12/2018	31/12/2017
Interest rate derivatives (Note 13.3)	(1,710,260)	(2,057,320)
Ineffective derivatives	81,963	13,260
Tax effect	407,074	511,015
Value change adjustments – Hedging operations (net of taxes)	(1,221,223)	(1,533,045)
Impairment financial assets unit (see Note 7.1.1)	(5,091,686)	(4,229,552)
Tax effect recognised	-	99,814
Decapitalisation tax credits from previous years	-	(99,814)
Value change adjustments – Impairment of financial assets unit (net of taxes)	(5,091,686)	(4,229,552)
Total value change adjustments	(6,312,909)	(5,762,597)

As indicated in Note 15.3, the Company has derecognised from the balance sheet any tax credits that will not be recoverable over the life of the Company according to its best estimates.

11.5 Equity position of the Company

The equity accountable for the purposes of the mentioned articles 317 and 363.1 e) of the Consolidated Text of the Capital Companies Act is as itemised below, and, therefore, the Company is not involved in any of those circumstances at 31 December 2018:

Thousands of euros	
Equity in the annual accounts of Sareb, S.A. at 31/12/2018	(5,135,891)
Less:	
<i>Value change adjustments for cash flow hedges</i>	1,221,223
<i>Value change adjustments for impairment of financial assets</i>	5,091,686
Equity for the purposes of reduction and dissolution 31/12/2018	1,177,018

are allocated to profit or loss in the corresponding year. The total fair value of this interest rate risk derivative, net of its tax effect, is recognised under the heading "Value change adjustments – Hedging operations". However, from a business perspective and according to the provisions of article 36 of the Code of Commerce, these value changes in the hedging derivative yet to be allocated to the income statement are not considered as equity for the purposes of profit distribution, mandatory reduction of share capital and mandatory dissolution for losses.

In turn, as established by article 2 of RD 4/2016, the Company has recorded the value adjustments of the units of assets established in Circular 5/2015 allocating them to the caption "Value change adjustments – Impairment of financial assets", net of taxes, although the Company decapitalised the tax credits that were capitalised during the year 2017 against that heading on the basis of updated future estimates. As established in that RD the adjustments referred to above will not be considered as equity for the purposes of profit distribution, compulsory reduction of share capital and compulsory dissolution for losses.

It should be mentioned that under prevailing accounting legislation, any changes in the value of hedging derivatives are recognised in equity until they

12. Provisions and contingencies

This caption of the balance sheet, at 31 December 2018 and 2017, includes the long-term provisions set up by Sareb with the object of covering certain liabilities, and also to cover other responsibilities

undertaken by Sareb in the ordinary course of its business, which are reasonably covered. The changes that took place under this chapter of the balance sheet in 2018 and 2017 are shown below:

	Thousands of euros	
	2018	2017
Opening balance for the year	9,530	10,947
Provisions	947	1,203
(Reversal)	(2,615)	(2,620)
Transfers and other changes	-	-
Closing balance for the year	7,862	9,530

The Company is party, as defendant, to certain lawsuits due to the responsibilities inherent to the business it is engaged in. The litigation for which it made provision in 2018 and 2017 are for amounts of little relevance if considered individually, and there are

no others of any particular relevance. In this respect, Sareb makes provision for any likely risks arising from litigation according to the assessment made by its legal advisors.

13. Breakdown of financial liabilities

Below is the breakdown of financial liabilities assumed by Sareb at 31 December 2018 and 2017, classified according to the breakdown required under applicable legislation:

2018

Categories \ Classes	Thousands of euros						Total
	Long-term financial instruments			Short-term financial instruments			
	Amounts owed to credit institutions	Debentures and other negotiable securities	Derivatives and others	Amounts owed to credit institutions	Debentures and other negotiable securities	Derivatives and others	
Debits and items payable	-	36,403,198	338,121	15,963	1,461,245	441	38,218,968
Hedging derivatives	-	-	1,710,260	-	-	-	1,710,260
Total	-	36,403,198	2,048,381	15,963	1,461,245	441	39,929,228

2017

Classes Categories	Thousands of euros						Total
	Long-term financial instruments			Short-term financial instruments			
	Amounts owed to credit institutions	Debentures and other negotiable securities	Derivatives and others	Amounts owed to credit institutions	Debentures and other negotiable securities	Derivatives and others	
Debits and items payable	-	36,891,090	425,268	22,947	3,907,378	38,666	41,285,349
Hedging derivatives	-	-	2,057,320	-	-	-	2,057,320
Total	-	36,891,090	2,482,588	22,947	3,907,378	38,666	43.342.669

13.1 Amounts owed to credit institutions

Furthermore, at 31 December 2018 and 2017 the Company has recognised 15,719 and 15,510 thousand euros respectively under the caption "Amounts owed to credit institutions" as "Accrued interest pending payment" on the hedging derivatives subscribed in 2013 (see Note 13.3).

13.2. Debentures and other long-term and short-term negotiable securities

The composition of the caption "Long-term debts - Debentures and other negotiable securities" and "Short-term debts - Debentures and other negotiable securities" at 31 December 2018 and 2017 is shown below:

Thousands of euros	31/12/2018		31/12/2017	
	Non-current	Current	Non-current	Current
Negotiable securities- Senior debt	3,973,638	1,460,962	35,461,530	3,906,970
Negotiable securities- Subordinated debt	1,429,560	-	1,429,560	-
Accrued interest pending payment	-	283	-	408
Total	36,403,198	1,461,245	36,891,090	3,907,378

Negotiable securities- Senior debt

The breakdown of the balances included under the caption "Negotiable securities- Senior debt" in the previous table at 31 December 2018 and 2017 is as follows:

31 December 2018

Denomination	Issue date	Contractual maturity date	Applicable rate in force	Thousands of euros
SAREB/VAR BO 20191231 2018-2	31/12/2018	31/12/2019	Eur 3m – 0.110%	10,262,600
SAREB/VAR BO 20190228 2018-1	28/02/2018	28/02/2019	Eur 3m – 0.100%	4,064,100
SAREB/VAR BO 20190228 2017-2	28/02/2017	28/02/2019	Eur 3m + 0.070%	5,557,600
SAREB/VAR BO 20190228 2016-2	26/02/2016	28/02/2019	Eur 3m + 0.516%	1,125,800
Total short-term contractual maturities				21,010,100
SAREB/VAR BO 20201231 2018-3	31/12/2018	31/12/2020	Eur 3m + 0.03%	1,647,400
SAREB/VAR BO 20211231 2018-4	31/12/2018	31/12/2021	Eur 3m + 0.05%	1,777,100
Total long-term contractual maturities				15,424,500
Total				36,434,600

31 December 2017

Denomination	Issue date	Contractual maturity date	Applicable rate in force	Thousands of euros
SAREB/VAR BO 20151231 2015-4	31/12/2015	31/12/2018	Eur 3m + 0.389%	3,684,300
SAREB/VAR BO 20161230 2016-4	30/12/2016	31/12/2018	Eur 3m + 0.040%	13,817,100
SAREB/VAR BO 20171229 2017-3	29/12/2017	31/12/2018	Eur 3m – 0.090%	10,262,600
SAREB/VAR BO 20170228 2017-1	28/02/2017	28/02/2018	Eur 3m – 0.010%	4,064,100
Total short-term contractual maturities				31,828,100
SAREB/VAR BO 20160226 2016-2	26/02/2016	28/02/2019	Eur 3m + 0.516%	1,850,000
SAREB/VAR BO 20170228 2017-2	28/02/2017	28/02/2019	Eur 3m + 0.070%	5,690,400
Total long-term contractual maturities				7,540,400
Total				39,368,500

The total amount of negotiable securities, at 31 December 2018 and 2017, is represented by book entries. In addition, they have an irrevocable and unconditional guarantee from the Central Administration, waiving the benefit of excussion.

Sareb has the unilateral option to renew the above-mentioned issues of senior debt upon maturity although at the time of the transaction there were no significant differences between their fair value and nominal value.

That unilateral option, and also its business forecasts and the experience acquired since it was set up, allows the Company to consider that the mentioned short term contractual maturities will materialise in the long term for an approximate amount of 19,549,138 thousand euros.

The interest rates accruing on those bonds are established as 3-month Euribor plus a spread. That spread is the same during the whole life of the issue.

2018

Amortisation of bonds in 2018

The summary of the amortisations of senior debt made by the Company in 2018 is as follows:

Denomination	Amortisation in cash	Amortisation Escrow Account (Note 10)	Amortisation by rectification (Note 1)	Amortisation through new issue	Total
SAREB/VAR BO 20160226 2016-2	514,800	209,400	-	-	724,200
SAREB/VAR BO 20170228 2017-2	90,000	42,800	-	-	132,800
SAREB/VAR BO 20170228 2017-1	-	-	-	4,064,100	4,064,100
SAREB/VAR BO 20161231 2016-4	127,600	42,100	-	-	169,700
SAREB/VAR BO 20151231 2015-4	1,312,500	594,700	-	-	1,907,200
SAREB/VAR BO 20171231 2017-3	-	-	-	10,262,600	10,262,600
SAREB/VAR BO 20161231 2016-4	-	-	-	13,647,400	13,647,400
SAREB/VAR BO 20151231 2015-4	-	-	-	1,777,100	1,777,100
Total	2,044,900	889,000		29,751,200	32,685,100

Rectification of deeds for asset purchases

As stated in Note 1, in 2018 the Company has amortised no bonds due to rectifications.

2017

Amortisation of bonds in 2017

The summary of the amortisations of senior debt made by the Company in 2017 is as follows:

Denomination	Amortisation in cash	Amortisation by rectification (Note 1)	Amortisation through new issue	Total
SAREB/VAR BO 20151231 2015-4	1,425,300	-	-	1,425,300
SAREB/VAR BO 20161230 2016-4	100,900	-	-	100,900
SAREB/VAR BO 20161230 2016-3	-	-	10,262,600	10,262,600
SAREB/VAR BO 20160226 2016-1	-	-	4,073,300	4,073,300
SAREB/VAR BO 20150228 2015-2	-	-	5,704,100	5,704,100
SAREB/VAR BO 20160226 2016-2	671,900	7,600	-	679,500
SAREB/VAR BO 20170228 2017-1	-	9,200	-	9,200
SAREB/VAR BO 20170228 2017-2	-	13,700	-	13,700
Total	2,198,100	30,500	20,040,000	22,268,600

Rectification of deeds for asset purchases

As stated in Note 1, in 2017 the Company amortised the following bonds, on the basis of the rectifications formalised during the year:

Thousands of euros	Banco Mare Nostrum, S.A.	Total
SAREB/VAR BO 20160226 2016-2	7,600	7,600
SAREB/VAR BO 20170228 2017-1	9,200	9,200
SAREB/VAR BO 20170228 2017-2	13,700	13,700
Total	30,500	30,500

Other information

The interest on those negotiable securities accruing in 2018 and 2017 was 4,699 and 5,471 thousand euros, respectively, and is recognised under the heading "Financial expense - For debts with third parties" on the accompanying income statement (see Note 16.5.). At 31 December 2018 and 2017, accrued interest pending payment was 283 and 408 thousand euros and is recognised under the caption "Short-term debts - Debentures and negotiable securities" on the accompanying balance sheet. At the date of preparing these annual accounts that interest has been paid in full.

At 31 December 2018 and 2017, the senior negotiable securities issued by the Company are listed and admitted for trading.

The Directors consider that the carrying amount of the negotiable securities approximates to their fair value.

Negotiable securities - Subordinated debt

The breakdown of the balances included under the caption "Negotiable securities - Subordinated debt" in the previous table, at 31 December 2018 and 2017, is as follows:

31 December 2018 and 2017

	Issue date	Maturity date	Applicable rate in force	Thousands of euros
SAREB/8,00 OBSUBDCONV 20271127 2013	26/02/2013	27/11/2027	8.00%	1,429,560
Total				1,429,560

The principal conditions of the unsecured subordinated debentures which are occasionally convertible is itemised below:

- All the securities belong to a single series, have the same terms and conditions and therefore grant the same rights to their holders. They can be freely transferred and are represented by book entries and have been registered in the accounts ledgers kept by Iberclear and its authorised participants.
- The interest rate accruing on those bonds is fixed and will be due on an annual basis provided that profits have been obtained as established and sufficient reserves being available. For this reason, in 2018 and 2017 the Company has no coupons due or paid for this item due to the difficulty of estimating future distributable cash flows.
- Total amortisation: compulsory on 27 November 2027.
- Partial amortisation: This is possible at the Company's discretion after the fifth year since issue, according to the existing solvency and leverage ratios.
- Conversion: The subordinated debt can be converted to capital in the event of insufficient company equity in the event of: i) cumulative losses equal to or more than the share capital plus the reserves of the Company or (ii) if there are

grounds for dissolution due to the fact that the losses have reduced the equity of the Company to an amount less than half of its share capital. If conversion takes place, the shares will have the same nominal value, be of the same class and series, and will have the same rights as the ordinary shares outstanding and it will be for an amount equivalent to 2% of the Company assets after the conversion. In 2016, after approval from the Shareholders General Meeting held on 5 May 2016, the Board of Directors approved the conversion of 2,170,440 thousand euros to share capital of the Company, by issuing 2,170,440 thousand shares each with a nominal value of 1 Euro. Following that conversion the balance of the subordinated debt was 1,429,560 thousand euros.

- Rank: the convertible subordinated debentures are placed, in terms of credit priority:
 - Behind all other common creditors (senior) of the Company;
 - Pari passu with any subordinated, simple or convertible debt of the Company, issued or to be issued in the future, or that has been incurred or may be incurred in the future under any other title.
 - Ahead of the Company's ordinary or preference shares.

13.3 Derivatives

At 31 December 2018 and 2017, the main source of Sareb's financing came from debentures and negotiable securities issued in 2013 and 2012, or, where appropriate, renewed upon maturity, for the intention of the acquisition of the property and credit assets described in Note 1, which are indexed to floating interest rates. Due to the high volume of the operation and in order to reduce the high exposure and the consequent risk for the Company to a possible rise in the interest rate, on 2 August 2013 the Company contracted an interest rate swap that enabled it to cover this risk for an initial notional amount of 42,221 million euros, which will be gradually reduced upon the maturity of each of the senior bonds hedged in future years, and establishing the debt at fixed interest rates within a range of between 0.491% and 3.145% per year. This operation is not for speculation purposes as it is not considered to be a cash flow hedge and, in reality, it involved converting part of the Company's borrowing during the period covered into borrowing at a fixed interest rate rather than the floating interest rate of the bonds issued.

The cash flow hedging was made in the context of time and market in which the interest rates were compatible with those contemplated in the Company's Business Plan, whereby under this operation a substantial part of it could be assured, reducing the risk that an increase in interest rates could jeopardise the Plan in question and the viability of the Company. In exchange, the operation meant waiving any possible benefits arising from a decrease in the reference interest rates for the portion and the period of time hedged.

The measures for easing monetary policy adopted by the European Central Bank since the end of 2013 have contributed to a gradual decrease in the interest rates which currently stand at historic minimums. That evolution has been transferred to the measurement of the hedging derivative contracted by the Company.

The market value of the interest rate derivatives (swaps) is obtained as the sum of the present value of all cash flows according to the contractual conditions and interest rates quoted on the market. The interest rates used for the future estimation of floating interest rates are obtained from instruments listed in financial markets and indexed to the 3M EURIBOR index. The discount interest rates used for updating cash flows are obtained from instruments listed in financial markets and indexed to the EONIA index.

The balance of the caption "Long-term debts – Derivatives" on the liability side of the balance at 31 December 2018 and 2017 corresponds entirely to the fair value of the mentioned interest rate risk hedging derivative taken out with various financial institutions. The fair value of this derivative, obtained by applying generally accepted measurement methods based on observable market-based inputs, at 31 December 2018 and 2017, is 1,710,260 and 2,057,320 thousand euros, respectively (see Note 11.4).

The breakdown of the amount of the notional value and fair value of these operations, in relation to the time periods in which the cash flows are expected to arise, and the years in which they are expected to have any effect on the income statement, is as follows (in thousands of euros):

INTEREST RATE SWAPS	Fixed rate range	Maturity	2019	2020	2021	2022	2023	Totals
Notional			19,872,000	16,782,000	14,009,000	11,397,000	2,967,000	65,027,000
	2.48%- 3.15%	2019-2023						
Fair value			(505,715)	(477,833)	(395,476)	(310,831)	(20,405)	(1,710,260)

The Company estimates that the effect of a 1 basis point increase in reference interest rates on the market value of those derivatives would have a positive impact of 5,695 thousand euros on the Company's equity. The estimated impact of a downward variation of 1 basis point in the reference interest rates would have a negative impact of a similar figure. That effect was also calculated at the close of 2017, when a positive impact of 7,927 thousand euros on the Company's equity was calculated and with a similar negative effect in the case of a downward variation.

Under accounting legislation in force, any changes in the value of hedging derivatives are recorded in the Company equity until they are allocated to profit or loss in the corresponding year. As set out in Note 4, in 2018 and 2017, the derivatives that hedge bonds issued over one year and part of the bonds issued over two years have maintained their effectiveness within the thresholds required under the Accounting and Measurement Rule 9. 6, but due to the downward trend in interest rates to which the hedged risks are indexed and to Sareb's application in 2018 and 2017 of a "floor" which stipulated that the interest rate could in no event go lower than 0%, it has lost part of that effectiveness. In consequence, the Company has recorded an amount of 68,702 thousand euros of greater financial expense, and 23,312 thousand euros of lower expense resulting from the measurement of those hedging instruments under the caption "Financial expense" of the accompanying income statement (see Note 16.5).

The rest of the value of the derivatives, net of taxes, is recorded under the caption "Value change adjustments" for the amount of 1,221,223 and 1,533,045 thousand euros, respectively, at 31 December 2018 and 2017. This effect, together with the impairment of the financial assets unit, places the Company in negative equity. However, from a business point of view, and according to the provisions of article 36 of the Code of Commerce on the distribution of

profits, the mandatory reduction of share capital and mandatory dissolution for losses, these changes in the value of the hedging derivative yet to be charged to the income statement are not considered as equity.

Similarly, the amount that has been taken to the income statement from equity at 31 December 2018 and 2017 was 640,161 and 525,423 thousand euros, respectively, recorded under the heading "Financial expense – For debts with third parties" (see Note 16.5).

The credit risk associated to derivative operations is minimised through contractual arrangements for exchanging collateral and by other types of guarantee which depend on the nature and type of counterparty, according to the rules of the "International Swaps and Derivatives Association" (ISDA).

At 31 December 2018 and 2017, for the purpose of ensuring compliance with the terms of the derivatives contracts mentioned, Sareb had set up monetary guarantees in the name of the counterparties of the derivatives contracted which at that date showed a negative value for the Company, in the amount of 1,597,400 and 1,968,600 thousand euros, respectively; these are recognised under the caption "Long-term financial investments - Other financial assets" of the balance sheet, and also deposits in the balancing entries for a total amount of 217,500 thousand euros in both years (see Note 7.1.2).

13.4 Other non-current financial liabilities

The breakdown of this caption of the balance sheet at 31 December 2018 and 2017 is as follows:

	Thousands of euros	
	31/12/2018	31/12/2017
Fair value of the Íbero bonds	330,140	411,288
Discount effect on Íbero bonds	968	3,061
<i>Total nominal amount of Íbero bonds</i>	<i>331,108</i>	<i>414,349</i>
Advance FAB 2013 Bull	670	2,626
Guarantees from lessees and Others	6,343	8,293
Total	338,121	425,268

In accordance with the provisions of Accounting and Measurement Rule 9, 5.6 of the General Chart of Accounts, the Company has measured the fair value of the bonds mentioned in Note 1 in relation to the Íbero Project. To calculate that update, the weighted average cost of the Company's debt was taken into consideration (see Note 13.1).

Based on the last estimates provided in the business plan of the FAB 2013 Bull, it is considered that, given its configuration and payment structure, there are 25,015 thousand euros (23,059 thousand in 2017)

of the advance received by the investor in the FAB, which will not be returned during the course of its life. Based on the above, the Company has recorded income under the caption "Financial income" on the accompanying income statement for the amount of 1,956 and 3,889 thousand euros in 2018 and 2017, respectively (see Note 16.6).

The Directors estimate that the fair value of the caption "Other non-current financial liabilities" does not differ from its carrying value.

14. Trade and other accounts payable

The breakdown of this caption of the balance sheet at 31 December 2018 and 2017 is as follows:

	Thousands of euros	
	31/12/2018	31/12/2017
Suppliers	60,049	2,064
Suppliers, invoices pending receipt	349,539	352,005
Staff	7,728	8,545
Current tax liabilities (Note 15.1)	-	-
Other payables to the Public Administrations (Note 15.1)	72,095	50,586
Customer advances	28,890	51,311
Total	518,301	490,511

The caption "Trade and other accounts payable" mainly includes the amounts pending payment for trade purchases and related expense, and the amounts of payments on account from clients received prior to the recognition of the sale of the properties or land.

At 31 December 2018, the caption "Suppliers, invoices pending receipt" includes amounts of 58,373 and 88,135 thousand euros (72,051 and 109,871 thousand euros at 31 December 2017) for expenses arising from management fees and sales commissions, respectively, and 203,031 thousand euros (170,083 thousand euros at 31 December 2017) for general and maintenance expenses of the assets managed by the Company, for which the Company has not received the corresponding invoices.

At 31 December 2018 and 2017, the caption "Customer advances" mainly includes the amounts received in advance on account of future transfers of certain properties included under the captions Property investments and Inventories (see Notes 5 and 8).

The Directors consider that the book value of trade payables approximates to their fair value.

Information on deferral of payments made to suppliers. Third Additional Provision. "Duty to provide information" under Act 15/2010, of 5 July

In accordance with the provisions of the Second Final Provision of Act 31/2014, of 3 December, in amendment of the Third Additional Provision of Act 15/2010, of 5 July, modifying Act 3/2004, of 29 December, which established measures to combat late payment in commercial transactions, and in relation to the information to be included in the Report accompanying the annual accounts on the deferral of payments to suppliers in trade transactions calculated on the basis of the provisions of Resolution of 29 January 2016 of the Institute of Accounting and Account Audits, the breakdown of the average period for payments made by the Company to suppliers in 2018 and 2017 is as follows:

	Year 2018	Year 2017
Average payment period to suppliers	41	34
Ratio of transactions paid	38	33
Ratio of transactions pending payment	65	50
Thousands of euros		
Total payments made	431,970	442,776
Total payments outstanding	60,049	26,651

15. Public Administrations and tax position

15.1 Current balances receivable from and payable to Public Administrations

The composition of the current balances receivable from and payable to Public Administrations at 31 December 2018 and 2017 is as follows:

31 December 2018

	Thousands of euros			
	Assets		Liabilities	
	Non-current	Current	Non-current	Current
Tax Authority deferred VAT	-	14	-	428
Tax Authority VAT/IGIC receivable	-	4,273	-	-
Deferred tax assets	507,152	-	-	-
Provision for taxes	-	-	-	30,781
Tax Authority VAT/IGIC payable	-	-	-	37,673
Tax Authority Personal Income Tax payable	-	-	-	2,582
Tax Authority IGIC payable	-	-	-	89
Social Security payable	-	-	-	542
Corporate Income Tax	-	2,832	-	-
Tax Authority payable/receivable for other tax items	-	-	-	-
Total	507,152	7,119	-	72,095

31 December 2017

	Thousands of euros			
	Assets		Liabilities	
	Non-current	Current	Non-current	Current
Tax Authority deferred VAT	-	29	-	647
Tax Authority VAT/IGIC receivable	-	5,342	-	-
Deferred tax assets	611,046	-	-	-
Provision for taxes	-	-	-	19,833
Tax Authority VAT/IGIC payable	-	-	-	25,755
Tax Authority Personal Income Tax payable	-	-	-	3,203
Tax Authority IGIC payable	-	-	-	626
Social Security payable	-	-	-	522
Corporate Income Tax	-	1,949	-	-
Tax Authority payable/receivable for other tax items	-	-	-	-
Total	611,046	7,320	-	50,586

The balances corresponding to provisions for taxes correspond to the provision made for non-deductible VAT related to the provision for invoices to be received (see Note 14) at year-end 2018 and 2017.

15.2 Reconciliation of accounting profit/(loss) and tax base

The reconciliation of accounting profit/(loss) and the tax base for the tax in question, is as follows:

2018

	Thousands of euros				
	Income statement		Income and expense taken directly to equity		Total
Balances of net income and expense for the period		(878,348)		(550,312)	(1,102,460)
Profit / (Loss)					
	Increases	Decreases	Increases	Decreases	
Corporate Income Tax		(654)	103,940	-	103,286
Permanent differences	4,956	(34,428)	-	-	(29,472)
Temporary differences	-	-	-	-	-
- Originating in the period	79,716	-	446,372	-	199,888
- Originating in previous periods	-	(6,641)	-	-	(6,641)
Tax base (taxable profit/(loss))	84,673	(920,071)	550,312	(550,312)	(835,399)

2017

	Thousands of euros				
	Income statement		Income and expense taken directly to equity		Total
Balances of net income and expense for the period		(564,576)		(485,382)	(1,049,958)
Profit / (Loss)					
	Increases	Decreases	Increases	Decreases	
Corporate Income Tax	30,671	-	251,356	-	282,027
Permanent differences	11,343	(39,373)	-	-	(28,030)
Temporary differences	-	-	-	-	-
- Originating in the period	5,136	-	234,026	-	239,162
- Originating in previous periods	-	(278,752)	-	-	(278,752)
Tax base (taxable profit/(loss))	47,150	(882,701)	485,382	(485,382)	(835,551)

At 31 December 2018 and 2017, the main temporary differences arise from charges to provisions and amortisations, amongst others. For its part, the permanent differences originate in surcharges, penalties, the results contributed by the FABs (see Note 4.7) and exemptions for income resulting from the transfer of certain properties.

The above tables are shown in accordance with the format required by the General Chart of Accounts of 2007. The amounts included under the caption "Income and expense recognised directly in equity" correspond to accounting adjustments not reflected in the tax base for the tax and, therefore are not effectively included in the tax base for Corporate Income Tax for the year.

The relevant tax effects recognised directly in equity at 31 December 2018 and 2017 correspond to the financial derivatives designated as hedging instruments for the amount of 407,074 and 511,015 thousand euros, respectively (see Note 11.4). For its part, the Company derecognised 99,814 thousand euros in equity corresponding to the tax effect associated to the impairment of the financial assets unit.

Shown below is the reconciliation between the expense for Corporate Income Tax booked by Sareb and the result of multiplying the applicable rate for Corporate Income Tax by the total income and expense recognised, before taxes, corresponding to 2018 and 2017:

2018

	(Income) / Expense (Thousands of euros)		
	Income statement	Amounts recognised directly in equity	Total recognised income and expense
Profit / (Loss) before taxes	(879,002)	(446,373)	(1,325,375)
Permanent differences	(29,472)	-	(29,472)
Total	(908,474)	(446,373)	(1,354,847)
Corporate Income Tax rate	25%	25%	
Total	(227,118)	(111,593)	(338,711)
Deductions and credits	(804)	-	(804)
(Profit) / Loss arising from Corporate Income Tax	(227,922)	(111,593)	(339,515)
Adjustment for Corporate Income Tax previous year	-	-	-
Corporate Income Tax non-deconsolidated FABs (Note 4.6.1.)	-	-	-
Adjustment for limitation on tax assets of previous years	-	-	-
Adjustment for limitation on tax assets of the current year	227,268	215,534	442,802
Total (income) / expense recognised in the income statement	(654)	103,940	103,286

2017

	(Income) / Expense (Thousands of euros)		
	Income statement	Amounts recognised directly in equity	Total recognised income and expense
Profit / (Loss) before taxes	(533,905)	(234,026)	(767,931)
Permanent differences	(28,030)	-	(28,030)
Total	(561,935)	(234,026)	(795,961)
Corporate Income Tax rate	25%	25%	25%
Total	(140,484)	(58,506)	(198,990)
Deductions and credits	(813)	-	(813)
(Profit) / Loss arising from Corporate Income Tax	141,297	58,506	199,803
Adjustment for Corporate Income Tax previous year	436	-	436
Corporate Income Tax non-deconsolidated FABs (Note 4.6.1.)	-	-	-
Adjustment for limitation on tax assets of previous years	31,774	99,814	131,588
Adjustment for limitation on tax assets of the current year	140,630	210,049	350,679
Total (income) /expense recognised in the income statement	30,671	251,357	282,028

During the course of 2017, the Company received confirmation from the General Directorate of Taxation of the principles applied and also the principles to be applied in respect of changes in the balance for the provision and account for "Value change adjustments" arising in the future. In this respect, any value adjustments that had been recognised subsequent to 1 January 2016, taken to the "Value change adjustments" account with the intention of increasing the amount of the provision for impairment of the financial assets unit are not considered to be tax-deductible expense. Any reductions in the amount of that provision credited to the account for "Value change adjustments" are disregarded when calculating the profit/(loss) for the year. For this reason, given that, after 1 January 2016, the corresponding charge would not have been considered a tax-deductible expense, it should not be included in the tax base, notwithstanding the comments in the following paragraph.

At 1 January 2016, the balance of the account for "Value change adjustments" included the amount of the provision for impairment of the financial assets unit, recorded at 31 December 2015, net of taxes, with those charges being classified as tax-deductible. Conversely, the charges made as from 1 January 2016 were not classified as tax-deductible. For the purposes of tax treatment of the reduction arising in the provision, and for determining if it relates to charges that were tax-deductible or not, the Company applies a FIFO principle, considering that the amounts reversed relate initially to amounts that were considered to be tax-deductible. Once an amount has been accumulated equal to that included in the tax bases for the tax periods 2012 to 2015 for considering the corresponding charges to be tax-deductible, the reductions in the balance of the provision credited to the account for "Value change adjustments" will not be included in the tax base.

The Company also considers that the increase in the balance for the provision that has been recognised for the year in the "Value change adjustments" account of the Equity of Sareb in application of RD 4/2016 is classified as a non-deductible item. The Company will make every effort to obtain confirmation of the principles mentioned from the Tax Authorities.

On 3 December 2016, Royal Decree-Law 3/2016 of 2 December was published in the Official State Gazette [BOE], under which measures are adopted in the area of taxation intended for the consolidation of public finances and other urgent social measures. That regulation introduces some amendments to the Corporate Income Tax Act 27/2014, of 27 November. It specifically adds the Fifteenth Additional Provision under which it establishes, indefinitely, the offsetting of tax losses up to a limit of 25 per cent of the previous tax base if the turnover for the preceding 12 months was less than 60 million euros.

The Company has analysed the recovery of all the

deferred tax assets based on the Resolution of 9 February 2016, of the Institute of Accounting and Account Audits which implements the standards for accounting, measurement and preparation of annual accounts for the accounting for Corporate Income Tax under tax legislation, including the amendment mentioned and in accordance with the forecasts of the Business Plan, which covers a nine-year time horizon (ten years in 2017).

In consequence, the deferred tax assets recognised by the Company at 2018 year-end, at a rate of 25 per cent (tax rate applicable under Corporate Income Tax), are those thought likely to be applied, according to future taxable profits or through the recovery of the measurement of the financial derivatives contracted by the Company (see Note 15.3). Said calculation was carried out as described considering the time horizon contemplated in its business plan, which anticipates generating future taxable profits to offset the tax assets booked.

The reconciliation between the tax base and the tax payable for Corporate Income Tax for the years 2018 and 2017 is as follows:

	Thousands of euros	
	2018	2017
Tax base (taxable profit/(loss))	(835,399)	(835,551)
Tax base according to tax rate (25%)	(208,850)	(208,888)
Deductions and credits	(804)	(980)
-Of which monetisable	(654)	(667)
Withholdings and payments on account	(2,178)	(1,282)
Tax (receivable) / payable	(2,832)	(1,949)

The breakdown of the tax bases recorded at 31 December 2018 and 2017 is as follows:

2018

	Thousands of euros	At 25 %	Amount capitalised
Tax losses			
2012	200	50	
2013	120,594	30,149	
2014	494,350	123,588	
2015	2,387,698	596,925	6,535
2016	706,118	176,530	5,408
2017	835,348	208,837	50,276
2018	835,399	208,850	-
Total	5,379,707	1,344,929	62,219

2017

	Thousands of euros	At 25 %	Amount capitalised
Tax losses			
2012	200	50	-
2013	120,594	30,149	-
2014	494,350	123,588	-
2015	2,387,698	596,925	6,490
2016	706,118	176,530	5,408
2017	835,551	208,888	68,545
Total	4,554,511	1,136,130	80,443

The above tax losses do not expire and can be offset at any time during the life of the Company.

For its part the Company has the following deductions at 2018 and 2017 year-end:

	Amount of deduction	Expiry date
Deductions for R+D		
2017	817	2035
Total	817	

The whole of the expense for Corporate Income Tax arising in 2018 and 2017 corresponds to ongoing operations.

15.3 Deferred tax assets

The breakdown of the balance of this account at 2018 and 2017 year-end is as follows:

	Thousands of euros	
	2018	2017
Tax credit		
- For tax losses	62,219	80,443
- For unused tax credits	-	-
Temporary differences 2013	2,917	3,966
Temporary differences 2014	12,452	13,062
Temporary differences 2015	723	723
Temporary differences 2016	552	552
Temporary differences 2017	1,284	1,285
Temporary differences 2018	19,931	-
Market valuation of derivatives	407,074	511,015
Others		
Total deferred tax assets	507,152	611,046

With regard to the deferred tax assets recorded as a result of the measurement of the derivatives at market value, the Company estimates they will be reversed against the caption "Value change adjustments" on

the accompanying balance sheet, according to the reversing of the valuation of the hedging derivatives contracted. The Company's provision for reversal is as follows:

Deferred tax assets	2019	2020	2021	2022	2023	Totales
Market valuation of derivatives	120,370	113,733	94,131	73,984	4,856	407,074

Both the prepaid taxes payable and the tax credits for tax losses were recorded on the balance sheet as the Directors consider that, based on their best estimate of the Company's future earnings, including certain tax planning measures, it is probable that these assets will be recovered.

15.4 Years open for inspection

Under current legislation, tax returns cannot be deemed definitive until they have been inspected by the tax authorities or the statute of limitations period has elapsed. At 31 December 2018, the Company has all the taxes submitted applicable to it since its incorporation open for tax inspection. As a result, amongst others, of the different interpretations of

current legislation, additional liabilities could arise in the event of a tax inspection. In any case, the Directors consider that those liabilities, should the case arise, would not have any significant effect on the annual accounts.

At 2018 year-end, the Company has no inspection procedures open with the Tax Authorities.

16. Income and expense

16.1 Turnover

The breakdown per branch of activity at the end of 2018 and 2017 is as follows:

	Thousands of euros	
	2018	2017
Income from sales of loans and credits (Note 7.1.1)	376,569	452,427
Income from interest on loans and credits (Note 7.1.1)	532,685	723,818
Income from sales of property investments (Note 5)	1,154,950	1,109,609
Income from sales of inventories	70,872	22,769
Income from rent (Note 6)	34,831	49,443
Income from remuneration of FABs (see Note 7.2.2)	3,506	1,778
Income from sale and liquidation of FABs (see Note 7.2.2)	2,467	4,800
Recovery of capital gains on loans and credits – net of debt remission (Note 7.1.1)	(238,296)	(220,844)
Total	1,937,584	2,143,800

All the Company's income has been obtained in Spain

In 2018 and 2017, and as a result of the principle of application of the amounts recovered by Sareb from its borrowers, which is applied firstly to interest and then to capital, the figure for "Recovery of capital gains on loans and credits" is negative for the amount of

238,296 and 220,844 thousand euros, respectively. Nevertheless, the total income taking into account the figure for income from interest amounts to 294,389 and 502,974 thousand euros, respectively.

16.2 Cost of sales and changes in Inventories

The composition of this caption of the accompanying income statement is as follows:

	Thousands of euros	
	2018	2017
Changes in inventories	(46,571)	(15,841)
Total changes in inventories	(46,571)	(15,841)
Cost of property investments (Note 5)	(1,009,977)	(962,234)
Sales costs of financial assets (Note 7.1.1)	(351,164)	(413,165)
Sales costs of the FABs (Note 7.2.2)	(2,799)	(2,614)
Total sales costs	(1,363,940)	(1,378,013)

16.3 Staff expense

The breakdown of staff expense for the years 2018 and 2017 is as follows:

	Thousands of euros	
	2018	2017
Salaries, wages and similar	30,504	34,890
Social Security	6,289	5,897
Total	36,793	40,787

The average number of people employed in 2018 and 2017, distributed per category, is as follows:

	Number of employees	
	2018	2017
Senior management	67	66
Managers and Technical staff	270	246
Administration and sales staff	52	61
Total	389	373

Similarly, the distribution according to gender, at 31 December 2018 and 2017, detailed per category, is as follows:

	2018			2017		
	Women	Men	Number of employees	Women	Men	Number of employees
Senior management	17	50	67	15	51	66
Managers and Technical staff	122	154	276	108	150	258
Administration and sales staff	37	14	51	42	21	63
Total	176	218	394	165	222	387

In 2018 and 2017 the Company employed two members of staff with a degree of disability that is 33% or higher.

16.4 External services

The breakdown of this item corresponding to 2018 and 2017 is as follows:

	Thousands of euros	
	2018	2017
Fees for assets management and marketing (Note 1)	203,825	242,926
Leases and ground rents	3,683	3,479
Repairs and conservation	101,633	88,872
Independent professional services	99,779	99,759
Insurance premiums	3,740	4,679
Advertising, publicity and public relations	3,581	2,942
Bank services	670	415
Supplies	11,612	10,983
Other services	7,059	6,509
Total external services	435,582	460,564
Total taxes	217,511	177,766

The caption "Repairs and conservation" in 2018 and 2017 mainly includes the expense of homeowner's associations of the real estate assets, for the amount of 43,213 and 42,388 thousand euros, respectively. The caption "Taxes" mainly contains the cost for Property Tax (IBIs) relating to the Company's the real estate assets and the non-deductible VAT it has paid in 2018 and 2017. That non-deductible VAT is largely charged on procedures for foreclosure and dation formalised by the Company during 2018 and 2017 (see Note 5).

Fees charged by PricewaterhouseCoopers Auditores, S.L. for auditing the Company's separate annual accounts for 2018 and 2017 were 1,115 and 1,133 thousand euros, respectively. In 2018 fees were

charged for other services for the amounts of 13 thousand euros for the issue of the annual report by the external expert in relation to the prevention of money laundering and financing of the terrorism. In 2017 fees were charged for other services amounting to 93 thousand euros which mainly correspond to issuing the annual report of the external expert in relation to the prevention of money laundering and financing of terrorism and also to the issue of a comfort letter in the context of the shares of Tempore Properties Socimi, S.A. being listed on the Alternative Stock Market.

16.5 Financial expense

Below is a breakdown of this caption of the income statement for the years 2018 and 2017:

	Thousands of euros	
	2018	2017
Interest from debentures and other negotiable securities (Note 13.2)	4,699	5,471
Interest from financial derivatives (Note 13.3)	571,524	548,735
Financial expense – Ineffective derivatives (Notes 4.9 and 13.3)	68,702	(23,312)
Other financial expense	16,849	17,600
Total	661,775	548,494

The caption “Other financial expense” mainly includes the finance cost arising from the funding granted by the investor of the FAB Bull 2013 for the amount of 2,380 and 5,066 thousand euros in 2018 and 2017, respectively, which has not been deconsolidated from the accompanying balance sheet (see Note 4.6.1) and the effect of discounting the Íbero bonds

for the amount of 2,093 and 1,517 thousand euros, respectively (see Note 13.4). Furthermore, at 31 December 2018 and 2017, that caption includes 4,942 and 2,419 thousand euros, respectively, arising from the negative remuneration that the Company has obtained on its cash balances (see Note 10).

16.6 Financial income

Below is a breakdown of this caption of the income statement for the years 2018 and 2017:

	Miles de Euros	
	2018	2017
For remuneration from cash and other cash equivalents (Note 10)	418	2,341
For remuneration from “Other financial assets”	1,377	1,366
Other financial income – Rectification (Note 1)	-	44
Other financial income (Note 13.4)	1,956	3,889
Total	3,751	7,640

17. Operations and balances with related parties and legal information relating to the Board of Directors

17.1 Operations with related parties

The breakdown of the balances held and the operations carried out by Sareb with related parties recognised in these annual accounts for the years 2018 and 2017 is as follows:

2018

	Thousands of euros				
	FROB and entities under FROB control.	Significant shareholders	Bank Assets Funds, group companies and other related parties	Board of Directors (*)	Senior Management (*)
Assets:					
Credits and loans	-	-	344	-	-
Long-term investments in Group companies and associates (Note 7.2.1)	-	-	324,244	-	-
Short-term investments in Group companies and associates	-	-	-	-	-
Cash and other cash equivalents	100	-	-	-	-
Liabilities:	-				
Debentures and other long-term negotiable securities	20,852,900	-	-	-	-
Debentures and other short-term negotiable securities	-	-	-	-	-
Gains and Losses:	-				
Income from sales of property investments	-	-	4,609	-	-
Income from services rendered	-		175		
Income from remuneration of FABs	-	-	3,506	-	-
Other operating expense	-	-	380	(1,374)	(4,431)
Impairment of financial instruments	-	-	(7,522)	-	-
Financial income	-	-		-	-
Financial expense	(2,690)	-		-	-
Other operations					
Purchase of property investments	-	-	3,308		
Contingent risks:					
Guarantees given	-	-	-	-	-

(*) Those amounts refer to the remuneration received by the Board of Directors and Senior Management of the Company during 2018 (see Note 17.3).

2017

	Thousands of euros				
	FROB and entities under FROB control.	Significant shareholders	Bank Assets Funds, group companies and other related parties	Board of Directors (*)	Senior Management (*)
Assets:					
Credits and loans	-	-	3,167	-	-
Long-term investments in Group companies and associates (Note 7.2.1)	-	-	182,867	-	-
Short-term investments in Group companies and associates	-	-	-	-	-
Cash and other cash equivalents	101	-	-	-	-
Liabilities:					
Debentures and other long-term negotiable securities	22,126,992	-	-	-	-
Debentures and other short-term negotiable securities	1,061,675	-	-	-	-
Gains and Losses:					
Income from sales of property investments	-	-	-	-	-
Income from remuneration of FABs	-	-	1,778	-	-
Other operating expense	-	-	-	(1,112)	(4,212)
Impairment of financial instruments	-	-	(1,047)	-	-
Financial income	-	-	3,889	-	-
Financial expense	(2,689)	-	(7,784)	-	-
Contingent risks:					
Guarantees given	-	-	-	-	-

(*) Those amounts refer to the remuneration received by the Board of Directors and Senior Management of the Company during 2017 (see Note 17.3).

The variation shown under the caption "Debentures and other negotiable securities" corresponds to the repayments of senior debt made by the Company during 2018 (see Note 13), while the variation undergone in the caption "Credits and loans" corresponds to sales and to cancellations as a result of the ordinary course of business of the Company.

17.2 Transparency in relation to the interests and activities of the members of the Board of Directors

In reference to any situations of conflict of interest, in accordance with the Regulations governing the Board of Directors (article 22) and the Policy on Conflicts of Interest and Related Operations, the Directors have to inform the Board of any situation of direct or indirect conflict between them and the Company's interests.

Once the Company has become aware of existing conflicts of interest, either on its own account or following notification from Directors, and in accordance with the procedure established in the Policy on Conflicts of Interest and Related Operations, the Company shall not provide any information on that transaction to the Directors in question, and they shall not participate in the debate nor vote on the issue giving rise to the conflict of interest.

Under the obligation of preventing situations of conflict with the interest of the Company, during the year the directors who have held office on the Board of Directors have complied with the obligations provided for in article 228 of the Consolidated Text of the Capital Companies Act and in the Company's Policy on Conflicts of Interest and Related Operations. Similarly, both they and any related persons have abstained from falling under any situation of conflict of interest set out in article 229 of that regulation.

17.3 Remuneration and other benefits paid to the Board of Directors and to Senior Management

For the purposes of preparing these annual accounts, Senior Management is taken to be 20 and 19 people at 31 December 2018 and 2017, respectively, of which 13 are men and 7 women (12 men and 7 women at 31 December 2017), who for those purposes are classified as key Sareb personnel. At 31 December 2018 and 2017, the Board of Directors was made up of 15 and 14 people respectively, of which 14 were men and 1 woman (13 men and 1 woman at 31 December 2017).

The amount for salaries, allowances and remunerations of any kind received in 2018 and 2017 by the members of the governing body and Senior Management of the Company was 5,805 and 5,324 thousand euros, respectively, according to the following breakdown:

2018

	Thousands of euros		
	Board of Directors	Senior Management	Total
Fixed remuneration	1,291 ⁽¹⁾	3,743 ⁽³⁾	5,034
Variable remuneration	83 ⁽²⁾	688 ⁽⁴⁾	771
Loyalty Incentive Scheme	-	-	-
Total	1,374	4,431	5,805

- (1) Includes the fixed remuneration at 31 December 2018 for the Executive Director of the Company, for the amount of 385 thousand euros.
- (2) It includes the last third of the variable remuneration for 2016 (32.5 thousand euros), a first third of the variable remuneration for 2017 (25 thousand euros) received in April 2018, and a second third of the variable remuneration for 2017 (25 thousand euros) received in January 2019, leaving the final third of the variable remuneration for 2017 still to be received in the first quarter of 2020. The Executive Director did not receive any variable remuneration for the 2018 financial year.
- (3) This sub-section includes the total information of the 20 members of Sareb Senior Management at 31 December 2018.
- (4) It includes the variable remuneration for 2017 received in 2018. However, as the variable remuneration is spread over the period, 5 of the 20 members of Senior Management have only received the last outstanding third of the variable remuneration for 2016 and two thirds of the variable remuneration for 2017 with the remaining third to be received during the first quarter of 2020. Senior Management received no variable remuneration for 2018.

2017

	Thousands of euros		
	Board of Directors	Senior Management	Total
Fixed remuneration	1,021 ⁽¹⁾	3,534 ⁽³⁾	4,555
Variable remuneration	91 ⁽²⁾	678 ⁽⁴⁾	769
Loyalty Incentive Scheme	-	-	-
Total	1,112	4,212 ⁽⁶⁾	5,324

- (1) Includes the fixed remuneration at 31 December 2017 for the Executive Director of the Company, for the amount of 385 thousand euros. In addition to the fixed remuneration included in this sub-section, the amounts itemised below have been paid as a result of the changes that took place in the Board during 2017: Effective on 13 December, 4 Proprietary Directors resigned from office, of which 3 had received the amount of 245 thousand euros for their services up until that date. The remaining Director did not receive any amount at all, having waived the remuneration due to him for holding office.
- (2) It includes the last third of the variable remuneration of the Executive Director for 2015 (25.5 thousand euros), a first third of the variable remuneration for 2016 (32.5 thousand euros) received in April 2017, and a second third of the variable remuneration for 2016 (32.5 thousand euros) received in January 2018, leaving the final third of the variable remuneration for 2016 still to be received in the first quarter of 2019. Furthermore, the Executive Director is due to receive the amount of 75 thousand euros as variable remuneration corresponding to 2017, which, according to the terms of the Policy on Remunerations for members of the Board of Directors of Sareb, is to be paid over the course of three years.
- (3) This sub-section includes the total information of the 19 members of Sareb Senior Management at 31 December 2017. Furthermore one member of Senior Management who resigned in 2017 prior to 31 December received the amount of 53.7 thousand euros.

- (4) It includes the variable remuneration for 2016 received in 2017; 2 of the 19 members of Senior Management have only received the last outstanding third of the variable remuneration for 2015 and 5 of the 19 members of Senior Management have received two thirds of the variable remuneration for 2016 as the variable remuneration is spread over the period with the remaining third to be received during the first quarter of 2019. This figure also includes the last outstanding third of the variable remuneration of 2015 (36 thousand euros) for two members of Senior Management for whom at that date the variable remuneration was deferred.
- Furthermore, there is a total aggregate amount of 665 thousand euros due to Senior Management for variable remuneration corresponding to 2017, payment of which will be deferred over three years, for those to whom it applied.
- Furthermore, one member of Senior Management who resigned in 2017 prior to 31 December is due 39.8 thousand euros of variable remuneration.

The Company has taken out civil liability insurance for Directors and Executives. Applying the criterion of the General Directorate of Taxation, the premium expense corresponding to each Director is not declared as remuneration in kind.

At 31 December 2018 and 2017, the Company had not given any guarantee or protection clauses in favour of the Executive Directors or members of Senior Management to cover the event of dismissal arising from changes of control in the company or from events depending totally or partially on the will of the board.

The Company has not entered into pension obligations with members of its Board of Directors or Senior Management.

The Company did not grant any advances, loans or guarantees to the members of the Board of Directors or to Senior Management, and it did not make any share-based payments to any members of the Board of Directors, or to Senior Management.

18. Third party guarantees and other contingent liabilities

At 31 December 2018 and 2017, the Company has given the following guarantees to third parties:

	Thousands of euros	
	2018	2017
For challenges to taxes and amounts levied	5,634	5,634
For amounts paid on account by clients	24,353	28,210
For outstanding liabilities on land, developments and others	21,744	16,924
Total	51,731	50,768

The Directors of the Company do not expect any additional liabilities to arise on account of those guarantees.

19. Subsequent events

On 28 February 2019, the Company carried out a simultaneous partial amortisation and novation of the maturity of the senior debt not paid during 2013 for the acquisition of assets in Group 2.

Denomination	Opening balance 2019	Depreciation	Novation	Outstanding amount	Maturity	Applicable rate in force	New ISIN novation
SAREB/VAR BO 20190228 2018-1	4,064,100		4,064,100	4,064,100	28/02/2019	E3M - 0.010	ES0352506259
SAREB/VAR BO 20190228 2017-2	5,557,600	85,700	5,471,900	5,471,900	28/02/2020	E3M + 0.060	ES0352506267
SAREB/VAR BO 20190228 2016-2	1,125,800	419,200	706,600	706,600	28/02/2021	E3M + 0.090	ES0352506275
Total Group 2	10,747,500	504,900	10,242,600	10,242,600			

Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A.

Directors' Report for the year ended

31 December 2018

1. Significant aspects of the period

Previous years

The scale of the challenge facing Sareb from the outset at the end of 2012 was evident from the significance of the figures: 50,781 million euros of assets transferred in the form of nearly 200,000 property and financial assets, over 18,000 borrowers to which more than 400,000 properties as collateral for loans and credit must be added.

This challenge becomes even more evident if seen in relation with the necessary creation of a human and technical structure to overcome the difficulties arising from the technological and commercial dependence of the banks who have transferred the assets. Even more so if those banks have also undergone deviations and shortcomings following their own restructuring processes, whereby in addition to sometimes providing limited information on the assets, their management and marketing of them was not always sufficiently active.

Years 2013 and 2014

In 2013 the recently created Sareb launched an accelerated process of creating an internal structure from scratch (teams, processes, procedures) and a framework of relationships between its departments and the assigning banks that will enable it to tackle the orderly liquidation of the assets received on a continuous basis and in significant volume. This growth in the organisation was accompanied in 2014 by a number of measures aimed at having a better knowledge of the various assets transferred which will allow for more efficient systematic marketing, focussing the action (sales and maintenance) on the more mature and liquid assets. Those measures gave Sareb a more defined commercial momentum in which certain business lines would be built up and streamlined, and above all, it was consolidated as a relevant agent in the institutional market, making a marked contribution to the revitalisation of this sector. Despite the transformations that will be described below, it managed to achieve sales figures in line with its Business Plan.

In any case, the final months of 2014 and a large part of the future operating and commercial structure of the company were marked by the implementation of the Íbero Project with the aim of changing to a professional and vocational model of outsourced management with which the targets would be better identified and brought into line between the parties. The process concluded with the assignment of the different portfolios to the four servicers, as described in Note 1 of the Report, who during the course of 2015, 2016 and 2017 would carry out the procedures for operational migration and management. In parallel to the bidding process, and as part of the agreements entered into, Sareb initiated a process of re-engineering its internal procedures with complex informational projects (Colabora, Medea, Alejandría and Carcasa) which have involved considerable effort over successive years.

2015

The most important aspect of 2015 for Sareb, once the Íbero bidding process was over, were operational migrations from the assigning banks to the new servicers. The complexity of the process (involving 14 migrations) made it a challenge that was satisfactorily resolved, inasmuch as all of them were concluded in the course of that year, except for two that were completed in the first quarter of 2016 and one that was completed in 2017. The technical and organisational efforts focussed on the transition from assigning banks to servicers meant that turnover was inevitably reduced.

To overcome this gap, in terms of marketing, Sareb has undertaken a matrix reorganisation involving a double parameter of products and servicers. The products side directs, guides and stimulates the various lines of business for all the agents, while the servicer side manages the implementation of business proposals and budgets in each servicer. In this way, business activities are monitored and in particular, commercial activities are energised.

As for its operational reorganisation, and under the name of Híspalis, developments started in 2014 were intensified in the critical technological projects

for interaction with the servicers and for internal management. Amongst these we would highlight: Medea – a data warehouse for holding information on operations carried out; Alejandría – a document management system dealing with the company's operations and assets; Colabora - channelling workflows (authorisations, communications, service levels, etc.); and Carcasa – implementing our own accounting system for real estate assets. Those tasks continued in the following years with various improvements depending on the requirements of the business.

A significant event occurred in October when Circular 5/2015 was published by the Bank of Spain. This instruction laid down the central lines of methodology in terms of which the accounting value of Sareb's assets is to be measured (but not necessarily for management which restricts future expectations), the main points of which are set out in this report below. Its primary application called for setting up an important fund in respect of impairment of financial assets, and it would be safe to say that this impairment of asset value originated from when the assets were transferred to Sareb. As it was produced against profits and losses, it consumed all the initial equity and opened up the process of converting subordinated debt into capital in a very significant amount.

2016

2016 saw the consolidation of the technological projects mentioned above and a gradual process of operational gearing with the servicers, which was concluded in 2017. And especially, as a result of the requirements of Circular 5/2015, the work initiated the previous year relating to the information and status of its assets (their legal situation, possession status, location, characteristics, identification, etc.) was completed. By achieving the objective of measuring (and therefore being familiar with) practically the whole portfolio, we were able to improve the management and sale of portfolios, and thus to follow the principle of generating resources and maintaining margins.

Bearing in mind that practically the whole of our portfolio was measured according to the aforementioned Circular, basically in terms of the ECO appraisal parameters, this involved an enormous effort as regards gathering information on the Company's

assets, in addition to the further task of measuring the immense portfolio of both our own and collateral properties (over 400 thousand assets identified in total). Along with these mass-scale refinements, lines of action have been reinforced with respect to refining legal aspects. Monitoring legal proceedings in course for the allocation of assets has been extended, thus broadening and specifying in more detail the underlying information available on loans and collaterals. The systems for monitoring prices and turnover for both the Company and third parties were also upgraded.

Being aware of the limitations of its assets in the condition received and of an evident improvement in the cycle of properties, Sareb implemented a new turn in its organisation, strengthening lines for creating value, with a clear intention for continuity: developing works in progress received as a property asset, support for the termination of building work in properties received as collateral, the transformation into land for development, opting for the renting residential and business properties, and very especially, the opening of a line of residential promotion on land with greater marketing possibilities.

Turnover was stabilised, given that decisions were affected by the regulatory value (as an approximation to the market value). This amount was difficult to beat or even get close to in a good number of the operations carried out.

Nevertheless, towards the end of the year RD 4/2016 was published. This Decree lays down that the impairment fund has to be noted as an equity adjustment rather than being set against the Income Statement. Its retroactive application gave rise to an aggregate re-establishment of shareholders' equity, which had been substantially reduced during the previous year.

2017

In 2017, this change in regulations, while involving an improved equity situation following the return of its shareholders' equity, also brought about a change that had important effects on our business, as it conditions the decisions taken on proposals. The book value for an operation will be that which matches the offer to the acquisition or transfer price, without any value adjustments. Therefore, we have to assess not

only the basic relationship between the offer price and the market price of an asset but the accounting profit/(loss) as well because the company has a limited amount of its own resources which have to be protected. In this regard, it is worth mentioning that the first quarter of the year was affected by operations that had been approved months beforehand under the previous regulations. As these transactions were linked to market values, they gave rise to considerable losses on the books.

Accordingly, during the course of the year selling activities were intensified with a view to focussing on operations with greater margins so as to meet the Company's structural costs. But since it was difficult to generate business (the universe for transactions is limited), sales systems were implemented and promoted by Sareb with the assistance of the servicers. Special mention is made of the "showcases" in which a number of assets are offered to a select group of possible clients involving a competitive setup among them so that, if Sareb sees fit to do so, it can carry out its transactions at the best price on offer. In this way the seed is sown for an open asset market in the future with greater depth and more players.

Moreover, in order to reinforce our lines of value generation noted in previous years, in 2017 a specific Development, Promotion and Investment Area was formally set up, whose first task in that year was to broaden the range of assets to be developed and organise channels for them to be built and marketed. And in the second six-month period, full promotion activity began with different development in strategic locations in cities with more promising demand for new-built property.

Also in 2017, all the work was carried out for creating the T mpore Properties Socimi as a vehicle created to channel our rental properties, but above all as a way of seeking out sales alternatives and energising markets through collective investment schemes. At the end of that year, the first assignment of assets took place, culminating with the company being listed on the alternative stock market (MAB) in April 2018. The commitment to this activity materialised during 2018 with a further assignment of assets, reaching a volume of 324 million euros.

With all of this, the Company's activity reached the figures for volume and margins that enabled it to return to a positive operating margin, even if low.

2018

In terms of business, the year recently ended must be qualified as one of transition and reflection. Transition because during a good part of the year, the basic lines of management are continued (balance between volume and margin generation) and reflection because in the second half-year period, emphasis is placed on defending the Company's value through the creation of value already aimed at the year before, and also by holding back on transactions that do not provide the margin expected from them. In that respect, we held back on the sale of portfolios where little profit would be generated (even losses in some cases) and those which would materialise with considerable discounts.

This shift is due to the fact that, because of changes in legislation, large portfolios of assets with significant discounts are being put on the market which, together with the fact that Sareb's portfolio is older and only part of it has the opportunity for positive, and increasingly smaller, margins, all of which translates as a significant reduction in the volume of transactions, and also lower margins obtained.

Internally, 2018 meant a reinforcement of the specific Development, Promotion and Investment Area. If the previous year served to define the range of assets for promotion, and to organise the channels for the building and marketing of that activity, this year has been for the consolidation of many projects, with building work and sales commencing, and for which the figures for acceptance prior to development have been very successful. For 2019 Sareb has raised the possibility of separating this obvious value-generating instrument as a separate operating activity.

As for the REIT T mpore Properties, as already mentioned above, 2018 saw its listing on the Alternative Stock Market and, above all, the extending of its perimeter with a new assignment of assets, mainly recently allocated developments. Having achieved a significant volume of management, and meeting the targets for management and return that were forecast when it was launched, Sareb feels this is the right moment for placing management in the hands of third parties; this process is expected to be implemented during the course of the first six months of 2019.

Over time it has been seen that part of the targets established at the launch of the Íbero Project have to be reformulated in respect of volume and business margins, and also the expected patterns for managing assets. For this reason, early this year, what is known as the Esparta Project was launched, which, in view of the imminent expiry of some of the servicing contracts, is intended to make a reflection on the future management model, placing the emphasis on the segmentation of the different types of asset and their degree of maturity, and also their future contribution to value. Based on that classification, it is proposed to apply a specific and more professional management model to each one (channel, servicers, procedures, metrics).

This reflection, which has to be materialised in the coming year, can be accompanied by a break with the current model of global servicer at national level whose portfolio under management is the result of the portfolios of the assigning banks being added to the Íbero Project, in order to go forward with a model of suppliers/servicers for each branch of activity. With the same vision, Territorial Centres have been created, not only with the aim of replacing the servicers, but in order to act as driving forces for them (or for any suppliers that might replace them in the future) with greater proximity to the assets. It is clear that this will allow for speedier decision-making in marketing work, based on close-hand knowledge of the assets and also on improved action related to the maintenance and reconditioning of our assets, steering investment toward those showing a higher degree of liquidity.

In any case, the mentioned Esparta Project is backed by a major technological project such as Sareb's implementation of its own applications for administrative and accounting management of the assets, in addition to adding some tools for monitoring sales. These applications, regardless of whether they are operated by our servicers or the future suppliers, ensure Sareb has a framework of independence from third parties, because as all the information (inventory, asset data, operating and marketing actions) go to Sareb systems, the mentioned range of segmentation is opened up, both in portfolios and in providers, without the conditioning factors arising from the current relationship structure.

Encompassed under the name of Ecuador, the main applications on which we have worked during 2018, and continue to do so in 2019, are:

- The **Mare** app which is used with real estate assets. Developed for Sareb in an SAP environment, it came into operation with the migration of the properties from Haya Real Estate in October. During the course of 2019 it is anticipated that all the assets from the other servicers will migrate, while it is possible that some may migrate in the first quarter of 2020.
- The **Capri** app which is used with financial assets. A bidding process was opened and a pre-existing platform contracted (Iris run by the company RSI), which is being introduced into the Sareb systems during the first months of 2019, with the anticipated migration of the different servicers over 2019 and 2020.
- The **GMAO** app for monitoring the maintenance and reconditioning of the Company's properties, which make it possible not only to control but also to send instructions for operators. All the servicers have to be connected to the system during the course of 2019.
- The **Prisma** app as a platform for monitoring the stages of recovery and collection from operations, deeply engrained with the conversion of assets through awards/dations.

The implementation of these operating devices is involving a heavy work load for the Company, although at no time has it affected the amount of business generated, to the extent that all other improvements and innovations in our systems have been orientated towards it.

Regarding the accounts corresponding to 2018 the following facts are worthy of mention:

- Losses before taxes for the year stand at 879 million euros, compared to losses of 534 million in the previous year; as such, in both years the same rules for recognition of the impairment were applied.
- At 31 December 2018 and 2017, in application of the method for measurement established by Bank of Spain Circular 5/2015, the Company set up an impairment fund for its financial assets unit for the amount of 5,091 and 4,229 million euros, respectively. As there is no tax adjustment applicable, the provision for this fund is charged entirely against equity in a specific account for value change adjustments.
- With regard to Turnover, there has been a marked decrease from the 2,144 million euros of the previous year to the 1,938 million of the current year. The amount in terms of gross income for the purposes of management - that is to say, not following an accounting principle - in this year was 3,644 million euros, as opposed to 3,817 in the previous year. A certain asymmetry is observed in its performance in the two blocks of portfolios, in that the figure for property sales has gone up by more than 220 million, while the volume of transactions in loans has gone down by close to 400 million.
- The following aspects are highlighted from the operating profit/(loss):
 - An operating loss of 221 million as against the 7 million of profit in the previous year. This difference is accounted for by the reduction in margins, particularly for financial assets.
 - The expenditure items show a slight upward deviation caused by the tax costs of the growing strategic business of assets conversion (foreclosures, dations and insolvency proceedings), and also by the higher Property Tax on an increasingly growing property asset portfolio. With all other expenses, Sareb continues making an important effort of restraint although for a considerable part of the expenses there is limited possibility of managing their accrual and amount.
- Property sales for the amount of 1,226 million compared to 1,132 million euros of the previous year, with a net margin of 148 million (representing 12% which is very in line with the result of the previous year). The block for residences shares volumes and margins with the other types of assets (land, commercial premises, rentals, etc.). On the other hand, the property segment includes 35 million in income received from rental properties.
- As we already mentioned, the financial assets segment of the business shows lower figures in all of its lines, both in volume and margins. In any case, special mention is made of the line for the cancellation and sale of loans (in which in addition to an 18% reduction in volume there is very little contribution to the operating margin) and the line for income from interest, which went down by around one third. Without doubt this line has most suffered the new market context marked by the large-scale transactions concluded during the year.
- Financial income for a total figure of 293 million euros (503 million euros in 2017), of which 537 million euros (724 million euros in 2017) related to accruals on loans and credits and 243 million euros of loss (221 million euros also of loss in 2017) with recoveries by way of collecting the nominal amounts of loans and credit acquired at a discount. The order of priority of the amounts recovered has to be taken into account, as it is first allocated to unpaid interest, which has brought about the increase under that caption on the income statement, to the detriment of the line of "Margin of recovery of loans and credits".
- The notable downturn in the margin is due both to the assets being sold with less margin (as the scope of assets with a capital gain lessens) and above all by a significant decrease in the interest accruing specifically for Sareb.
- The expense for maintenance, amortisation/ depreciation and structure stands at 765 million euros (762 million euros in the previous year), largely corresponding to the costs of property maintenance, local taxes, homeowner's associations and commissions on the management and sale of assets, as well as the tax costs arising from the foreclosure and

dation procedures that Sareb cannot pass on, which has resulted in the aggregate growth. In any case, except for the tax costs, none of the lines has undergone any significant change. After the summer Sareb began a programme of reduction (in absolute terms) and efficiency (grouping suppliers) in its expense that has made it possible to reduce it as much as is possible under its management. That programme continues to be implemented during the course of 2019, with the result that its main effects will be seen in future years.

From the aspect of cash generation, in its sixth year of existence the Company has managed to generate a cash surplus sufficient for amortising 1,439 million euros of the senior debt in that year in addition to the 605 million that were paid with a charge to the cash of the previous year, and the 889 million of the Escrow Account that has remained stagnant over the 5 preceding years, which was finally applied to reducing debt. All of which after covering the corporate structure expense, the asset maintenance expense and the management and marketing expense, and, particularly, the amount of nearly 645 million of finance charges associated to the senior debt and its hedging derivatives.

Since no rectification was made with the assigning banks in 2018 the Company has reduced the volume of senior debt issued by 2,934 million, which, added to the 11,413 million euros from previous years, brings the amount of reduction to 14,347 million, i.e. 28.2% of the volume of original debt, a percentage that would increase to 29.2% if we take into consideration the amortisation of 505 million made in February 2019, financed from the funds generated in the previous year.

Lastly, it is worth mentioning that the average payment period to suppliers in 2018 was 41 days, as described in Note 14. Payments to suppliers made in a period in excess of 30 days correspond to invoices paid within the periods arranged with those suppliers, and do not exceed 60 days, as established by Act 11/2013 in amendment of the Late Payment Act (Act 3/2004 of 29 December).

2. Foreseeable evolution of the Company

As already mentioned in the previous point, the imminent expiry of the first servicing contracts brings about a deep reflection on the future management of the assets, centring it on two fronts: on the one hand wagering more intensely on conservation and increasing the value of the company's assets even at the cost of assuming sacrifices in the sales figures in the short term; and on the other hand, improved segmentation of our assets, creating sub-portfolios in order to handle them on a more specialised basis, including using specialist suppliers in each category.

As we already said, Sareb has been indicating that the current model of universal servicer can be the object of improvement in terms of sales effectiveness, asset management and, as mentioned, preserving or adding value.

The permanent appeal to a group of assets with a capital gain, which is subject to a marketing management model centred on pressure on transaction prices is a course that is becoming not only increasingly shorter (there are less and less assets) but also narrower (the margin achieved is also less and less).

Meanwhile, regarding the provision of services other than selling, we think it would benefit of a greater emphasis placed on using specialised suppliers for each type of service instead of general servicers.

With this in mind, 2019 is seen as a year for redirecting towards optimising the amount achieved from the sales price, and maintaining and generating value.

To do so, we will go into a deeper, more thorough knowledge and segmentation of the portfolio that will make it possible to focus sales action on the segments that are more likely to result in transactions at competitive prices and very significantly on maintaining a group of assets in our portfolio with an expected trend toward an increase in value (per se or through development) in order to be sold once those improvements are consolidated or at interim moments at prices that fall within that expected trend.

In this process of segmentation and specialisation, the strategic ambition of the Company to consolidate

its own corporate technological infrastructure to which our servicers will migrate becomes an absolute necessity. This will allow us to face the coming years with greater flexibility in decision-making, a framework in which we optimise the efforts for management and information, and with this achieving greater operating efficiency for the Company.

In terms of business, and as a result of this change in strategy, in the short term we expect a more subdued activity in respect of volume which will be balanced by greater requirements for the margins obtained and the investment in assets likely to increase in value. In this scenario, and given the inflexibility of our costs (in respect of which Sareb has little possibility of taking action), and however much the market may evolve positively, we do not expect any improvement in our results in the short term, but we do however expect a positive impact in the medium and long term.

These improvements in information management (more, better, higher quality, more granular) fuel the Company's Business Plan, which better identifies those assets (in segments and groups) upon which commercial activities should be focussed and also serves to facilitate the important development levers for the Company's own real estate assets.

The Business Plan is updated annually. Its time horizon extends to cover the whole life of the Company. It is based on cash flow projections of the Company derived from the orderly divestment of assets according to the amount that is expected to be recovered for each asset as of the date of divestment. That Plan delves deeper into the lines for creating value, which were consolidated in 2018 and which are still being reinforced now; early marketing of those assets that have a limited expectation of price; improvement and refurbishment of assets that show stable increases in price; focalisation of development of the Company's real estate assets where they are more liquid; and reactivating development of land that has well-founded expectations. All this is based on the collection of more and better information on our asset portfolio, as stated above, to the extent that such action does not result in significant negative margins in the accounts.

As in the case of the business plans for previous financial years, this year's Business Plan incorporates in its cash flow projections the effects on equity that may be produced by variations in asset impairment, although these are not included in the Income Statements. Any losses will be incorporated into these cash flows as of the date of divestment. In this way the principle of offsetting the value of the assets and of their long-term measurement is applied to the Business Plan.

With regard to the evolution of the market expected for 2019, it is likely that some symptoms already evident in 2018, such as the geographical fragmentation of the property market, the instability of the Spanish political situation, and a certain slowing down of the domestic economy, could hinder a stable or sustained increase in transactions and prices. To the extent that such concerns can be dispelled, it is anticipated that there will be a reactivation in the crucial block of final domestic buyers, especially as there is beginning to be a reactivation in mortgages, which is a key aspect of any stable growth. The effect on prices will depend on the segment in which that demand takes place, and also on the stiff competition that will arise between the various providers holding extensive stocks of property.

It is clear that some sub-markets (certain municipalities in the provinces of Madrid and Barcelona or the provinces on the Mediterranean coast comprising residences), have been functioning as the driving force behind the escalation of transactions and prices of the last quarters. But it is no less true that this does not apply to the same extent to the rest of the country, and not even within the same provinces. And in any case, these movements are centred on specific segments of location and standard. Their transfer to the Sareb portfolio, with evident differences in respect of geographical areas, uses and age, does then not take place with the same degree of intensity. The more than evident effect of Sareb's competitors should also not be forgotten, with portfolios partly composed of large funds which, with purchases recently made at low prices will give a boost to a market with lower margins.

While Spain is a country that is attractive for international and institutional investors, for Sareb they will play a very limited role as only transactions with lower discounts will be able to take place. That strategy will continue to be promoted through the loan auction platform, in the spirit of promoting greater competition among participants, and prices on the increase.

In any case, we are relying on 2019 producing an improvement in the domestic market which will make it possible to broaden the limited range of our operations with margin. The recent increases in certain geographical locations (Andalusia, Catalonia, Regions of Valencia, Murcia or Madrid), will give a boost to the market for sites, and we will take a more active position in areas where the offer is not saturated or even where the demand is not met, either by the development of promotions or by building on the land.

Consequently, the consolidation of positive expectations in the medium-term macroeconomic environment, the new segmented organisation of the company, the strong operational capacity of our retail sale channels, the improved information on our assets, all allow us to predict a framework of greater possibilities for margin and Company value in the medium term. This perspective materialises for 2019 in the already mentioned optimising of margin, sacrificing the volume of transactions, with the object that the expected future path of prices will bring income greater than that forecast in a framework of immediate implementation. This organisational and sales approach is defensible from an evident programme of segmentation of our portfolio into different blocks of activity and specialisation in the management of each one.

And, of course, in any case, without renouncing our status as one of, if not the principal, stakeholder in the Spanish property market and, most particularly, in the retail segment.

3. Main business risks, risk management and use of financial instruments

In addition to the factors of financial risk and risk management described in Note 7 of the accompanying Report, the Company has in principle identified the following risk factors that might adversely affect our ability to achieve our targets:

- Crisis in the property market (prices, occupation levels, non-payment).
- Decrease in asset values (although recent movements in the property market suggest not just stabilisation but even a steadily upward path).
- Financial and liquidity crisis, which might affect potential buyers of the Company's assets. This risk is mitigated by a certain improvement in the Spanish economy on a macroeconomic level although the effects on potential buyers are not yet clear. At Sareb, we perceive faint signs of a possible rise in interest rates, though more in the medium term than in the short term.
- Effects of possible changes in fiscal/legal legislation. In this report, and particularly in last year's report, we have pointed out the effects of Royal Decrees 3/2016 and 4/2016 in accounting and fiscal terms. As far as Sareb is concerned, possible changes in tax legislation may be important in improving the Company's financial position, especially with regard to better conditions for offsetting tax losses.
- Also, and as already mentioned in this report, those changes in legislation that partially or entirely remove the obligations imposed on shareholders' equity by the Capital Companies Act, could improve the universe of Sareb's sales activity, as it is operates exclusively under the model of market price.
- It cannot be ruled out that regional regulations will extend to the real estate assets (all of which are unoccupied) made available to Sareb, following recent Constitutional Court judgements.

- Once the Íbero process had concluded (migration, taking control) with the servicers, the risks of operational malfunction had gone down noticeably in the past years. Nonetheless, for this and the following years the Esparta Project could bring new operating migration processes which could have an adverse effect on generating business.
- As mentioned in the Report as regards the use of financial instruments for the purpose of interest rate risk hedging, in the 2018 financial year the hedging system that was implemented in 2013 was maintained, the aim of which is to reduce the possible negative impact of a rise in interest rates which might even put the viability of the Company at risk.

In this respect, Sareb is required to update its Business Plan every year for all of its remaining life and to apply the accounting principles and standards in force in its financial reporting. The most recent updating of the Business Plan reflects a change that emphasises the company's strategy regarding the preservation of the financial value of its assets, in accordance with its mandate. Even though the Company's goal is the total divestment of the assets, it has to adapt to the circumstances of the market and to those of the assets themselves in order to protect that value, which, according to the current Business Plan, involves accumulating the stock of assets on the Company's balance sheet toward the end of the period considered in that Plan. It must be considered that the assumptions used and the long-term nature of the projections involve a high degree of uncertainty in the scenario of the Business Plan approved. Based on the actual evolution of the market and of the Company's own ability to divest in accordance with that forecasting, the Company could see its own funds used up in the medium term, although in any case this would not occur during the coming twelve months. In any event, this possible situation would not imply the Company's inability to fulfil its financial and payment commitments. If that situation arises, within the deadlines established in the Capital

Companies Act, the Company and its shareholders should adopt the measures necessary for restoring the balance of equity, one of which, and at an early stage, being converting the Company's subordinated debt (see Note 13). In addition, and on the basis of the necessities that might become evident, the directors

will evaluate additional or alternative measures that will enable it to restore that balance, as well as any others available under commercial legislation. In consequence, based on the above, the Directors of the Company have drawn up these annual accounts based on the going concern principle.

4. Acquisition of own shares

In 2018 the Company had neither carried out no transactions with its own shares nor held any at 31 December 2018.

5. Environment

Given the business in which the Company is engaged, it has no responsibilities, expenses, assets, provisions or contingencies of an environmental nature which could be significant in respect of its equity, financial position and profit or loss. For this reason, no specific disclosures relating to environmental issues are included in this Report.

Consequently the Company considers that it complies substantially with legislation on the protection of the Environment.

6. Staff

Notes 16.3 and 17.3 itemises the number of employees, members of Senior Management and the Board of Directors of the Company at 31 December 2018 and 2017 and the distribution per gender and professional category. This note also gives details of the number of employees with a degree of disability that is 33% or higher.

7. Information on related parties

Note 17 of these annual accounts describes the transactions carried out with related parties.

8. Subsequent events

No further significant events have occurred other than those already mentioned in Note 19 of this Report.

9. Research and Development

No significant investments in research and development were made in 2018 due to the nature of the Company's business.

On 27 March 2019, and in compliance with the requirements established in article 253 of the Capital Companies Act and in article 37 of the Code of Commerce, the Board of Directors of Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria, S.A. has signed off the annual accounts and Directors' Report for the year ended 31 December 2018, which comprise the accompanying documents preceding this statement.

D. Jaime Echegoyen Enríquez de la Orden

Chairman

D. Eduardo Aguilar Fernández-Hontoria

Director

D. Enric Rovira Masachs

Director

D. Javier García-Carranza Benjumea

Director

D. Antonio Cayuela Gil

Director

D. Jorge Mondéjar López

Director

D^a. Francisca Ortega Hernández-Agero

Director

Fondo de Reestructuración Ordenada Bancaria (representada por D. Jaime Ponce Huerta)

Director

D. Jaime Rodríguez Andrade

Director

D. Joseba Iñaki Goikoetxea González

Director

D. Pedro Antonio Merino García

Director

D. Isidoro Lora-Tamayo Rodríguez

Director

D. José Poveda Díaz

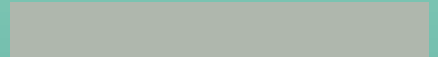
Director

D. Francisco Javier Bartolomé Delicado

Director

D. Juan Ignacio Ruiz de Alda Moreno

Director



For more information, consult the Sareb website www.sareb.es
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*Sociedad de Gestión de Activos
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