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PRESENTATION

Iñigo Velázquez - *Bankia, S.A. - Head of IR & Rating*

(Interpreted) Good morning to all of you, and welcome to the presentation results for the second quarter for Bankia. Just like in previous occasions, the presentation is going to be done by our CEO, Mr. Sevilla; and our Financial Director, Leopoldo Alvear. Without further ado, I'll give the floor to the CEO.

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Perfect. Thank you very much, Iñigo. Let's start this presentation of results. As always, we have certain comments -- general comments on the evolution of the semester, and then we'll talk more specifically about the second quarter.

Let's start with clients. As you can see here, the indicators -- the quality indicators, the internal ones that we use in Bankia, which are the ones that you can see on the graph on the left, but also the external indicators carried out by external people, show that there's an improvement in the feeling that customers have on the service that we provide.

If you remember last year with the integration of BMN, we had a decrease on those indicators. But as you can see in the first half of this year, especially the NPS score for the branches can now be seen to beat historical records. So therefore, we can see greater customer satisfaction that is combined with the growth in everything that has to do with digitization.

As you can see, the amount of digital customers is now close to 50%. Our objective in the strategic plan was to be close to 65% by the end of next year, and we still believe that we will achieve that target.

We've also seen a growth in digital sales, as you can see, especially more in the last year, up to 24.4%. The channel Connect with your Expert remote managers is still growing and has been chosen by increasingly more customers with a growth of 22%. And the customer satisfaction is very high regarding these remote experts.

And also, instant transfers have increased, instant transfers that were launched just about 1.5 years ago. And you can see the intensive market share, 1 of every 3 instant transfers done by the sector is carried out by Bankia. And so the digitization continues to improve and customer satisfaction, together with digitization, is leading to also a growth -- accelerated growth in the number of new customers.

You can see the performance over the last 12 months. This is the graphs that we normally present. We can see the net growth of customers. We have increased by 153,000 new customers in the last 12 months. And maybe something that is even more important than that are those customers with direct income deposits to whom we will be able to sell other products like consumer loans, mortgages, et cetera. They have also increased and they are now at 144,000 in the last 12 months. And we can see that there is an increase accelerated trend that started in 2018 and is still increasing.

We can also confirm what we saw the previous quarter, the growth of performing credit stock, including home mortgages, plus consumer lending, companies and real estate developers. Over the last few years, we had a decrease year-on-year in terms of performing credit that happened in 2016, in 2017, in 2018. You can see how in the first semester that credit figure decreased. And in this semester, following on the trend of the first quarter, we can see an increase on performing credit stock.

On the right, you can see the year-on-year variations of the different segments. And all in all, we are still in a process in which the fall of the mortgages is offset greatly by growth in lending to companies, consumer lending and to developers. So good news from the point of view of credit performance.

And if we look at credit and we break it down into different elements, you -- we can see here the image for mortgages. We can find new mortgages that were awarded in the second quarter and the first quarter of the year. As you can see, for the total of the semester, there is a growth of 5.4%.

The second quarter, new mortgages have been somehow affected by the change on the new mortgage law. That means that for new mortgages, we have to have a waiting period of approximately 11 days. And that has meant that in the second half of June, once the new regulation came into force, there were fewer new mortgages due to this waiting period. So we calculate that that could account to a total of EUR 100 million of turnover that would have taken us to growth of over 10% year-on-year.

These new mortgages will continue to recover over the next few months as the new flow of mortgages come and as the new mortgage processes become more stable. We can also see here the new mortgages market share. We continue the fixed rate mortgages at 58%. Between 55% and 60% is -- are right. 34% of the mortgages are to new customers. And as we can see, the loan-to-value indicators are still what we've had in the past, 65% for new mortgages.

Here we can see consumer lending. If you remember, this is the branch consumer lending, consumer lending with clients that have direct deposit with us. And this is consumer lending that is a business, we believe, with low default rates.

New consumer lending grew by 16% this first half of the year compared to last year, more dynamic in the second quarter than in the first quarter. That means that we are growing June-on-June. The consumer lending stock growth is growing at 15.2%, confirming the growth trend that we've had in the past and with our consumer lending stock market share that has grown over the last 12 months at 20 basis points.

It's also been a good semester and a good quarter in terms of companies funding. On the first graph, you see the performing credit stock to companies that is growing at 4.5%, above the trend in the sector, which is still decreasing. That means that the market share, as you can see at the bottom left, the company stock market share has increased by 52 basis points over the last 12 months to 7.57%.

On the top right, you can see the market share of new credit to companies that has grown 96 basis points, and we still have a market share of new creditors above the stock. And as we've said other times, the more dynamic segments in terms of loans are still those related to working capital, COMEX, discount, factoring and reverse factoring.

The first semester was also a very good semester for Bankia in terms of mutual funds. Here you can see that over the last 6 months, the stock for mutual funds managed by Bankia has grown by 8.4%, and this means that in the whole of the semester, we have grown and we have captured over EUR 630 million if we include the first and the second quarter.

With those net new contributions, we've been leaders in the first 6 months. We have been #1 in the sector in terms of net contributions to mutual funds, and that has also meant that our market share has grown in this first 6 months by 24 basis points up to 6.79%.

It's also been a good semester in terms of payment methods and insurance. On the left, you can see the performance of cards turnover that are growing at 14.4% June-on-June, accelerating its growth trend that we had seen over the last few quarters.

At the bottom left, you can see the market share for cards turnover. As you can see, that has grown by 53 basis points over the last 12 months to 12.3%. 12.3% of all purchases done in stores are done with Bankia cards.

And on the right, you can see the insurance performance. In the first quarter, we have seen already a huge leap in our cruising speed that is maintained in the second quarter, and that gives us a growth of 36% for the first half versus the first half of last year with homogeneous growth both for life insurance premiums but also for nonlife insurance premiums.

Just a couple of comments. On the top side of the P&L, here we can see the gross customer margin, and Leo will go into more detail about that. We can see that there is an upward trend in the gross customer margin, and we are now at the highest level. And that can also be seen in the core result.

You know that the core result is a result of net interest income plus fees and commissions minus OpEx. And here we can see that in the last quarter, it has grown by 9%, up to EUR 333 million. The attributable profit for the semester has been EUR 400 million, and that is a return on equity of 6.3% for the first half.

Just a quick comment regarding the NPAs and their performance over the last 18 months. That is, since we launched the strategic plan. In the strategic plan, we had a goal, you can see that on the graph on the left, of reducing by EUR 8.9 billion the total of NPAs. And in -- by June 2019, we have reduced those by EUR 6.9 billion. So nearly EUR 6 billion last year and another additional EUR 1 billion in 2019. That means that we have a more or less stable coverage. And therefore, the NPAs, net of provisions, are also reduced by 43% over the last 18 months. Therefore, we continue with an accelerated growth of NPAs.

And in terms of capital, this semester we can see here the CET1 fully loaded ratio that has increased by 52 basis points, up to 12.91% or 35 basis points if we didn't take into account the unrealized capital gains, which is the internal ratio that we use, up to 12.63%. And we can see that the year-on-year growth are the same when we talk about the total solvency.

And now let's go into the second quarter results.

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) Thank you, Pepe. Good morning. As always, let's first assess the income statement and the balance sheet more specifically.

So let's start with a comparison between semesters, first half of '18 versus first half of '19. We can see the net interest income has gone down by 2.3%, is softening this reduction when we compare it in previous quarters. In previous quarters, we had reductions of 10%. And we expect that as the year progresses, this reduction will net until we get the guidance that we had for the year, which is a net interest income that is very similar to 2018.

We also see that we have a lower result in terms of net trading income due to the following: 2018, we rotated a great amount of the ALCO portfolio; and we also see a reduction on operating expenses that have gone down by 3% due to the crystallization of the synergies with BMN.

At the bottom of the income statement, we can see that the provisions are stable, about EUR 220 million for the 2 semesters, and we can see a profit attributable to the group of EUR 400 million. And the main difference with the first half of 2018 is due to the lower net trading income that I mentioned before.

If we look at the results or the quarterly results, we compare the first quarter of 2019 with the second quarter, we can see there's an increase on net interest income by 2.9%. We believe this performance will continue over the whole 2019. Quarter-on-quarter, we also see a positive advance in net fees and commissions that has grown by 4.8% quarter-on-quarter.

In other revenue, we must think that in the second quarter, the banks in Spain have to include the provisions for the Single Resolution Fund, which, in the case of Bankia, was EUR 64 million.

And at the bottom of the income statement, we can see that the provisions are a little bit higher than in the first quarter because, as we said, in the first quarter, the provisions were very low, only 14 basis points of capital risk, whereas our goal for the year was to be around 20, 25 basis points.

And so we have a profit attributable to the group of EUR 195 million versus the EUR 205 million of the first quarter. Bear in mind that in the second quarter, we have to include the contribution to the Single Resolution Fund that I mentioned before, which was EUR 64 million for Bankia.

When we look at the evolution of the interest margin per quarter, we can see that we are practically at the same level as the second quarter of 2018, bearing in mind that between the first and second quarter of 2018, there was a decrease on the net interest margin, whereas, as you can see, this year, what we have is a positive evolution. From the first to the second quarter, we can see an increase of 2.9%.

What's this saying? Our net interest margin is the greatest of the last 4 quarters, and we expect that this will continue to perform favorably over the next few quarters. This is mainly due to 2 factors. On the one hand, an increase on performing loans. That is increased, as José mentioned. And also, the increase on the customer margin. As you can see, it has increased this quarter by 5 basis points, and it reaches 1.75%.

This increase is due to an increase in the yield of the -- lending yield of the stock that goes from 1% to 1.65%, and that's due to the new lending that is positive. We're generating more consumer loans and more loans to companies. And therefore, that means that the average interest rate for new lending is 2.6%, very much in line with what happened in 2018 and nearly 19 basis points above the average rate of the credit stock that, as you can see, is 1.75%.

As I was saying, we expect that this gross customer margin will continue to increase in the third and fourth quarter of 2019, making sure that there's a great net interest income over the next 2 quarters.

In terms of fees and commissions, we can see a good evolution. We can see that we've had the best quarter in terms of fees and commissions over the last few quarters. Versus the same period of last year, we've increased by 1%. Versus the first quarter of this year, we have increased by nearly 5%.

And what's most important is that this progress is supported -- is based on fees and commissions from products that we consider are of added value. So assets under management very much based on mutual funds but also on insurance and pensions and also payment services that have increased by 12.3% when compared to the first period of last year.

In terms of expenses, we are crystallizing the synergies with BMN, and so the OpEx have gone down by 3% versus the same period of last year. And that means that we have maintained our position -- our competitive advantage versus our peers when we look at that total operating expenses versus risk-weight assets. In our case, this ratio is 2.25%. In the case of our competitors, this ratio is 3.30%. So we have an advantage of 105 basis points. We have 105 bps in RWAs when we compare ourselves to our peers.

And that means that there's a positive advancement in the core result, what Pepe mentioned, the recurring profit of the bank, net interest income plus fees and commission, minus OpEx.

So here, we -- if we look just at net interest income plus fees and commissions, we can see that there is a core result that is the greatest of the last 5 quarters with an advance versus the previous quarter. You know that our result -- our objective for the core result was to be 5% higher than in 2018, and we can see that we are very much in line to achieve the core result that we wanted to achieve. We wanted to be at least 5% higher than in 2018.

At the bottom of the income statement, as you can see, we have the total of provisions of loans and others. We can see a total of EUR 218 million in the first half of '19, very much in line with the EUR 217 million that we obtained in the first half of 2018.

I would like to remind you here that our guidance is to have cost of risk between 20% and 25% -- sorry, basis points in the low 20s. In the first semester, it's 17 basis points, and so in the first quarter, we had a cost of risk that was very low, around 14 basis points.

If you'll remember, what we expected was to more or less repeat in terms of provisions and allocations versus the previous year, excluding one-off provisions that we carried out in the fourth quarter of 2018. And therefore, we consider that we are very much in line with the goal that we have set ourselves.

And finally, we have attributable profit which goes up to EUR 195 million in the second quarter. And for the first half of the year, it's EUR 400 million. And if we look at attributable profit, we can also look at the tangible book value per share. This tangible book value in June 2018 was EUR 4.19 per share. In June 2019, it's EUR 4.23 per share, 1% more. And if we added the dividend that's been paid out, we would have a value -- a tangible book value of EUR 4.35 per share. Therefore, an increase of nearly 4%.

If you look at asset quality, very good evolution, as Pepe was saying, of the NPAs, now reduced by EUR 1 billion in the first half of 2019 down to EUR 9.9 billion. Remember, our goal is EUR 7.9 billion in 18 months' time, so at the end of 2020. And the coverage of NPAs is stable or is slightly increased up to 48.6%.

If we look at the NPA ratio, gross, and to put this into context, remember that when we launched our strategic plan, it was at 12.5%. Nowadays, at the equator of the strategic plan, we are at 7.5%, so we've reduced it by 5 percentage points. And our goal is to reach and to be below 6% in 18 months' time. So to reduce 1.5 percentage points more.

In terms of net NPA ratios, we are 3.8%, and remember that our goal is to be slightly below 3%.

In terms of NPLs, we've also had a very good evolution. We have reduced by EUR 900 million in the first semester. Half-on-half, more or less spread around the 2 quarters, the NPL ratio for the first time is below 6% at 5.7%, and the NPL coverage ratio is kept around 55%.

In terms of liquidity and solvency just quickly, we have seen that this quarter, we have issued EUR 500 million of senior non-preferred debt and EUR 750 million of senior preferred debt. All of this, plus what we did in the first quarter, we have issued within MREL a total of EUR 1.25 billion in eligible instruments in the first half of the year.

In terms of liquidity metrics, we have advanced in deposits, and so our loan-to-deposit ratio is at 90.5%. Remember, 86% of our deposits are in the hands of retailers.

If we look at the liquidity regulatory ratios, we can see that the liquidity coverage ratio is at 185%. Remember that the limit is 100%. Our LCB (sic) [LCR] position is still the same, and we now have an excess of liquidity of EUR 12.2 billion (sic) [EUR 12.1 billion, to which we will add the issuance that we'll carry out over the next 18 months -- or rather 12 months plus the commercial gap in order to return everything by June next year, so in 12 months' time.

In terms of rating, we see that we have advanced 1 notch according to the Fitch rating. Now we are BBB. And in terms of outlook, we've increased our outlook in DBRS, and now we have -- instead of a Stable outlook, we now have a Positive outlook.

Also a very good quarter, instead of -- liquidity and solvency. The solvency ratio, the fully loaded performance, has increased. Here we are -- we have the regulatory ratio plus the dividend that we had paid out last year. So 51% of cash payout.

Additionally -- or with this, we'll get to a ratio of 12.63% in terms of management. If to that we add the unrealized capital gains of the portfolio, we go to 12.99%, which is the regulatory ratio of CET1 fully loaded comparable to our peers. After that, we add the transaction that we signed last Friday and that was published as a relevant fact, we'll be at 12.71% in terms of management ratios or 13% in terms of regulatory ratios. As I said before, comparable to our peers.

We have a leverage ratio of 5.6% and an MREL ratio, when we add the operation on Friday, we'll be at 20.8% (sic) [20.7%]. Remember that our requirement is 23.63% to be obtained by July 2021, so in 2 years' time.

And in terms of capital, well, in a negative context with negative interest rates, we've managed to generate over EUR 1.1 billion of excess capital or 100 basis points over the last 12 months. And this divided by the EUR 354 million that was paid out for the dividend against 2018 results; plus the EUR 515 million, which are due to excess capital over 12%, that is the CET1 fully loaded management ratio for June '19 without capital gains; plus the EUR 203 million, which is 51% of the EUR 400 million profit that we generated in the first semester and that we'll deduce from the capital because that will be saved to be paid out as dividend; and the EUR 65 million that we generated with the transaction that we signed on Friday. So a total of EUR 1.137 billion. Pepe?

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Thank you very much. Just some very brief conclusions. Remind you that 18 months ago, we launched the strategic plan, a strategic plan that had 4 main pillars, 4 great drivers in terms of company management.

The first one was to carry out successfully the integration of BMN that we finished in the first semester of last year. And with that, we have achieved to increase the initial synergies figure and we've also accelerated. I mean instead of 3 years, it's taken us 2 years to -- we will get EUR 190 million in cost synergies, which was about 50% of the cost basis of BMN by the end of 2019.

And to do the integration and also allow for it to be compatible with an acceleration of commercial activity and commercial done activity after the merger. And since June last year, we have seen how quarter-on-quarter we have increased our cruising speed in key segments for us: for company stock, consumer lending stock and mutual funds stock as well as payment services and insurance.

Here we can see the evolution of some of those market shares and the goals that we have set in our strategic plan. The consumer lending stock is growing about the 15% that we had expected even though it's true that the market share growth is a little bit lower because the market is growing faster than we had expected. For companies stock, it's quite the opposite. We are growing at about 5%, and we have set ourselves 7% higher, but we are gaining greater market share in companies stock.

And in terms of mutual funds at the equator of the strategic plan, we have increased 50% we have from -- to 80 basis points that we had set ourselves as a target. So the commercial dynamism is going as expected, and we are very happy with the commercial activity.

The other main issue was to reduce NPAs during the strategic plan. And we have mentioned that of that goal of EUR 8.9 billion, we've already reduced by EUR 6.9 billion. So what we have left to reach our target seems very reasonable for the next 18 months, and we should be well above that figure.

And in terms of capital generation, as Leo mentioned, we had the goal to generate an excess capital of EUR 2.5 billion at a ratio of 12% CET1 fully loaded. In the first 18 months, we have generated EUR 1.137 billion, and we believe that our objective of reaching EUR 2.5 billion will be attainable over the next 18 months.

And so that is all. If that's okay with you, let's go and look at any questions you may have.

QUESTIONS AND ANSWERS

Iñigo Velázquez - *Bankia, S.A. - Head of IR & Rating*

(Interpreted) Thank you very much. So now we go to the Q&A session. (Operator Instructions) First question.

Operator

(Interpreted) Ladies and gentlemen, we'll start the Q&A session. (Operator Instructions) And the first question comes from Alvaro Serrano from Morgan Stanley.

Alvaro Serrano Saenz de Tejada - *Morgan Stanley, Research Division - Lead Analyst*

(Interpreted) I have 2 questions. In terms of outlook for the margin, the Q2 went quite well. But obviously, rates -- there's another expectation in terms of rates. So I would like to know if you could tell us what is your expectation not just for this year but also for the rates for 2020. What is your outlook on that?

And the second question has to do with capital generation. It's still very strong. It's very good. But the other question is the capacity to distribute. You said at some point to -- that an interim dividend could carry out. If I look at the dividend distribution that has taken place, let's imagine the future one for 2019 will be similar to the previous one, there is a huge gap then for the EUR 1.5 billion. Is it realistic to think that we can reach the EUR 1.5 billion, distributing such a significant amount next year?

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Well, thank you very much, Alvaro. Would you like to answer the first question? And I'll answer the second one.

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) Okay. In terms of the margin, as we were saying, we still think that 2019 should be good. We should continue to increase our net interest income quarter-on-quarter. Based on what I said before, on the one hand, we are seeing an evolution of the credit stock that is better than expected.

As we said in the first quarter, our expectation was to have it flat towards the end of the year, and we have managed to increase it from the first quarter. So we are leveraging. And so therefore, all those volumes will accumulate and will provide a yield over the next few quarters. So that is positive. It's a positive issue that we didn't take into account at the beginning of the year.

The mix in terms of profitability is as expected with an average profitability of 2.6% that I mentioned before, well above the back book. So that's also tailwind for us.

And therefore, we will also have wind against us, which will be the interest rate evolution. But as you know, interest rates take time to re-appreciate and to revalue. And so in the third quarter, we'll start seeing some impacts -- negative impact, mainly August, September, and obviously in the fourth quarter, too.

So the global snapshot that we have is that the net interest income will continue to increase in the third and fourth quarter. And therefore, we are within our target to have a net interest income of 2019 that was in line with the one that we obtained in 2018.

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Very good. As for capital generation, I agree. The first half of the strategic plan, these first 18 months of the capital generation has gone really well despite the fact that the interest rate context was worse than expected, and that means that we're optimistic. We believe in the second half of the strategic plan we'll be able to generate that excess capital that we still target.

As for the distribution, I think that, well, the Board will want to see over the next few months not many uncertainties and so the distribution can be done in a cautious and responsible manner. And what are the main things ahead of us? Maybe the only issue that we could mention would be the ruling by the court of Luxembourg regarding the IRPH, that even though it's true that in comparable times that portfolio is small.

But any contingency that could be there, I think it would be good to wait and see if over the next quarter, the general [tone of] mix statement and therefore, we'll feel more comfortable when making any decision for capital distribution. So we'll see over the next few quarters.

Alvaro Serrano Saenz de Tejada - *Morgan Stanley, Research Division - Lead Analyst*

(Interpreted) What about interest rate sensitivity?

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) Oh, yes. I think you know already because we've already mentioned 50 basis points, to summarize, is more or less 3 percentage points of return on own funds or ROE. So 10 basis points are about EUR 60 million the first year and EUR 28 million the second year, just to give you an idea.

Operator

(Interpreted) The next question is by José Abad from Goldman Sachs.

José Maria Abad Hernandez - *Goldman Sachs Group Inc., Research Division - Executive Director*

(Interpreted) I have a question regarding one of the questions that was mentioned before. It has to do with the extraordinary dividend. Pepe, you said that the Board will have to decide. Over the last 2 months, the Bank of Spain has been very voiceful (sic) [vocal] regarding how banks need to strengthen their capital and linking the cash payout, the guidance, to the profitable -- to the attributable profit. So the idea is to strengthen capital as much as possible in a context of slowdown of the economy.

So my question is would it be possible to carry out your capital reinvestment plan to the shareholders? And if you say yes, is still 12% the level after which you can see that there's capital excess? Because the feeling is that maybe that 12% should be higher, it should be more [lies] around 14% such as the target capital of [Nataisha].

And about negative interest rates, I wanted to say that the -- in negative interest rates could you imagine or could you tell us what would be the potential to take that to the deposit base and if you're able to transfer it to SMEs and families?

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) I leave you -- the second question to you.

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Okay. With regard to the extraordinary dividend, the comment by Bank of Spain of strengthening the capital position, whether this is due or not to an economic slowdown, well, I would like to make 2 -- 3 comments about that.

First, when the Bank of Spain talks about strengthening capital, I understand that it means up to certain levels. Our capital ratio, CET1 fully loaded, is the highest of the -- of our peers. So I think the message is more to those who have it below our ratio. We meet without any problems. The P2R that our supervisor has required from us, we don't expect many changes on that.

And it's true when we did a future analysis of our P&L within the internal exercise of the stress tests that we do of our P&L accounts, we have to bear in mind that we have EUR 7 billion less of NPAs versus what we had 18 months ago. And obviously, that generates less volatility, less uncertainty on the future income statement. There's lower sensitivity of our future income statement based on the potential economic cycle.

All in all, we still believe that 12% is an appropriate ratio. We understand that is quite conservative and that above those levels, any capital excess that we generate should be distributed. And there was another question about the interest rate transfer to customers.

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) Well, we have already transferred the negative interest rate, especially to funds and large companies. And obviously, logically, what we're doing is to go deeper into that analysis. And obviously, in this context of interest rates, just like many other institutions, we will have negative interest rates from companies and financial institutions.

José Maria Abad Hernandez - *Goldman Sachs Group Inc., Research Division - Executive Director*

(Interpreted) Leo, what about the percentage of the total of corporate deposits? I guess it will not be 100%, right?

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) No, obviously not. But we have to differentiate between the companies with whom we have transactions and those with whom we don't, those with only deposit amounts of treasuries, so we'll charge them what the Central Bank charges us. And this is -- it will be done on an individual basis. In any case, it's not going to be a very relevant figure. Remember that 85%, 86% of our deposits are in the hands of retailers.

Operator

(Interpreted) Next question comes from the line of Marta Sánchez from Bank of America Merrill Lynch.

Marta Sánchez Romero - *BofA Merrill Lynch, Research Division - Director and Analyst*

(Interpreted) I have a follow-up on the capital. Of the EUR 2.5 billion, how much do you reckon will come from internal rearrangements? And do you know anything about the timing for the positive effect? What's your expectation in terms of operational risk impact of Basel IV? And does it make sense to accumulate capital, bearing in mind there will be an effect in 2022?

And in this environment of interest rates, where do you see the profitability, the bank's profitability? And would it make sense to use the capital -- the excess capital that you have or give it another use, not just distribute it with the shareholders, maybe using it for larger restructuring -- a large restructuring or to buy something else in Spain?

And about ALCO, could you tell us what you expect to be the contribution over the second half of the year, the volumes that you wish to add and the average life and sensitivity to interest rates and strength of the capital?

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Well, it's a very intelligent way of asking 2 questions. You think about ALCO and I'll respond to the others.

You're saying the EUR 2.5 billion, to what extent -- well, their achievement depends of -- on to what extent do they depend on internal models and the timing of those models. Of the capital that we have generated over the last 18 months, I'm not depending much on -- have not depended much on internal models.

In fact, our capital generation has included about 20 basis points of negative effect of the review of the TRIM process, which we believe maybe is exaggerated based on some models that are already quite penalizing. But anyway, this is something that we've mentioned in the past.

We've also had the IFRS 16 effect. And so there are about 30 basis points against us over the last 18 months in terms of internal models. Well, we do not expect this to have those negative effects over the next 18 months in the second half of the strategic plan in itself. That is good news. And also, if the approval of the behavioral model for mortgages gives us additional advantages, then it would be added to all the positive things we've had up to now.

In terms of timing, as we have said, the review process of the NPV model started in June. We have the supervisory team working on it, and we believe that before the end of the year, we'll have some conclusions of that analysis even they are only preliminary conclusions. And we'll share them with you when we have them.

The operational risk effect and Basel IV and to what extent this could require to be more conservative in terms of capital, it's true that within what we call Basel IV, the partner could affect us negatively as that related to operational risk. Here we still have some preliminary calculations, but it also depends on events -- those are considered recurrent or nonrecurrent events in terms of operational risk.

When we put together this analysis of operational risk together with other issues related to Basel IV that mainly affect credit risk globally, what we can see is that the global effect of Basel IV should be quite neutral in our capital ratio.

As for interest rate -- negative interest rates, profitability and the possibility to give another use to the capital with acquisitions or other alternatives. Well, I think that in fact, when we established the strategic plan, what we wanted was to stress that the excess capital was not going to be used for corporate operations like we did with BMN because we thought that we already carried out the operation that we needed to carry out, that we were not going to have opportunities to carry out these type of operations in the future.

And we were very explicit about the fact that the free capital that was generated was to be distributed with shareholders and was not to be used for nonorganic growth operations in the future. That's the scenario that we have. And I think over the next 18 months, that is what we'll see. We don't think we'll have great opportunities in the future to make a profitable use of that capital through nonorganic operations. ALCO?

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) There was one question, right? Or 22? I'm not sure. Regarding the second half of the year, the contribution, well, we gave you guidance that for 2019, we expected the contribution of the portfolio to be about EUR 30 million, EUR 40 million lower than what we had in 2018, and I think it's going to be more or less the same maybe more -- closer to a minus EUR 40 million than minus EUR 30 million. But we do not expect large deviations from that.

As for the volume, we have to -- finished with EUR 25 billion this quarter -- EUR 25 billion and a bit versus the EUR 28 billion that we had in the first quarter. And if we have opportunity, we do not rule out increasing the portfolio volume over the next few quarters as long as the profitability of those are acceptable.

What we are not going to do is to invest in things that have a large profitability but also large risk because we will assess other types of investments, and we believe that they do not give the return that we would ask from an investment by the bank. So the portfolio will continue to be on sovereign bonds.

As for the duration, I think you've asked me about the duration, the life cycle. Well, at fair value, it has a duration of about 1.3 years more or less. The total of the portfolio would be 3.4 years.

And I think you were also asking about the interest rate sensitivity, which is about EUR 9 million at basis points.

Operator

(Interpreted) Next question is from Daragh Quinn from KBW.

Daragh Joseph Quinn - *Keefe, Bruyette & Woods Limited, Research Division - Analyst*

(Interpreted) I had a question about ALCO and also about the margin. About ALCO, I had written down the duration of 3.4 years, you've said. But when we look at the yields of the Spanish bond, in practice how long will the ALCO contribution last? I guess with a yield of 1%, how long in practice will the yield maintain -- be maintained before it goes -- before it changes?

And the second question is a follow-up on the net interest income in the first and second quarter. In 2020, with your credit growth expectation, do you expect to grow in 2020 in net interest income?

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) Okay. Regarding the portfolios, basically as I said, this year the portfolio contribution, in any case, to the net interest income is not very relevant, not very significant. Last year, maybe they contributed by EUR 200 million, net maybe. Net of the income that they provided this year, I don't know, there'd be a reduction of EUR 30 million, EUR 40 million.

For next year, we have EUR 2 billion of -- that will mature. And for the rest of 2019, we do not have any maturities. So the yield that they have currently will be maintained for a few quarters with small variations.

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) As for the net interest income, the guidance we had for the year is maintained for the whole of the year. And NII, that will be more or less flat. This means that we will have a second semester that will be a bit higher than the first semester in terms of NII, and so that will give us a flat result.

If you look at 2020, then we'll do a more fine-tuned budgetary -- budget by -- in September, October. We expect an interest rate cap that will be a little bit more stable even though stability doesn't last too long. And once we have the estimates for 2020 towards the end of the year, we will share it with you.

Operator

(Interpreted) The next question is by Ignacio Cerezo from UBS.

Ignacio Cerezo Olmos - *UBS Investment Bank, Research Division - Executive Director & Equity Research Analyst*

(Interpreted) I had a couple of quick questions. First, regarding the mutual strategy. It's not just about the average stocks that have grown, but it seems that the fees and commission has grown. I would like to know what's behind that.

And also from the point of view of impairments, this has been a first semester that has been quite strong in terms of net trading income and also incredible capital gains at the bottom of the income statement. So I would like to know within total provisions what percentage of non-recurrents can you imagine. Do you think that is -- percentage is nonrecurrent? Or what would be a recurrent figure for the next quarter and the next year?

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Well, regarding mutual funds stock, rather than average -- an improvement on the average commission and fees, what we see is a change in the mix. We launched a year ago the World of Bankia Gestión Experta, which basically goes from the concept of fund by fund to the management of portfolios, and maybe that is increasing our average fees.

But I think mainly, it's due to the volume, due to the average volume that we see in mutual funds. And so as we are able to continue growing in the second half of the year, we should also see how the fees and commissions increase accordingly.

As for total recurrent and nonrecurrent, the idea that I would like to give you is that the guidance that we gave at the beginning of the year was a figure of flat year-on-year except for the sale of the green portfolio, which was about EUR 122 million, if I'm not wrong.

And this first half of the year, if we include all the cleanup and all the structuring and some capital gains due to the sale of some real estate, et cetera, we believe that there will be a similar contribution to the one of the first semester of last year. And the trend is the same, is to remain flat at that level. Obviously, quarter-on-quarter, there'll be some volatility. But when we look at the semester as a whole, it's quite similar to the first half of 2018.

Operator

(Interpreted) The next question is from Carlos Cobo from Societe Generale.

Carlos Cobo Catena - *Societe Generale Cross Asset Research - Equity Analyst*

(Interpreted) I think you've answered quite a lot of the questions that I had. But just a couple of specific questions on provisions and ALCO. Despite the sales that you made in the quarter, the yield for the total portfolio, including the [rep] bonds, is still at 65%, and I would like to know how you've managed to keep the yield and the capital gains. And also...

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) I'm really sorry, the question was not heard.

Operator

(Interpreted) Sorry, we didn't hear the second question.

Carlos Cobo Catena - *Societe Generale Cross Asset Research - Equity Analyst*

(Interpreted) Can you hear me now?

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Yes.

Carlos Cobo Catena - *Societe Generale Cross Asset Research - Equity Analyst*

(Interpreted) I wanted to say that in terms of provisions, I would like to understand why they're still high or higher than expected, the ones for real estate. Even though the market is recovering in terms of price, the appraisals should not demand greater provisions. And the portfolio has gone down.

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) Thank you. Well, regarding the ALCO portfolio, what you mentioned has a yield of 0. So it has no impact. In the ALCO portfolio, what we've done is to sense -- to sell certain things that we had that had a profitability lower than the average. And maybe there's a slight modification on this profitability, but this is quite stable. There's nothing behind it. As I said, the portfolio continues to be on sovereign bonds. We haven't bought a senior debt or non -- senior non-preferred debt. Nothing of that.

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) With regard to the provisions for real estate, 2 comments. First, those provisions are included in expenses related to the management of foreclosed assets, which is quite a relevant figure in that item, tax, expenses, et cetera. And also, the appraisals of the foreclosed assets should increase. And what we're seeing is that a great amount of those appraisals are increasing. But some of them, there are still some segments that are lower.

And over the last 18 months, there's been a review by the Bank of Spain on the amount of how conservative appraisals should be, and I think that has been -- has had an effect. And from an accountable point of view, when there's a decrease on the appraisals, then there's a greater need for additional provisions.

I think that this is a process that should stop. From now on, we'll see that most of the appraisals will be positive or will increase their value, and that's what I would expect. But it's also true that we were quite surprised or we were a little bit surprised to see that nowadays, there are still some recent appraisals that are still negative.

Operator

(Interpreted) The next question comes from the line of Andrea Filtri by Mediobanca.

Andrea Filtri - *Mediobanca - Banca di credito finanziario S.p.A., Research Division - Research Analyst*

I'll ask my questions in English. I just wanted to understand the answer -- or really I just wanted ask you just one single question on capital return. You reduced -- question is -- or what determines excess capital if your strengths were indeed reduced in line with the reduction in risk that you are doing with the derisking on the balance sheet?

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) Thank you, Andrea. We believe that the 12% that we set as the threshold is what we consider to be as the bank's managers reasonable for the bank bearing in mind its current balance sheet. And so in principle, we do not expect to change that 12%, regardless of what happens with the SREP.

Operator

(Interpreted) And our next question comes from the line of Carlos Peixoto from Caixabank-BPI.

Carlos Peixoto - *Banco Português de Investimento, S.A., Research Division - Analyst*

(Interpreted) Some of the questions have already been answered. But regarding the provision evolution, just to understand a little bit better what you mentioned, you said that in euros, if we adjust the provision levels of last year, I think it's EUR 120 million, including sales of portfolios. So the level of provision should be stable, right, this year according to the guidance. Does it include anything else or just the cost of risk?

And also, a second question related to net interest income. I'm sorry if I'm repeating this, but I've seen the guidance for this year. For next year within your outlook of the interest rates, do you think that what we should do is incorporate the sensitivity that you've given us to the net interest income? Or do you think you'll be able to offset the decline on the interest rates with other measures such as growth of volumes or whatever, just to get an idea about the midterm?

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Thank you very much. With regard to provisions, the idea is to talk about the provisions as a whole for credit for foreclosed assets and the rest, which is a small figure, which are other items of profit and losses. And there on the Page 25 of the presentation, we try to explain that this semester, the 6 months have been more or less a similar amount to the previous year, and our idea is excluding one-offs from last year to have a total of provisions in line or to repeat the volume of the previous year.

And as for the net interest income, the truth is that to talk about the net interest income of 2020 is a bit complex for us because as we were saying, there was still several elements. We'll have to really make a good analysis based on a good interest rate curve. So we'll do that in November. And I think that a positive thing on that side is that the average stock is growing. The net interest income difference between the first quarter and the second quarter is due to the growth of those average -- of the average stock. But obviously, we'll have more negative interest rates in the future. So we'll analyze that. And today, we cannot give you an accurate answer about that for 2020, about the net interest income for 2020.

Operator

(Interpreted) The next question is by Fernando Gil from Barclays.

Fernando Gil de Santivañes d´Ornellas - *Barclays Bank PLC, Research Division - Research Analyst*

(Interpreted) I wanted to understand better your commercial policy and the growth of new mortgages. The new mortgages have fixed rate, is still quite strong. But I wanted to understand if you have any limit based on deposits or to what -- how far could interest rates -- or could the fixed-rate mortgages go? And with the new mortgage loan, this is the second question, have you recovered those adjustments that were done in the second half of June? Or how long will it take to adapt to it and go back to normal?

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Well, with regard to limits on fixed-rate mortgages, we do not have any limits, any internal limits. We are around 55%, 60%, but that depends mainly on our customers' decision. We believe that in the long term, it makes sense to take on a fixed-rate mortgage, and that's what we recommend to our customers. But all in all, it's -- the decision is in their hands. We will not be concerned if we had 80%, 90% of new mortgages are fixed rate. It could be done. The policy is to cover fixed rate. And for us, it also gives us peace of mind because our customer is willing to pay today more for the mortgage. To guarantee a fixed rate in the future is also a cost of risk -- the future cost of risk or the premium risk of that customer would be quite low. So the noncompliance of those customers will be lower.

And regarding the new mortgage law, well, it's gone slower than the whole mortgage process went. As you know, from now on, all new mortgages are -- well, for them, we have to use our technological IT platform of the public notary so that we can communicate with the public notaries. That platform is still not perfect. It's still giving problems. In fact, there has been an extension to -- by the government to use other methods that are not on the platform. Even public notaries themselves are changing their way of acting. They have new requirements to fulfill. And so it will take a few months. And a few months would be, I don't know, by August, September. I hope that when we come back in September, the process is working normally.

Operator

(Interpreted) The next question comes from the English questions. So we have Britta Schmidt.

Britta Schmidt - *Autonomous Research LLP - Non-Designated Member*

Yes. I've got 2 questions on liquidity and funding, please, then just one clarification. With regards to the TLTRO II plan, what is your plan for repaying it? And do you have any interest in taking up any TLTRO II or III? My second question would be do you have a subordinated MREL target. And if so, what is it? Or are you aiming for in terms of structuring your MREL? And then can you just clarify again the interest sensitivity that you've given? I'm not quite sure it was quite clear on the English version of the call.

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) Okay. Regard the TLTRO II, as we've said in previous occasions, our strategy within the plan was to return it and we keep the same strategy. It matures, most of it, in June 2020. And as explained before, we have an excess of liquidity that should help us to return them with no problems at all.

As for the TLTRO III, we haven't made a decision, and we'll make a decision as time goes by, soon, I guess, well, maybe June next year, according to the terms that we can see that are more appropriate. In any case, I do not expect that we will take on the same amount that we had to take. Not at all.

As for the target of MREL subordination. The truth is that we do not have it yet. As you know, that target was established by the new regulation, by the new banking package. But the MREL letter that we received -- the institutions have received until now have to do with the previous regulation. And so there is no subordination level that is clear. If we look at the new regulation, we could estimate, but they haven't informed us if from the regulation, we guess, our subordination level could be about 19.5%, 19.7%. Currently, our subordination level is above 19%. And so we do not estimate -- we do not expect that we'll have to issue a lot to reach that.

And finally, in terms of sensitivity, the sensitivity that I gave you is plus 50 basis points, 3% of ROE -- additional ROE. At negative sensitivity of 10 basis points in the first 12 months, we would have a negative impact of EUR 16 million. In the second 12 months, we have a negative additional impact of EUR 28 million. That is due, just like in the positive one, to the fact that our mortgages take about 10 months to have -- to be revalued. So we do not see the positive or negative impact in the first 12 months. We have to wait for the following 12 months to see the accumulated impact.

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Operator

(Interpreted) And the last question is from the line of Sofie Peterzens from JPMorgan.

Sofie Caroline Elisabet Peterzens - *JP Morgan Chase & Co, Research Division - Analyst*

Here is Sofie from JPMorgan. So I was just wondering on the consumer loans and real estate developer loans that are growing 15% or so year-on-year. What kind of cost of risk do you see for these products? And then my last question would be on DTAs. Can you remind us how much DTAs you have and how much of that is included in your core equity Tier 1?

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) Perfect. You start.

Leopoldo Alvear Trenor - *Bankia, S.A. - Deputy General Director of Financial Management*

(Interpreted) Okay. Well, regarding the DTAs we have, EUR 10.5 billion DTAs, of which EUR 2.5 billion, EUR 2.4 billion are tax credits. And so they are deducted at 100% euro by euro. And the rest, about EUR 8 billion, are in DTAs mainly that are monetizable. Of those EUR 8 billion, EUR 7.5 billion are -- can be monetized and reduce or increase their RWAs by -- increase or decrease their RPAs. And we have EUR 600 million that are DTAs that are non-monetized but that fit within the buffer. And so, therefore, they increase the RWAs to 250%, more or less. All of that is included in the fully loaded ratios that I mentioned before.

José Sevilla Álvarez - *Bankia, S.A. - CEO & Executive Director*

(Interpreted) As for the cost of risk of the consumer loans portfolio, it's quite stable over the last 2 or 3 years, about 2%. 2%, bearing in mind that it more or less in agreement with the default that we have in the consumer world. As you know, the provision calendar for consumer loans is very accelerated, and the coverage is equity increased 100%. So it's costing us 2% year-on-year.

Iñigo Velázquez - *Bankia, S.A. - Head of IR & Rating*

(Interpreted) Okay. Perfect. Well, thank you all very much, and thank you. As you know, the Investor Relations team is always available to you for any questions you have. I wish you all a happy summer.

Editor

Portions of the transcript that are marked (interpreted) were spoken by an interpreter present on the live call. The interpreter was provided by the Company sponsoring this Event.

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