

Director's Report**DIRECTORS' REPORT OF THE CONSOLIDATED GROUP BANCO GUIPUZCOANO FOR THE YEAR 2007**

In 2007, the Banco Guipuzcoano posted net earnings attributed to the Group totalling 61,506 thousands of euros, which represents a 13.2% increase over the previous year. This successfully completes the final year of the Strategic Plan 2005/2007 - "Banking in Action". The following points are particularly noteworthy with regard to this 3-year period:

- Customer Loans increased by 106.4%
- Resources Managed increased by 78.1%
- Net Earnings increased by 54.8%
- 31 branch offices have been opened. This means that the Bank now has a presence in every single Autonomous Region.

Specifically, in 2007, 16 branch offices have been opened. Noteworthy are the offices opened in Santander, Cáceres and Badajoz, which complete Banco Guipuzcoano's presence in all the Autonomous Regions of Spain. We shall also mention the four new branch offices that have been opened in Andalusia (Vera-Almería, Dos Hermanas-Sevilla, Cordoba, and Granada), the ongoing expansion in the Canary Islands where offices have been opened in Tenerife (Los Cristianos) and in Gran Canaria (Playa del Inglés), the opening of offices in La Coruña and Oviedo, the three new offices in Madrid (a new one for Businesses, Majadahonda, and La Vaguada), the Rubí Office in Barcelona, and the Office for Businesses in Valencia. As of December 31, 2007, Banco Guipuzcoano has 266 branch offices open for business.

The number of shareholders of the Bank, now standing at 27,717, is up by 26.8% on the previous year. Banco Guipuzcoano's market capitalisation at the end of 2007 was 1,666.7 millions of euros, slightly lower than at the end of the previous year.

This year marketing focused on launching new products aimed at bringing in Funds. The excellent response to the issues of an Energy Fund and different combined Deposits is particularly noteworthy. There has also been a great response to the launching of the mortgage interest rate CAP in a year when the markets have greatly fluctuated. In the business segment, the development of specialised financing (factoring, confirming, leasing, renting) has been outstandingly successful. Global interest rate hedging has been further strengthened and has consolidated as interesting products for SMEs.

Particular mention should be given to the improvement in ratings granted to the Bank's bank deposits by Fitch, the international rating agency, be it the rating for long term, which has moved up to "A", or the short-term rating, which has been upgraded to "F1", with a "stable" outlook. The international rating agency Moody's has also analysed the Banco Guipuzcoano for the first time and given it the following ratings: "A2" for long-term deposits, "P-1" for short-term deposits. In all cases the outlook is "stable". The improvement in Fitch's ratings and the good ratings given in the first assessment carried out by Moody's are a sign of the Bank's strength and the good performance of the business, as well as its levels of solvency, liquidity, quality of assets, and the sound management achieved by the Banco Guipuzcoano.

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Economic Scenario

The points worthy of mention regarding the economic scenario in which the Bank has been carrying on its business are as follows:

- 2007 will go down in history as the year of the "subprime mortgages" crisis which was the result of indiscriminately granting loans to high-risk customers in the United States. The fact that they were subsequently securitised and the first defaults in early August led to the tension that is now found in the economy worldwide.
- The lack of confidence generated by this type of structured product spread rapidly to all the financial markets, leading to a shortage of liquidity in the system which created major tension in financing terms. It has made the markets unstable and endangered the solidity of the economy not just in the United States but around the world.
- In the United States, 2007 has been the third year in a row of a slowdown in the growth of the economy, and the first year where the growth rate has changed markedly. Its year end growth rate could be 2.3% compared to 2.9% the year before. Foreign demand, supported by a weak dollar, has increased its share, which has become positive, and offset the drop in domestic demand.
- The euro area started off the year with high growth rates of around 3%. The economic expansion was expected to consolidate over the year with a larger contribution from private consumption. However, the figures for the third quarter of 2007 showed that growth was still based on investment and exports and private consumption had yet to take over as a driver of demand. The year is likely to end with average growth of 2.6%, lower than the 2.9% recorded for 2006.
- In 2007, the Spanish economy's growth has slowed down a little, indicating a change in trend, as both private consumption and investment in real estate have slowed. GDP as a whole has grown 3.8% this year, and is showing clear signs of slowing. As was the case all round the Euro zone, inflation was higher than expected. The CPI at the year end was slightly above 4% for the year, as the gap of more than one percent compared to the average for the euro zone widened once again. The difference is even greater when we compare our price index to the indices of Germany, the United Kingdom, Italy and France.
- Worthy of note in the foreign currency market is the strength of the euro compared to the other major international currencies (+10.57% against the dollar, +3.78% against the yen +9.13% against the pound).
- Stock markets around the world, except for the Nikkei in Japan (-11.13%) and a few stock markets in Europe such as Italy (-6.46%) or Switzerland (-3.43%), ended the year with overall increases. The strength of global economic growth, valuations that are still attractive and the firm commitment on the part of central banks in their monetary policies have been the basis supporting these rises. In Europe, the main stock market index, DJEurostoxx 50, ended the year up 7.32%, while the Ibex 35 increased by 6.79%. In the United States, the Dow Jones, the S&P 500 and the Nasdaq were up at the end of 2007 by 6.43%, 3.53% and 9.81% respectively.

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Balance Sheet:

The Group's Balance Sheet totalled 9,915,703 thousands of euros, an increase of 10.0% over the previous year.

Customer Loans totalled 7,784,257 thousands of euros, up by 17% on the year, including Securitised Loans. The pace of growth has slowed, for mortgage loans and for loans as a whole.

Customer Deposits totalled 8,458,734 thousands of euros, an increase of 2,179,854 thousands of euros, in other words 34.7%. Noteworthy in this section is the good performance of term deposits which are up by 60.1%. The issue of Bank Promissory Notes is still getting a favourable response and there are now 2,267,127 thousands of euros outstanding.

Managed Funds totalled 10,218,864 thousands of euros, 21.3% higher than last year. Assets managed in Investment Funds and Pensions amounted to 1,538,019 thousands of euros a little lower than last year. The number of participants went up by 8.7%, to 102,423.

Results:

The Banco Guipuzcoano Group has recorded net earnings totalling 61,506 thousands of euros, which makes for a 13.2% increase on the previous year.

Net Interest Revenue totalled 163,496 thousands of euros, a 19.7% improvement on the previous year's figure. This is due to increased business volumen, and the great sales effort by the Branch Network. This Margin represents 1.76% of Average Total Assets, compared to 1.70% the year before.

The Contribution Margin totalled 235,413 thousands of euros, 34,242 thousands of euros more than last year, a 17.0% increase in relative terms. It represents 2.47% of Average Total Assets, compared to 2.44% the year before. These two margins are the best proof of the excellent performance of our Branch Network.

Net Ordinary Revenue totalled 259,121 thousands of euros, 19.3% higher than in the previous year.

General Expenses as a whole increased by 7.8%, accounting for 1.28% of Average Total Assets, compared with 1.38% the year before. They include the expenses of the 31 new offices of the Expansion Plan of the Strategic Plan 2005/2007, which in their early years produce expenses but hardly any revenues.

In 2007, in accordance with the Bank's traditionally conservative criteria, 73,114 thousands of euros have been appropriated to Provisions for Bad Debts and Other Provisions, making for a very sound Balance Sheet.

Impairment Losses on Credits, Loans and Discounts (net) totalled 62,315 thousands of euros, 34,035 thousands of euros more than last year. After these appropriations, as of December 31, the Provision for Bad Debts totalled 179,189 thousands of euros, which represents a coverage rate of 188.1%, not including mortgage guarantees. Recovery of previously written-off loans totalled 4,027 thousands of euros, 1,141 thousand more than last year, 39.8% up in relative terms. The default rate was 1.2%.

Net Operating Revenue was 134,661 thousands of euros, an increase of 31.7% over the previous year. If we include provisions for bad debts and other items and the Corporation Tax expense, we arrive at a Net Profit of 61,506 thousands of euros, which is 7,193 thousands of euros up on the previous year in absolute terms, a 13.2% improvement in relative terms.

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Proposed Distribution of Profit:

The proposal for the distribution of profits of Banco Guipuzcoano, S.A. made by the Board of Directors to the General Meeting of Shareholders envisages appropriating 29,075 thousands of euros to Reserves and distributing a Dividend of 28,103 thousands of euros. This will allow for a dividend to be distributed against 2007 earnings totalling 0.1875 euros per ordinary share and 0.28125 euros for non-voting preferred shares. The total amount distributed in dividends exceeds the figure distributed last year by 13.6%. As an interim dividend was distributed in October, a complementary dividend of 0.1275 euros per ordinary share and 0.19125 euros per preferred share has yet to be distributed. If the General Meeting approves the Board's proposal, it shall be distributed on Monday April 7.

Capital and Treasury Stock:

During the year the par value of the Bank's shares was halved 2 x 1, and the par value of the shares changed from 0.50 euros to 0.25 euros. Later, in June, the Capital increase of one new share per eleven old shares was completed, and fully covered. This issue was made at 10 euros per share.

At the end of 2007 the Bank's share capital totalled 37.4 millions of euros, represented by a total of 149,760,000 registered shares, each having a par value of 0.25 euros. Of total shares, 149,513,328 (99.8%) are ordinary shares and 246,672 (0.2%) are non-voting preferred shares. Trading in the non-voting preferred shares is insignificant.

The Consolidated group, in accordance with the authorisations voted by the General Meetings of Shareholders held on February 25, 2006 and March 10, 2007 for acquiring the Bank's own shares has, during 2007, acquired a total of 593,769 shares in the Bank, for a par value of 151,118.75 euros. Furthermore, during the same period, a total of 501,603 shares were sold, for a par value of 172,772.5 euros. Many shareholders opt to reinvest their dividends in shares in the Bank. The balance of treasury stock held by the Group as of December 31, 2007 was 325,693 shares, with a par value of 81,423.25 euros.

Significant post balance sheet events:

No significant event in the development of the Consolidated Group worthy of note has taken place between the year end and the date the Board of Directors drew up the Annual Accounts and this Directors' Report on January 18, 2008, apart from those mentioned in the Notes to the Accounts.

Outlook:

2008 is expected to be a year in which the economy worldwide will slow down as a result of international financial instability. The depth and length of the slow-down in the economy will depend on how the major

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macroeconomic variables (interest rates, inflation, employment and euro) behave, and on trends in the tensions in world financial markets. Gross world product could grow at a rate of 4.8%, compared with an estimated growth of 5.2% in 2007, strongly supported by the emerging economies.

Europe is expected to have balance growth of around 2.1% although trends in the United States economy will have major repercussions.

The outlook for Spain in 2008 is for a certain amount of caution, even though the Government keeps up its forecasts of growth of around 3%. Trends in the real estate market and the employment market will be fundamental variables for growing as forecasted.

One also needs to bear in mind that the Federal Reserve is likely bring down interest rates, and that the European Central Bank is likely to keep them up in the medium term.

During 2008, Banco Guipuzcoano is starting a new two-year Strategic Plan 2008/2009 "Bow to 10", which will be guided by developments in the economy. We aim to reach the year 2010 with a mark of 10 for excellence in our banking services, adapting our work force and our resources to the most sophisticated requirements.

During this time, the Bank will work on implementing Basle II.

Now that it has gained a presence in every single Autonomous Region, the Bank will continue to consolidate geographically.

The evolution of the Bank's Results will depend on growth in the economy, trends in interest rates and defaults.

As far as retail business in 2008 is concerned, the financing of private consumption, specialised financing for SMEs and commercial financing will continue to grow. The products designed for businesses to manage their cash and bank accounts will continue to be boosted, with interest-rate and foreign currency hedging, and the effort to launch customised products aimed at private individuals will continue.

Further information under Section 116 bis SMA:

a) Capital Structure.

The Share Capital of Banco Guipuzcoano, S.A. stands at 37,440,000 euros, and consists of:

- Common shares: 149,513,328 (99.8%) ordinary shares with a par value of 0.25 euros per share.
- Non-voting preferred shares: 246,672 (0.2%) non-voting preferred shares with a par value of 0.25 euros per share. Non-voting preferred shares do not entitle their holders to a vote, and are paid a higher dividend than ordinary shares.
- At the present time, there are no securities issued that entitle their holders to convert them into shares of Banco Guipuzcoano, S.A.

b) Restrictions on the transferability of securities: there are no restrictions in the Articles of Association on the transferability of the shares that make up the company's share capital.

c) Major holdings in the share capital.

Bilbao Bizkaia Kutxa 14.498%

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Caja de Ahorros y M.P. de Guipuzcoa y San Sebastián (Kutxa) 9.997%
Joaquín Martínez López 10.750%
Surfolk S.L. 5.018%

d) Restrictions on voting rights.

To qualify to vote, one must hold at least 200 fully paid-up shares with a par value of 0.25 euros, which may be added to the shares held by another shareholder in order to attain said figure (Art. 19 of the Articles of Association).

Moreover, except for the cases provided for in Articles 5 and 6 of Royal Decree 567/1980 and in Title Three of Law 26/1988, no shareholder, regardless of how many shares he may hold, may have a number of votes exceeding 10% of the votes that qualify to be made at the General Meeting (Art. 19 of the Articles of Association).

e) Para-social agreements: there are none.

f) Rules on appointments and changing the Company's Articles of Association:

The Directors are appointed by the General Meeting of Shareholders or by the Board itself (cases of co-option, which have to be ratified by the next General Meeting of Shareholders) in accordance with the terms of the Companies Act and the Articles of Association. Its proposed appointments must be for candidates presented by the Standing Delegate Committee. In the event that the proposal of said Committee is not taken up, the Board must give due grounds for its decision (Article 5 of the Governing Rules).

Under the terms of Article 30 of the Bank's Articles of Association, under no circumstances may any person or Company who fails to meet the requirements of honourable commercial and professional repute of a bank administrator referred to in Article 2 of Royal Decree 1245/1995 dated July 14, regarding the setting up of banks, cross-border business and other issues relating to the legal system governing credit institutions, become a director.

Article 8 l) of the Rules on the Governance of the Board of Directors provides that a director must step down in the event that he no longer has enough time or professional capacity to meet the Company's obligations and in such other cases where, as a result of his acts in relation therewith, or in areas not related thereto, the Company's credit and reputation may be severely impaired. Article 8 m) provides that a director appointed by a shareholder must step down in the event that the shareholder he is representing reduces its holding in the share capital below the level or percentage that enabled him to be elected.

The quorums for General Meetings are higher for altering the Articles of Association than is provided in the Companies Act, but no majorities over and above those required by law are required for such decisions to be approved. As a general rule, Article 6 of the Articles of Association stipulates that there must be a quorum of shareholders when General Meetings are called for the first time who represent 2/3 of the paid-in share capital and, when called for the second time, half of the paid-in share capital. Quorums of 70% and 60% of the paid-in share capital are only required respectively when meetings are called for the first and second time for the purpose of modifying said Article 26.

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Changes in the Articles of Association shall be submitted to the Ministry of Economy and Finance for approval, in accordance with the terms of R.D. 1245/1995, dated July 14, regarding the setting up of banks, cross-border business and other issues relating to the legal system governing credit institutions.

- g) Powers of the members of the Board of Directors: no notarised general or special powers of attorney have been granted to members of the Board.

This notwithstanding, it is pointed out that the Board of Directors, in accordance with the appropriate decisions taken validly by the shareholders at the Ordinary General Meeting held on March 10, 2007, has been granted powers to increase the share capital in accordance with the terms set out in Section 153 of the Companies Act up to the limit of one half of the present figure for share capital, and to acquire up to 20 millions of euros of the Company's own shares, for a price between 5 and 25 euros per share, within a term of up to 18 months as from when the General Meeting took its decision.

- h) Significant agreements: there are none.

- i) Agreements between the company and its administrative and management officers providing for severance in certain cases.

The employment contracts of some members of the company's management which, in view of their parts of responsibility, provide for the right to severance in the event the employment is terminated as a result of a takeover bid or other similar situations.