2018 EU-WIDE TRANSPARENCY EXERCISE AND RISK ASSESSMENT REPORT

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Background Briefing with analysts and journalists | 14 December 2018

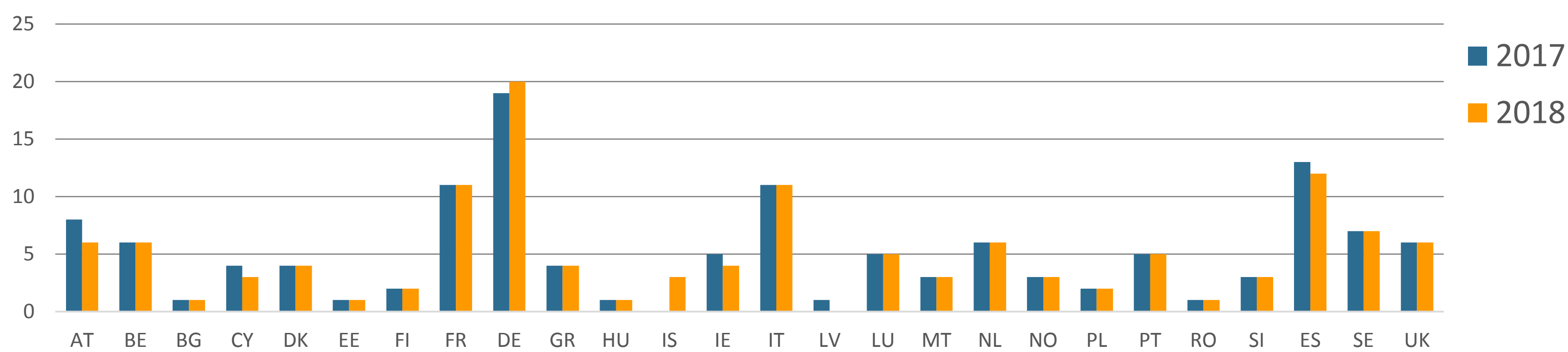
Outline of the presentation

- **Transparency exercise – what we publish today**
- Risk Assessment Report: main findings, outlook and recommendations

Main features of the EU-wide 2018 Transparency Exercise

- Fifth EU-wide Transparency exercise (2018, 2017, 2016, 2015, 2013) excluding the transparency data provided in the Stress Tests.
- More than 7,000 data points per bank, 130 banks from 25 EEA countries.
- Reference dates: **December 2017** and **June 2018.**
- Exclusively based on supervisory reporting data (FINREP, COREP). Information mostly in line with previous exercises to ensure continuity in the time series.
    - Sovereign exposures are now included in regular supervisory reporting.

Country distribution of the participating banks



Wide coverage of bank-by-bank information

Template content overview

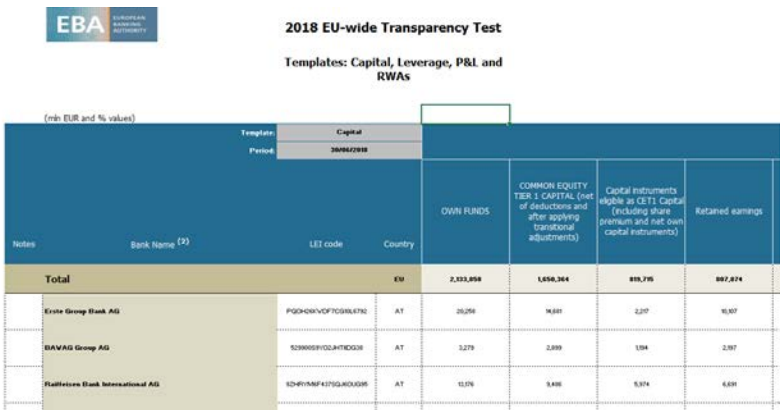
Capital	• Capital positions: components and transitional adjustments
Leverage	• Leverage ratio under both transitional and fully phased-in definition
RWA	• Aggregate risk exposure amounts by risk type
P&L	• Detailed main P&L items: net interest income, net trading income, provisions….
Credit risk	• Original exposure, EAD, RWA and provisions (including securitisation) • Country by country breakdown (where available)
Market risk	• RWAs by different sources of risk
Sovereign	• Sovereign exposures information, including aggregates and country-specific information (where available) also with the residual maturity information for the reference date 30/06/2018
Asset Quality	• Non performing exposures: provisions and guarantees • Forbearance: exposures and provisions

What's on the website: the full package

- **Database:**
  - ✓ **CSV Data** : Credit risk, Market risk, Sovereign debt exposures, Other templates
  - ✓ **Data dictionary**
  - ✓ **Metadata**
  - ✓ **Manual for using and managing data**
- **Single bank PDFs**
- **Interactive tools:**
  - ✓ **Excel tools**
    - Capital, P&L and RWAs (1 file)
    - NPE and forborne exposures (2 files)
    - Credit Risk (3 files)
    - Sovereign (3 files)
    - Market risk (1 file)
  - ✓ **Map tool**

Exploiting data in an interactive way

- **Excel interactive tools (downloadable!):** user friendly excel tools for each template that allow analysing and retrieving data. Comparison by template at bank and country level.



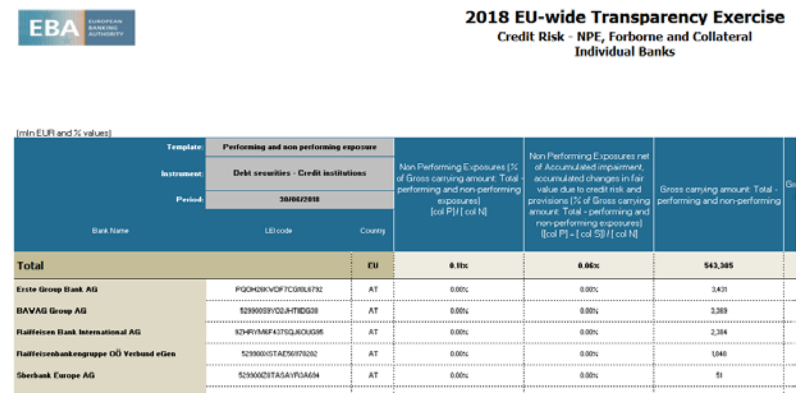
2018 EU-wide Transparency Test

Templates: Capital, Leverage, P&L and RWAs

(mln EUR and % values)

Template: Capital
Period: 30/06/2018

Notes	Bank Name (2)	LEI code	Country	OWN FUNDS	COMMON EQUITY TIER 1 CAPITAL (net of deductions and after applying transitional adjustments)	Capital instruments eligible as CET1 Capital (including share premium and net own capital instruments)	Retained earnings
	Total		EU	2,333,058	1,650,364	819,795	807,874
	Erste Group Bank AG	PQOH26KWDF7CG10L6792	AT	20,256	14,681	2,217	10,107
	BAVAG Group AG	529900S9YO2JHTIIDG38	AT	3,279	2,899	1,194	2,197
	Raiffeisen Bank International AG	9ZHRYM6F437SQJ6OUG95	AT	13,176	9,406	5,974	4,691



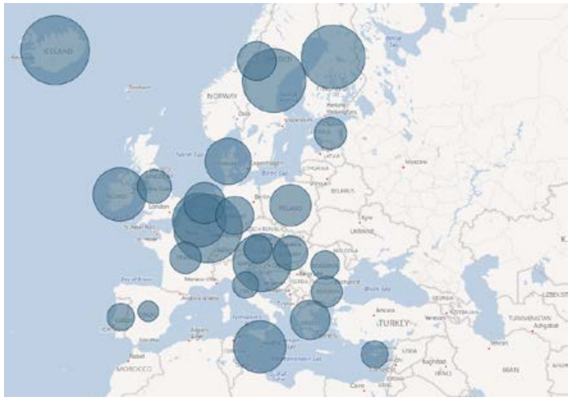
2018 EU-wide Transparency Exercise
Credit Risk - NPE, Forborne and Collateral
Individual Banks

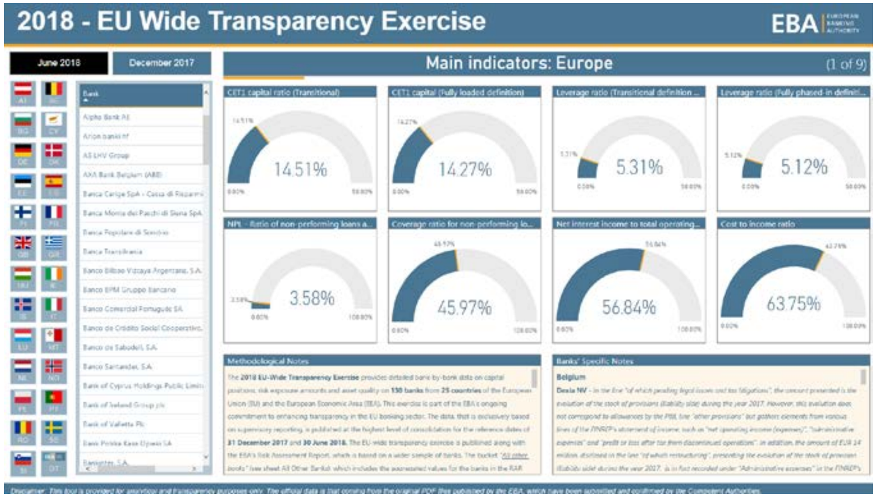
(mln EUR and % values)

Template: Performing and non performing exposure
Instrument: Debt securities - Credit institutions
Period: 30/06/2018

Bank Name	LEI code	Country	Non Performing Exposures (% of Gross carrying amount: Total - performing and non-performing exposures) [col P] / [col N]	Non Performing Exposures net of Accumulated impairment, accumulated changes in fair value due to credit risk and provisions (% of Gross carrying amount: Total - performing and non-performing exposures) ([col P] - [col S]) / [col N]	Gross carrying amount: Total - performing and non-performing
Total		EU	0.11%	0.06%	543,385
Erste Group Bank AG	PQOH26KWDF7CG10L6792	AT	0.00%	0.00%	3,431
BAVAG Group AG	529900S9YO2JHTIIDG38	AT	0.00%	0.00%	3,369
Raiffeisen Bank International AG	9ZHRYM6F437SQJ6OUG95	AT	0.00%	0.00%	2,384
Raiffeisenbankengruppe OÖ Verbund eGen	529900XSTAE56I178282	AT	0.00%	0.00%	1,040
Sberbank Europe AG	529900Z8TASAYRGA694	AT	0.00%	0.00%	51

- **Interactive dashboards:** allowing country/banks comparison through maps and advanced charts.





Outline of the presentation

- Transparency exercise – what we publish today
- **Risk Assessment Report: main findings, outlook and recommendations**

Main findings

EXTERNAL ENVIRONMENT

- **Positive macroeconomic developments** have supported further improvements in banks' resilience and the increase in lending. However, **risks to and vulnerabilities of the global economy** can potentially affect EU banks.

SUPPORTING RESILIENCE

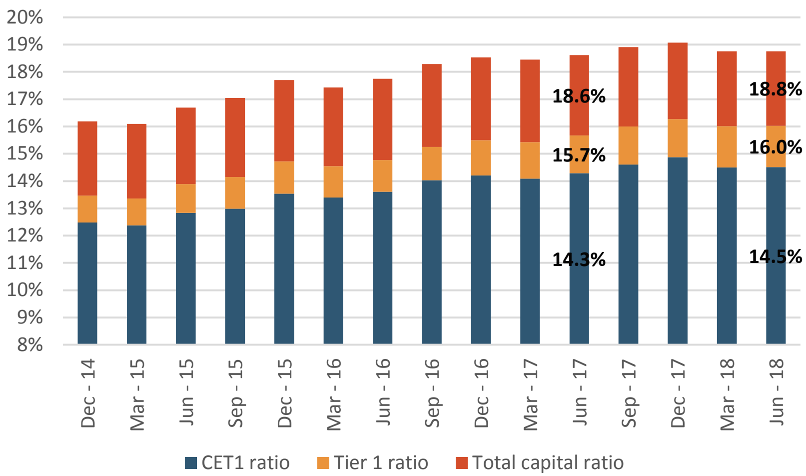
- **Capital ratios have further increased despite increasing RWAs.**
- **Asset quality has further improved** with the NPL ratio decreasing from 4.4% to 3.6% in one year.

KEY CHALLENGES

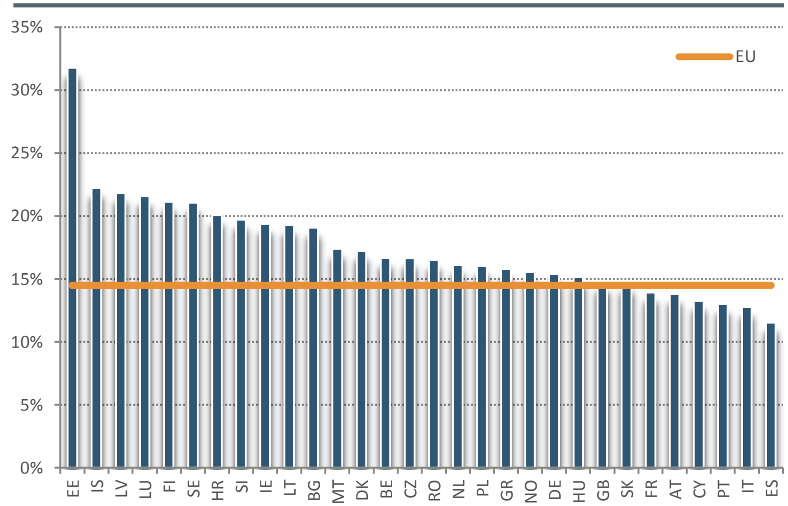
- **Profitability is unchanged, with ROE at 7.2%. Concerns remain about its sustainability**, as interest margin further decreases, efficiency deteriorates and fees and commissions increase only slightly. Lower impairments remain a key driver of recovery.
- **Funding** supported by growth in customer deposits. **The challenges looking ahead** are connected to **replacement of central bank funding and fulfillment of MREL** requirements.
- **Operational risks in EU banks are expected to increase.** ICT-related risks are the main challenges. AML cases drive up conduct risk.

Further improvements in capital ratios despite increasing RWAs

Capital ratios (transitional)



CET1 ratio dispersion — by country and EU average (June 2018)



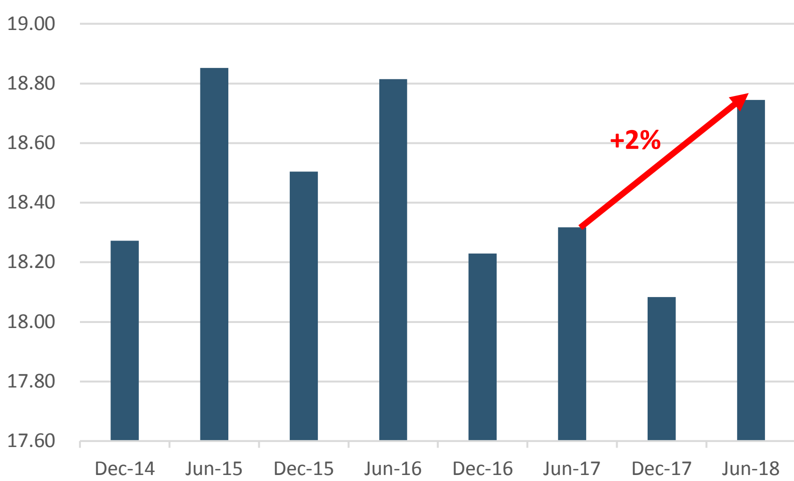
Source for all charts: EBA supervisory reporting data.

- Since June 2017, **CET1 ratios have increased** from 14.3% to 14.5% on a transitional and from 14.0% to 14.3% on a fully loaded basis.
- The composition of capital keeps moving towards a greater reliance on retained earnings and other reserves, which together represent almost 70% of total common equity.
- Throughout 2018, **RWAs were increasing**. Year to date they increased by more than 1%. This was mainly driven by an increase in credit risk and somewhat by an increase of market risk.
- Notwithstanding the **dispersion, 88% of the banks in the sample have a CET1 ratio above 12%**, and 45% of the banks have a CET1 ratio of above 16%.
- In the near future, banks do not expect to issue more CET1 instruments. In addition, very little AT1 issuances are expected in the next 12 months.

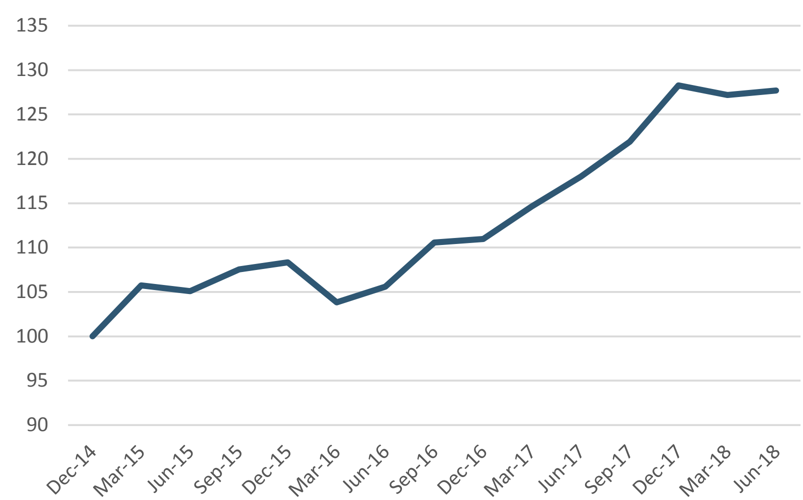
Increasing lending, but assets remain stable

- EU banks' **total assets remained stable** between June 2017 and June 2018, which is in contrast to a decreasing trend over the past years. In the same period **total loans and advances increased by 2%.** However, the restart of lending was offset by the decline in debt securities, derivatives and equity instruments.
- Loans to **non-financial corporates (NFCs) increased by 6%,** mainly driven by exposures to **small and medium-sized enterprises (SMEs, +8%) and commercial real estate (CRE, +9%)**. During the same period, loans and advances to households increased by 3%.
- In June 2018, banks' total SME exposures accounted for EUR 1.9 tn, up from EUR 1.75 tn a year before. **Further growth in SME loans is expected** as, according to EBA RAQ, 90% of banks plan to increase their portfolios in SME lending.

Total loan volumes (EUR tn)



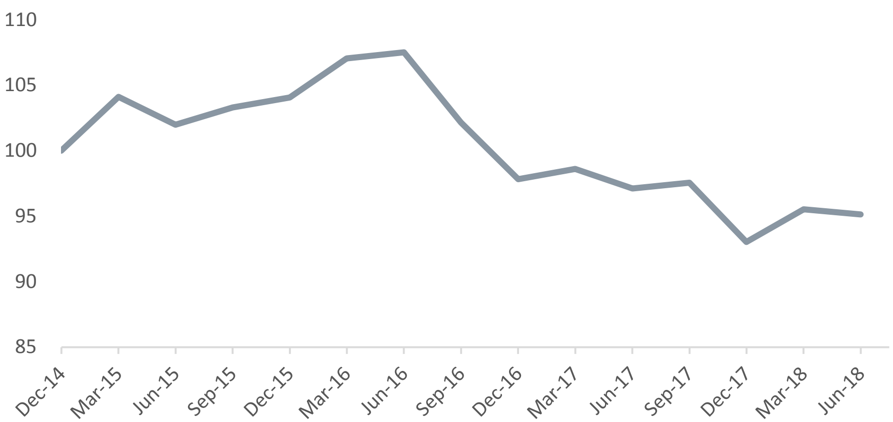
Total exposures to SMEs (2014=100)



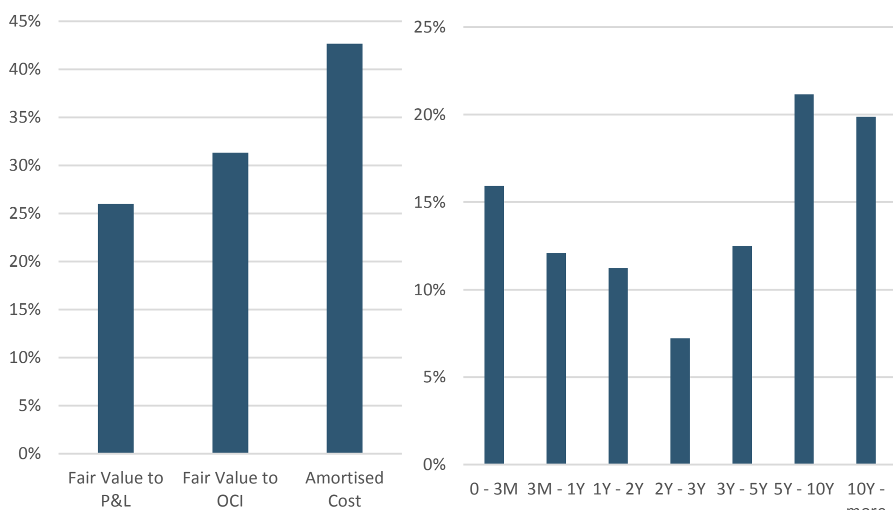
Source for all charts: EBA supervisory reporting data.

Sovereign exposures are on a decreasing trend. About half of them are towards domestic counterparties.

Evolution of total loans and advances and debt securities to general governments (2014=100)



Breakdown by accounting treatment (left) and maturity (right) of exposures to general governments (June 2018)



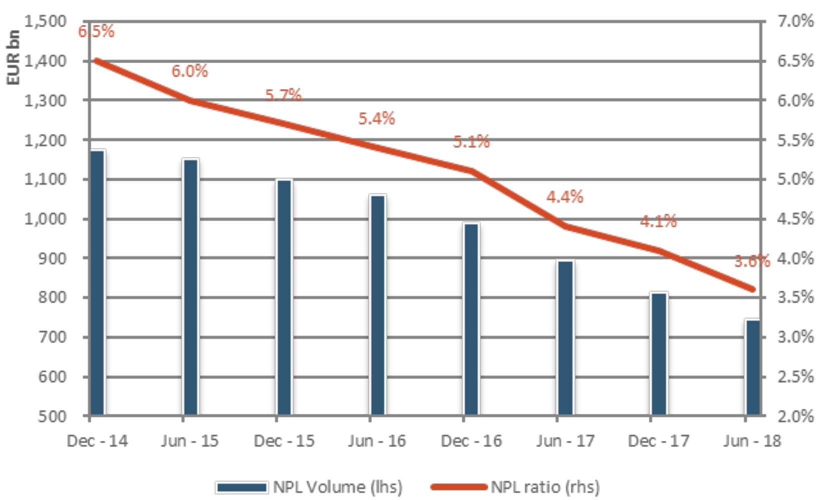
Source for all charts: EBA supervisory reporting data.

- **Total sovereign exposure** of the EU banking sector stood at EUR 3.0 tn as of June 2018, **a 2% decrease compared with June 2017** and a 10% decrease compared with 2 years ago.
- The **largest share of sovereign exposures were measured at amortised cost (43%),** followed by fair value through other comprehensive income (31%) and fair value through profit and loss (26%).
- Geographically, nearly **50% of these exposures were towards domestic counterparties** (June 2018), with significant dispersion across countries. For the vast majority of the countries, foreign sovereign exposures are mostly concentrated in EEA countries.
- In terms of maturities, **more than 40% of sovereign exposures have a maturity above 5 years**, while about 15% of them had a maturity within 3 months.

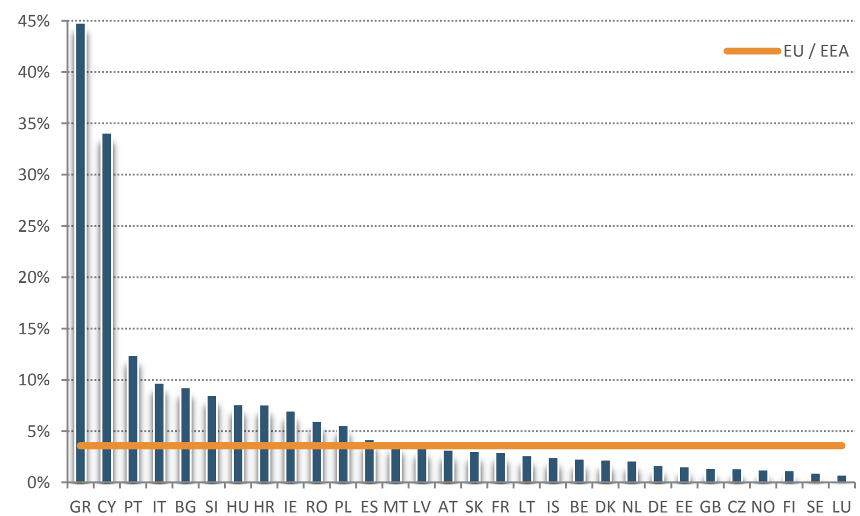
NPLs decreased by more than EUR 400bn in the past 3 years. SME NPL ratio decreased the most.

- The average **non-performing loan (NPL) ratio of EU banks has decreased** from 4.4% (EUR 893bn) in June 2017 to 3.6% (EUR 746bn) in June 2018. It is the lowest level since the NPL definition was harmonised across European countries in 2014, when the NPL ratio stood at 6.5% (EUR 1.174bn). A big driver of reduction were NPL sales.
- **SMEs are the sector in which banks have reduced their NPLs the most** (from 13.5% a year ago to 9.8%). The EU average NPL ratio for large corporates in June 2018 was 5.0% (6.2% in June 2017) and 3.7% for households (4.3% in June 2017).
- The average **coverage ratio of NPLs** was 46.0% as of June 2018 (EU weighted average). It had **increased by 1 pp** in June 2018 compared with 1 year earlier.
- **In the next 12 months both banks and analysts expect an improvement in asset quality**. In particular, more than 50% of banks expect SME, residential mortgage and corporate loans to improve in quality.

EU banking sector NPLs (EUR bn) and ratios of NPLs and FBLs (%)



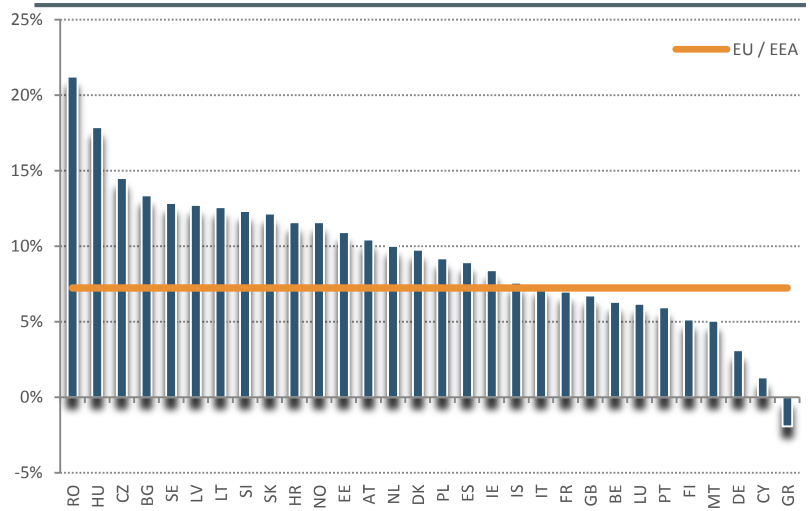
NPL ratios by country (June 2018)



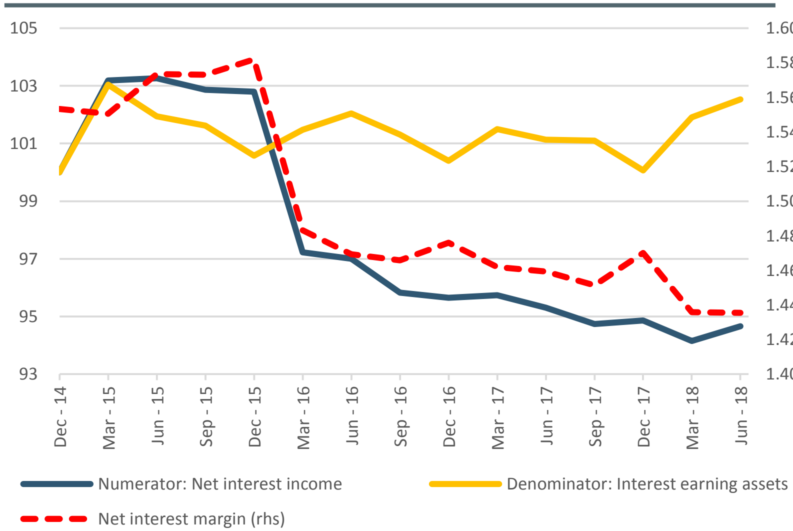
Source for all charts: EBA supervisory reporting data.

Further decrease in NII and impairments. No signs of improving efficiency.

RoE by country



Net interest margin

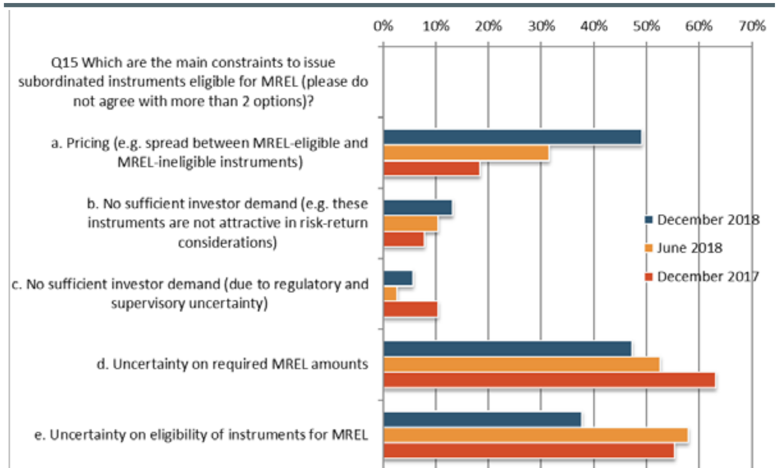


Source for all charts: EBA supervisory reporting data.

- **Profitability has remained stable** since last year with an average return on equity (RoE) of 7.2% as of June 2018. According to the EBA RAQ, most banks believe they can operate on a long-term basis with RoE levels of 10% or higher, indicating that **sustainable RoE levels have still not been reached. Dispersion across banks and countries persists.**
- EU banks' **net interest income (NII) has continued its declining trend** in recent quarters (almost -1% compared with the same period of 2017), despite growing lending volumes. This was driven by a **decreasing net interest margin**, reaching 1.44% in June 2018 (the lowest since the supervisory data has been collected).
- Net fee and commission income has increased by almost 1% in the first half of 2018 compared with the same period in 2017. EU banks' **profitability has further benefited from decreasing impairments**, which remain a key driver of recovery.
- Efficiency in the EU banking sector has not improved. The **cost to income ratio increased to 63.8%** in June 2018 from 61.7% a year ago. Costs dynamics are affected by elevated IT related expenses and investments into FinTech.

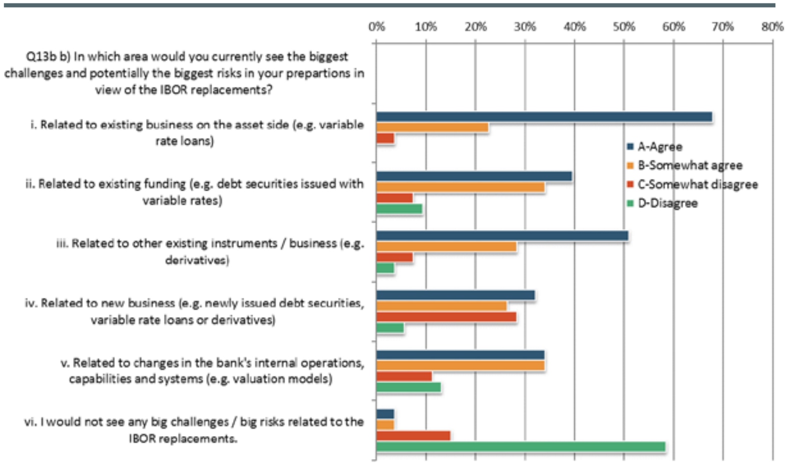
Funding risks and challenges ahead include MREL issuances and replacement of central bank funding

Constraints to issuing MREL eligible instruments



Source: EBA RAQ for banks, December 2018.

IBOR replacements: main challenges and risks



- Issuance volumes in 2018 were affected by **market volatility and increasing prices**. However, issuance volumes of senior bail-in-able debt instruments increased markedly compared with 2017.
- Going forward, in particular **medium-sized banks**, **small banks** required to hold MREL funding and banks with **weaker market perceptions** might face challenges to meet MREL requirements.
- Against this backdrop, RAQ responses show that banks consider the **pricing of instruments eligible for MREL** as the most relevant constraint to issuing these instruments. Other aspects, like legal / regulatory uncertainties, have declined in relevance.
- Going forward, also the replacement of **central bank funding** (TLTRO, Funding for Lending/Term Funding Scheme) poses a key challenge for banks.

Source for all charts: EBA RAQ for banks, December 2018.

Outlook and recommendations

- **Risks to the global economy are on the rise.** Banks need to be prepared for adverse scenarios, which might affect funding, asset quality and profitability.
- **Banks should develop strategies and plans to address large refinancing** needs in the upcoming years, to replace central bank funding and meet requirements to build up loss absorbing capacity.
- Lending has started to increase, including to highly leveraged companies. **Banks must maintain prudent lending standards** and should not weaken their pricing or covenant requirements.
- **Elevated volatility in financial markets has shown banks' vulnerabilities stemming from holdings of financial instruments, especially sovereign exposures.** Value adjustments of such exposures directly affect banks' capital.
- **Despite its rising trends, bank profitability continues to be a key concern.** Business models need to be further adapted in order to achieve sustainable profitability and to increase the resilience of institutions to a more challenging economic environment.
- **Cyber attacks are one of the major threats to the EU banking sector, and conduct and legal risks have again been on the rise in 2018.** Banks should address potential operational weaknesses and identify and strengthen the control and governance framework.

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