

# PORTUGUESE BANKING SECTOR OVERVIEW

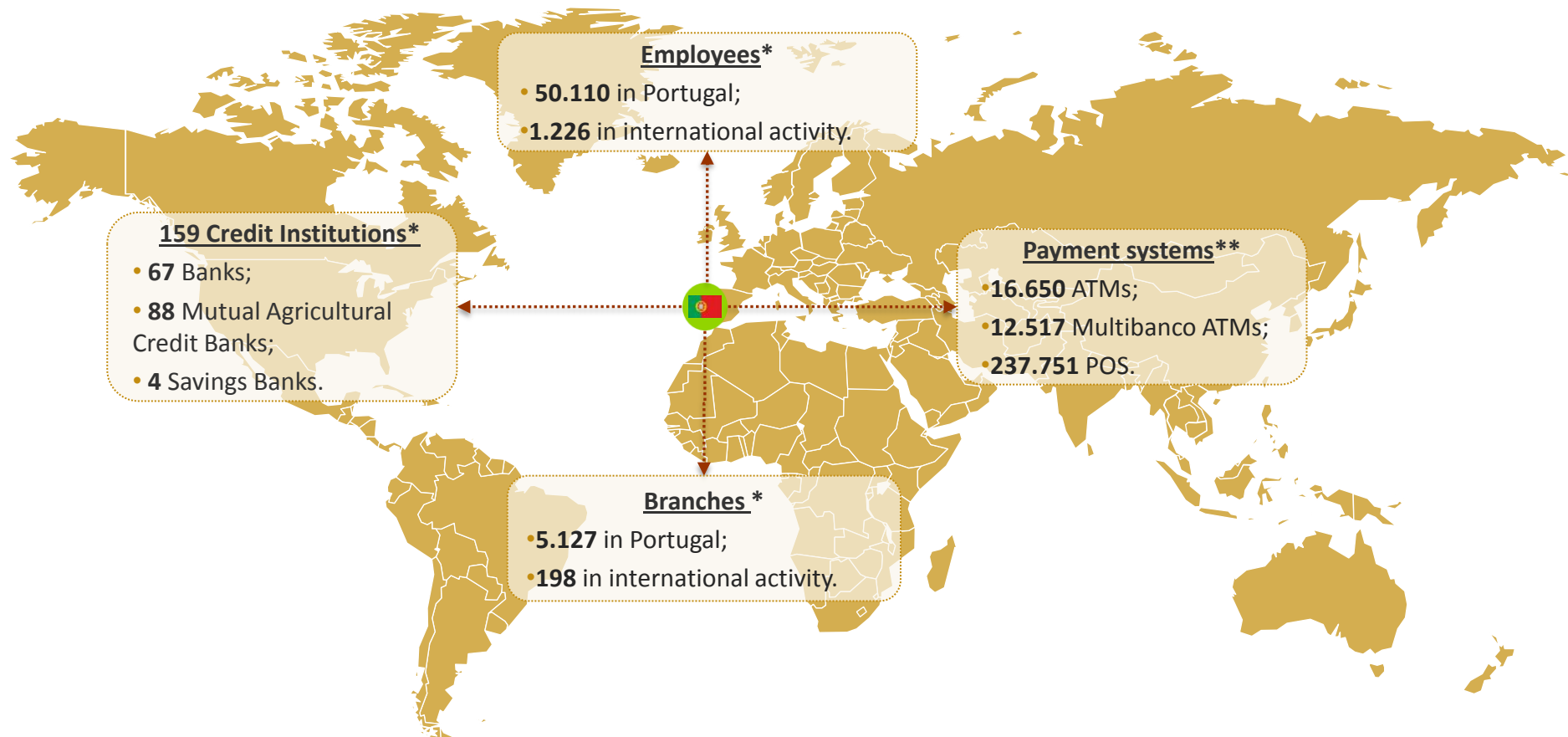
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# PORTUGUESE BANKING SECTOR OVERVIEW

- I. Main indicators of the Portuguese banking sector

# PORTUGUESE BANKING SECTOR (I/III)



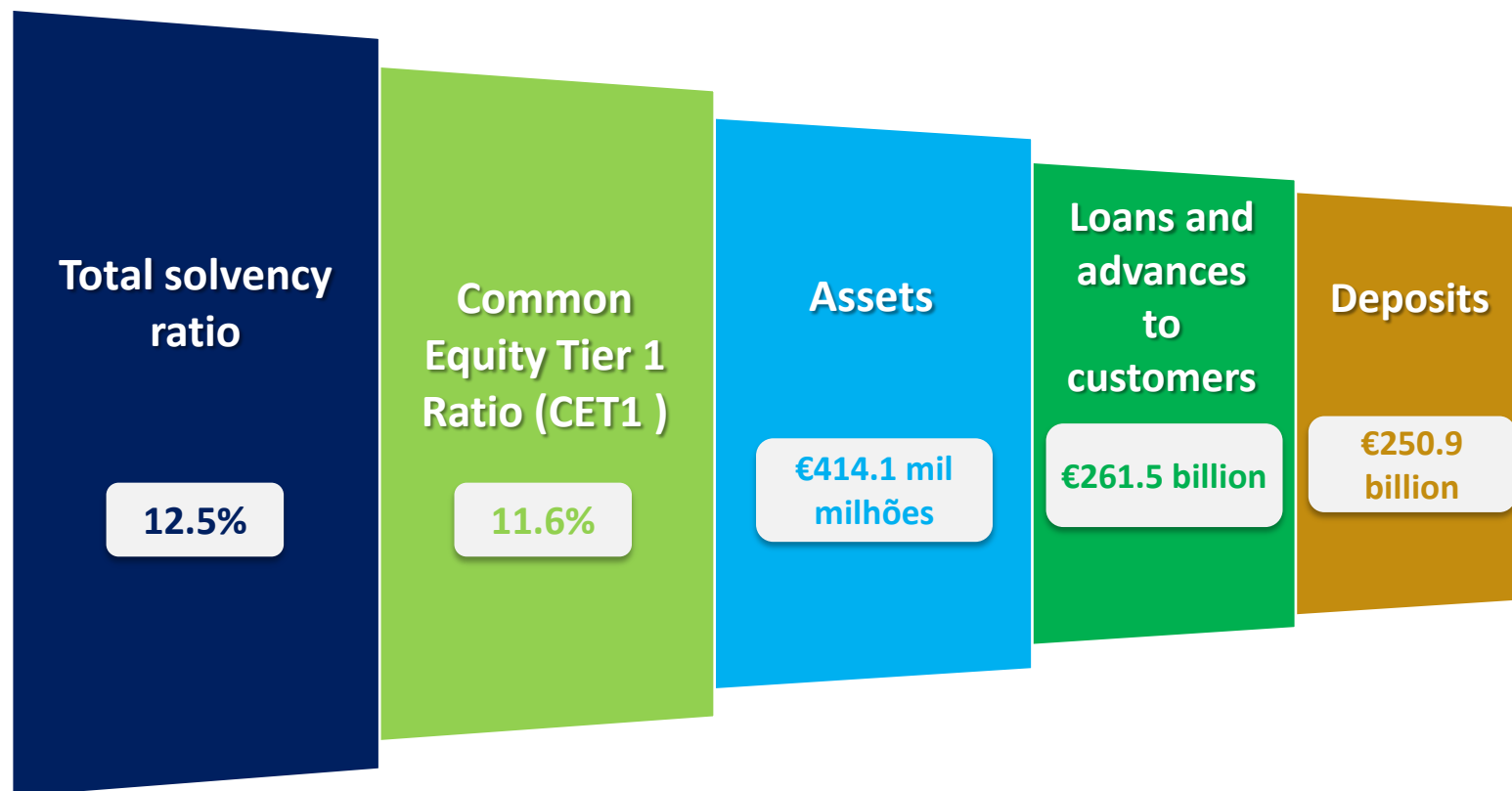
Source: APB, Banco de Portugal, ECB, INE.

\* June 2015

\*\* December 2015

# PORTUGUESE BANKING SECTOR (II/III)

Main indicators as at September 2015



Source: Banco de Portugal

# PORTUGUESE BANKING SECTOR (III/III)

## Recent developments (June to September 2015)

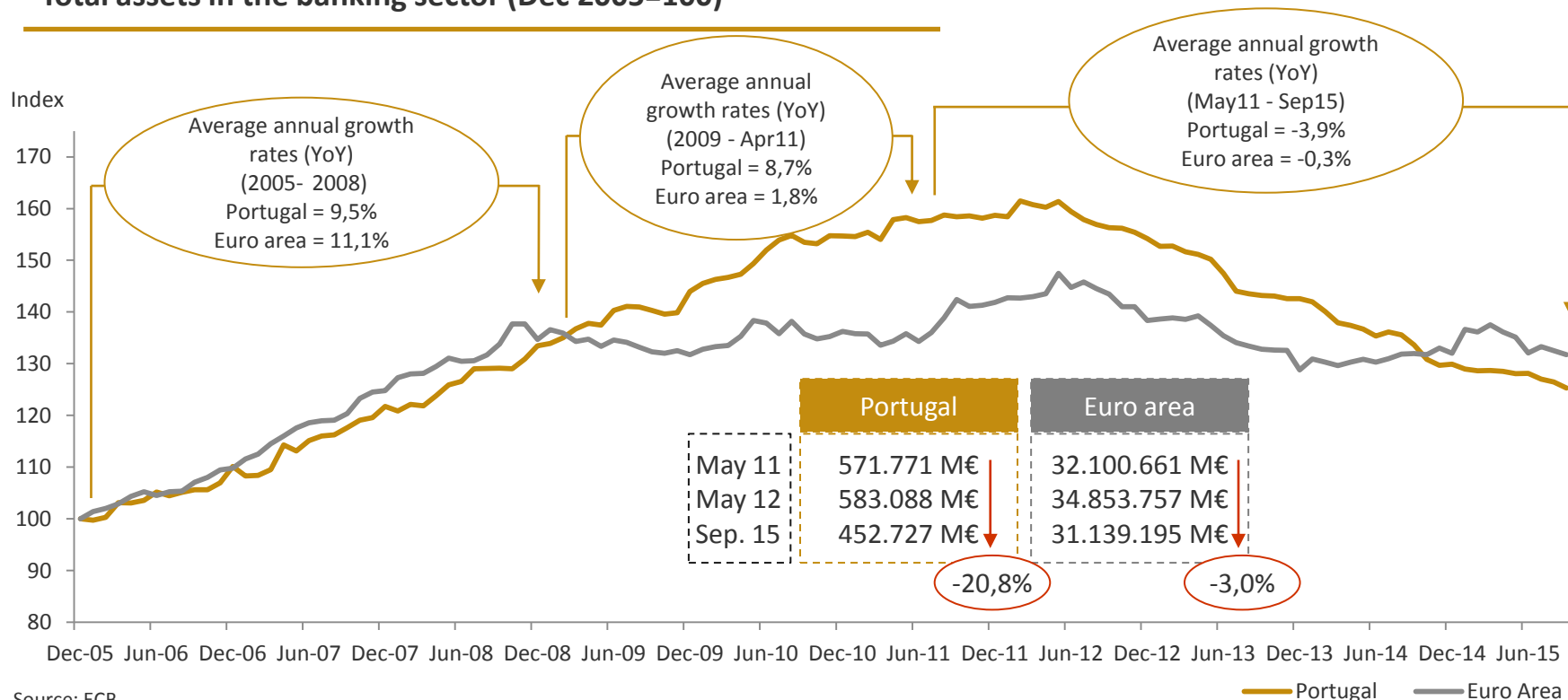
- **2.1% reduction in sector's assets in the period, making a total fall of 3.5% in the year. Loans and advances decreased 1% in the quarter and 2.4% in 2015.**
- **The credit standards remained practically unchanged in the quarter. Demand for loans and advances increased in consumer credit and mortgages, and remained unchanged in the non-financial firm sector.**
- **Deposits from the non-monetary sector grew 0.5% and remained practically unchanged over the year, and continued to be the Portuguese banks' main source of funding.**
- **The amount of borrowing from the ECB by the Portuguese banking sector continued to fall (-9.4% in the quarter and -25% year on year).**
- **Risk-weighted assets followed their downward trend of recent years.**
- **The Portuguese banks continued to meet their minimum capital ratios. Their Common Equity Tier 1 ratio (11.1%) was comfortably above the required 7% minimum.**

# PORTUGUESE BANKING SECTOR OVERVIEW

## II. Importance of the banking sector to the economy

Contrary to the euro area, growth in the Portuguese banks' assets continued after the 2008-2010 financial crisis and only began to fall after the Economic and Financial Adjustment Programme (EFAP).

**Total assets in the banking sector (Dec 2005=100)**

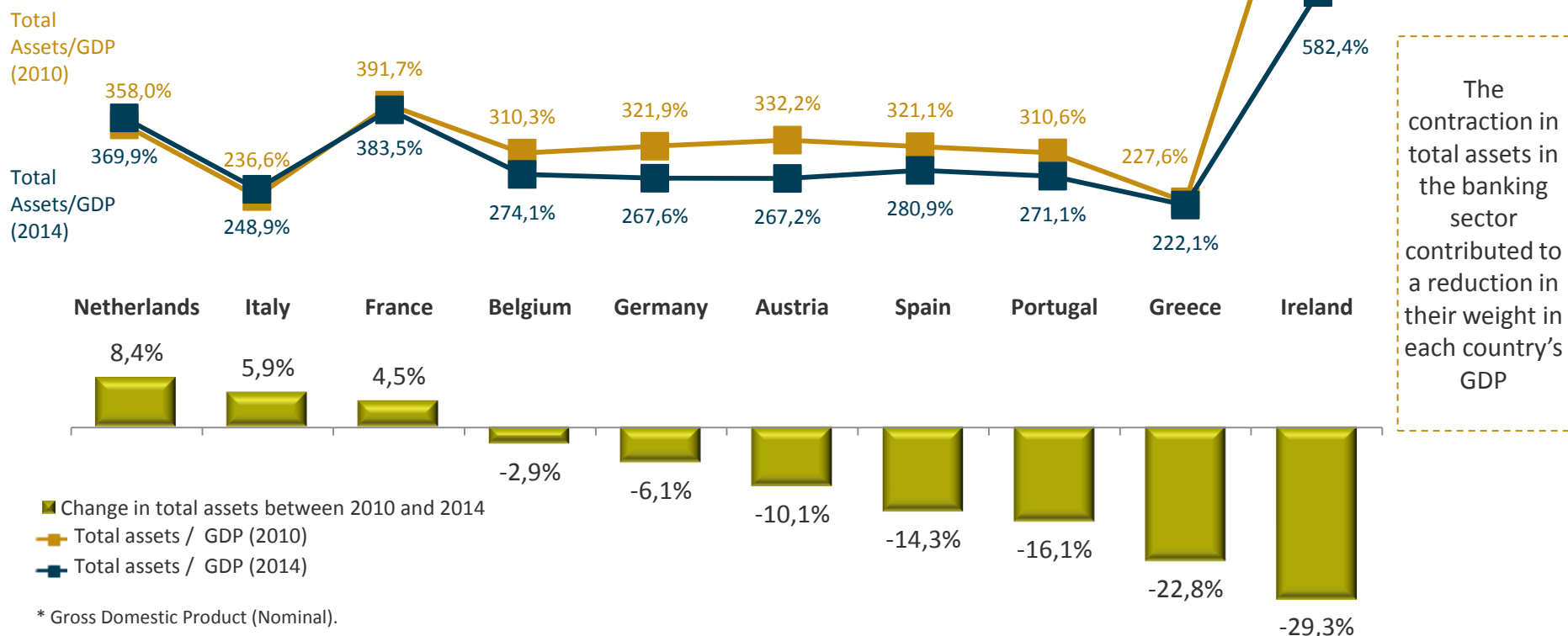


Source: ECB



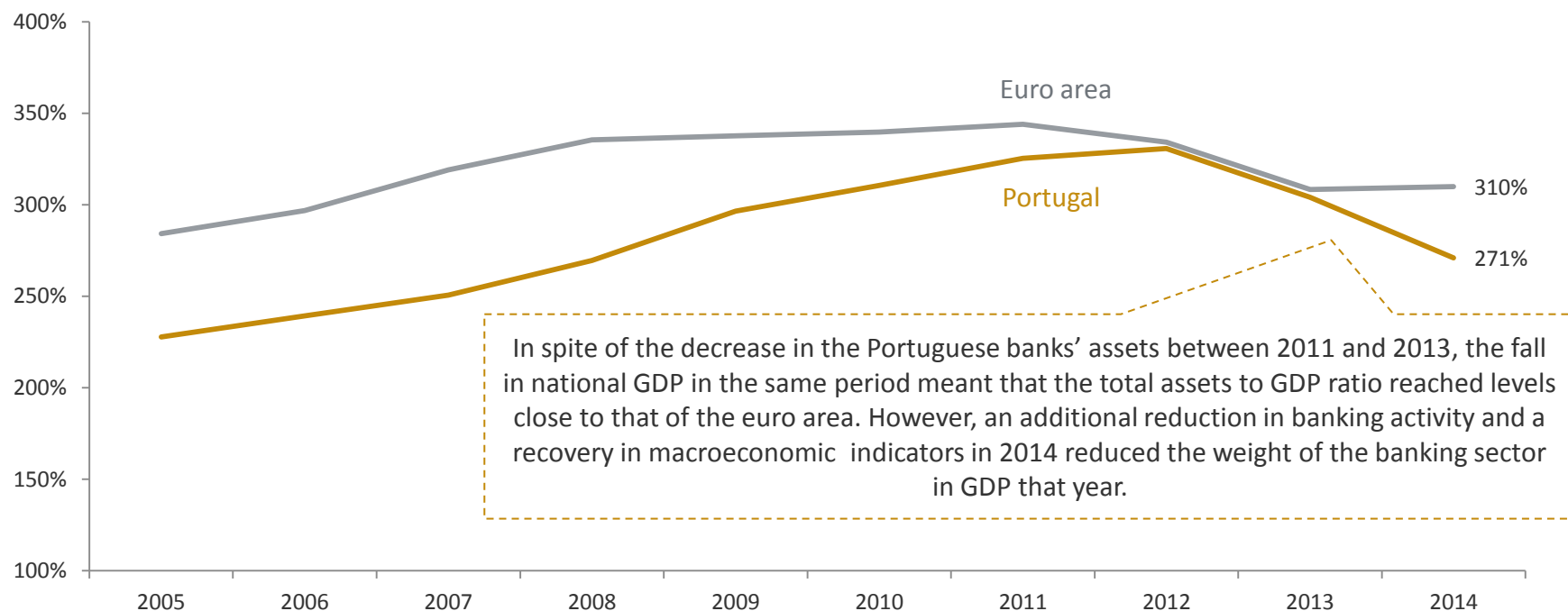
# The resizing of the banking sector took place not only in Portugal, but also in most euro area countries .

**Total assets over GDP\* and variation in total assets (2010 to 2014)**



The Portuguese banking sector plays an important role in the economy. Nonetheless, the weight of its assets in Portugal's GDP has been falling since the start of the EFAP.

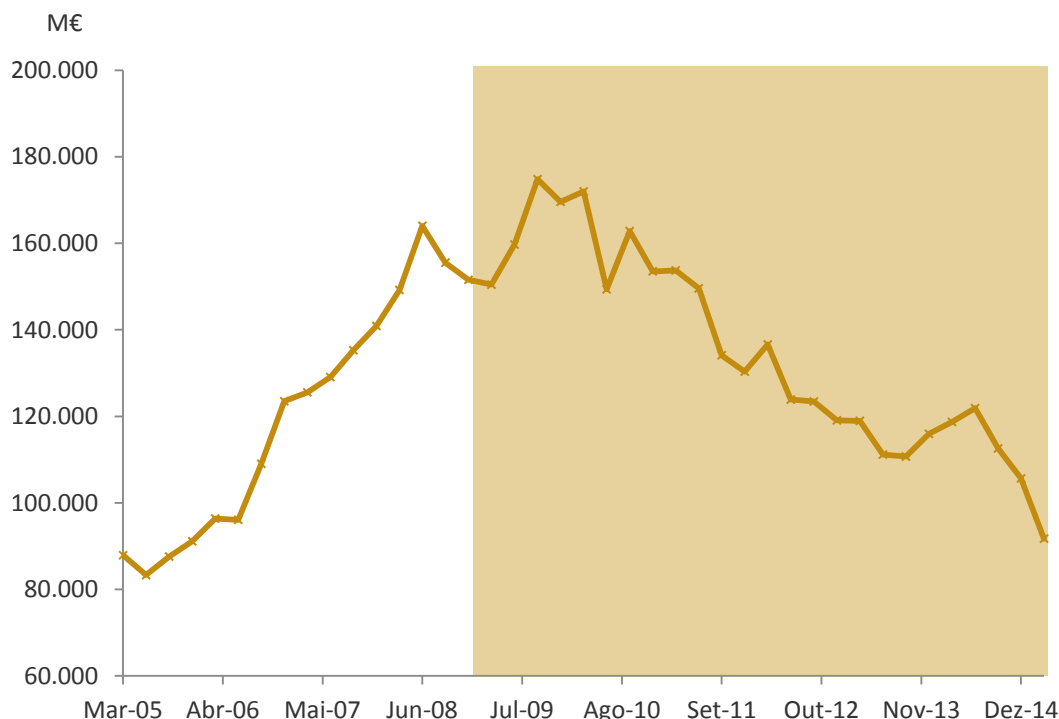
**Total assets of the banking sector in proportion to GDP, in Portugal and the euro area**



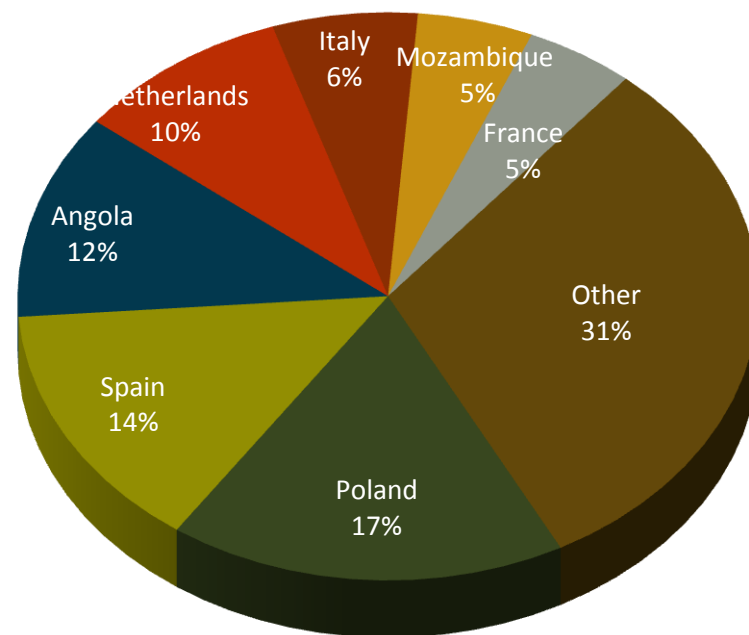
Source: ECB

## The deleveraging of the Portuguese banks resulted in a reduction in their international exposure.

### Loans and liabilities of the Portuguese banking sector to international entities \*



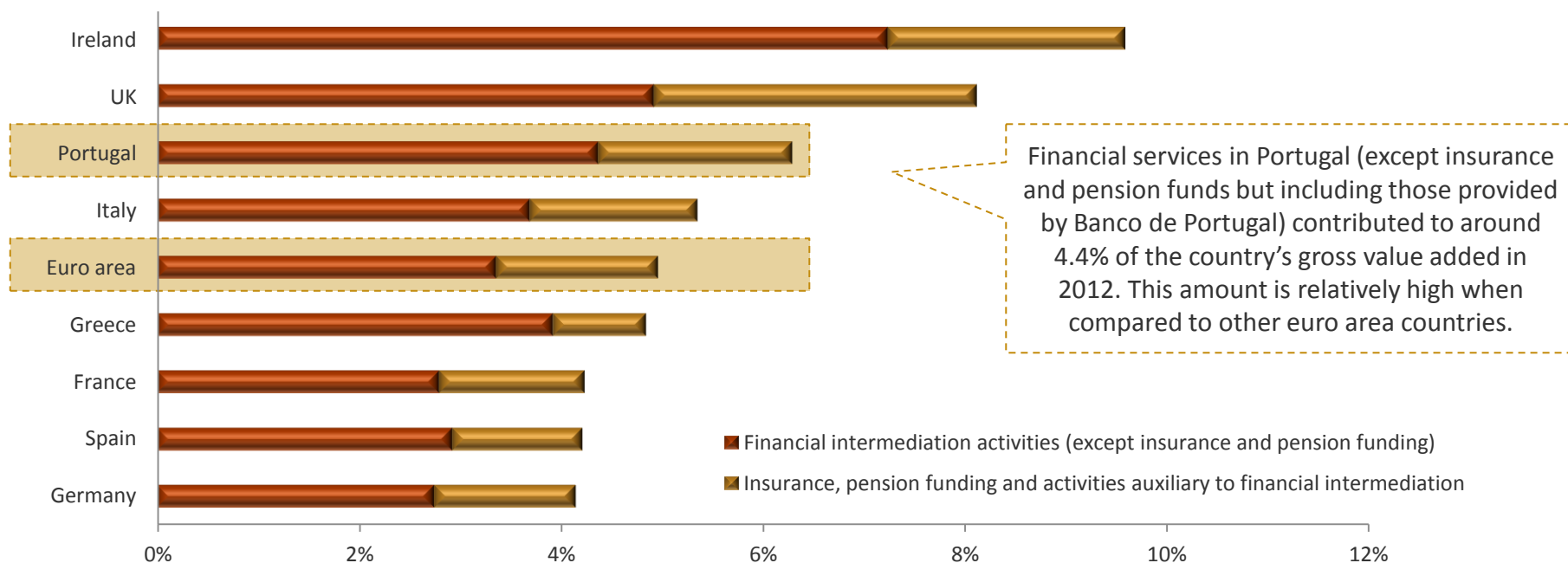
### Exposure by country (March 2015)



\*Defined as loans and liabilities of Portuguese banking groups on a consolidated basis, excluding intra-group exposure in relation to international entities, including loans, advances and deposits with other banks, loans and advances to non-banking entities and debt securities. It excludes derivatives and other risk-transfer instruments  
Source: Bank for International Settlements

## The contribution of financial services to national gross value added in Portugal is above that of the euro area.

### GVA\* of financial services in proportion to total GVA in Portugal and other European Union countries (2012)

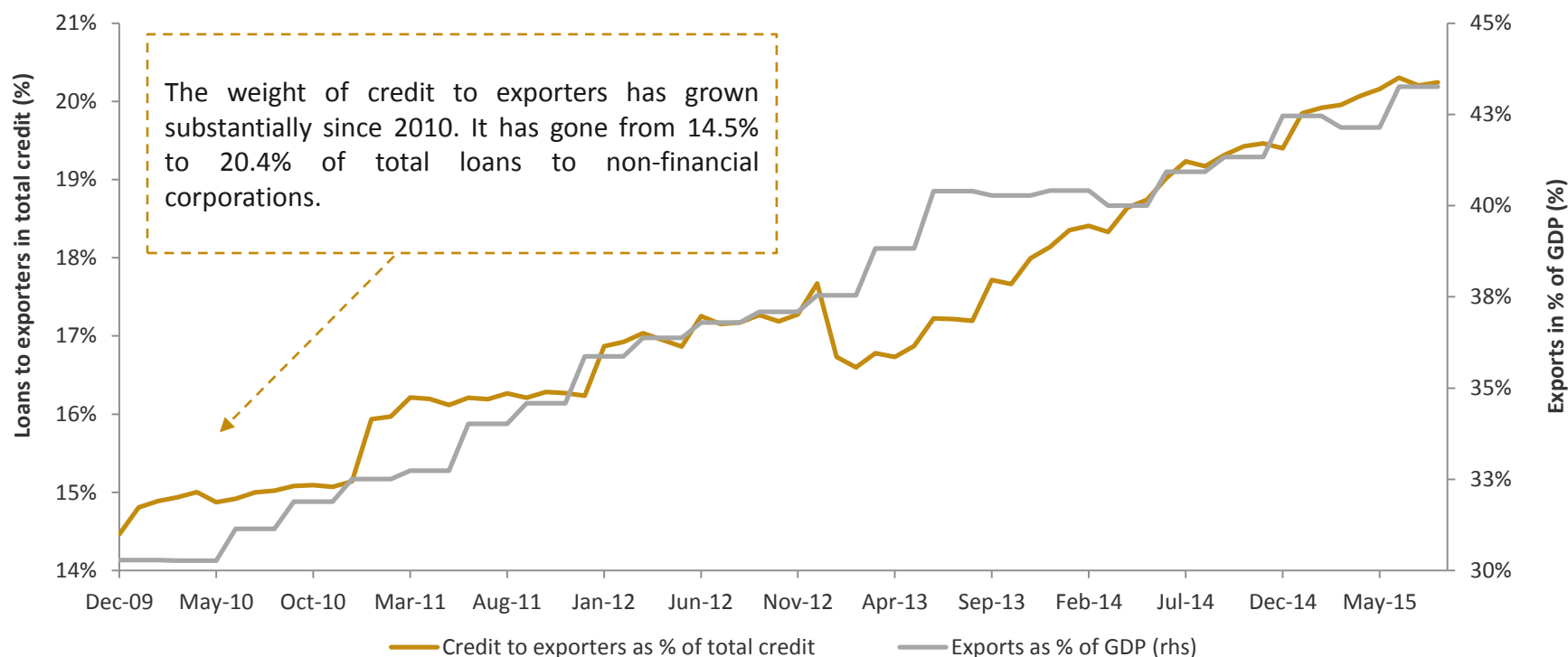


\*Gross Value Added, current prices.

Source: Eurostat, INE, Central Statistics Office Ireland

The increase in the weight of exports in GDP accompanied the trend towards growth in loans and advances to exporters by the Portuguese banking sector.

**Exports as % of GDP and credit to exporters as % of total credit**



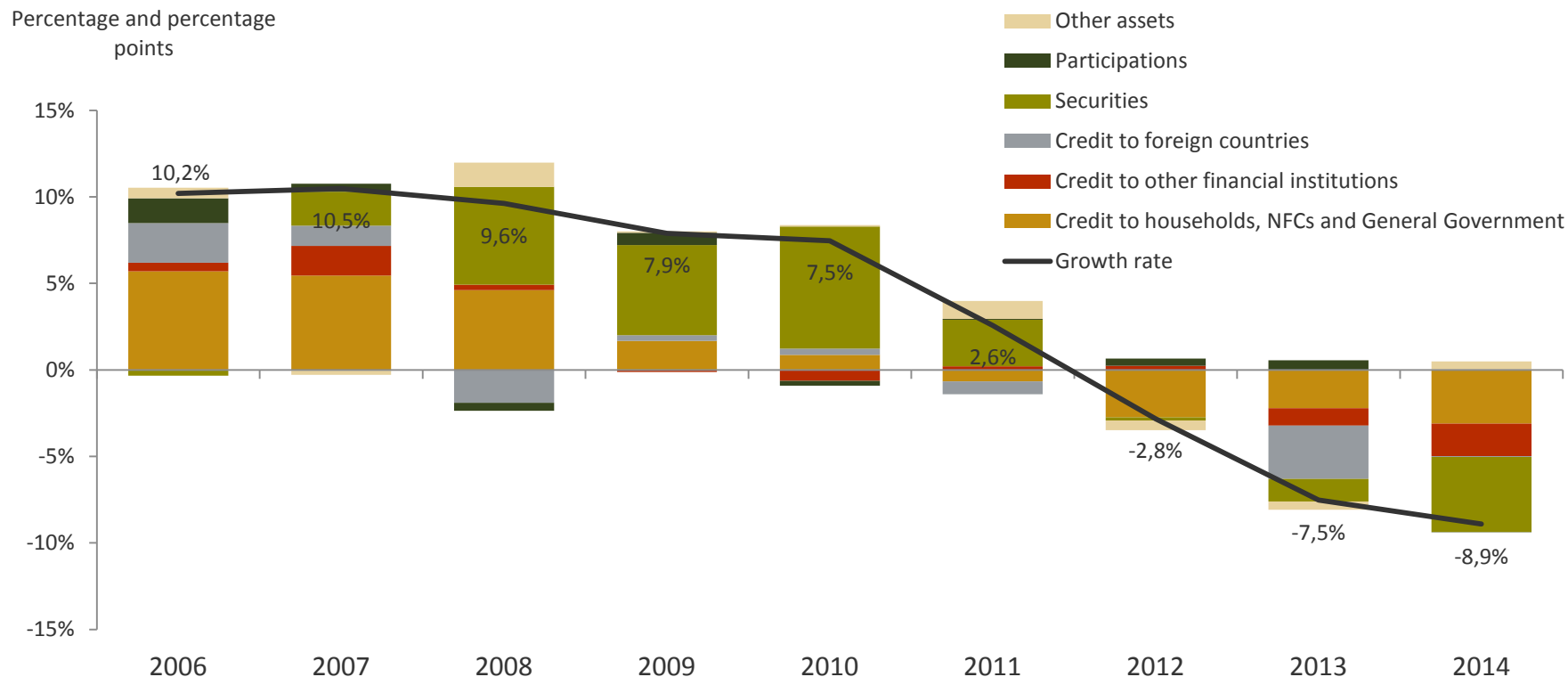
Source: INE, Banco de Portugal

# OVERVIEW OF THE PORTUGUESE BANKING SYSTEM

## III. Lending

The performance of total assets in 2014 was mainly due to a contraction in loans and advances and in securities portfolios.

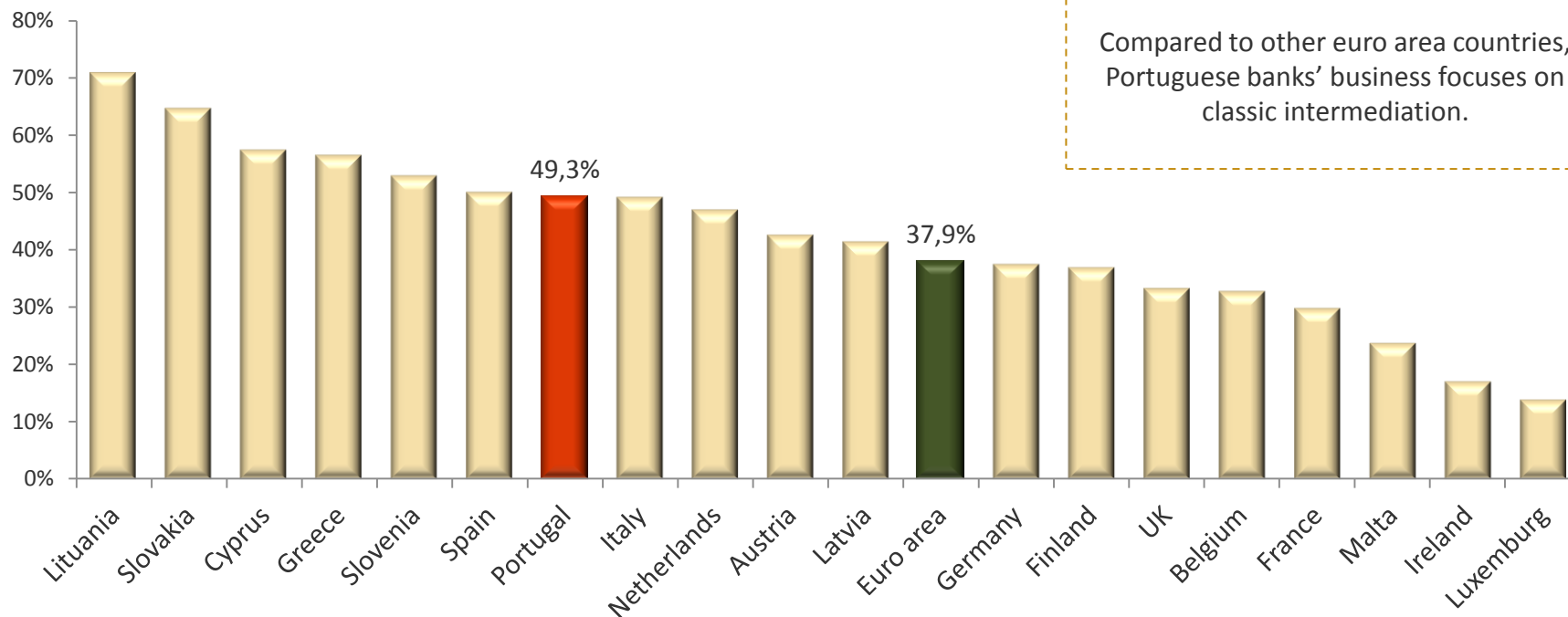
### Contribution of each asset item to aggregate annual variation



Source: Banco de Portugal

In spite of the contraction, loans and advances to customers continue to absorb almost 50% of the Portuguese banks' total assets.

**Loans to customers\* in proportion to total assets (September 2015)**



\* Loans to the non-monetary sector (gross end-of-month balances)

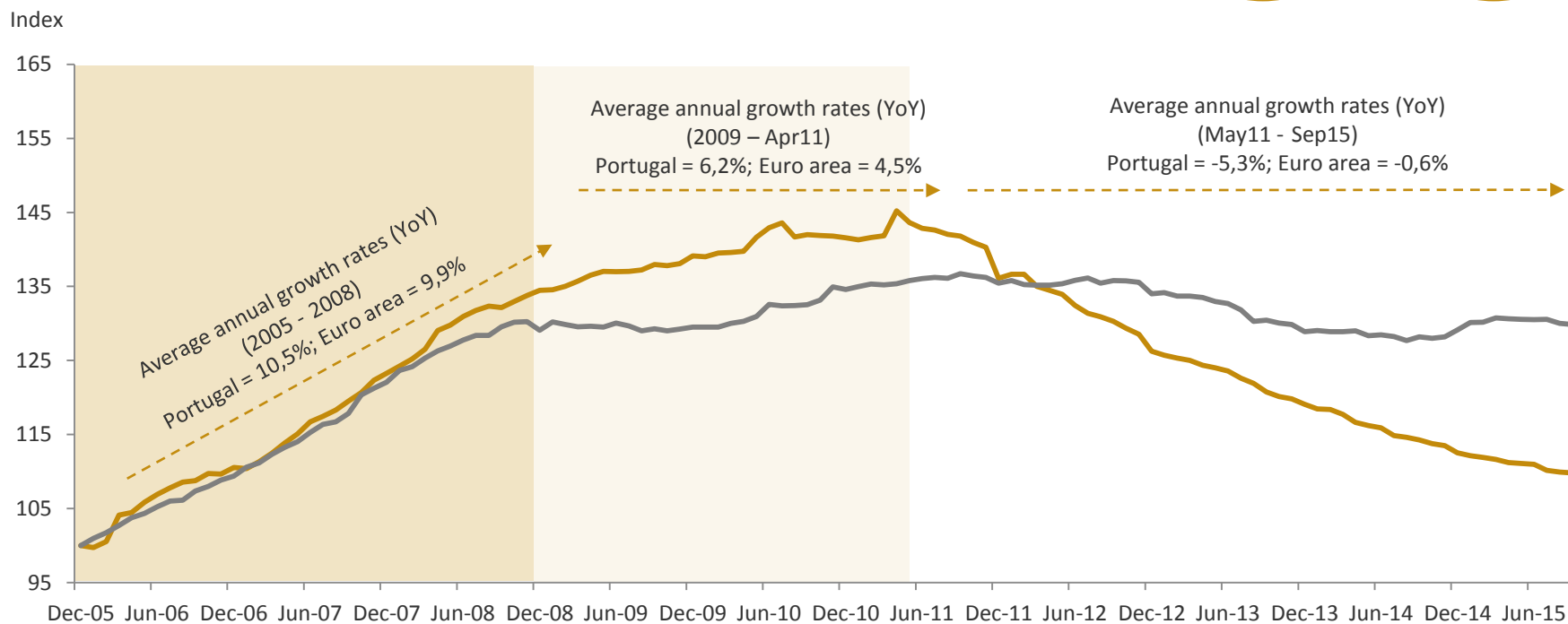
Source: ECB



Before the financial crisis, loans and advances were showing a sharp upward trend in Portugal and the rest of the euro area.

	Portugal	Euro area
May 10	295.313 M€	12.357.311 M€
May 12	275.381 M€	12.319.235 M€
Sep. 15	225.821 M€	11.817.157 M€
	-23,5%	-4,1%

**Loans and advances\* in Portugal and the euro area (Dec 2005=100)**



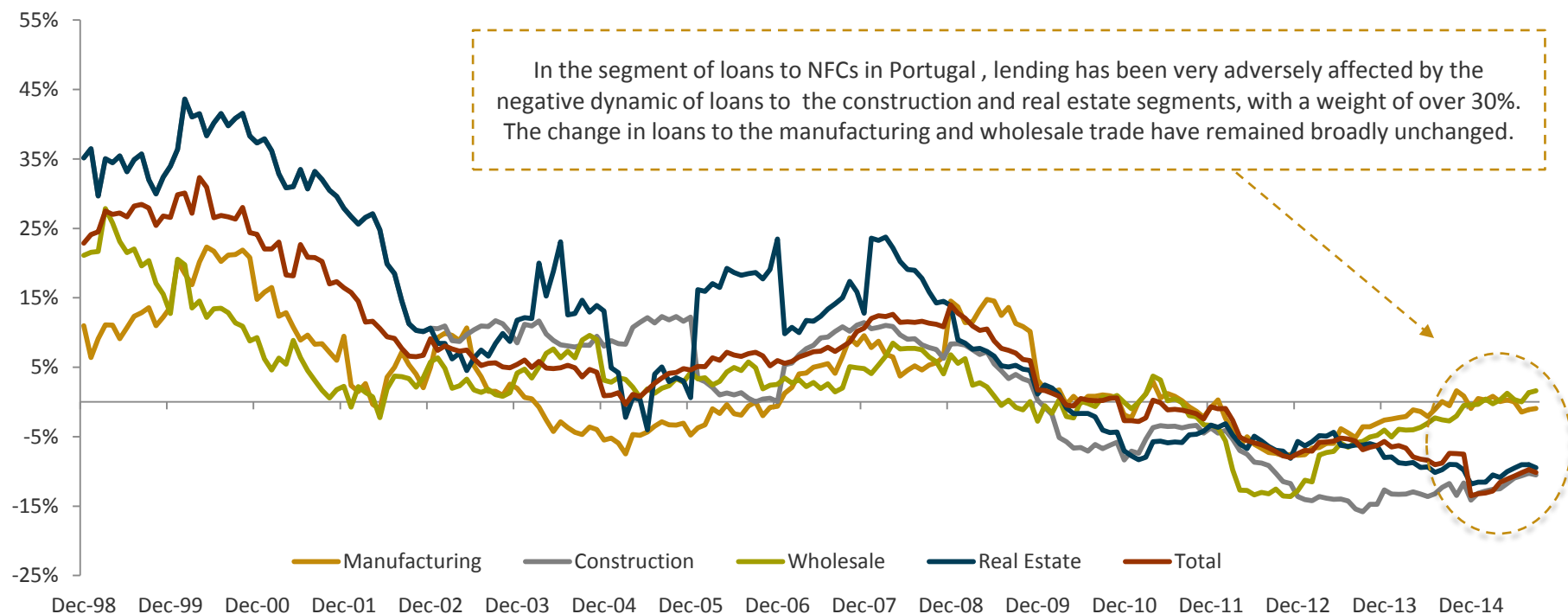
\* Loans to the non-monetary sector (gross outstanding amounts at the end of period).

Source: ECB

— Portugal — Euro area

The high weight and downward trend of loans to construction and real estate sectors has adversely affected the performance of total loans to non-financial corporations.

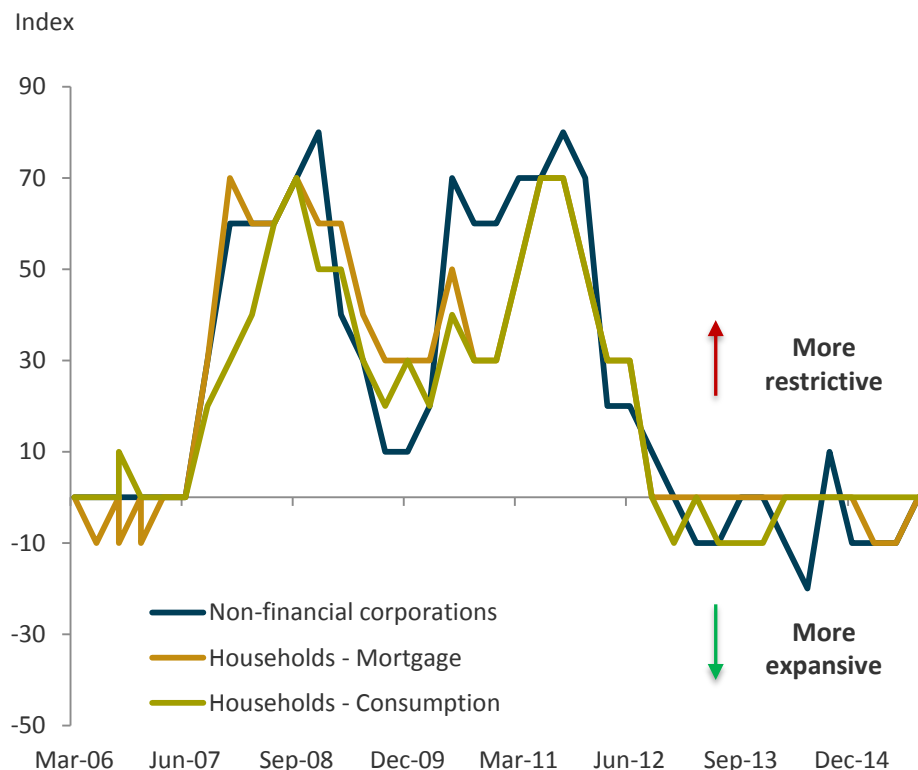
### Loans to non-financial corporations (YoY%)



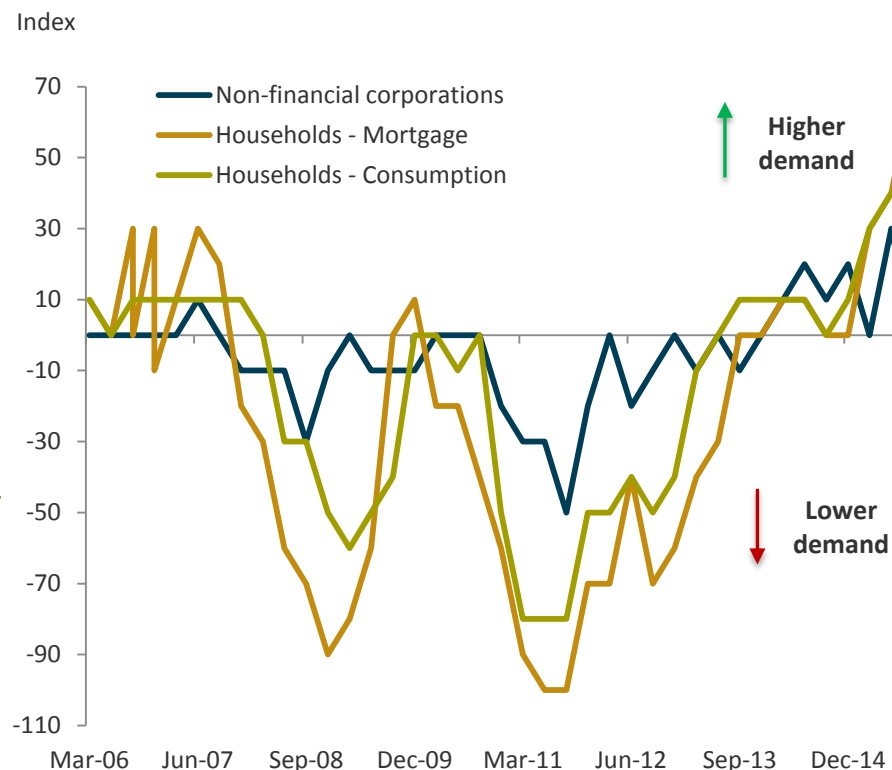
Source: ECB

In the recent past, demand for loans and advances increased and credit standards became more expansive.

**Diffusion index - Credit standards**



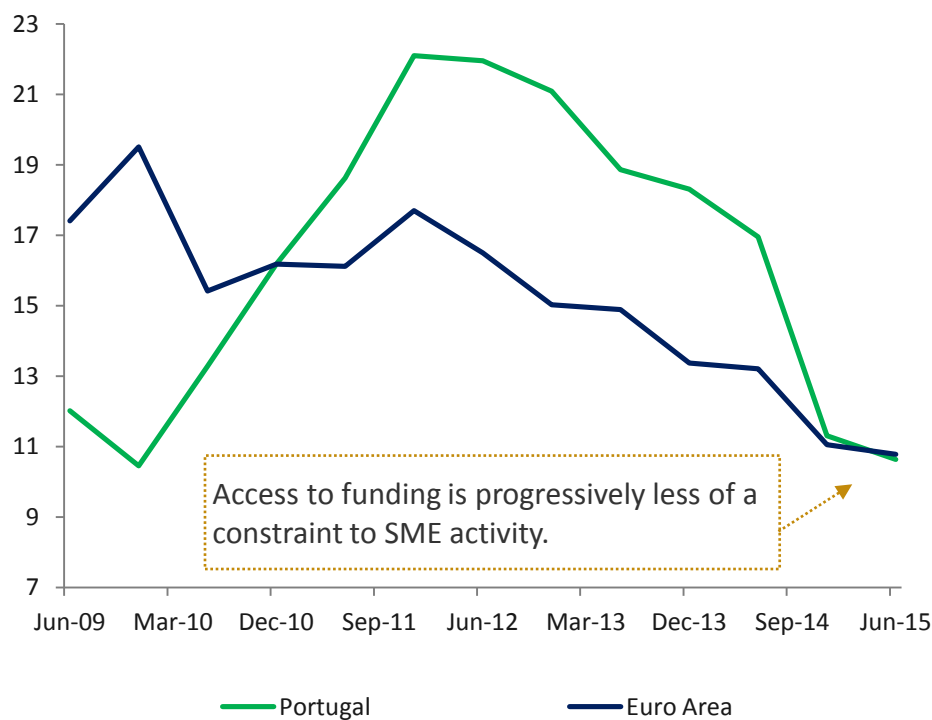
**Diffusion index - Demand for loans**



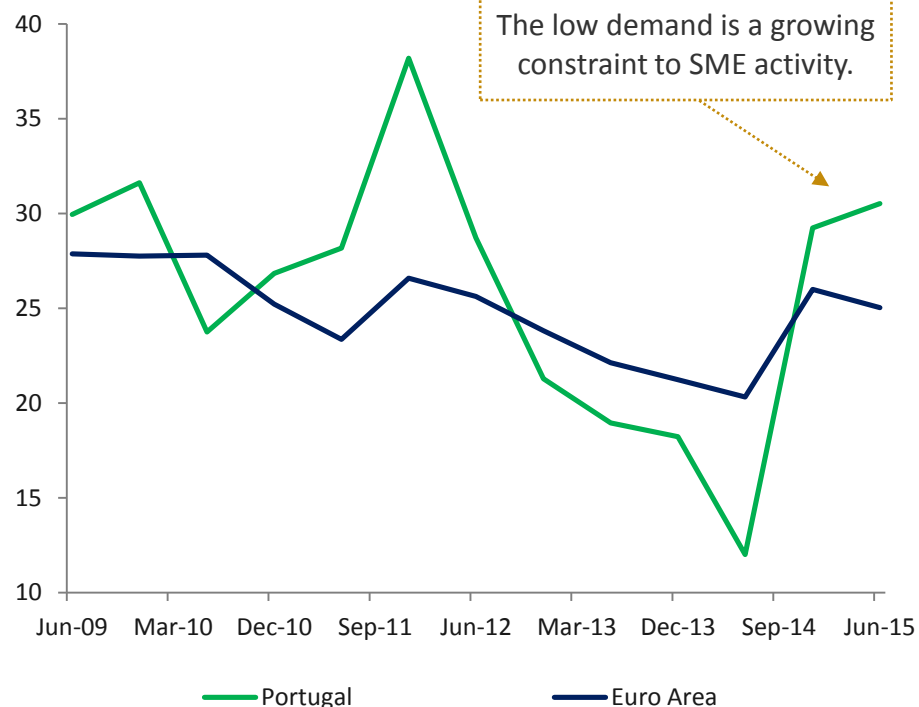
Source: Banco de Portugal (Bank Lending Survey)

# Access to funding constitutes less of a restriction on the business of SMEs, as opposed to the performance of demand.

**Main constraints on SMEs – access to funding**



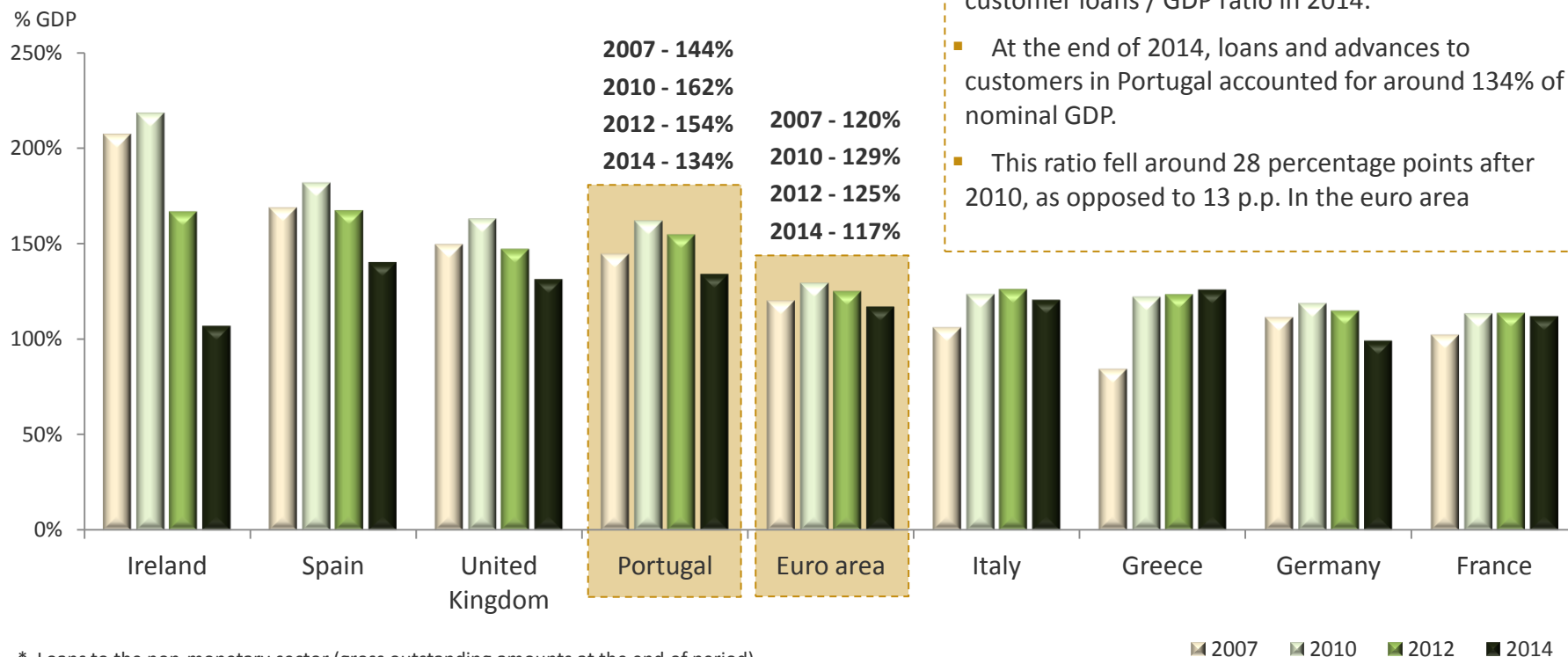
**Main constraints on SMEs – low demand**



Source: ECB

# The level of borrowing from banks in the Portuguese economy has been decreasing, coming closer to the rest of Europe.

## Customer loans\* / GDP ratio

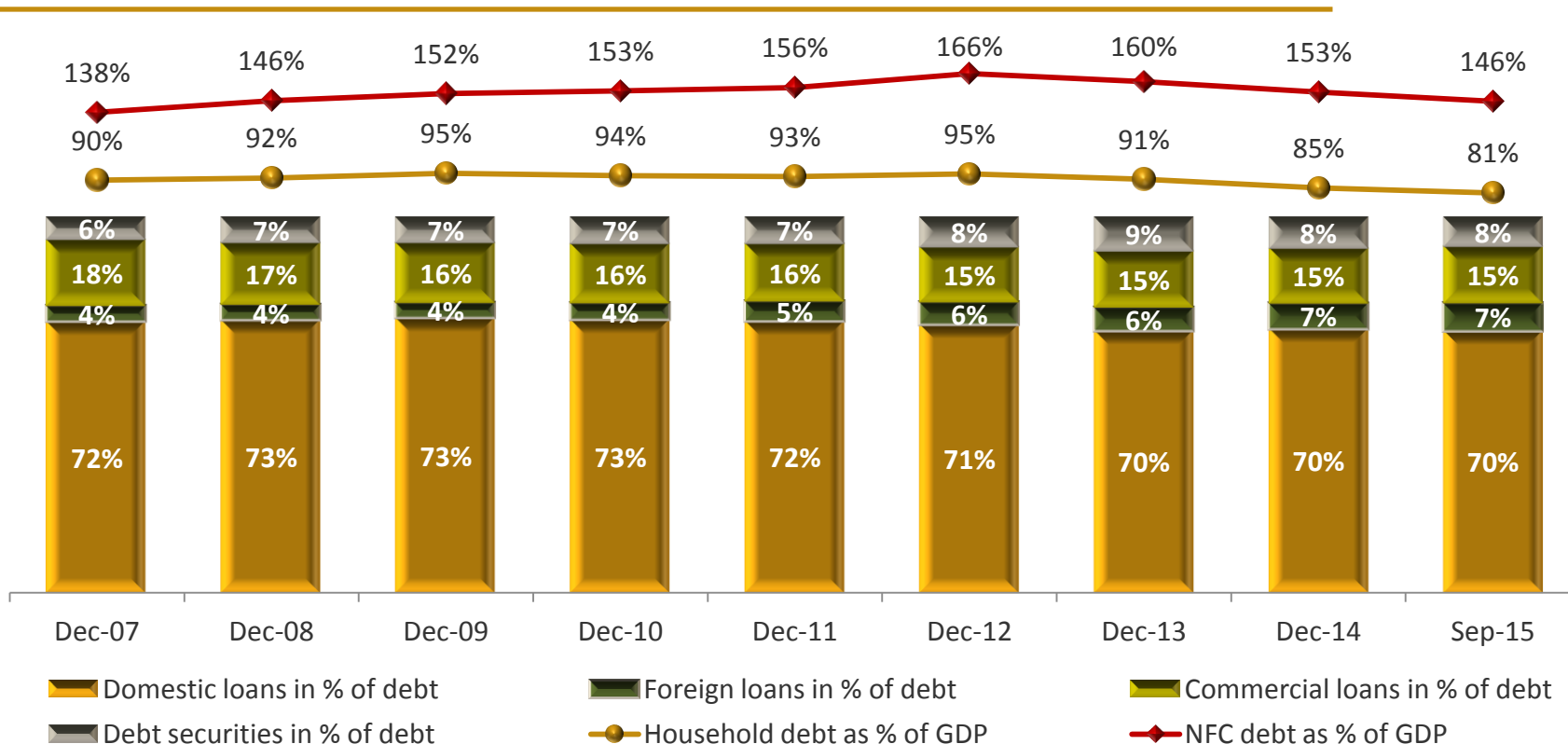


\* Loans to the non-monetary sector (gross outstanding amounts at the end of period)

Source: ECB, Eurostat

# Bank loans represent approximately 77% of the funding needs of the private sector of the Portuguese economy.

**Bank loans as a % of total debt and debt as a % of GDP – private sector \* (2007 – Sep 2015)**

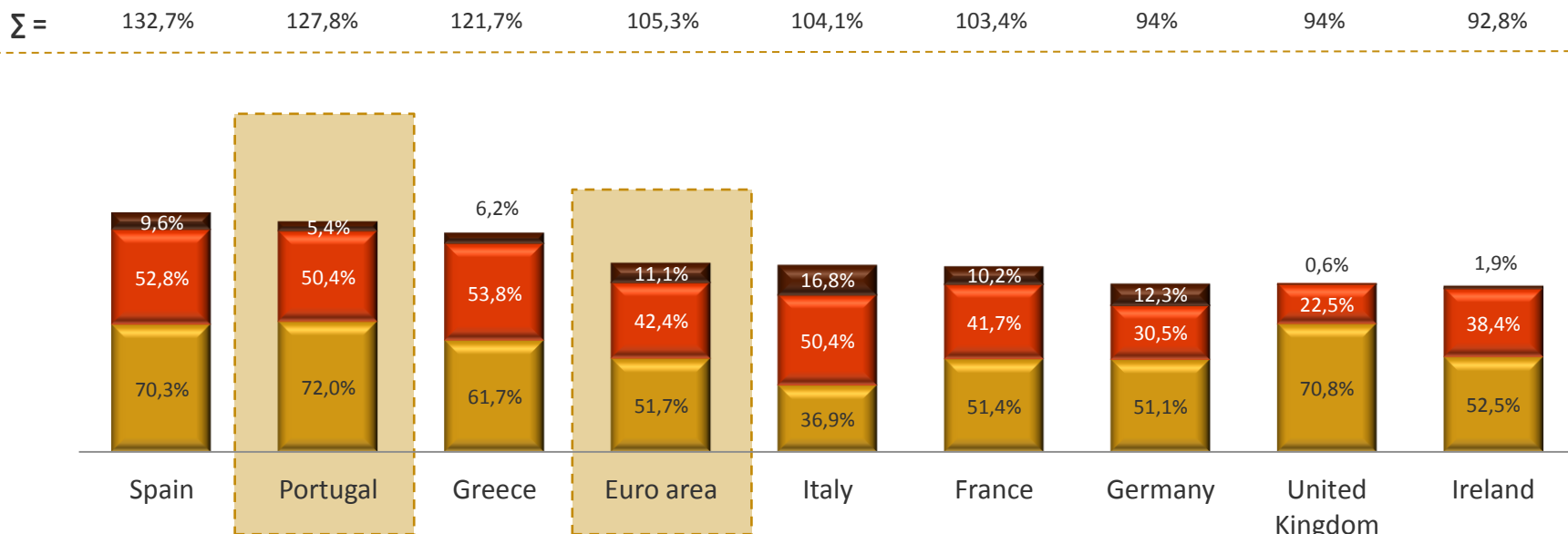


\* Includes households and non-financial corporations (outstanding amounts, end of month).

Source: Banco de Portugal

The weight of loans and advances to individuals and non-financial firms (NFCs) in Portugal's GDP is significantly higher than in most countries in the euro area.

**Weight of loans to private customers, non-financial corporations and the public administration in GDP\* - Portugal and other EU countries (December 2014)**



\* Includes only loans but not public debt securities

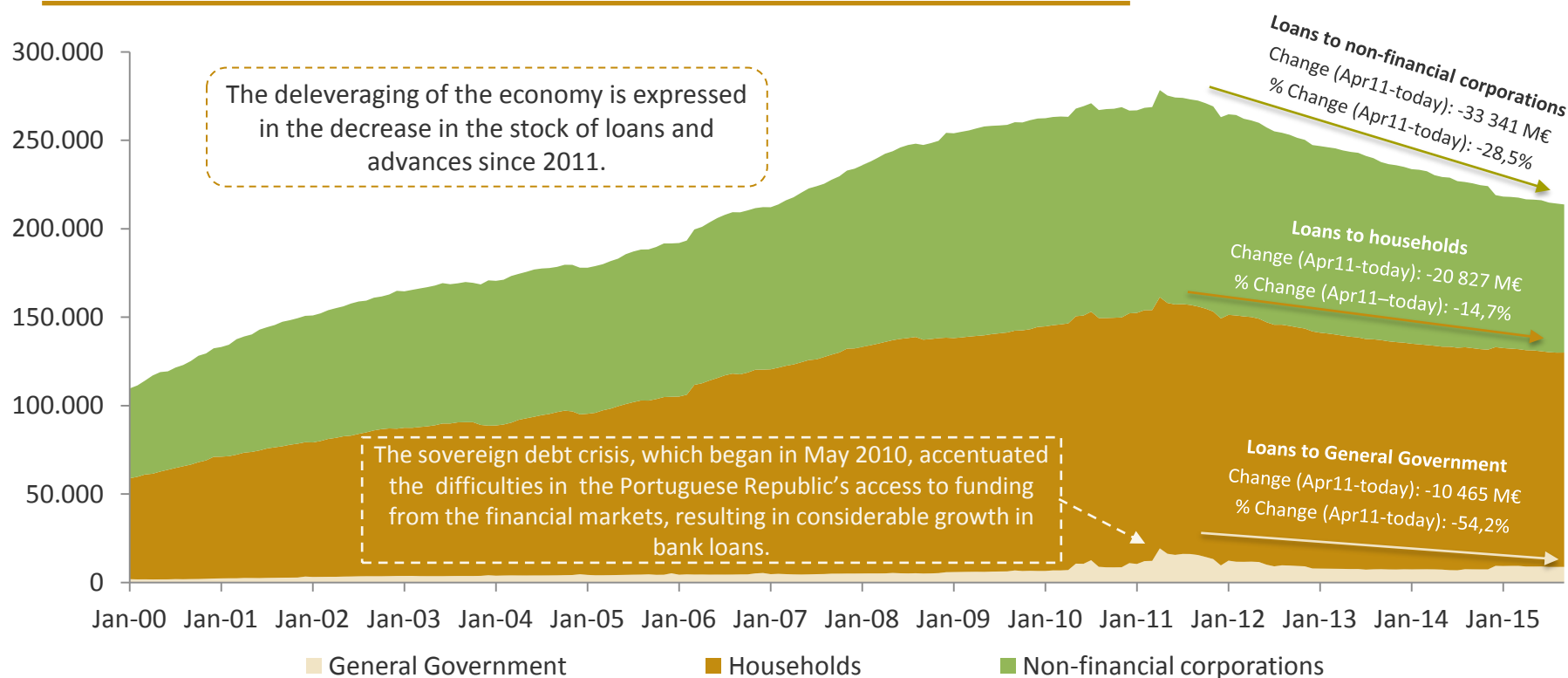
\*\* Includes publicly owned companies

Source: Ameco, ECB

■ General Government\*  
 ■ Non-financial corporations\*\*  
 ■ Households

# The stock of loans to the economy has continued to go down, and is at the lowest level since September 2006.

**Amount of loans and advances\* by institucional sector (EUR billion)**



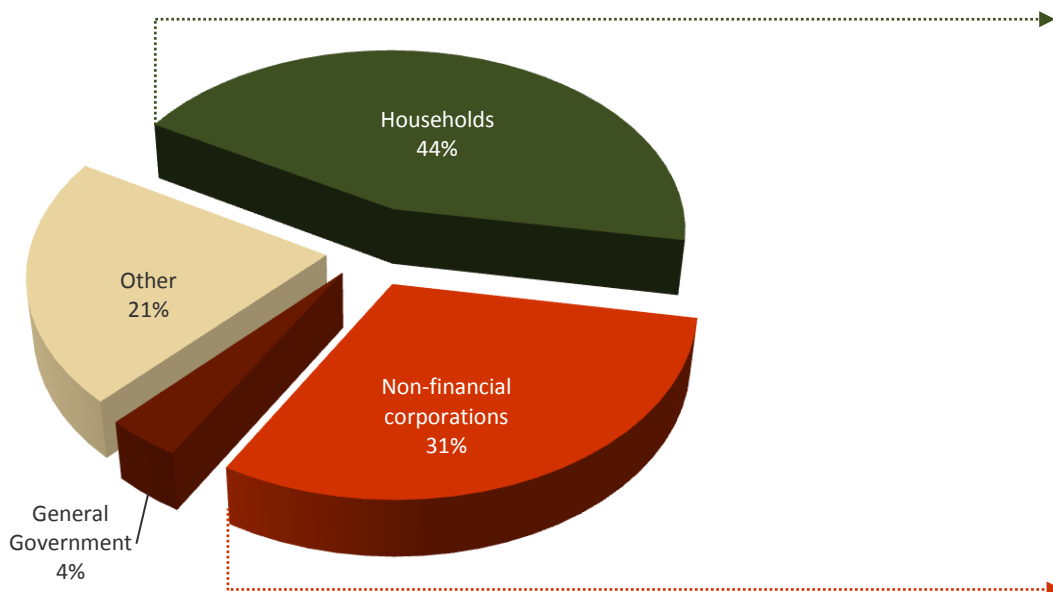
\* Gross outstanding amounts, end of period. Includes only loans (does not include public debt securities). Non-financial corporations include state-owned corporations.

Source: Banco de Portugal

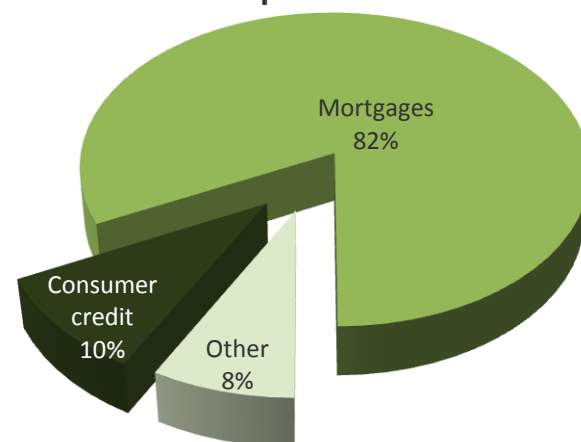


While loans to private customers are mostly mortgages, loans to non-financial firms are mainly for the construction and real estate sectors.

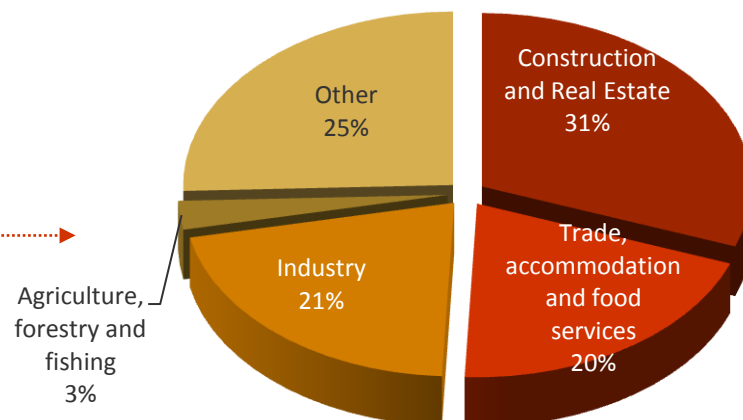
**Loans\* (September 2015)**



**Loans to private customers**



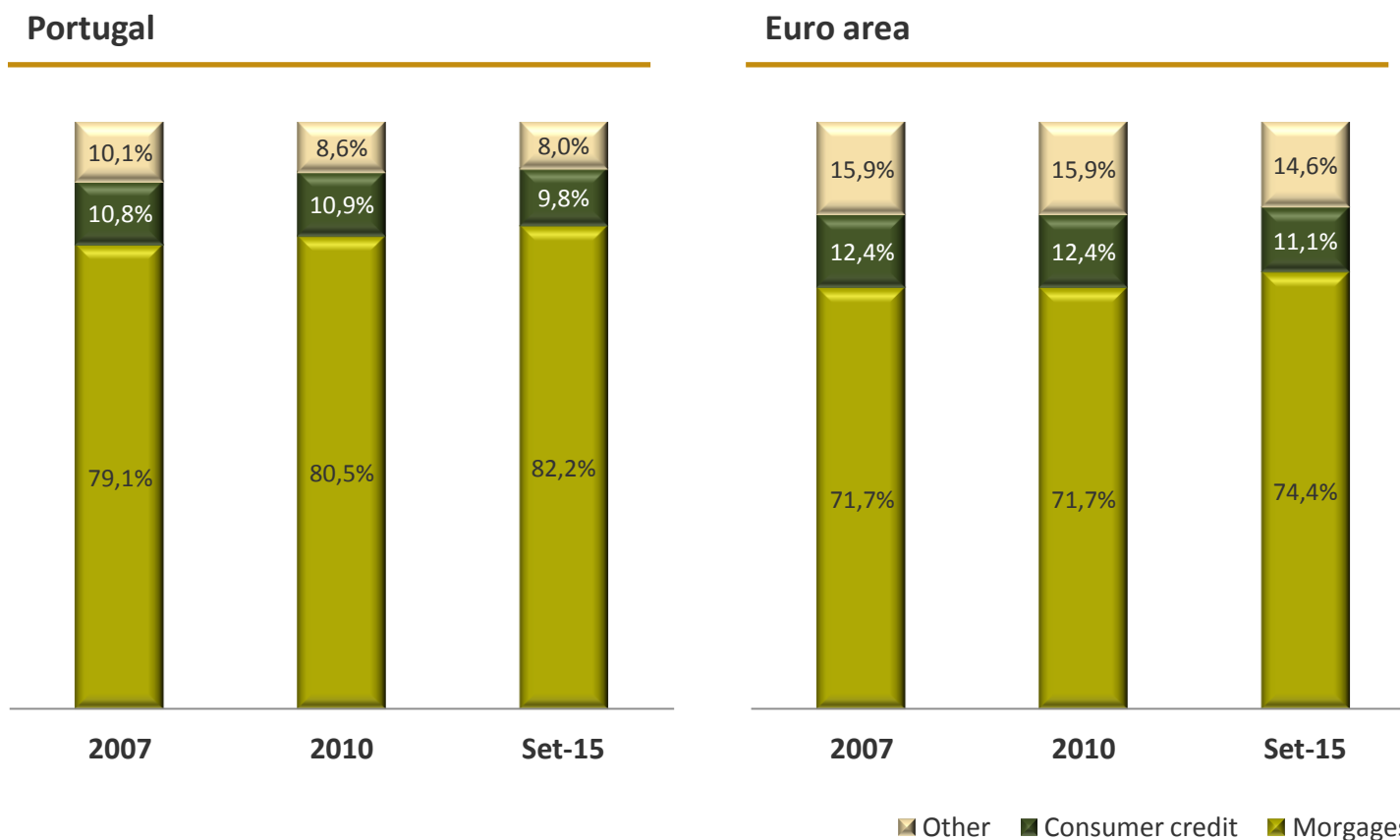
**Crédito a sociedades não financeiras**



\* Loans to the monetary and non-monetary sectors, including non-residents (gross outstanding amounts at the end of the period).

Source: Banco de Portugal

The proportion of mortgage loans in total loans is higher in Portugal than in the euro area.

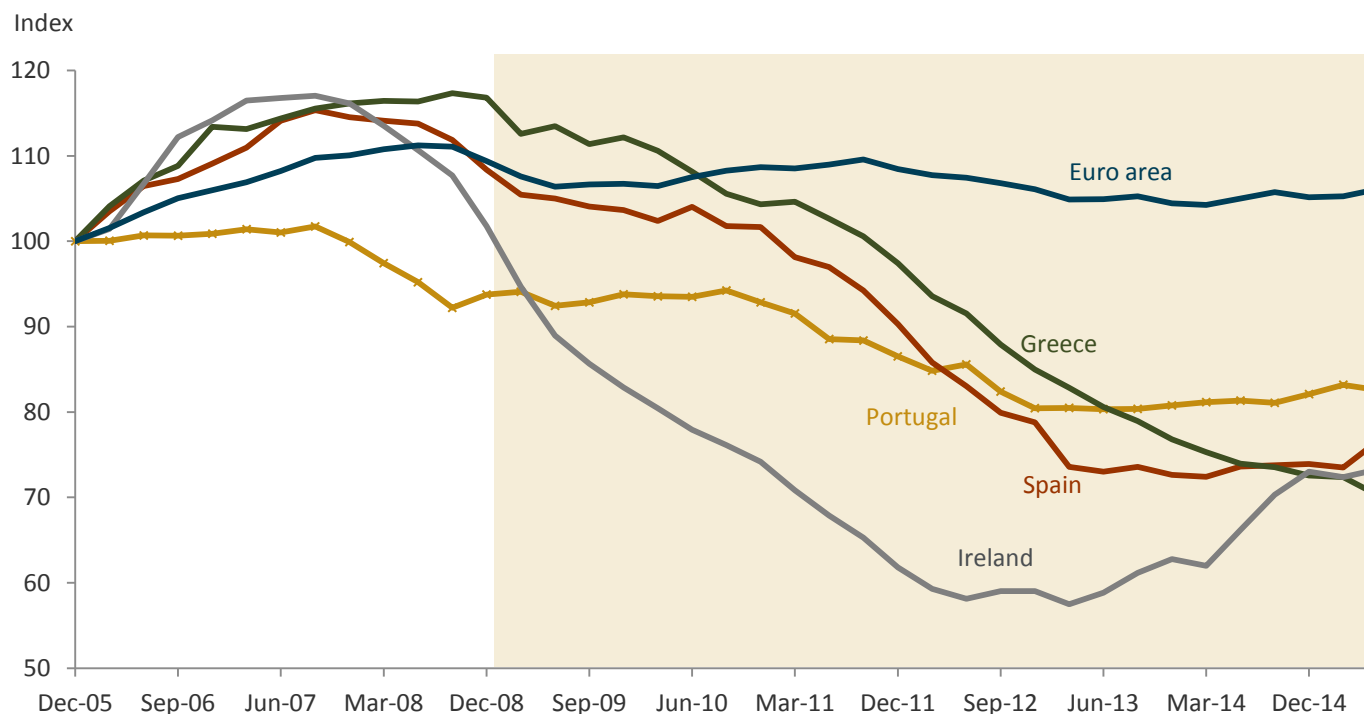


The weight of consumer credit in total loans granted to private customers has been falling in Portugal and the euro area. This is of credit is less important in Portugal than in the euro area, however.

Source: ECB

Housing prices in the peripheral euro countries have been falling, though less markedly in Portugal.

**Housing price index in Portugal and other euro area countries (Dec 2005=100)**



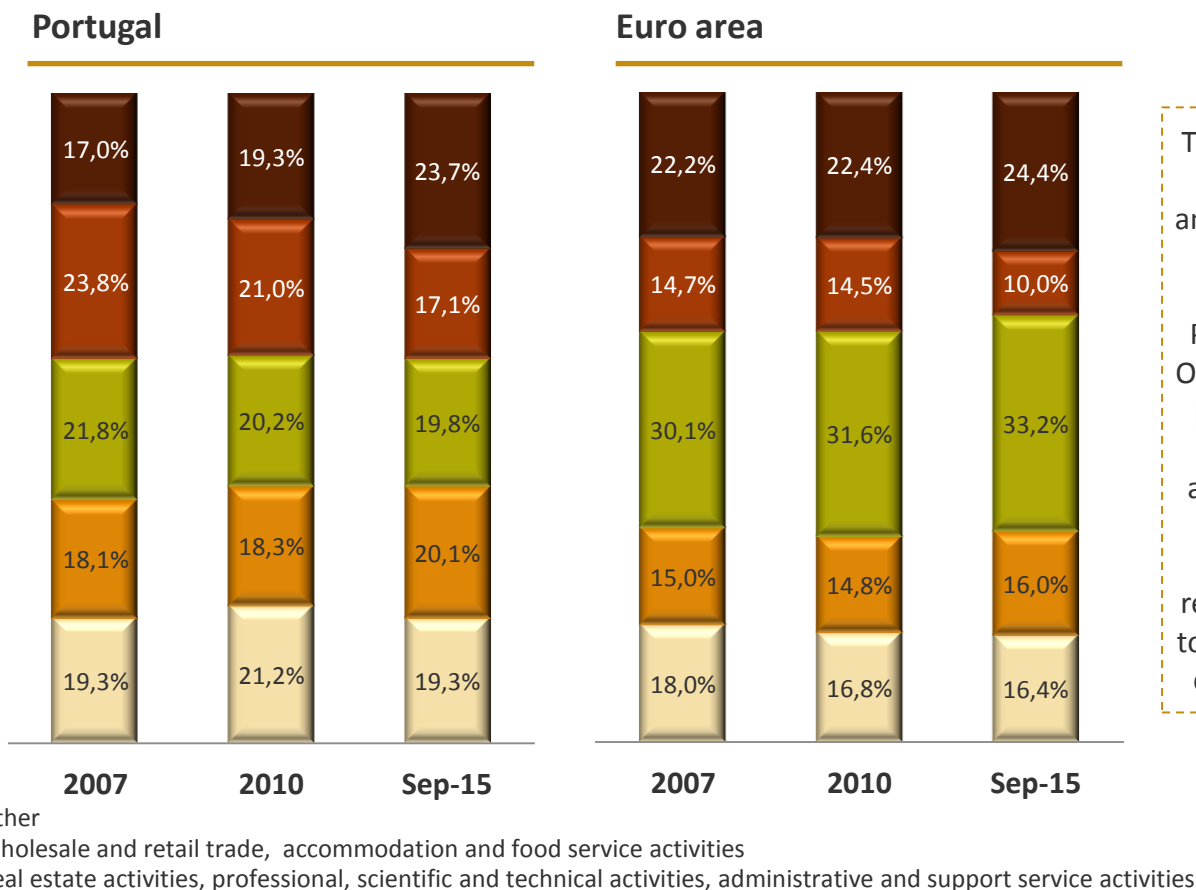
The property sector in Portugal did not experience a speculative boom prior to the crisis, unlike Spain, Ireland and Greece.

Source: ECB

## The proportion of loans and advances per sector in Portugal is more evenly distributed than in the rest of the euro area.

Loans to agriculture and industry carry more weight in the rest of the euro area than in Portugal. However, this segment's share in total loans to NFCs has increased considerably in Portugal in recent years and come closer to European figures.

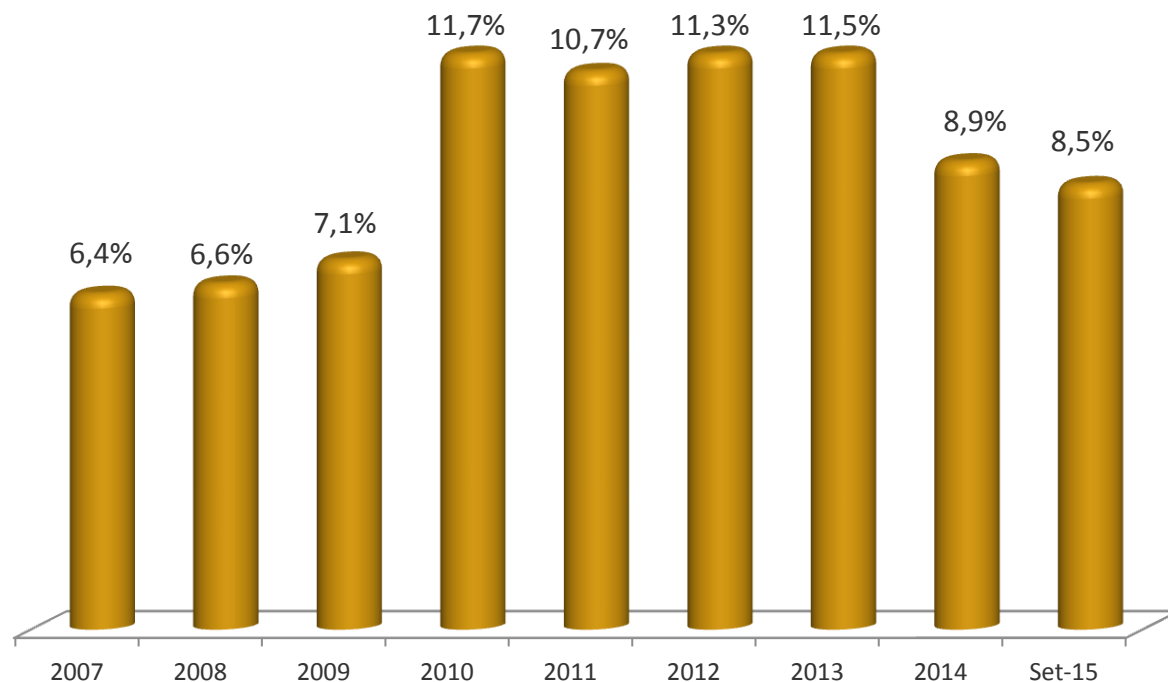
The aggregate weight of the construction and real estate sectors has been falling in aggregate terms in Portugal since 2007. On the other hand the proportion of these sectors in the euro area grew until 2012 due to real estate activity. The trend reversed recently due to a contraction in the construction sector.



Source: Banco de Portugal, ECB

## State-owned companies account for around 9% of the total debt of non-financial corporations to the resident financial sector.

### Debt of state-owned non-financial corporations to the financial sector in Portugal\*



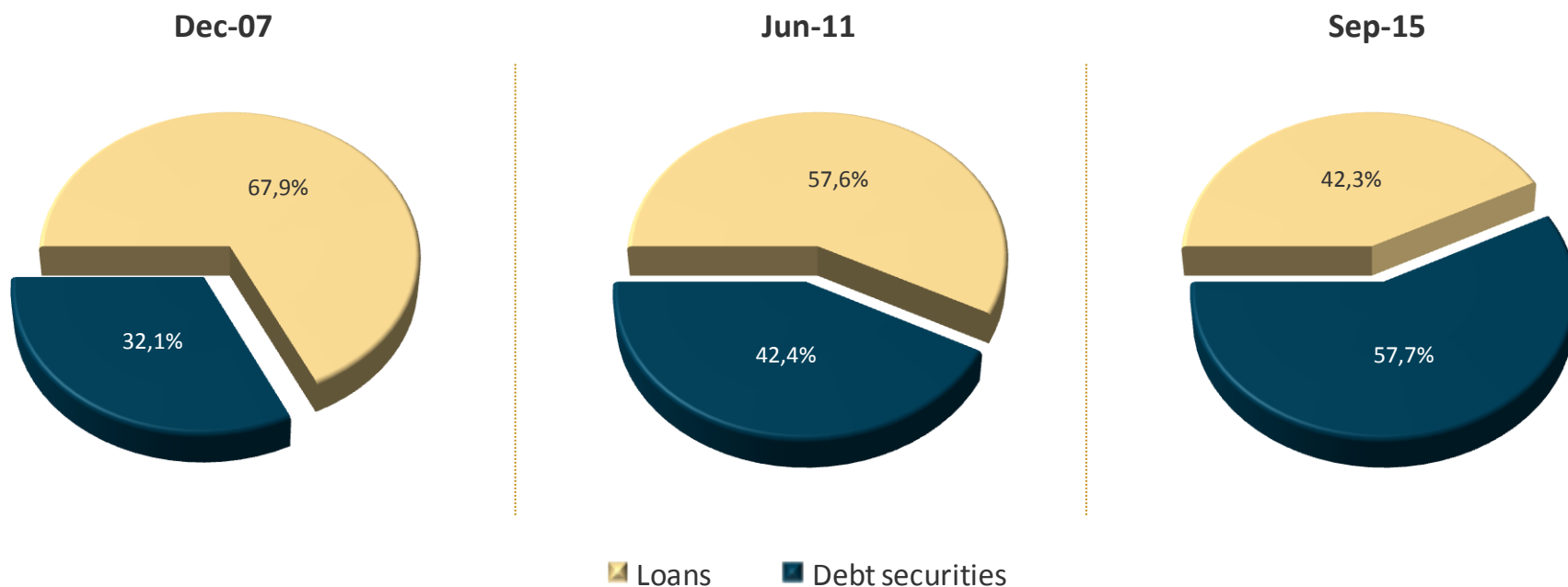
The debt of the state-owned non-financial corporations account for a substantial part of total funding to non-financial corporations in Portugal. The amount increased considerably after 2009 due to the sovereign debt crisis. In spite of a reduction up to 2015, it is still higher than before 2010.

\* As a percentage of the balances of loans obtained and bonds issued by non-financial firms as opposed to the resident financial sector. The concept of resident financial sector includes banks and other financial institutions.

Source: Banco de Portugal

The debt of publicly owned companies to the resident financial sector in the form of securities has been gaining importance over loans.

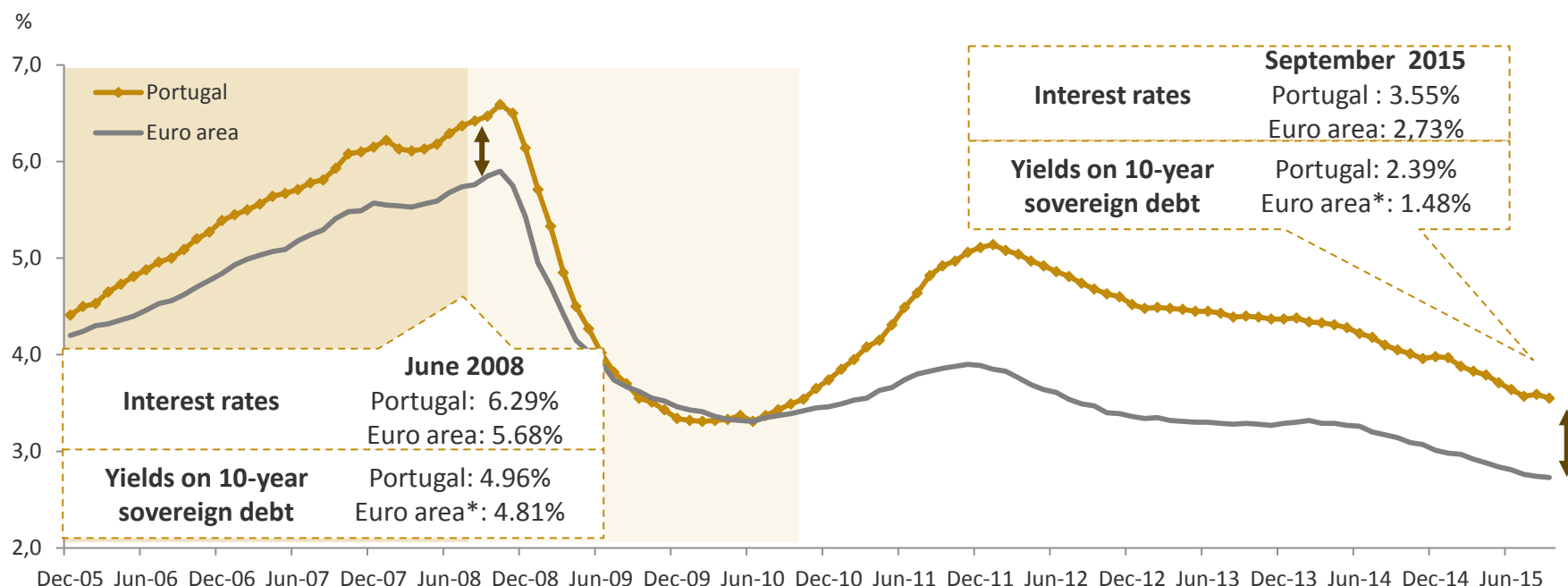
**Debt of state-owned non-financial corporations to the financial sector in Portugal, by instrument**



Source: Banco de Portugal

## The difference between average interest rates on loans to NFCs in Portugal and the euro area increased after the onset of the sovereign debt crisis.

**Average interest rates on loans from monetary financial institutions (stock on balance sheet) to non-financial corporations in Portugal and the euro area**

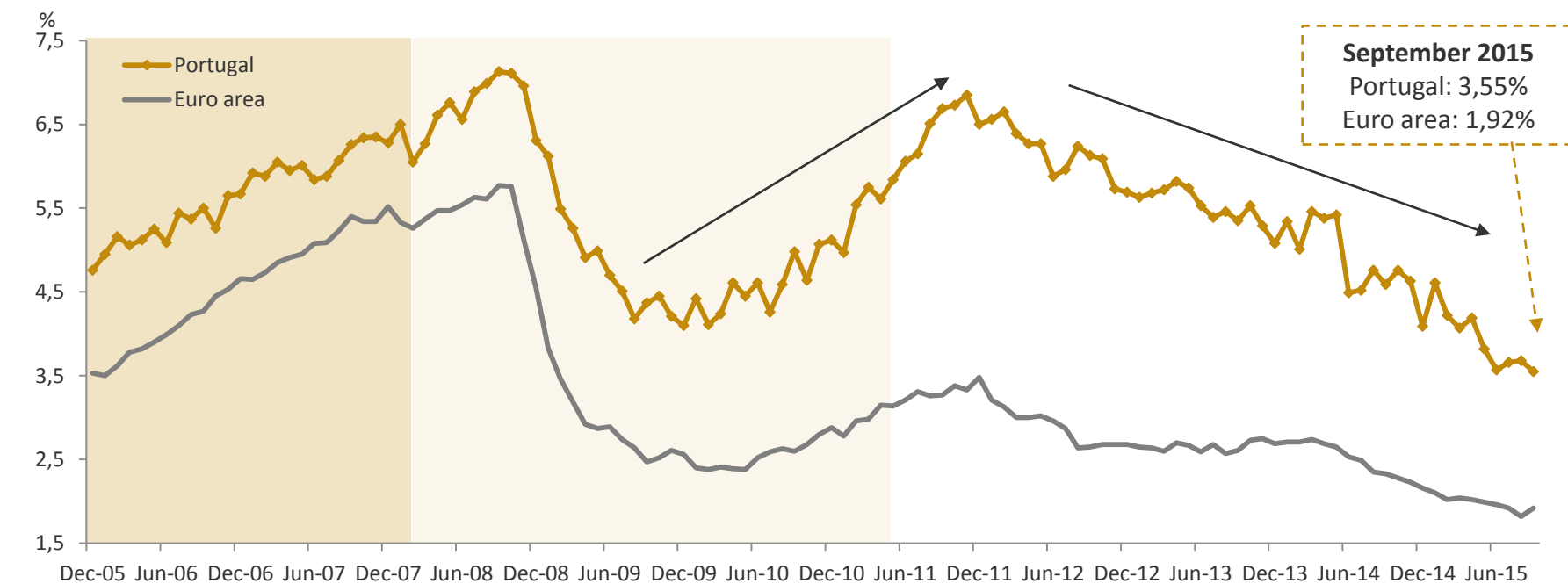


\* Euro area benchmark bond – Changing composition. Calculated as a weighted average of yields on sovereign debts of euro area countries using the outstanding amounts of 10-year sovereign debt as weights.

Source: ECB

Interest rates on new loans to NFCs in Portugal increased as of mid-2009, but have been falling since early 2012.

**Average interest rates on loans from monetary financial institutions (new operations) to non-financial firms in Portugal and the euro area**

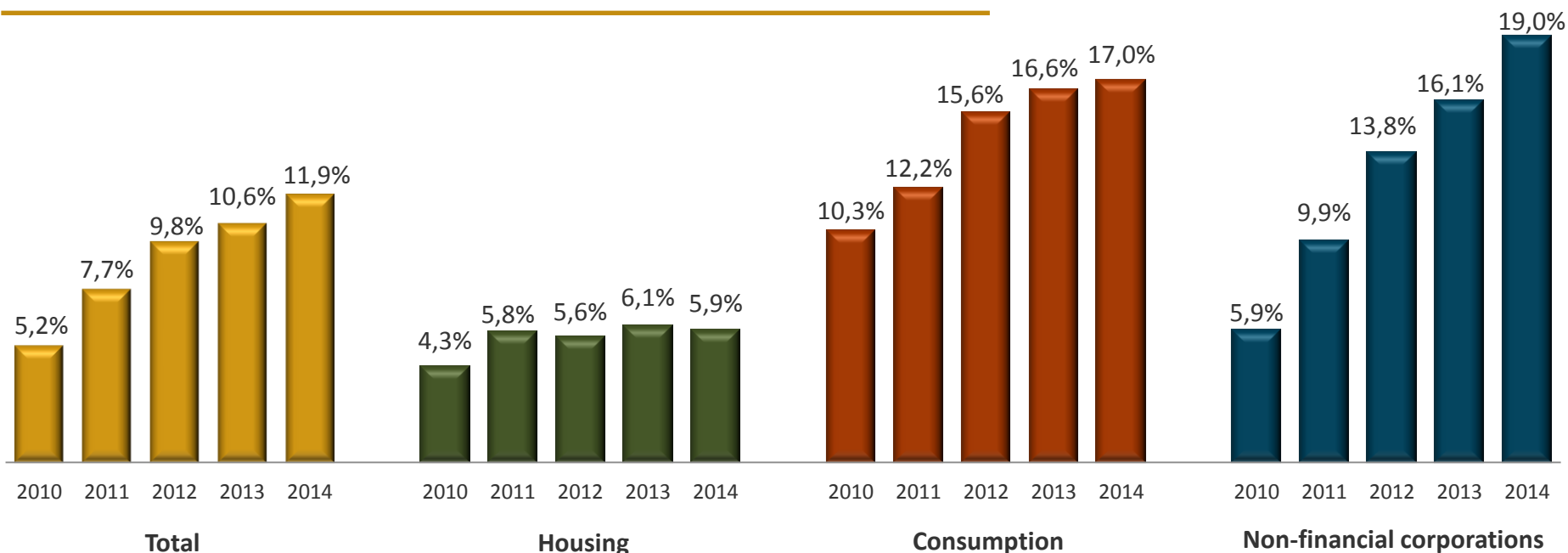


Source: ECB



The quality of loans granted deteriorated after 2010, particularly in consumer credit and to non-financial corporations.

**Non-performing loans\* as a percentage of total corresponding credit**

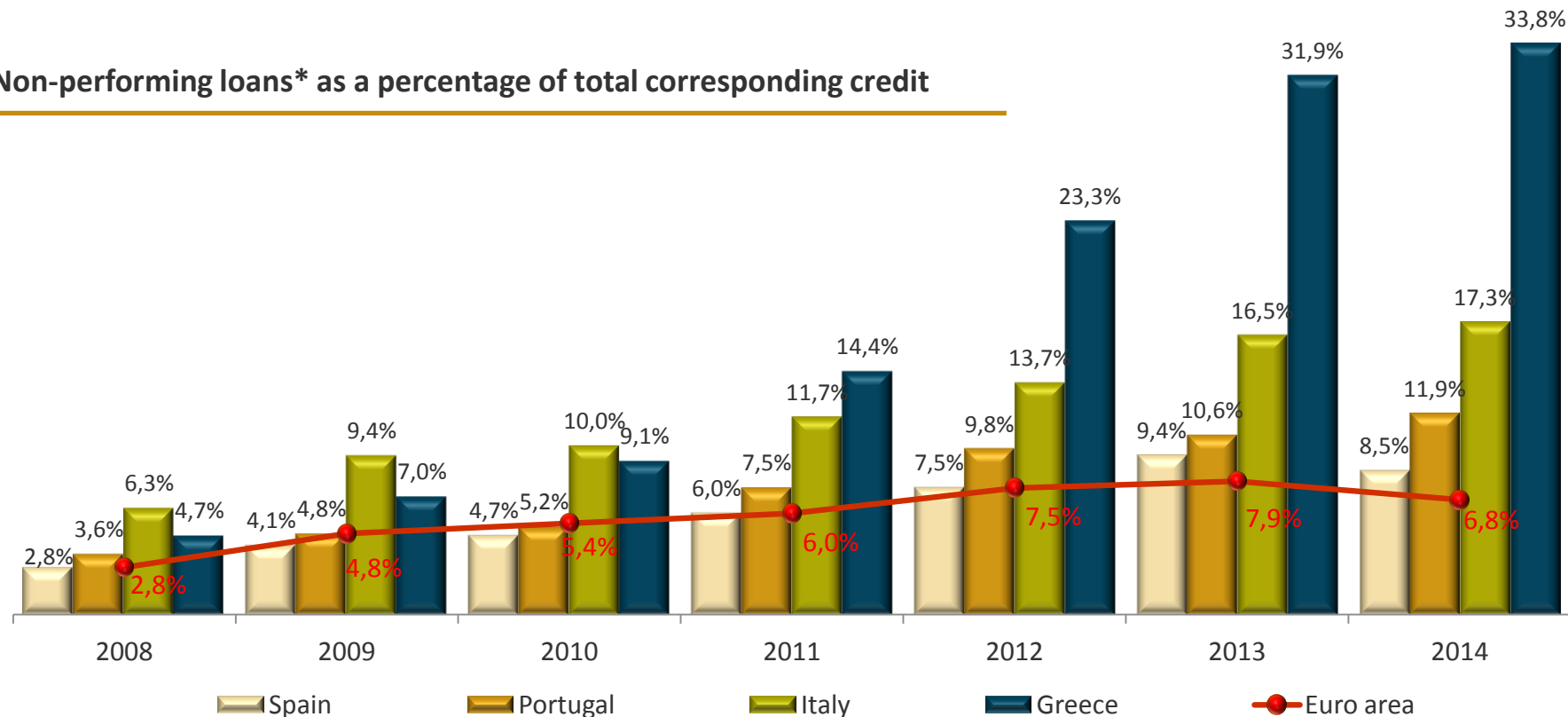


\* Including the total amount owed : i) of loans that have repayments of principal or interest in arrears for more than 90 days, ii) restructured loans whose repayments of principal or interest have been in arrears for 90 days or more and their repayments have been capitalised or refinanced or their payment date postponed, but the guarantees provided have not been reinforced or the debtor has not fully paid up overdue interest and other and iii) of loans with repayments of principal or interest overdue for less than 90 days, but for which there is evidence warranting their classification as credit at risk.

Source: Banco de Portugal

## NPLs showed a general upward trend in the euro area countries, particularly the most vulnerable ones.

**Non-performing loans\* as a percentage of total corresponding credit**

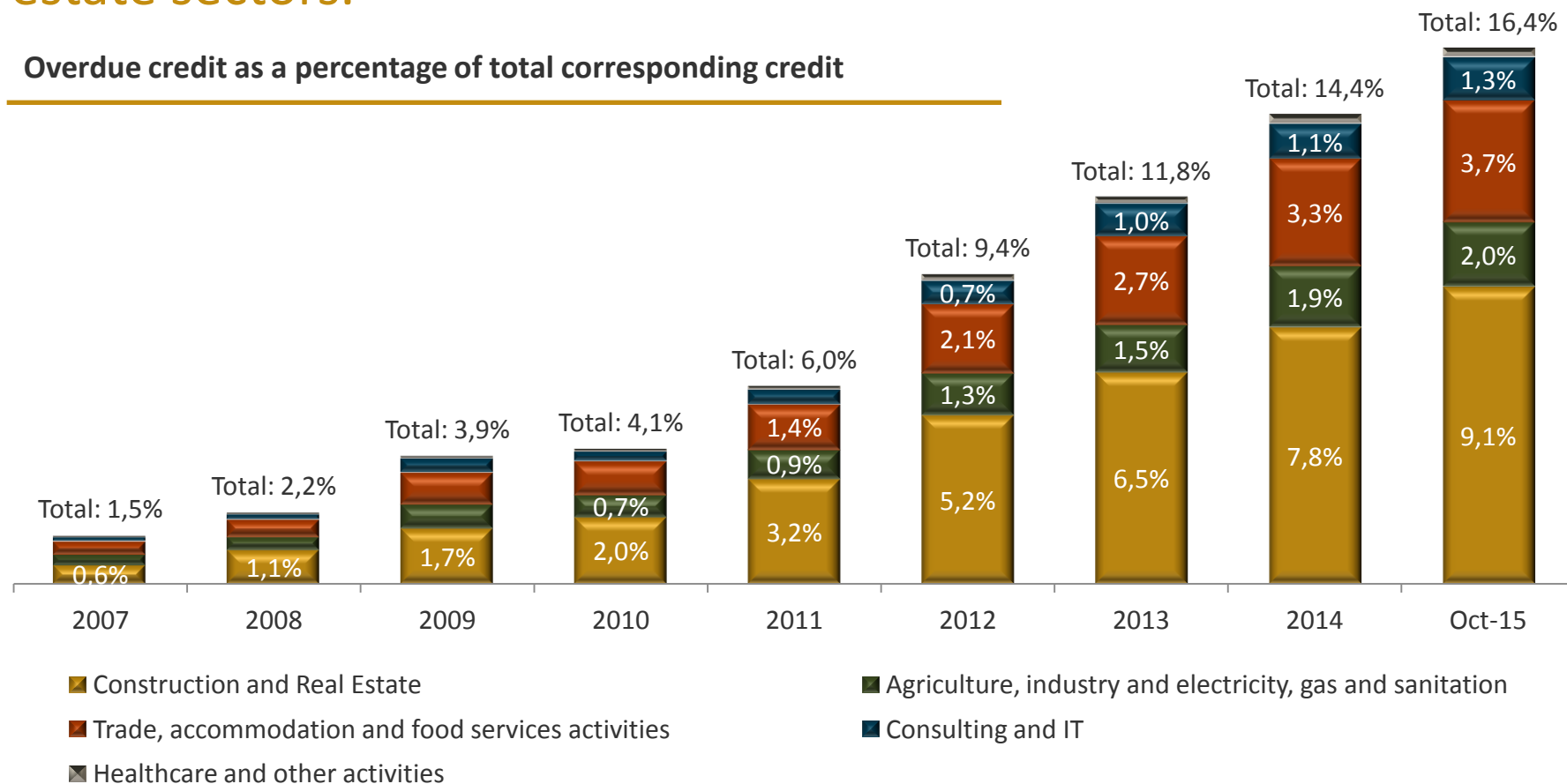


\* Including the total amount owed : i) of loans that have repayments of principal or interest in arrears for more than 90 days, ii) restructured loans whose repayments of principal or interest have been in arrears for 90 days or more and their repayments have been capitalised or refinanced or their payment date postponed, but the guarantees provided have not been reinforced or the debtor has not fully paid up overdue interest and other and iii) of loans with repayments of principal or interest overdue for less than 90 days, but for which there is evidence warranting their classification as credit at risk.

Source: Banco de Portugal

Developments in non-performing loans are mainly due to the deterioration in quality of credit in the construction and real estate sectors.

**Overdue credit as a percentage of total corresponding credit**



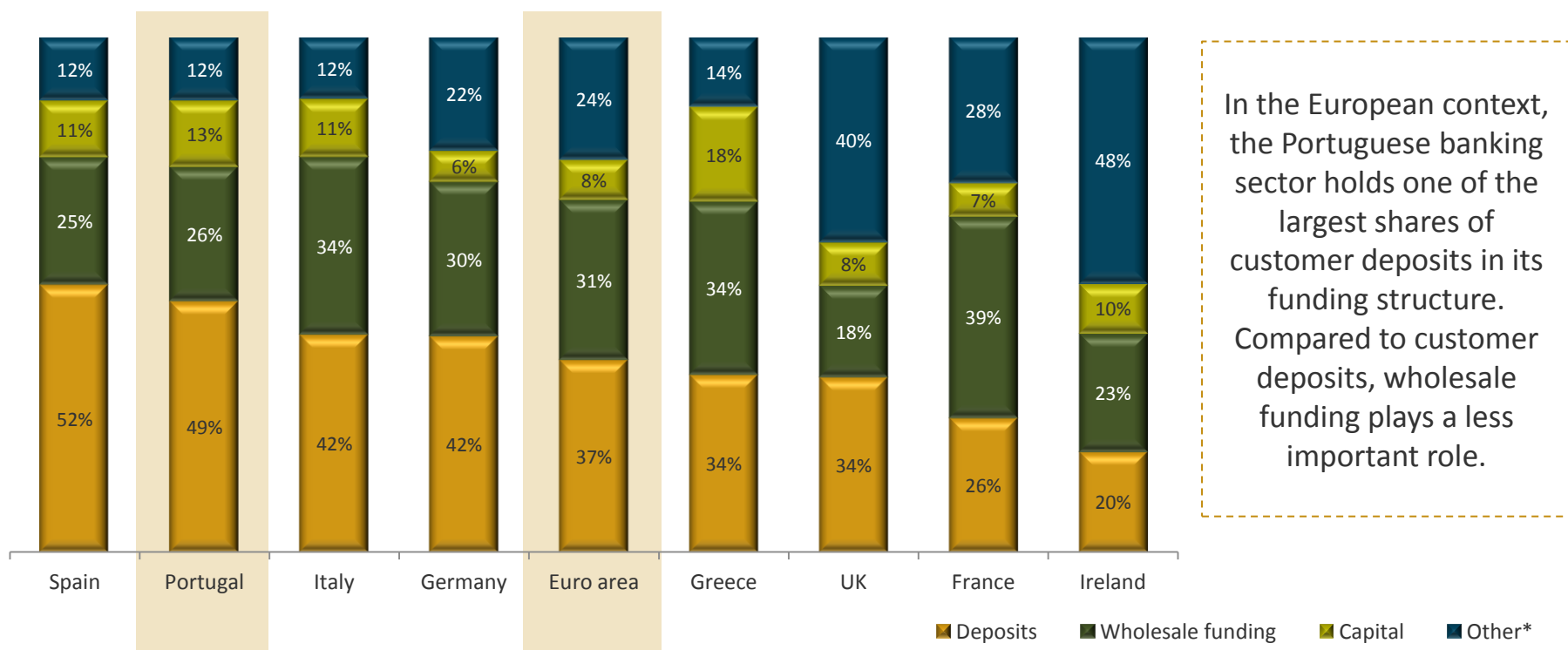
Source: Banco de Portugal

# OVERVIEW OF THE PORTUGUESE BANKING SYSTEM

## IV. Funding

# Customer deposits are the Portuguese banks' most important source of funding.

Comparison of the funding structure of Portuguese banks with that in other EU countries (September 2015)



In the European context, the Portuguese banking sector holds one of the largest shares of customer deposits in its funding structure. Compared to customer deposits, wholesale funding plays a less important role.

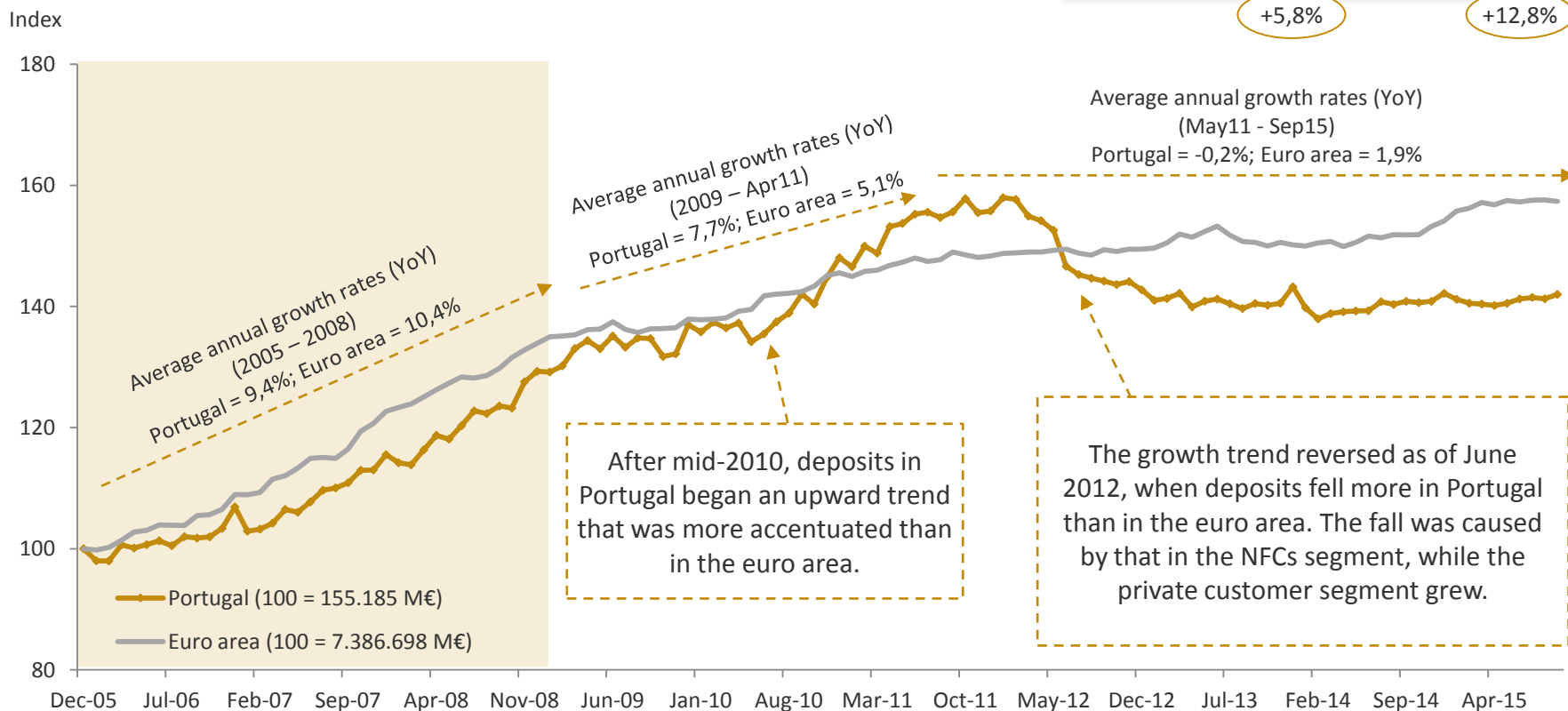
\* Includes liabilities to entities non-resident in the euro area, except for the United Kingdom, for which it includes liabilities to non-residents in the country.

Source: ECB

# The growth trend in deposits in the euro area has been more stable than in Portugal.

**Deposits\* in Portugal and the Euro area (Dec 2005=100)**

	Portugal	Euro area
May 10	208.241 €bn	10.304.518 €bn
May 12	236.799 €bn	11.027.581 €bn
Sep. 15	220.364 €bn	11.622.462 €bn
	+5,8%	+12,8%

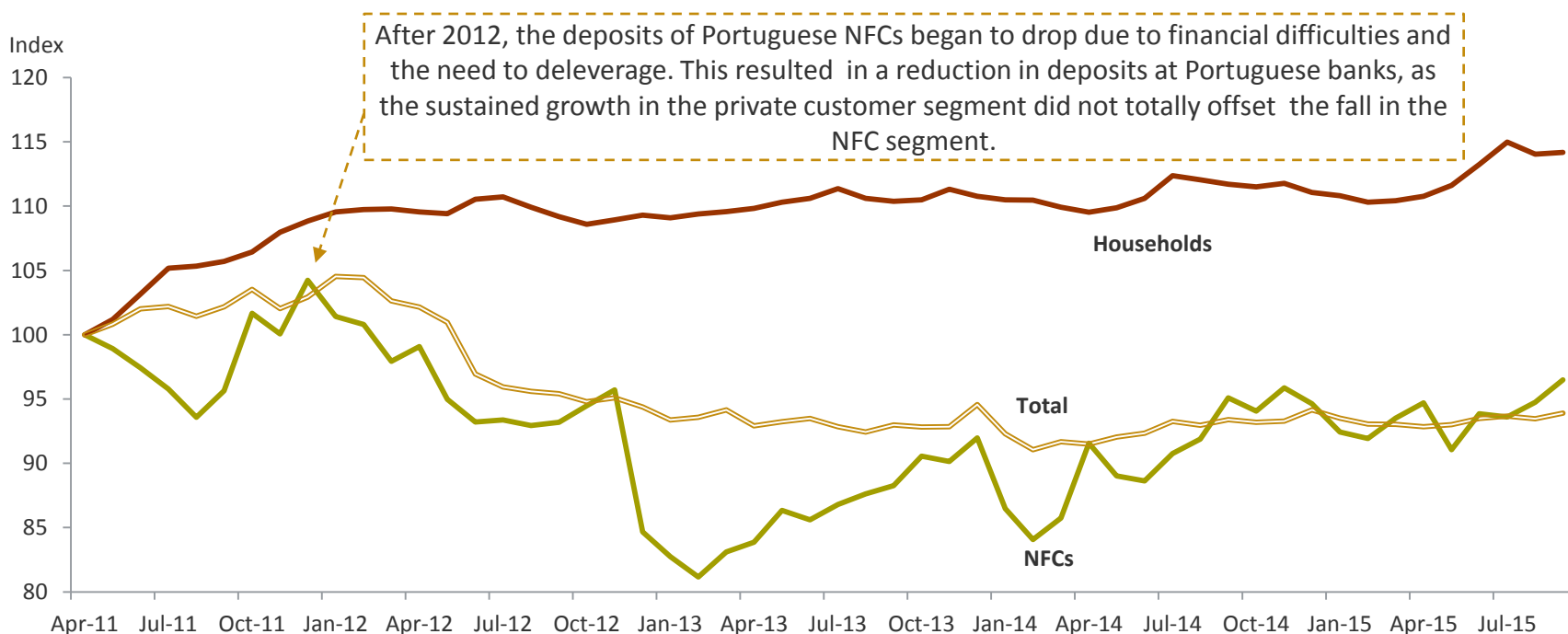


\*Deposits from the non-monetary sector (end-of-period balances)

Source: ECB

Despite the austerity imposed by the EFAP in Portugal, private customers' deposits remained stable and reached their highest level ever in June.

**Deposits\* in Portugal by institutional sector (Apr. 2011 = 100)**

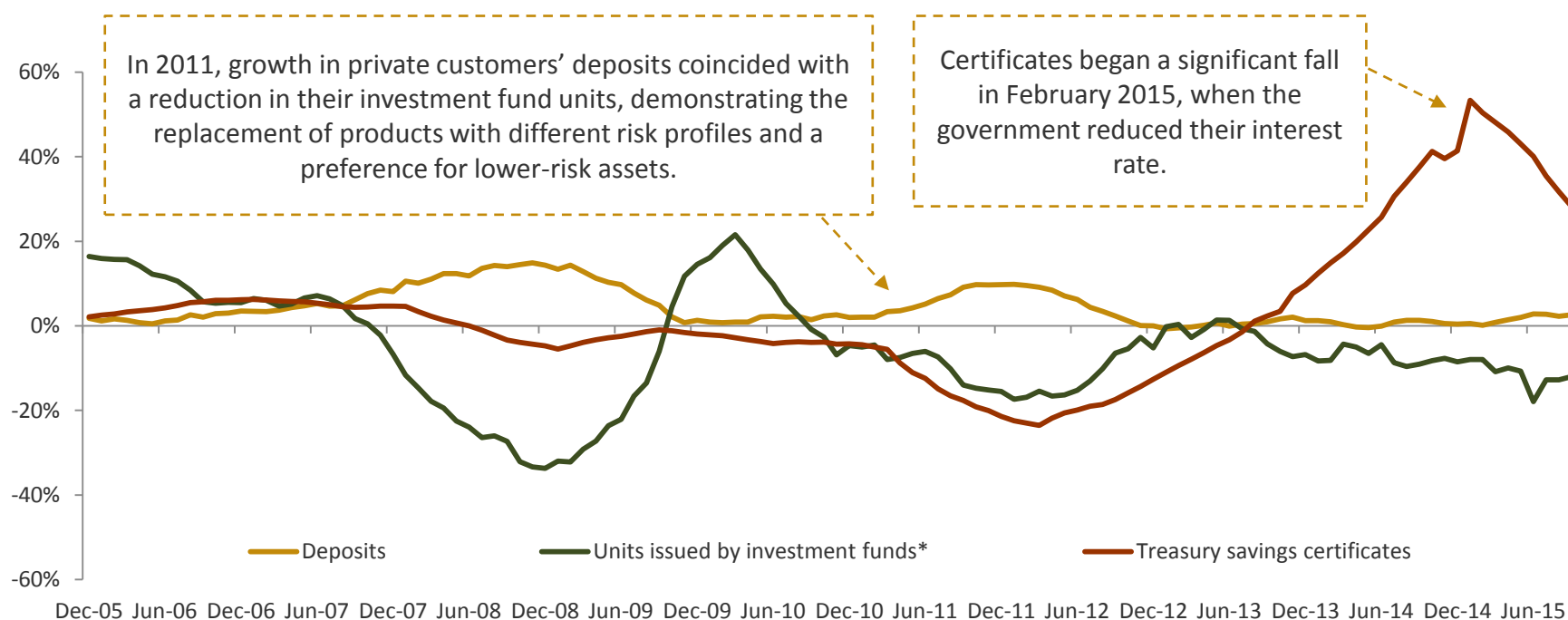


\* Deposits from the non-monetary sector (end-of-period balances), including emigrants

Source: Banco de Portugal

Attractive returns from savings certificates have stimulated their growth since 2013, coinciding with a reduction in units in investment funds.

**Growth rates in deposits, investment fund units and savings certificates held by private customers in Portugal (YoY%)**

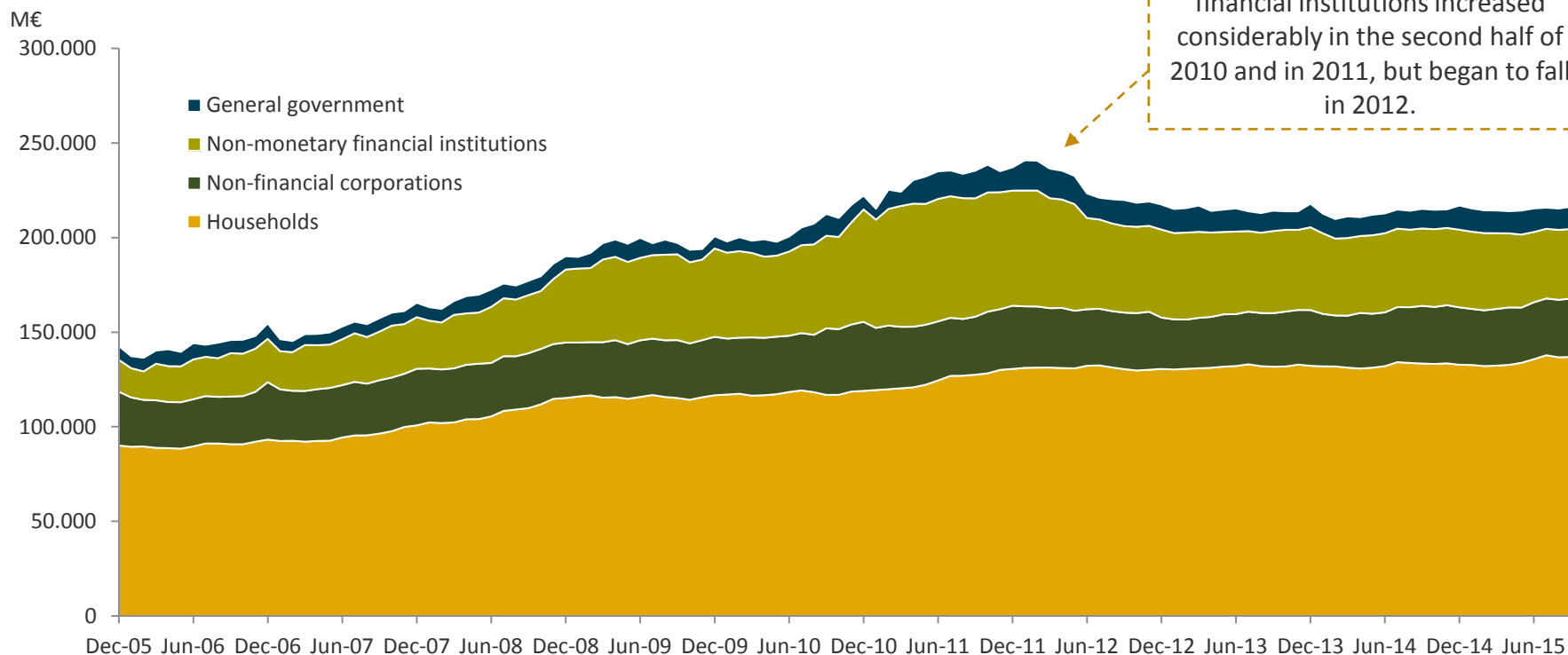


\* Includes stock funds, bond funds, treasury funds, money market funds, retirement savings funds, funds of funds and mixed funds.  
Source: Banco de Portugal



In Portugal, deposits are mainly held by private customers and their weight has been increasing.

### Deposits\* in Portugal by institutional sector



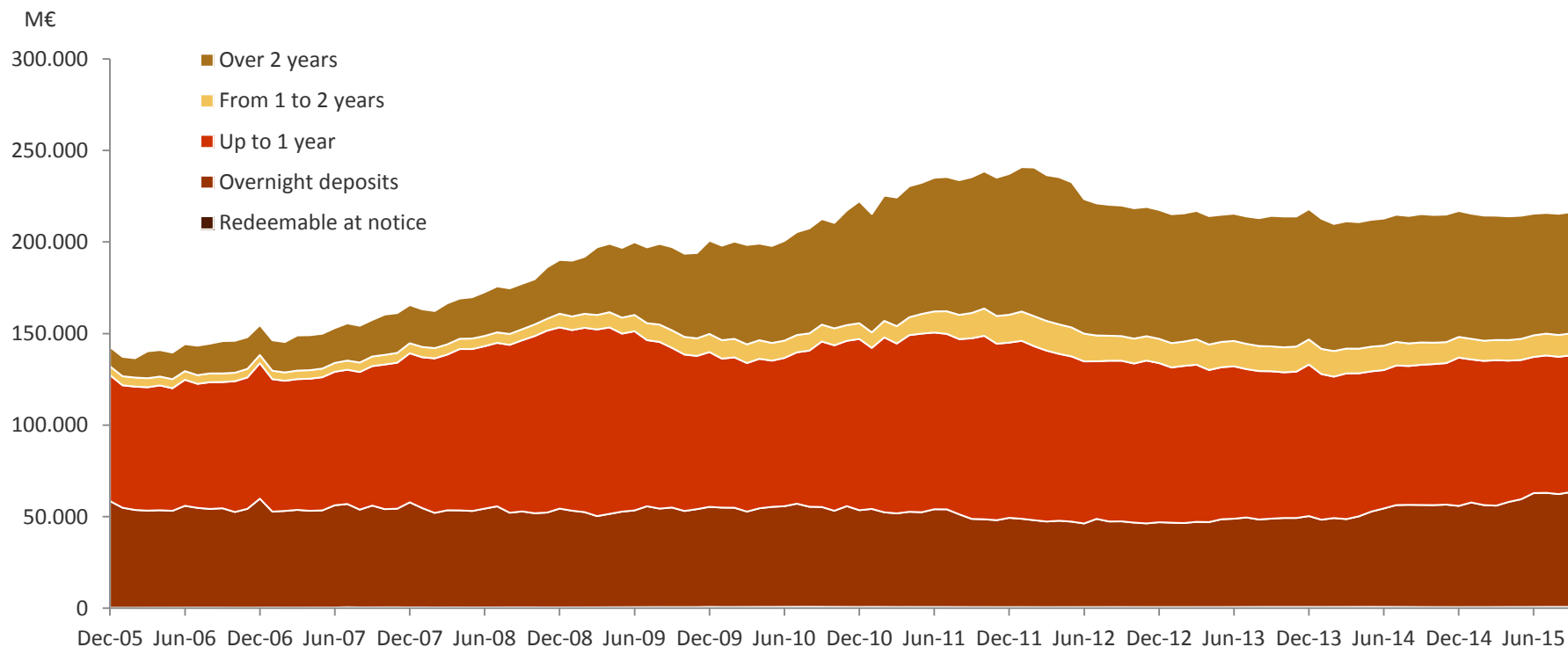
The weight of non-monetary financial institutions increased considerably in the second half of 2010 and in 2011, but began to fall in 2012.

\* \*Deposits from the non-monetary sector (end-of-period balances)

Source: Banco de Portugal

Deposits with a maturity of less than one year are the most numerous, in spite of recent growth in longer-term deposits.

### Deposits\* in Portugal by maturity

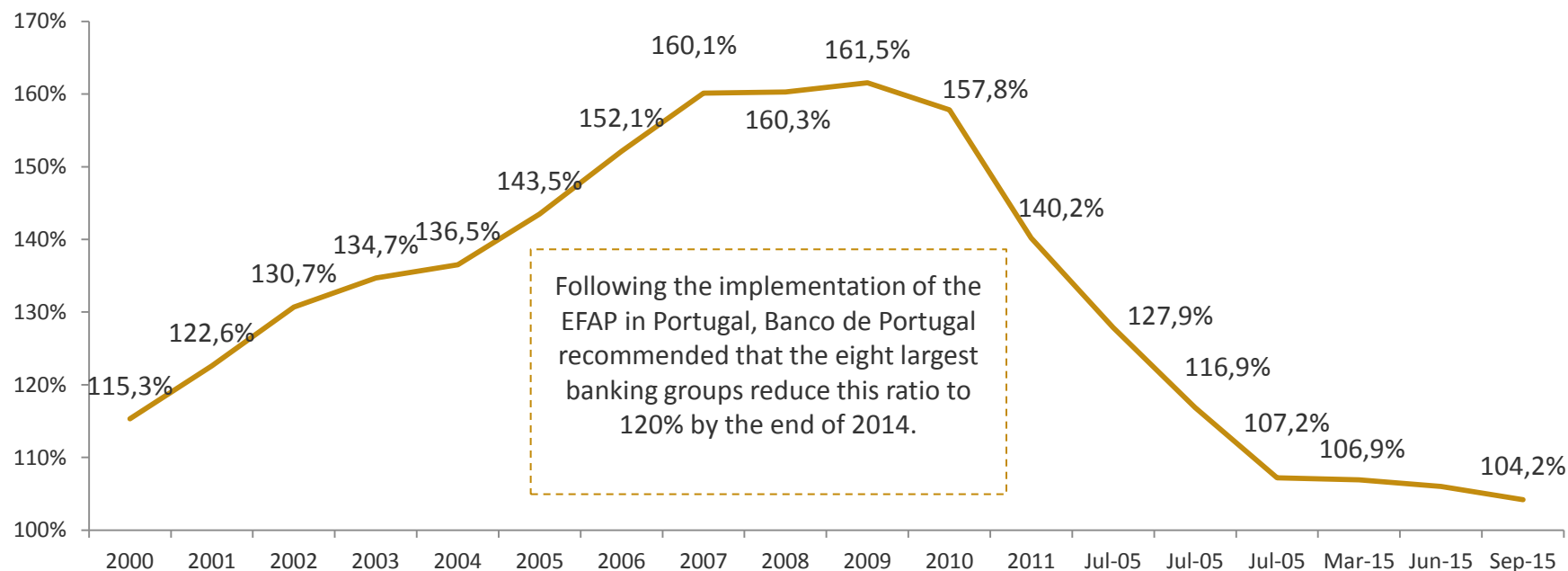


\* Deposits from the non-monetary sector (end-of-period balances)

Source: Banco de Portugal

A reduction in the credit-to-deposit ratio reflects deleveraging by the Portuguese banking system.

### Consolidated credit\* to deposit ratio

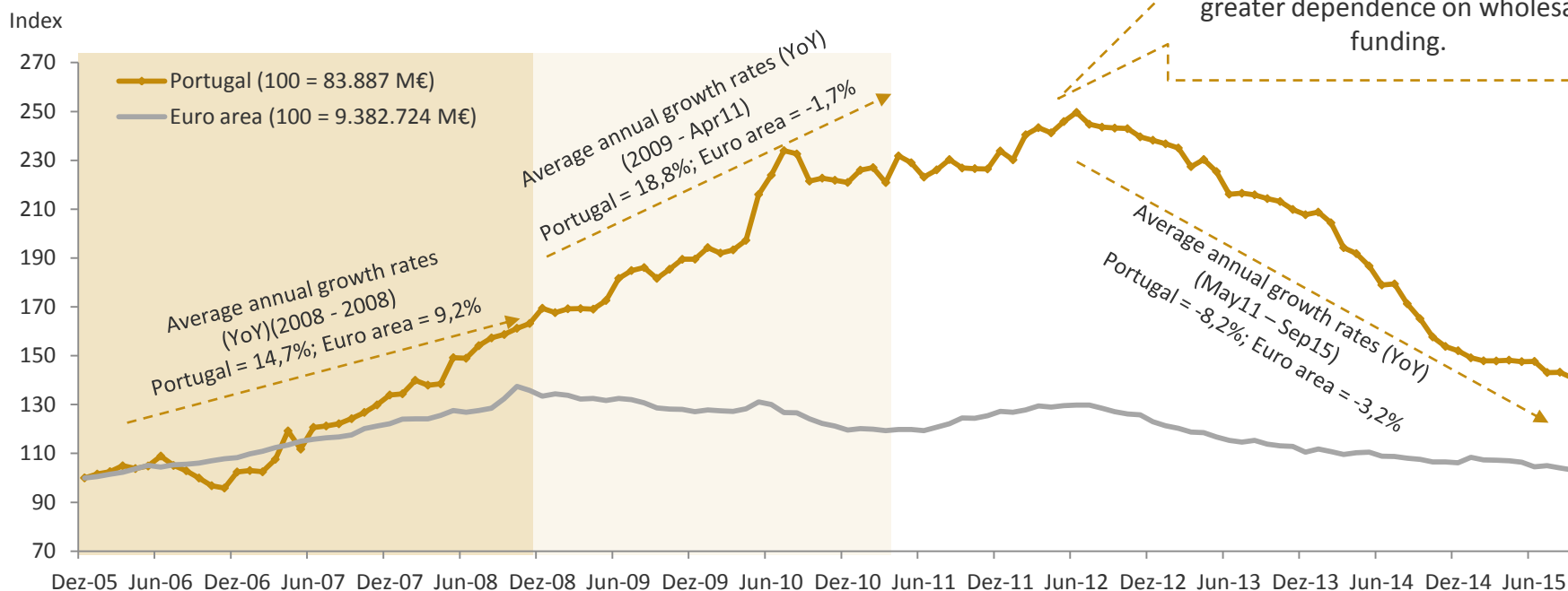


\*Credit net of impairments (including securitised and non-derecognised loans). End-of-of period balances

Source: Banco de Portugal

Recourse to wholesale funding by the Portuguese banks was growing much faster than in the euro area, a trend that has reversed in recent years.

**Wholesale finance\* in Portugal and the euro area (Dec 2005=100)**

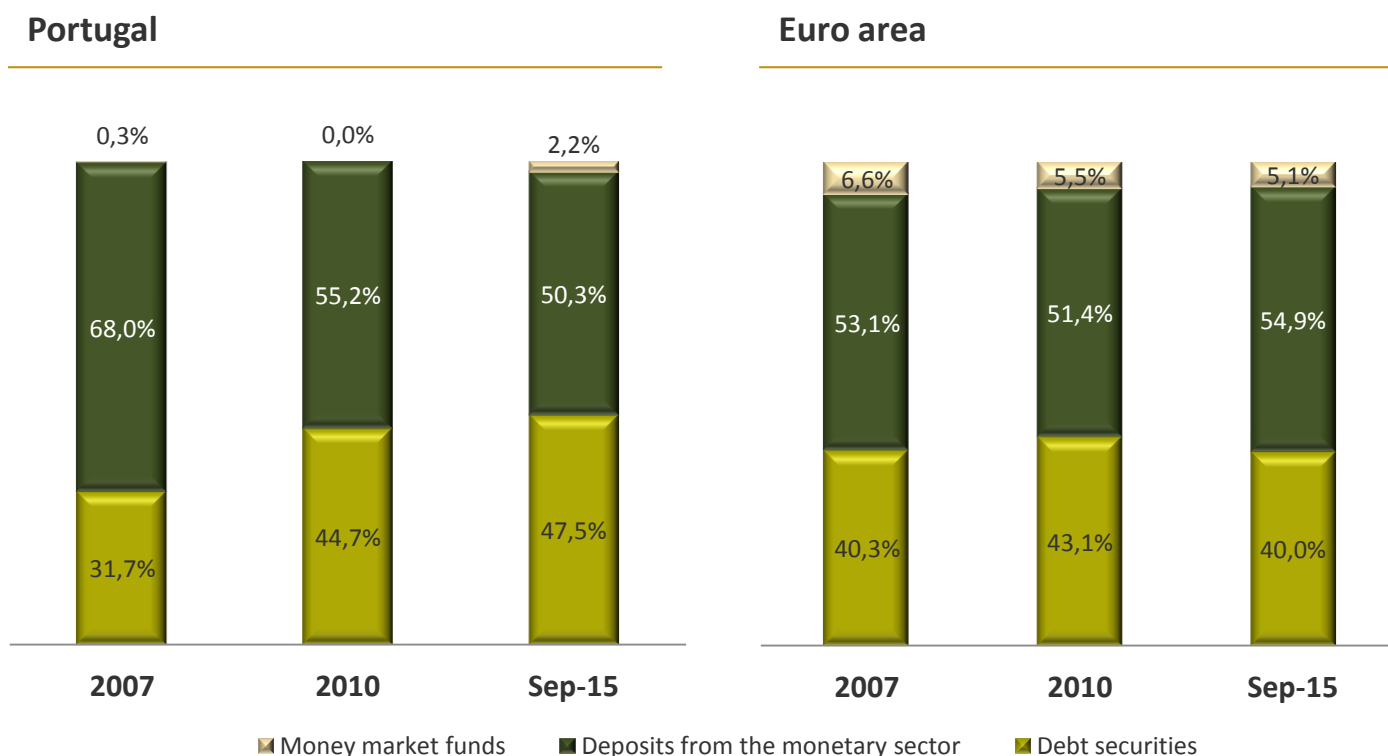


\* Wholesale funding includes deposits in the monetary sector, debt securities issued and money market funds (end-of-period balances).

Source: ECB

Both in Portugal and the euro area, deposits from the monetary sector are the main component of wholesale funding of the banking sector.

### Wholesale funding structure by type of instrument



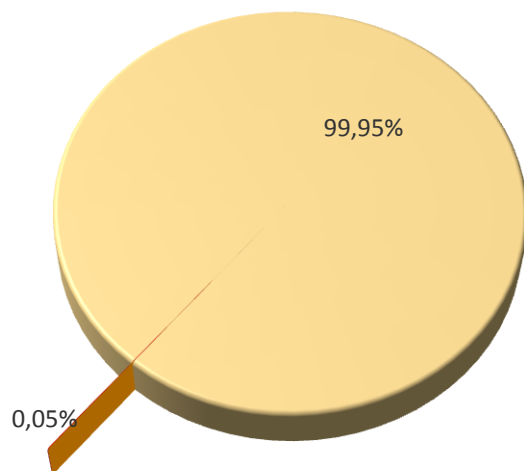
In Portugal, however, the weight of the debt securities issuing market increased against 2007. This source of funding is more important to the Portuguese banks than for those in the rest of the euro area.

Source: ECB

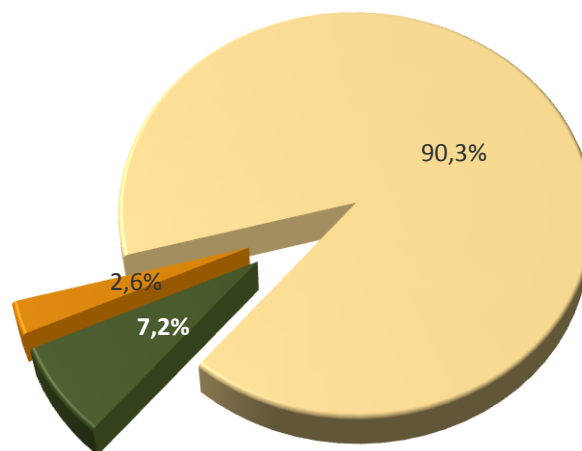
Both in Portugal and the euro area, debt securities issued by banks are predominantly long term.

**Debt securities structure by maturity on date of issue (September 2015)**

**Portugal**



**Euro area**

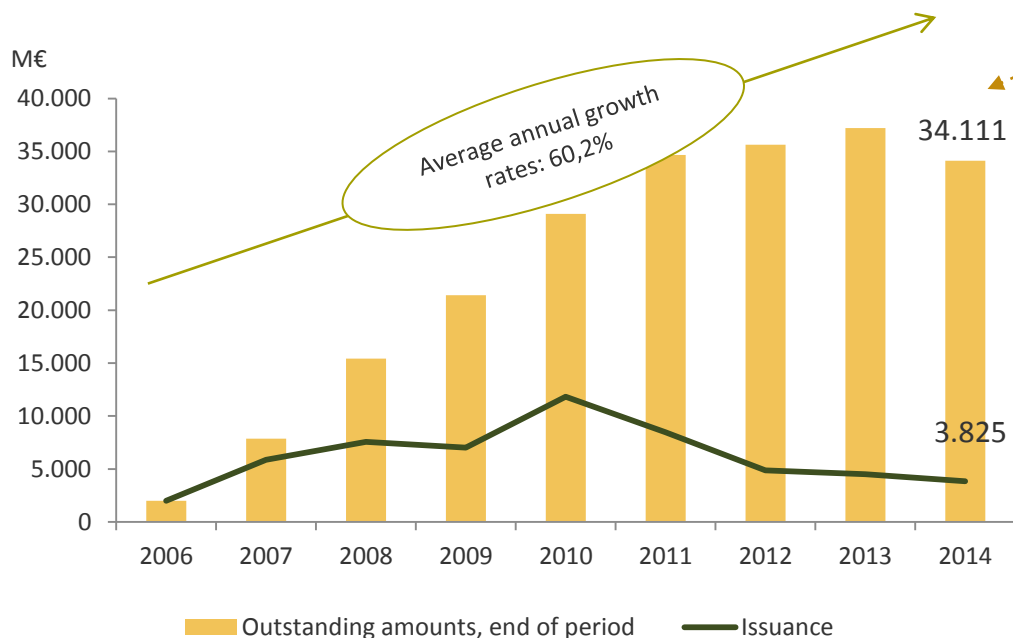


■ Up to 1 year ■ From 1 to 2 years ■ Over 2 years

The weight of debt issues maturing in less than two years has shown a downward trend in the recent past. Their weight is only negligible in the Portuguese banking sector, as opposed to in the euro area.

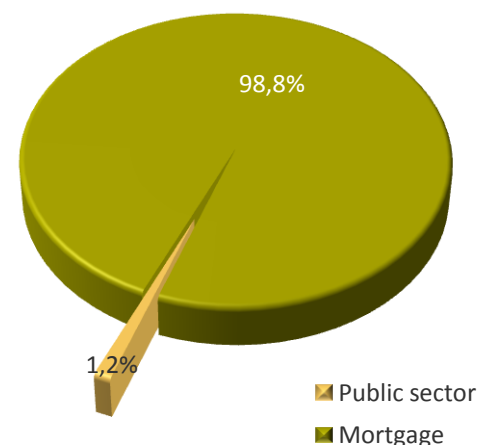
Up to 2011, covered bonds gained importance as a source of funding for Portuguese banks. More recently, however, the amount issued has been falling.

### Issue and balances of covered bonds in Portugal



At the end of 2014, the balance of covered bonds represented around 7.3% of Portuguese banks' funding.

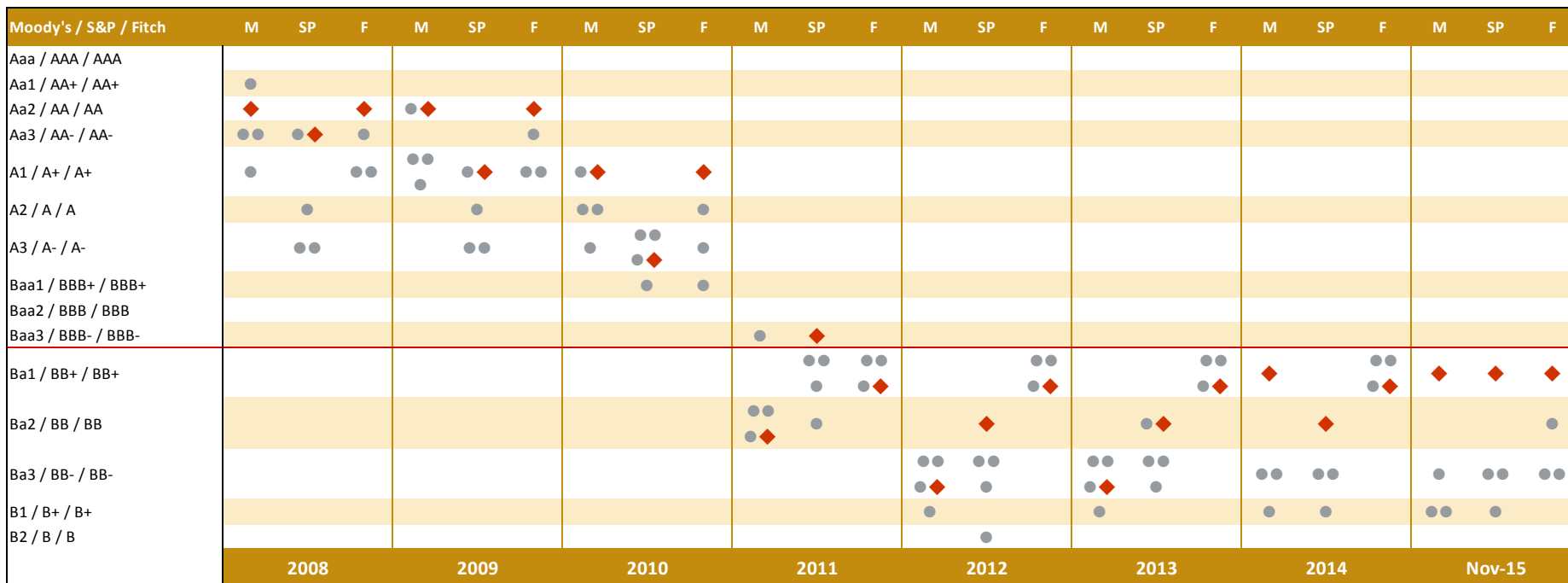
### Covered bonds by type of underlying asset (2014)



Source: ECB, European Covered Bond Council, Factbook, 2014

# The downgrades of the Portuguese Republic's risk adversely affected the Portuguese banks' ratings\*

Ratings of the Portuguese Republic and Portuguese banks by Moody's, S&P and Fitch



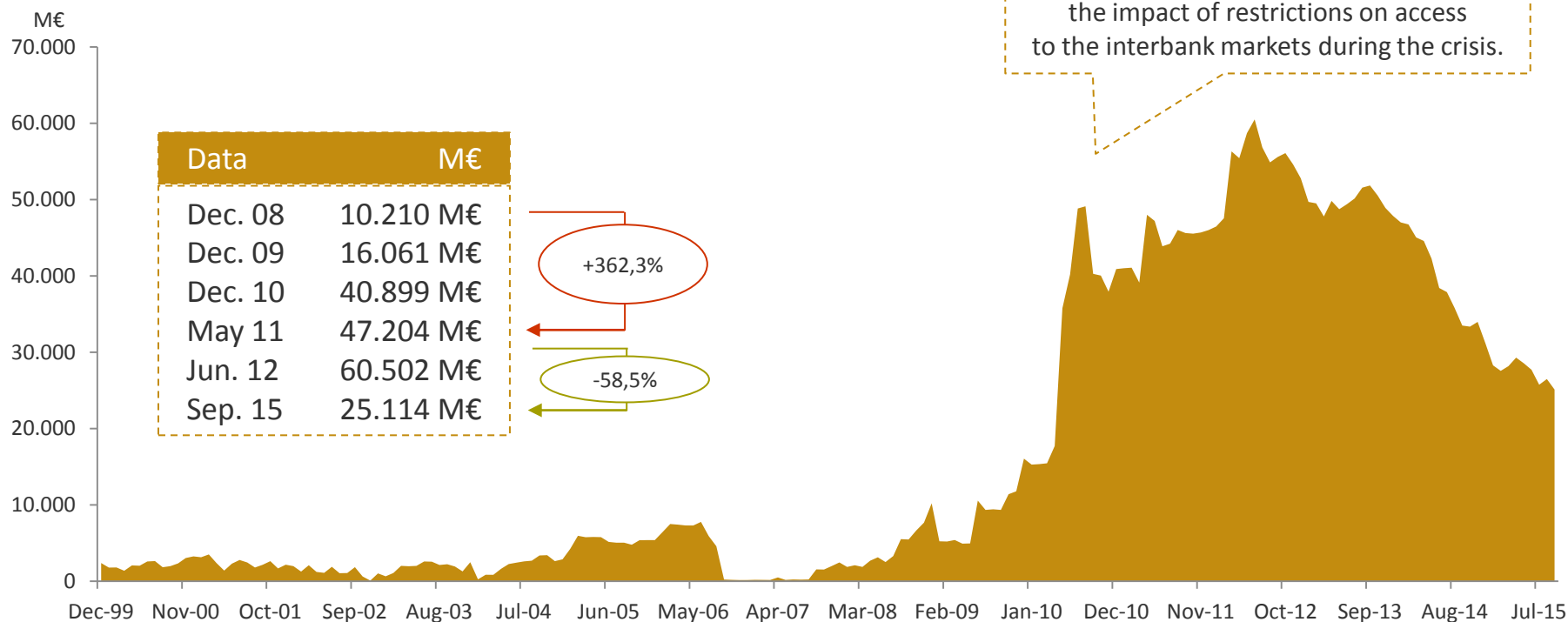
- ◆ Portuguese Republic
- Portuguese Banks (CGD, BCP, BPI and BES up to 2013)

\*At the end of the period.



# The amount of borrowing from the ECB by Portuguese banks has been decreasing steadily since June 2012.

## Borrowing from the European Central Bank \*



\* End-of-period balances.

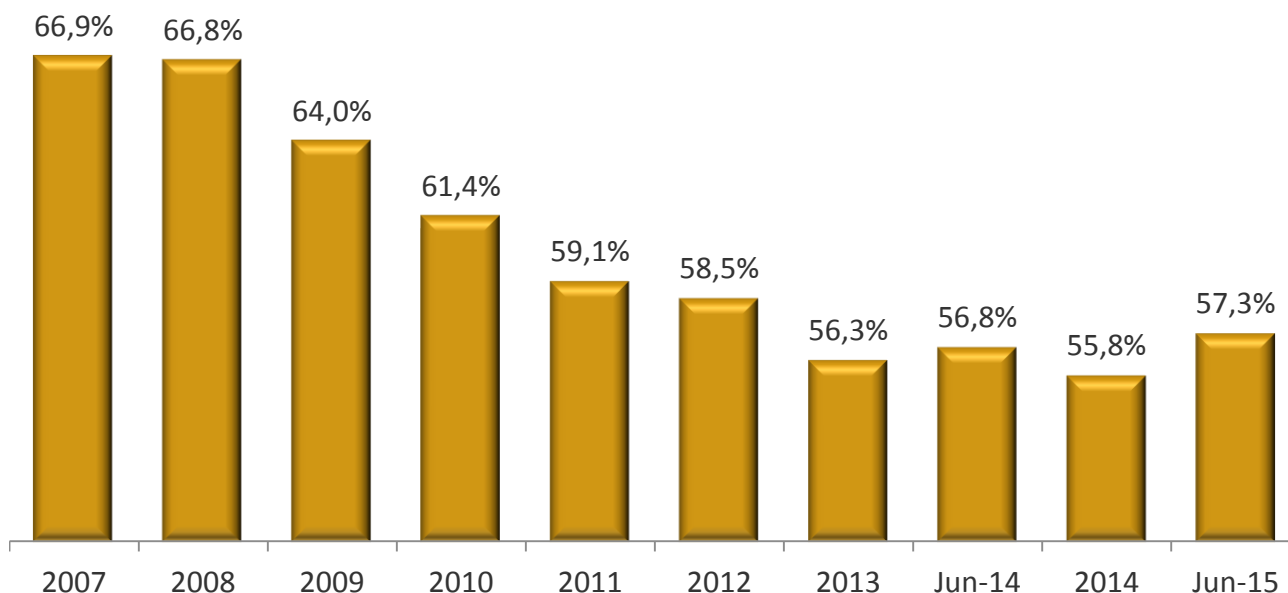
Source: Banco de Portugal

# OVERVIEW OF THE PORTUGUESE BANKING SYSTEM

## V. Solvency

The degree of risk of Portuguese banks' assets has been decreasing in recent years.

**Risk-weighted assets in proportion to total assets\***



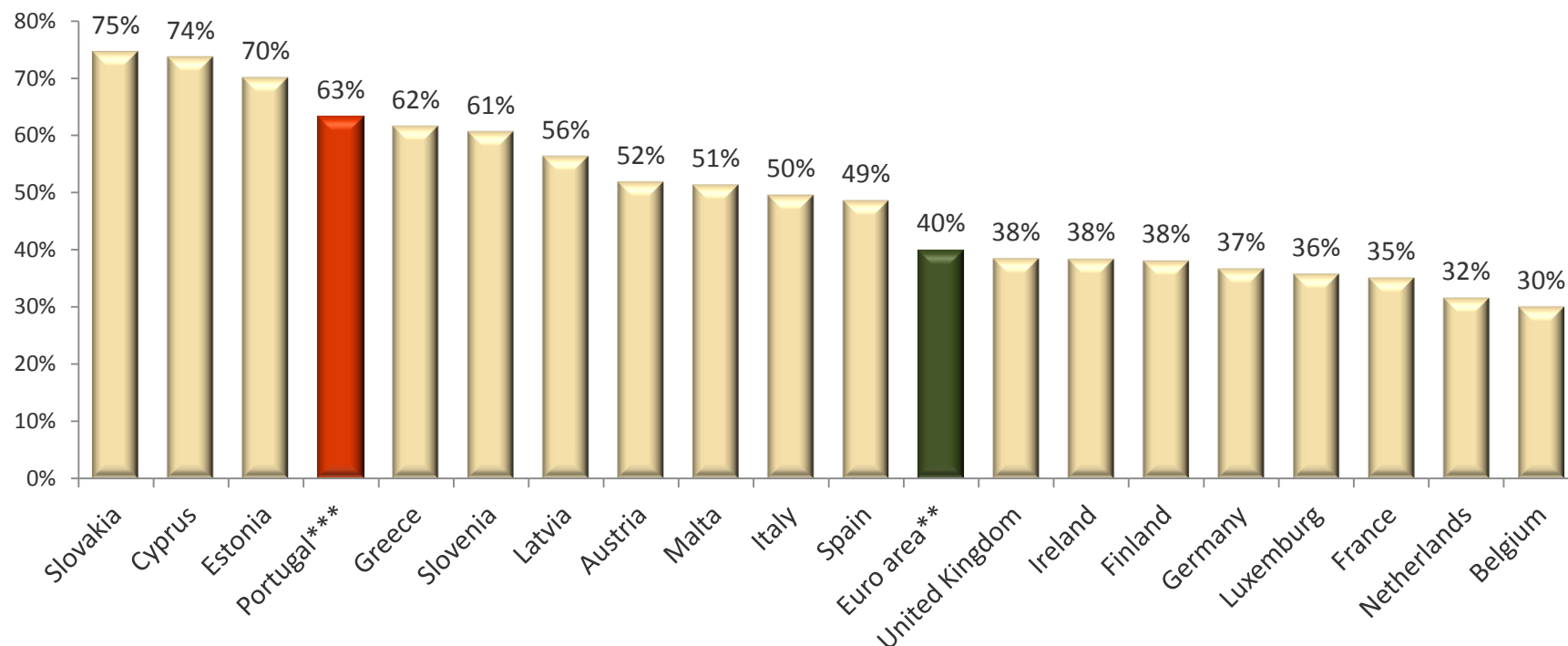
The risk-weighted assets to total assets ratio of the Portuguese banks fell considerably in recent years. This trend grew after the EFAP and reflects a reduction in the average risk of assets making up the Portuguese banks' balance sheet. In the first six months of 2014, this ratio increased slightly due to changes in the calculation of RWAs introduced by CRD IV / CRR, but began to fall again at the end of the year

\* Risk-weighted assets include off-balance-sheet items, consolidated data

Source: Banco de Portugal

## The risk-weighted asset to total risk ratio is above the euro area average, however.

**Risk-weighted assets in proportion to total assets\* (June 2014)**



\* Risk-weighted assets include off-balance-sheet items. The data differ from the previous slide as they refer only to bank groups and domestic banks on a consolidated basis.

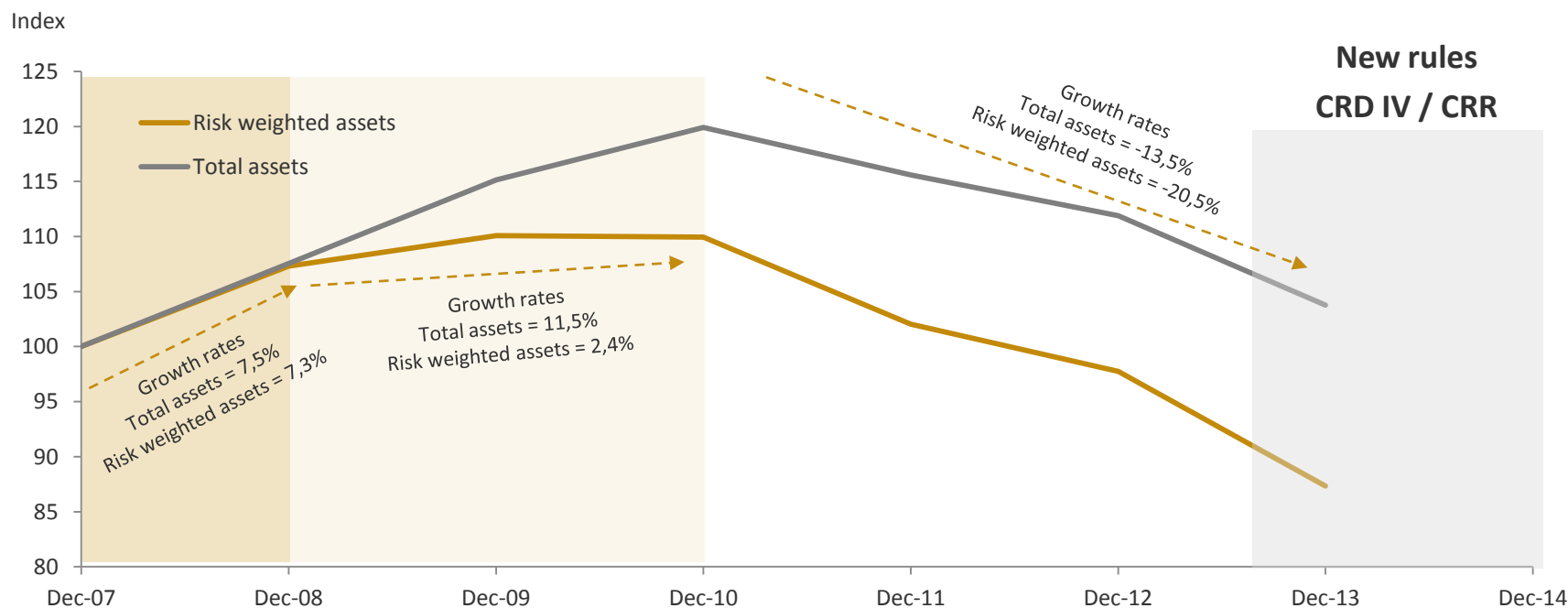
\*\* Euro area with 18 countries

\*\*\* The data for Portugal may differ from those shown in the previous slide due to slight differences in methods used by Banco de Portugal and the ECB.

Source: ECB

Total assets have been falling at a slower rate than risk-weighted assets due to optimisation of exposure to risk by the Portuguese banks.

**Risk weighted assets and total assets of Portuguese banks\* (Dec 2007=100)**

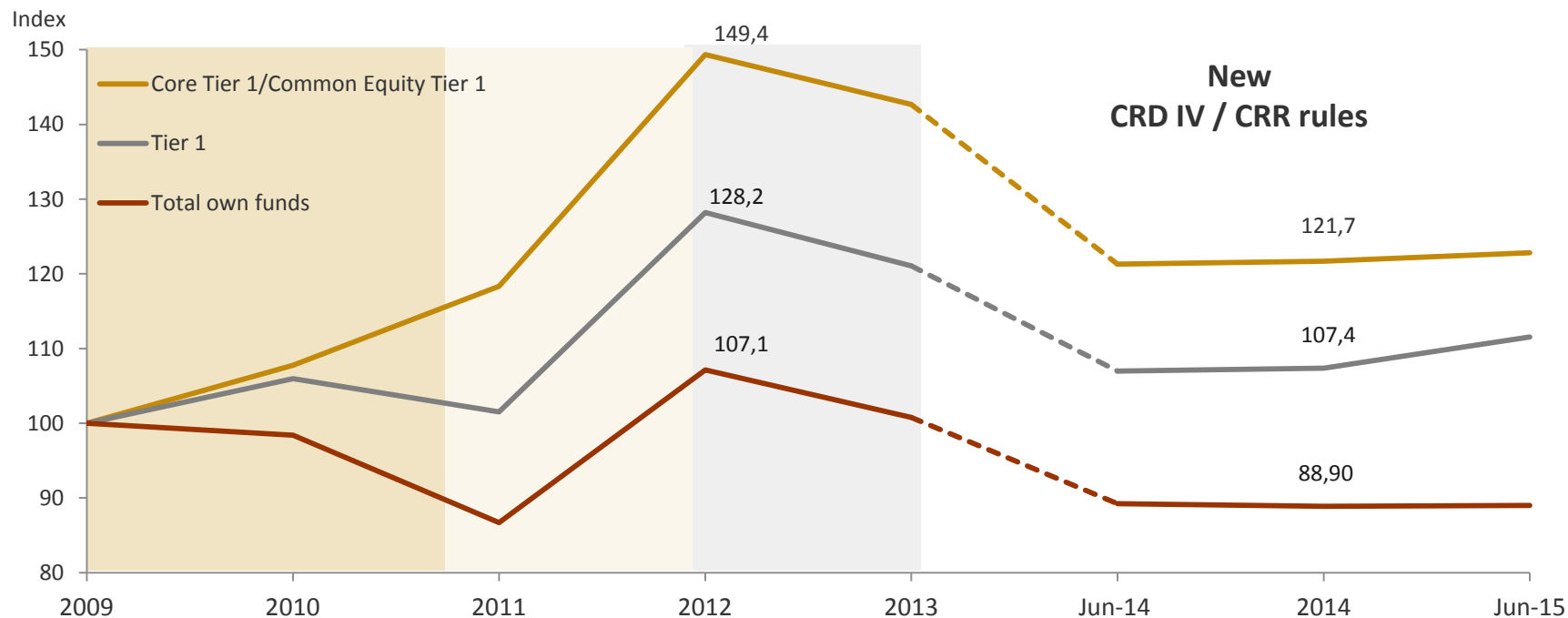


\* Data from bank groups and domestic banks on a consolidated basis, excluding the insurance business

Source: ECB

The better quality own funds at the Portuguese banks, core Tier 1/CET1, have increased significantly since 2009.

**Own funds of Portuguese banks\* (Dec 2009=100)**

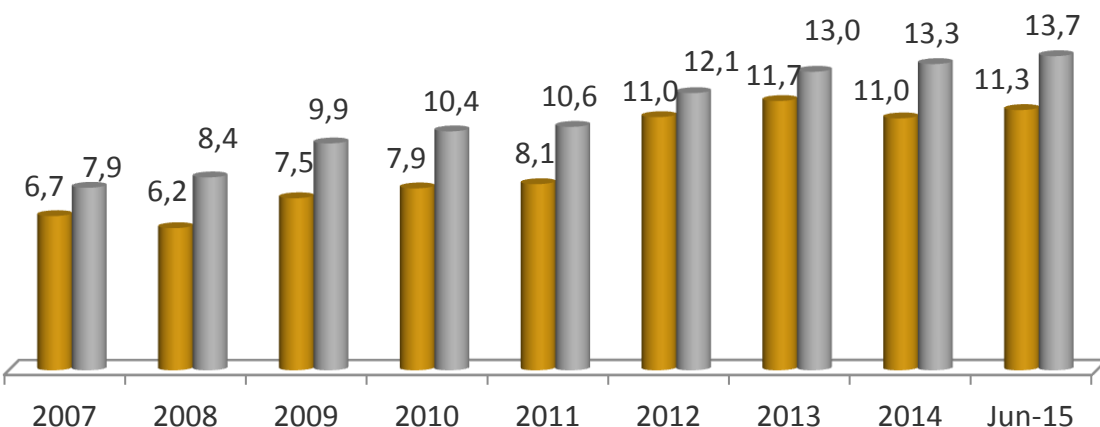


\* Data from bank groups and domestic banks on a consolidated basis, excluding the insurance business

Source: Banco de Portugal

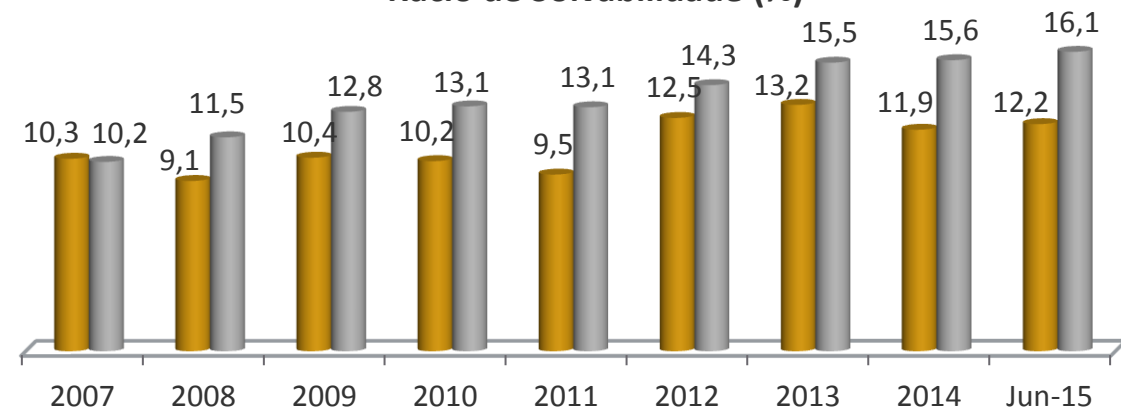
Historically, the Portuguese banks' capital levels have always been above the minimums required by law..

**Rácio Tier 1 (%)**



Basel II required financial institutions' Tier 1 ratio to be 4% or more and their solvency ratio to be no lower than 8%. The new regulatory framework adopted after Basel III, which has been in effect since the beginning of 2014, focuses on the Common Equity Tier 1 ratio. In 2014, according to the CRD IV/CRR transitional arrangements, the requirement was 6% for the Tier 1 ratio and 8% for the solvency ratio.

**Rácio de Solvabilidade (%)**

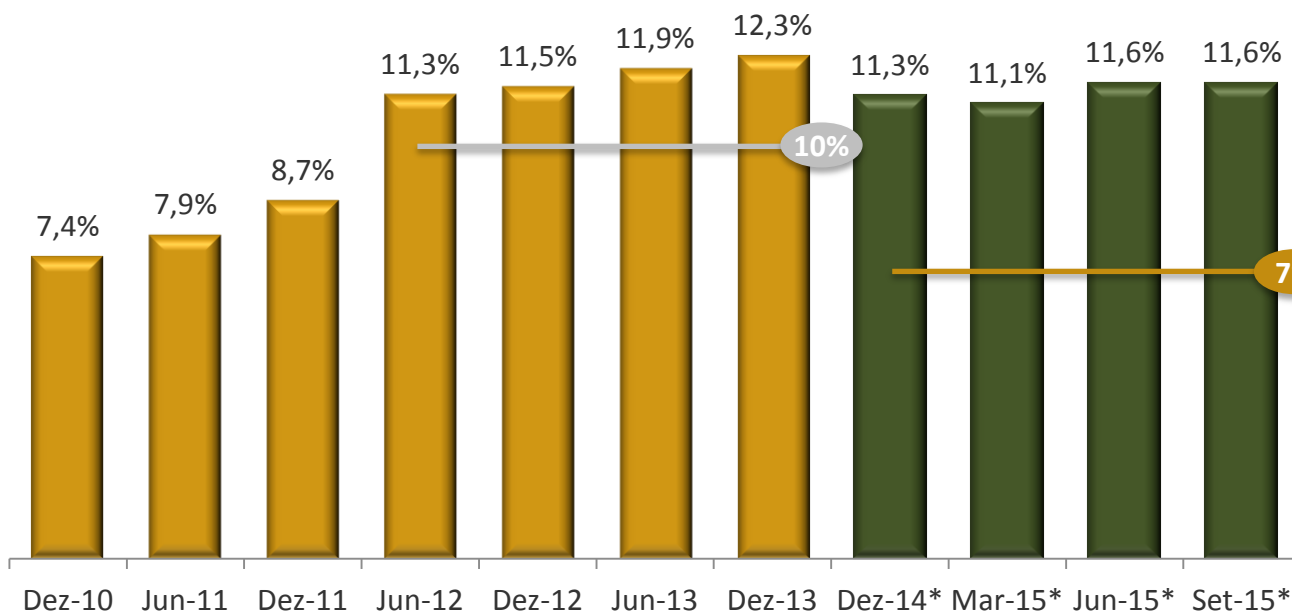


■ Portugal  
■ Euro area

\* Data from bank groups and domestic banks on a consolidated basis, excluding the insurance business  
Source: ECB

The solvency of the Portuguese banks improved substantially after 2011, so that the new CET 1 ratio is comfortably above the minimum requirements.

**Core Tier 1 ratio / Common Equity Tier 1 ratio**



Since the beginning of 2014, the Portuguese banks have had to follow the new CRD IV/CRR transitional arrangements for adequacy of own funds, which imposes a Common Equity Tier (CET) 1 ratio of 7%. Up to the end of 2013, the Portuguese banks were obliged by Banco de Portugal to satisfy a Core Tier 1 ratio of no less than 10%.

\* CET 1 ratio calculated in accordance with the new CRD IV/CRR transitional arrangements

Source: Banco de Portugal



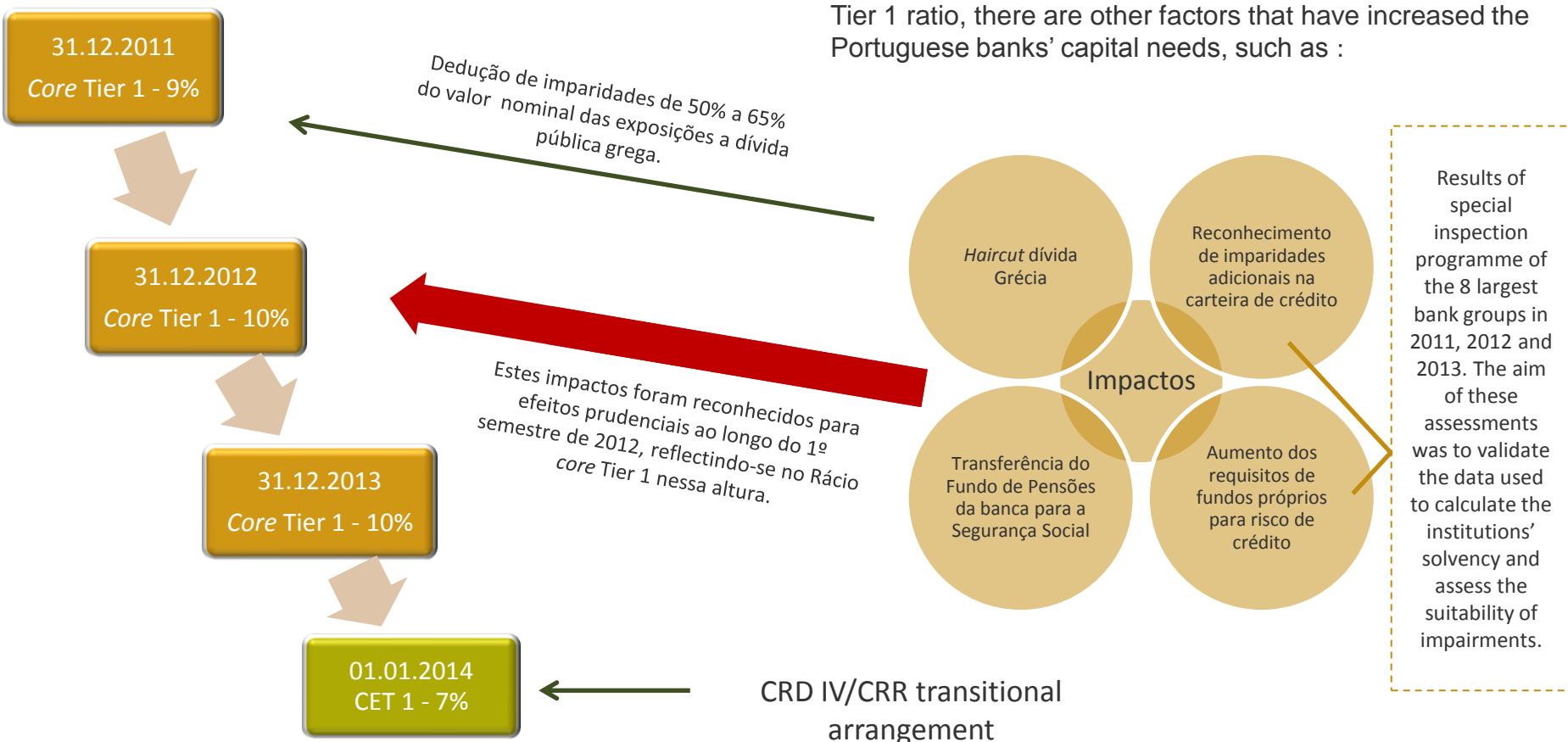
## In the recent past, the banking sector has had to face new regulatory requirements ...

	<b>Basel I</b>	<b>Basel II</b>	<b>Basel 2.5</b>	<b>Basel III</b>
	<b>1992</b>	<b>2004</b>	<b>2009</b>	<b>2014</b>
<b>Capital requirements</b>	<ul style="list-style-type: none"> <li>• Definition of Tier 1 and Tier 2</li> <li>• Requirements: Tier 1 – 4%; Own funds – 8%</li> </ul>	<ul style="list-style-type: none"> <li>• Requirements same as Basel I</li> </ul>		<ul style="list-style-type: none"> <li>• New definition of capital</li> <li>• New buffers</li> <li>• Leverage ratio</li> <li>• Systemic risk</li> </ul>
<b>RWA requirements</b>	<ul style="list-style-type: none"> <li>• Pillar 1 – market risk (change made in 1997)</li> <li>• Pillar 1 – Credit risk</li> <li>• Requirement: 8%</li> </ul>	<ul style="list-style-type: none"> <li>• New Pillar 1 – credit risk</li> <li>• Pillar 2 – ICAAP</li> <li>• Pillar 3 – disclosures</li> <li>• Requirements same as Basel I</li> </ul>	<ul style="list-style-type: none"> <li>• Revisions of securitisation instruments and trading book</li> </ul>	<ul style="list-style-type: none"> <li>• Counterparty risk</li> <li>• Requirements: CET – 4.5%; Tier 1 – 6%; Tier 1 + Tier 2 – 8%</li> </ul>
<b>Liquidity requirements</b>				<ul style="list-style-type: none"> <li>• Liquidity coverage ratio (LCR)</li> <li>• Net stable funding ratio (NSFR)</li> </ul>

All figures are for full implementation of the Basel agreements

## ... with special focus on capital requirements.

In addition to compliance with the new figures for the Core Tier 1 ratio, there are other factors that have increased the Portuguese banks' capital needs, such as :

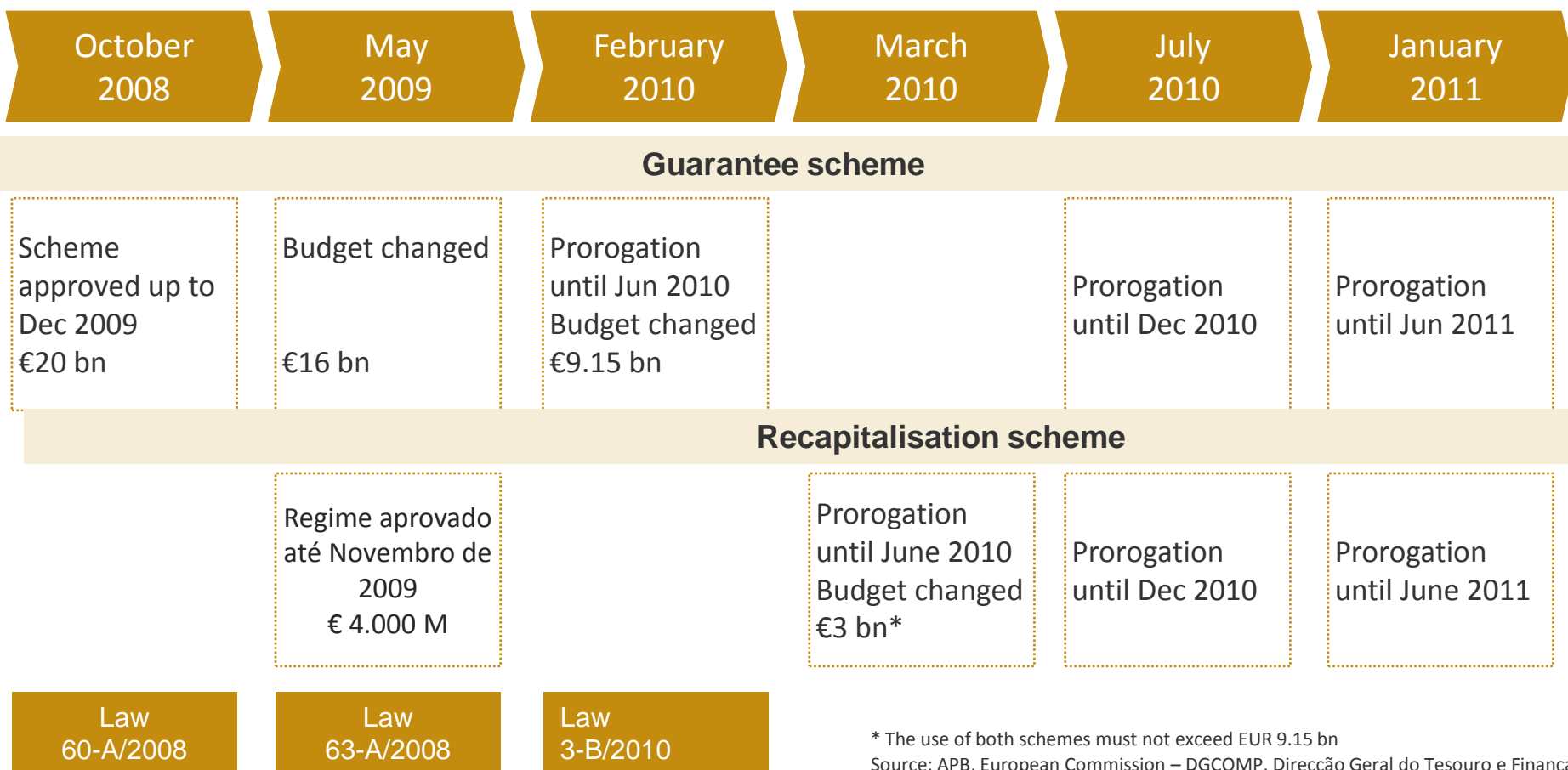


Source: APB, Banco de Portugal

# OVERVIEW OF THE PORTUGUESE BANKING SYSTEM

VI. Public recapitalisation schemes and personal guarantees from the state to credit institutions

## Timeline of public recapitalisation schemes and personal guarantees from the state to credit institutions before the EFAP



\* The use of both schemes must not exceed EUR 9.15 bn

Source: APB, European Commission – DGCOMP, Direcção Geral do Tesouro e Finanças

# Timeline of public recapitalisation schemes and personal guarantees from the state to credit institutions during the EFAP



## Guarantee scheme

Prorogation until Dec 2011, budget changed €35 bn	Prorogation until Jun 2012	Prorogation until Dec 2012	Prorogation until Jun 2013	Prorogation until Dec 2013	Prorogation until Jun 2014	Prorogation until Dec 2014	Prorogation until Jun 2015	Prorogation until Dec 2015
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## Recapitalisation scheme

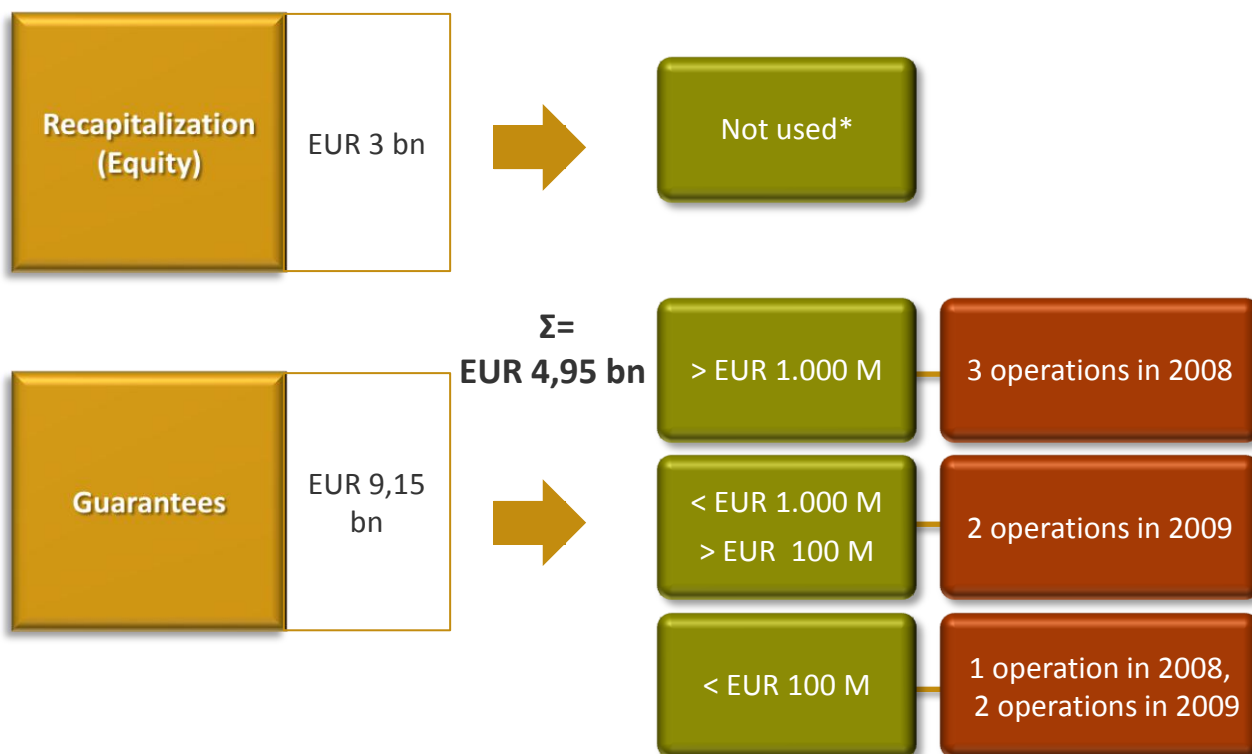
Prorogation 31 Dec 2011 budget changed €12 bn		Prorogation until Dec 2012		Prorogation until Dec 2013	
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Lei nº 48/2011  
Lei nº 4/2012

Source: APB, Comissão Europeia – DGCOMP, Direcção Geral do Tesouro e Finanças

# The Portuguese banks survived the financial crisis without state support in terms of recapitalisation ...

## State support schemes used until the end of June 2011



Up to the end of June 2011:

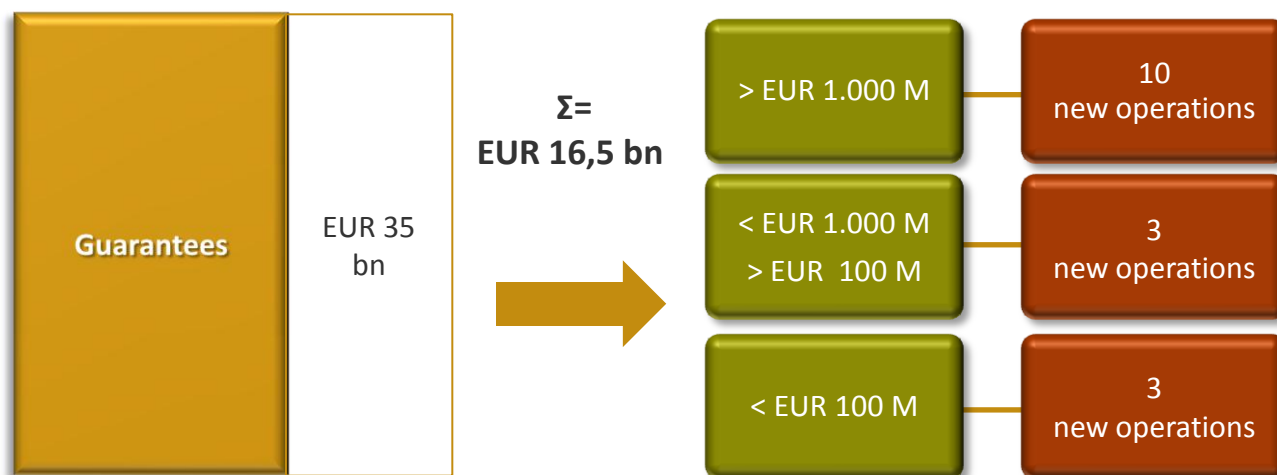
- 6 banks (including CGD) had used the guarantee scheme
- 2 operations in the amount of EUR 75 m had been amortised (one in 2009, the other in 2010)
- The guarantees in effect totalled EUR 4.875 bn, i.e. 53% of the existing budget

\* It was not used by private banks. In December 2010, CGD increased its capital by EUR 550 m, EUR 56 m of which came from the budget of the recapitalisation scheme.

Source: APB, European Commission – DGCOMP, Direcção Geral do Tesouro e Finanças

... meanwhile the public debt crisis led to an increase in the use of state guarantees.

### Use of guarantee scheme after July 2011



- After the July 2011:
  - **6 banks** used the guarantee scheme in new funding operations
  - New operations totalled **EUR 16.525 bn**, i.e. **47.2%** of the budget

Use of the recapitalisation scheme occurred later, to comply with the rules imposed by Banco de Portugal and the EBA.

### Use of recapitalisation scheme



\* Does not include recapitalisation of CGD in June 2012, to the amount of EUR 1.65 million.

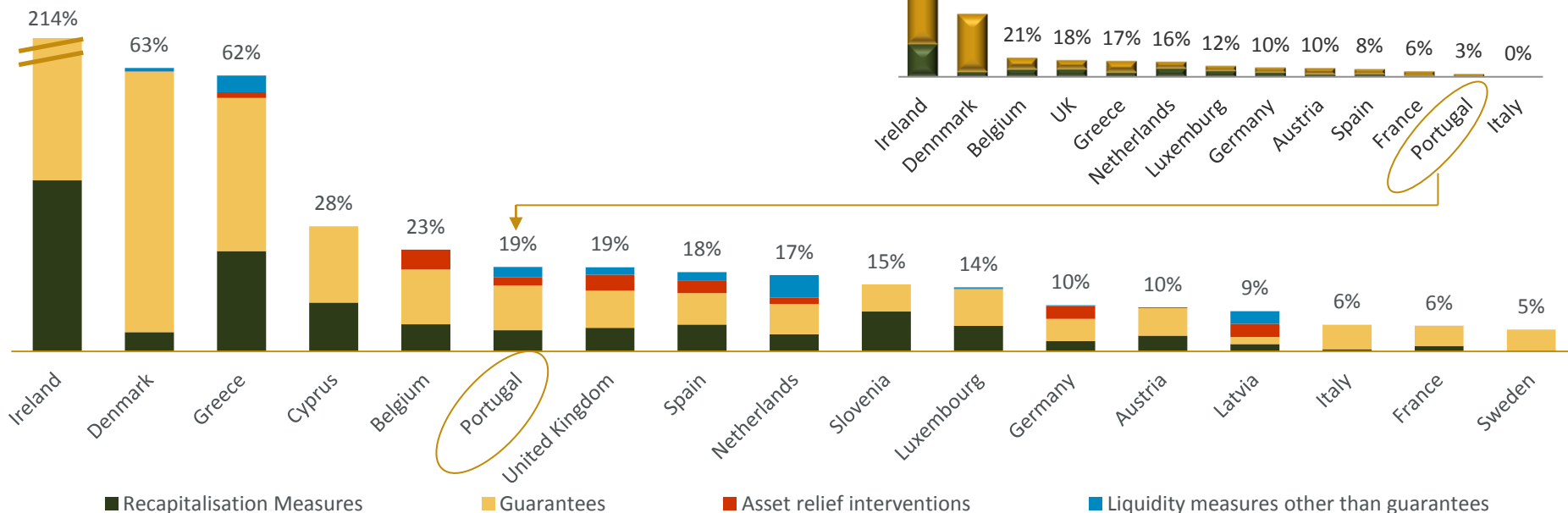
Source: APB, European Commission – DGCOMP, Direcção Geral do Tesouro e Finanças



# State aid used by Portuguese banks up to 2010 was 3% of GDP, rising to 19% in 2013.

State aid to the financial sector as a percentage of GDP \*

## 2008-2013

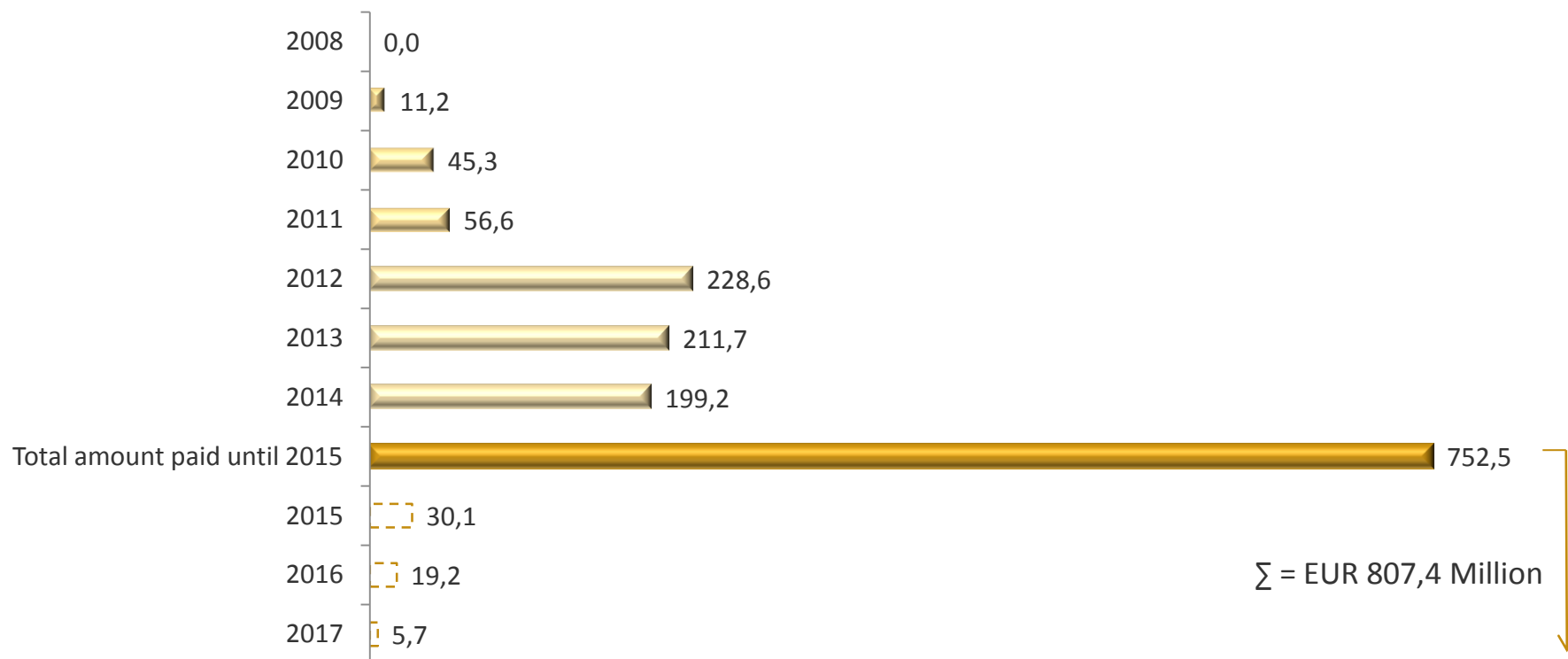


\* The data on guarantees and injections of cash are for 2009, at the peak of use of these instruments in Europe.

Source: European Commission

## Guarantee commissions paid and payable by credit institutions.

### Commissions paid and payable annually\* (EUR millions)



\* Estimates.

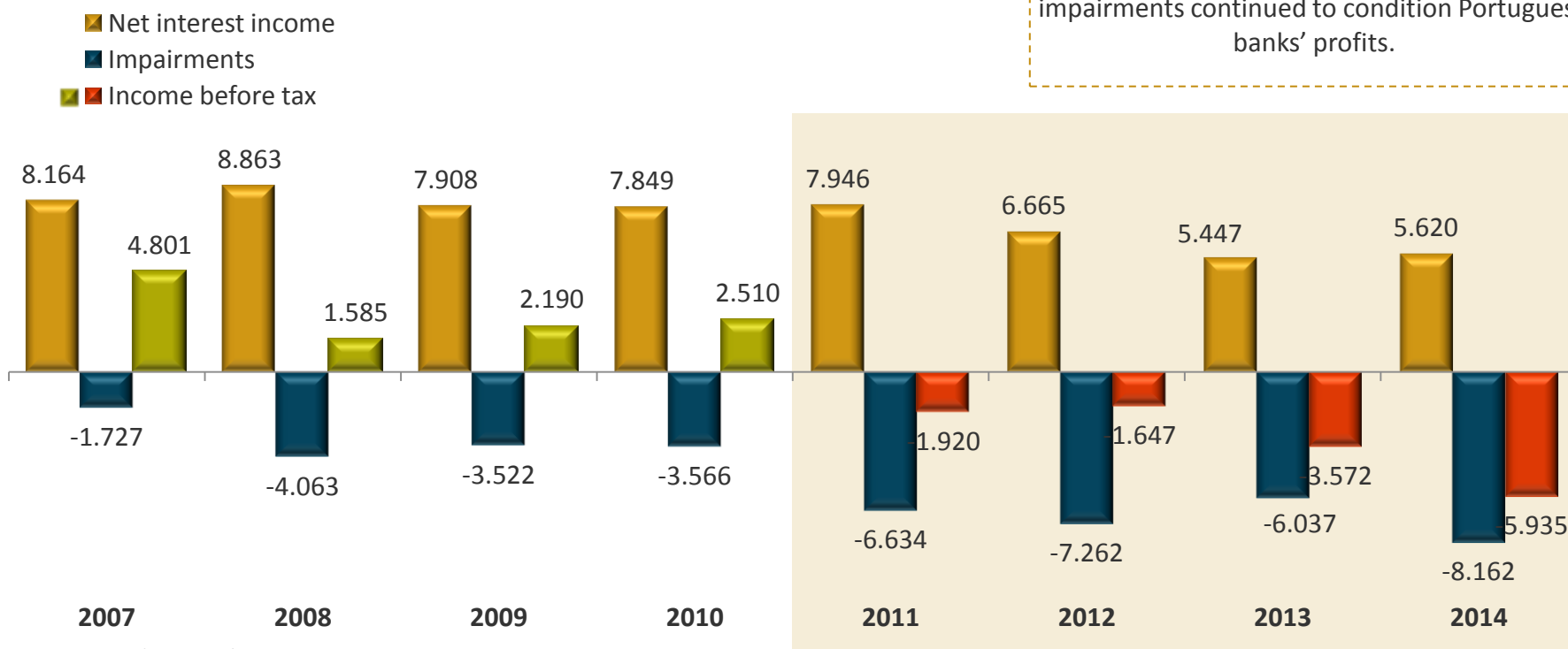
Source: APB, Direcção Geral do Tesouro e Finanças

# OVERVIEW OF THE PORTUGUESE BANKING SYSTEM

## VII. Profitability

# The rise in credit risk in Portugal led to an increase in impairments recorded by the banks, which affected their profits.

**Portuguese banks' consolidated net interest income, impairments and profits before tax (€millions)**



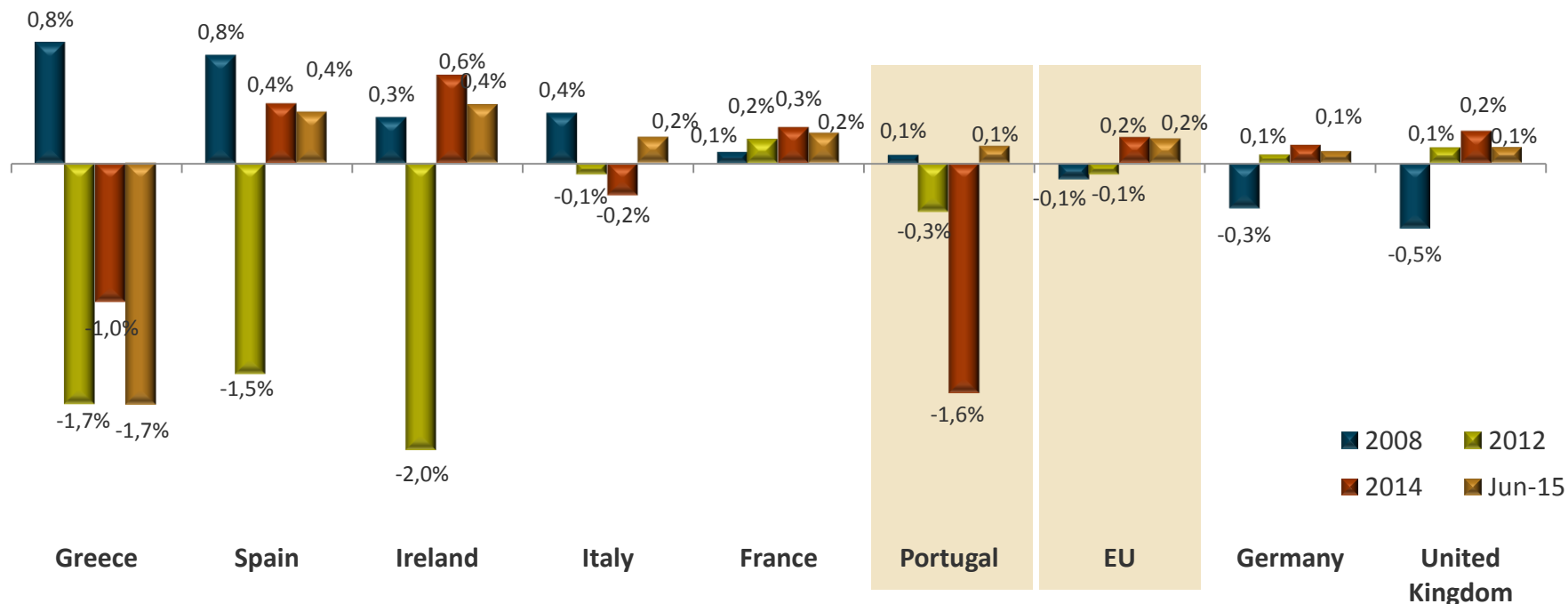
the profits of the Portuguese banking sector were adversely affected not only by an increase in impairments but also a reduction in net interest income. In spite of the stabilisation of net interest income in 2014, the high level of impairments continued to condition Portuguese banks' profits.

Source: Banco de Portugal

# Return on Portuguese banking assets has fallen in recent years and has not kept up with the European recovery.

## ROA - return on assets\*

ROA and ROE of the Portuguese banking sector were positive in the first half of 2015 for the first time since 2012. Profits benefited from lower levels of impairment and operating costs and gains in financial operations.



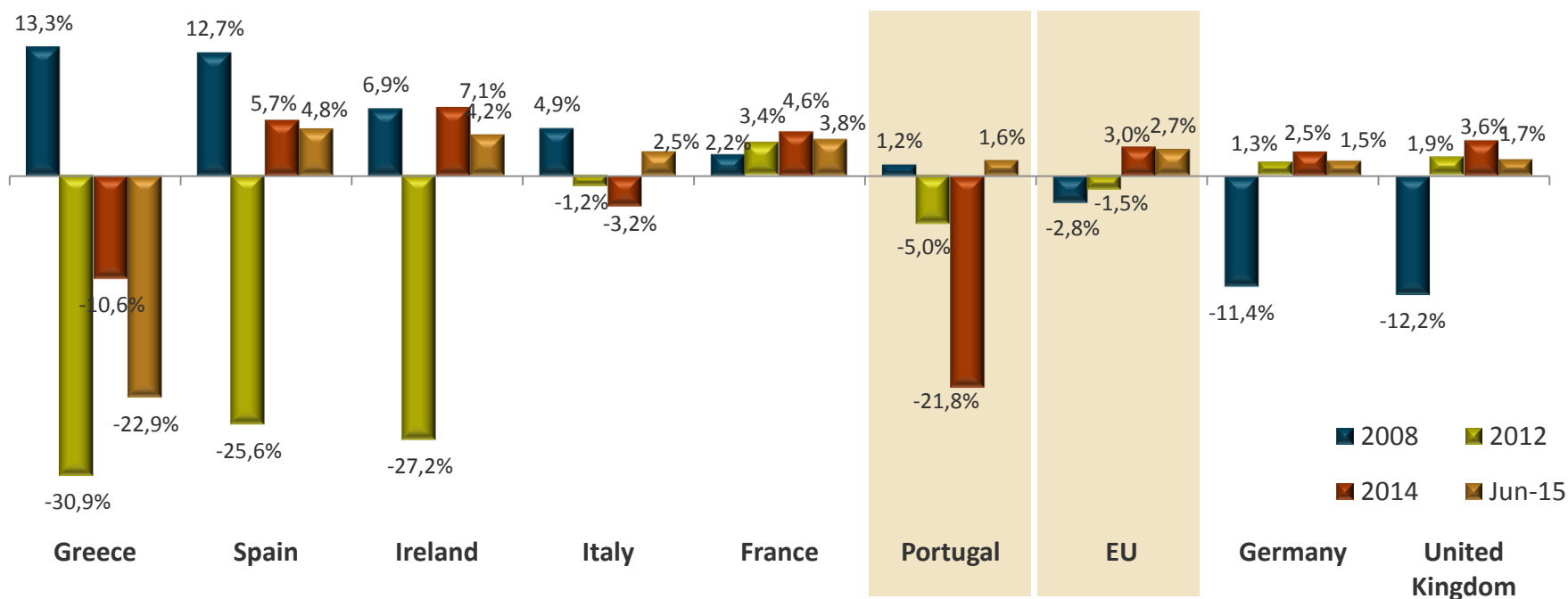
\* Data from banking groups and domestic banks on a consolidated basis.

Source: ECB

## Performance was similar if we look at return on equity..

### ROE - return on equity\*

ROA and ROE of the Portuguese banking sector were positive in the first half of 2015 for the first time since 2012. Profits benefited from lower levels of impairment and operating costs and gains in financial operations.

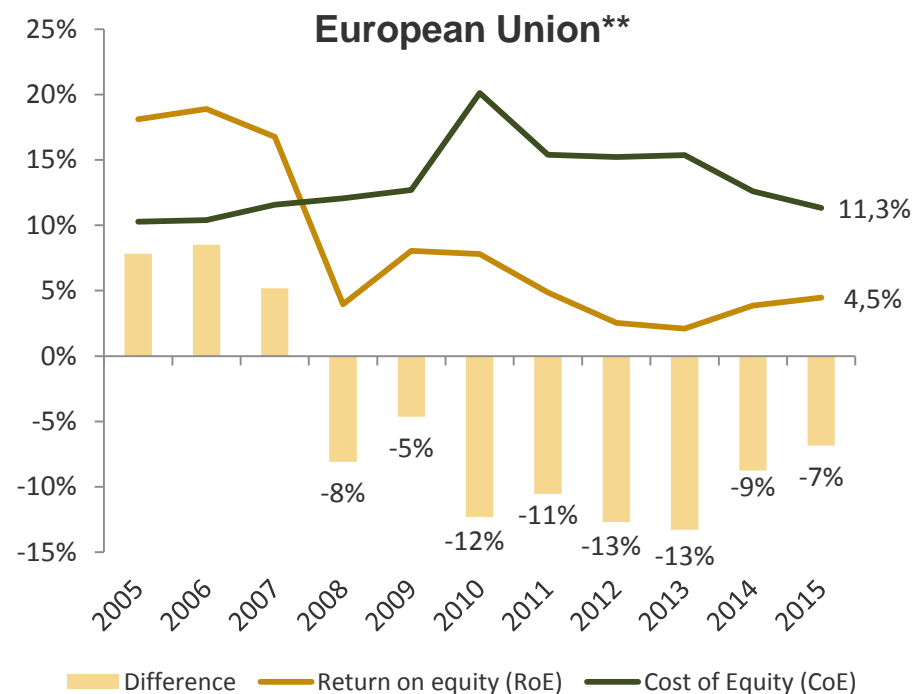
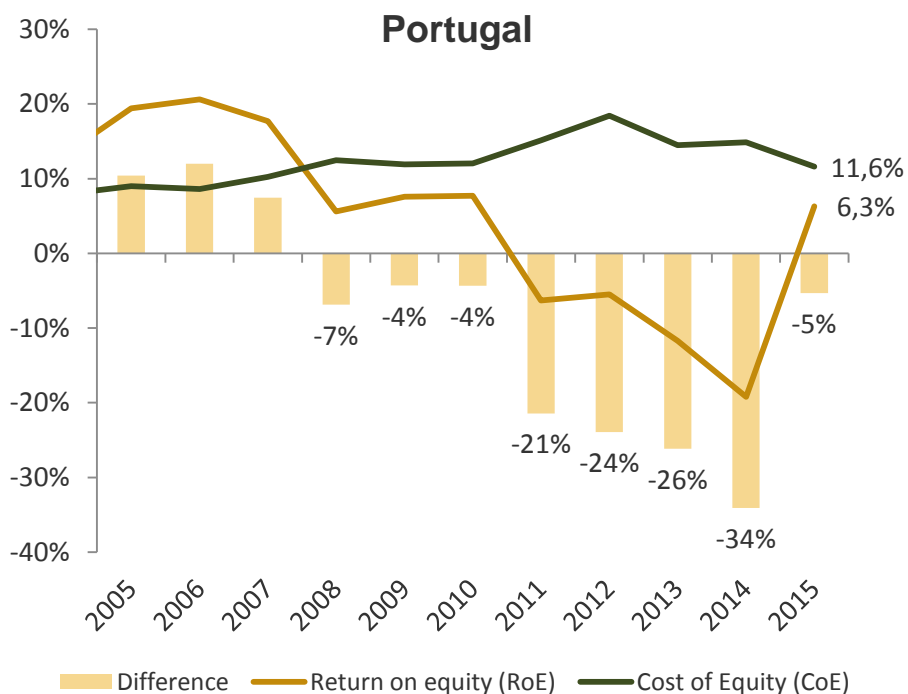


\* Data from banking groups and domestic banks on a consolidated basis.

Source: ECB

In addition to low profitability in the sector, the cost of equity was higher than the return on equity, resulting in value destruction.

### Return on Equity vs. Cost of Equity\*



\* 2015 figures correspond to the first semester.

\*\* Global Systemically Important Banks (G-SIBs)

Source: APB, Banco de Portugal, Bloomberg

Since 2011, Banco de Portugal has conducted several inspections of the largest Portuguese banking groups to assess whether they had reached an appropriate level of impairment.

	1st exercise 2nd half 2011	2nd exercise 2nd half 2012	3rd exercise Jun – Jul 2013	4th exercise Oct 2013 – Mar 2014
<b>Reference date:</b>	30 June 2011	30 June 2012	30 April 2013	30 September 2013
<b>Scope:</b>	<ul style="list-style-type: none"> <li>Assessment of credit portfolio (EUR 281 billion - 72% to 100% of each bank's total portfolio)</li> <li>Validation of capital requirements for credit risk</li> <li>Assessment of parameters and methods used in in stress test exercises.</li> </ul>	<ul style="list-style-type: none"> <li>Assessment of credit portfolio—exposure to construction and real estate sectors in Portugal and Spain (56% of population analysed – EUR 69 billion)</li> </ul>	<ul style="list-style-type: none"> <li>Assessment of credit portfolio (EUR 93 billion analysed)</li> </ul>	<ul style="list-style-type: none"> <li>12 economic groups (EUR 9.4 billion)</li> </ul>
<b>Results:</b>	<ul style="list-style-type: none"> <li>Need to reinforce impairments : EUR 596 million</li> <li>Increase in capital requirements: 0.6%</li> <li>Impact on Tier 1 ratio: from 9.1% to 8.8%</li> </ul>	<ul style="list-style-type: none"> <li>Need to reinforce impairments : EUR 474 million</li> </ul>	<ul style="list-style-type: none"> <li>Need to reinforce impairments : EUR 1.127 billion (reinforced by 30 June 2013)</li> </ul>	<ul style="list-style-type: none"> <li>Need to reinforce impairments : EUR 1.003 billion</li> </ul>

Source: Banco de Portugal



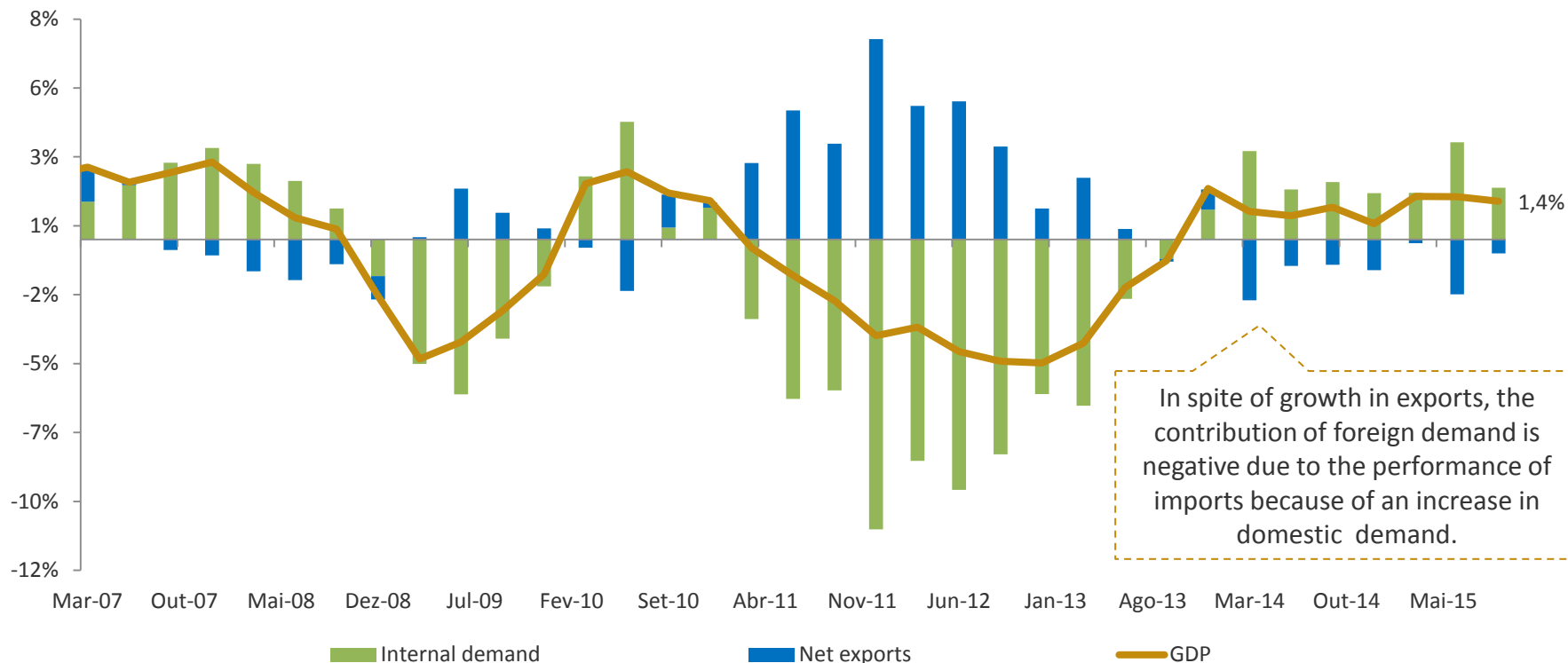
# OVERVIEW OF THE PORTUGUESE BANKING SYSTEM

Annex 1:

Macroeconomic background

Portugal's GDP has stabilised in positive territory in the last two years, after a deep recession. It is still 6.4% lower than in 2007, however.

**Growth in GDP (contribution per component %)**

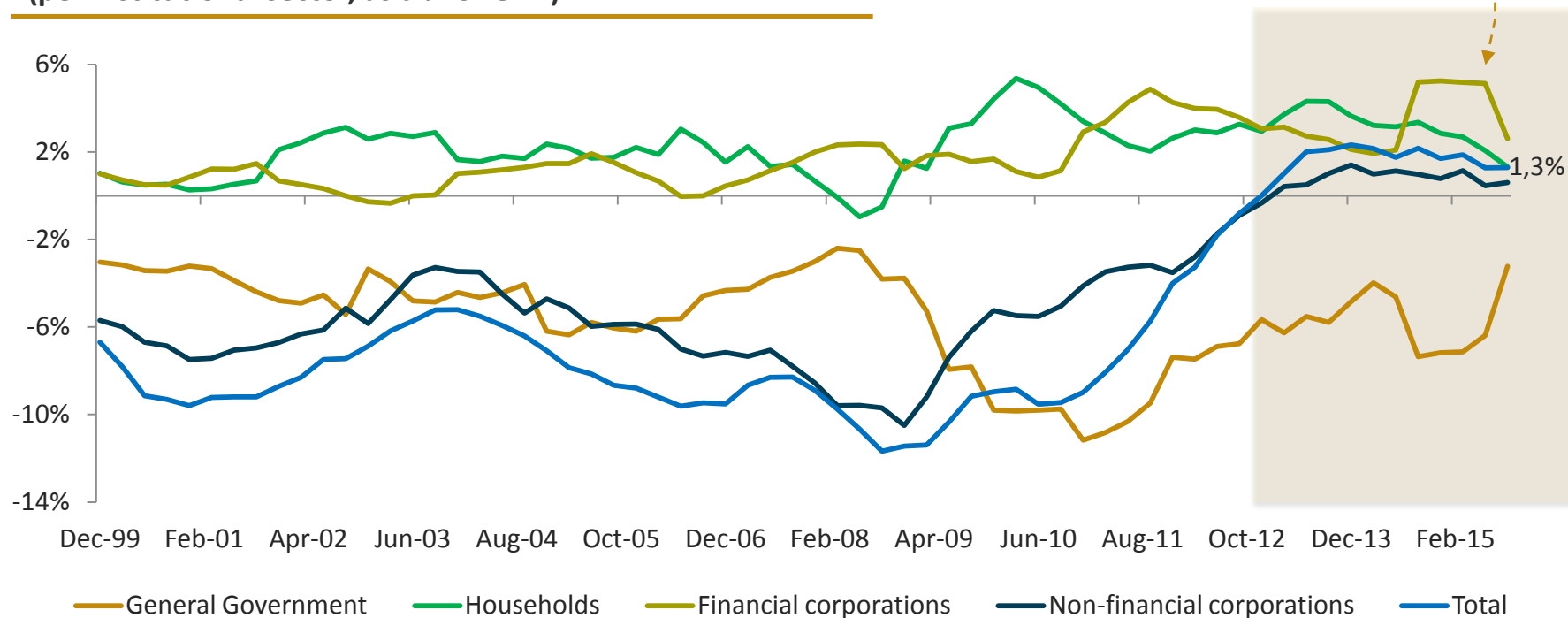


Source: INE

Since the beginning of the EFAP, the economy's need for foreign funding fell. Since then, it has reached and preserved positive readings for the first time.

The funding capacity of financial firms fell from 5.1% to 2.6% from the second to the third quarter of 2015. This reflected the basic effect of the recording of the capitalisation of Novo Banco as a transfer of capital in the third quarter of 2014. The symmetry effect dictated a reduction in the need for funding from the public administration.

**Need/ funding capacity of the economy (per institutional sector, as a % of GDP)**

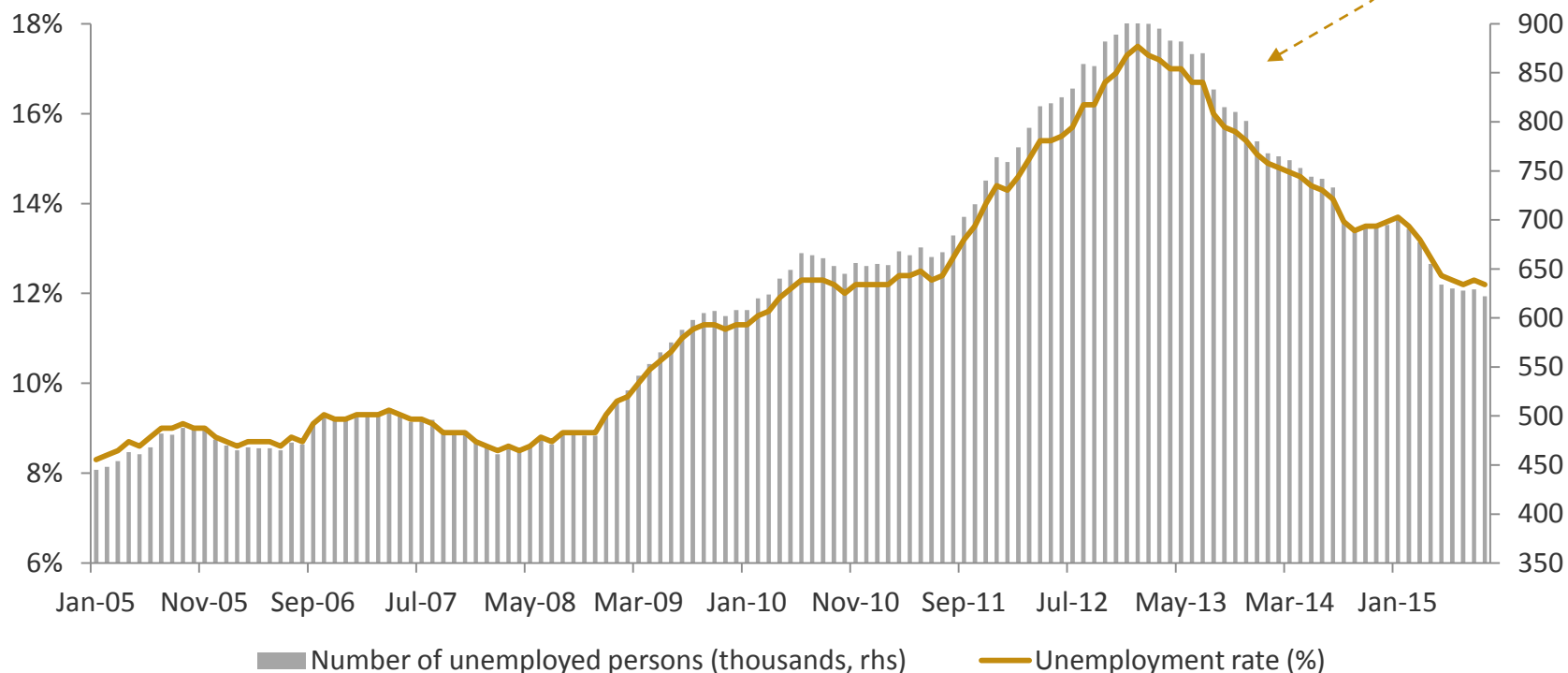


Source: INE

The unemployment rate fell considerably as of 2013, though it is still high from a historical perspective.

**Number of unemployed (in thousands) and unemployment rate (%)**

After reaching an all-time high of 17.5% in 2013, the unemployment rate has been falling and was 12.2% in the third quarter of 2015



Source: INE

# OVERVIEW OF THE PORTUGUESE BANKING SYSTEM

## Annex 2: Methodology

## Methodology

- Unless otherwise explicitly indicated, all the balance sheet data are aggregates of the total banking system of the country in question.
- The balance sheet data analysed in this publication are mostly on a separate basis, aggregated for the whole banking system.
- The item credit balance includes the following financial instruments :
  - Loans, certificates of deposit, repurchase agreements, certificated credit operations, non-performing loans and doubtful debts.
- The solvency analyses were based on the financial institutions' consolidated data.

# OVERVIEW OF THE PORTUGUESE BANKING SYSTEM