

PORTUGUESE BANKING SECTOR OVERVIEW

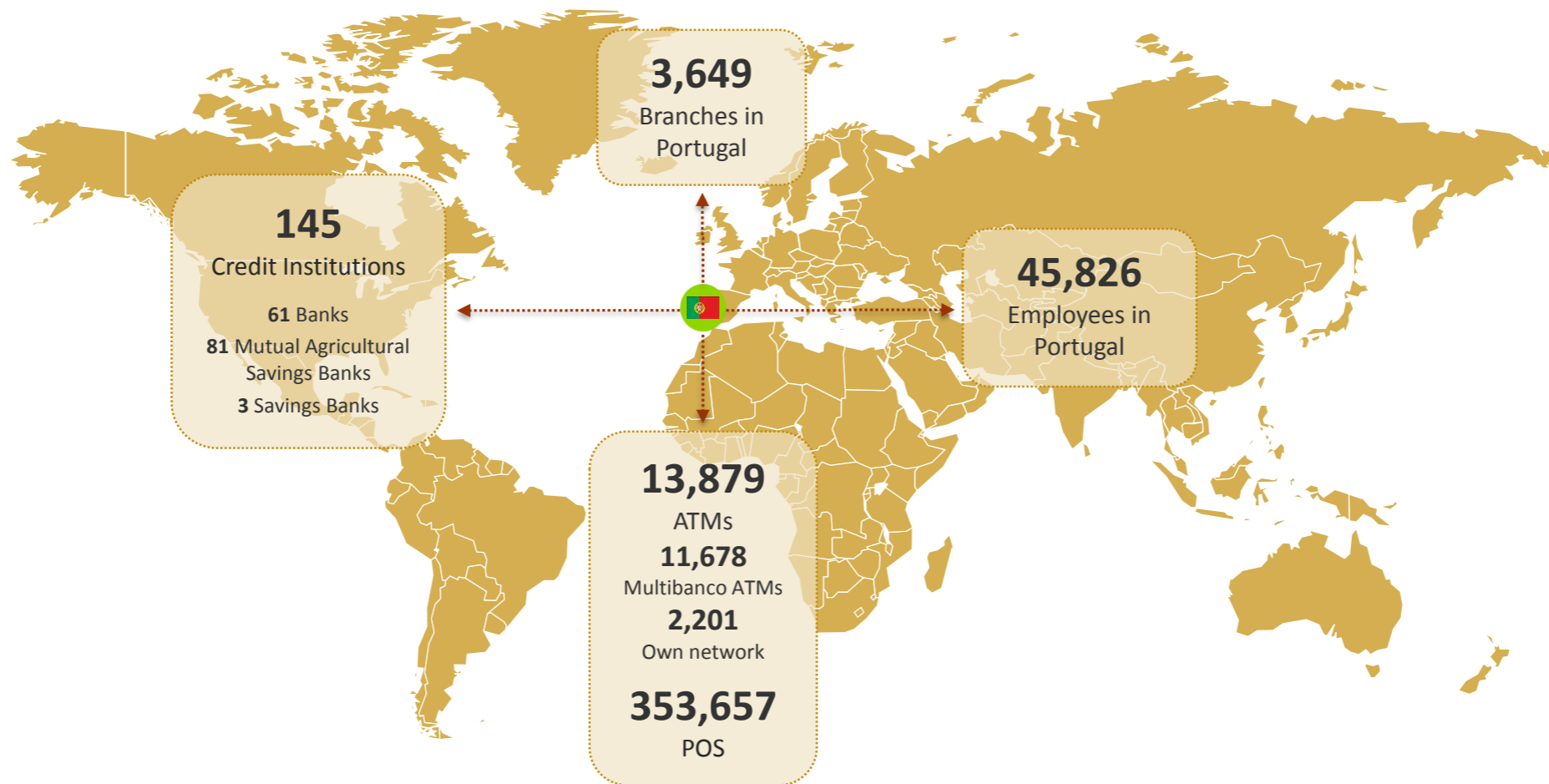
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- ❑ **The progress made by the Portuguese banking sector, since the great financial crisis, has been extremely important to increase the sector's resilience to adverse shocks** and allowed banks to play a critical role in supporting the economy's financing and liquidity needs in the current context of the pandemic crisis.
- ❑ **In the first half of 2021, total assets of the Portuguese banking sector rose significantly over December 2020**, as a result of the increase in cash balances at central banks, loans to customers, and government debt securities. The stock of loans to customers maintained the positive evolution experienced in 2020, which is largely explained by the measures to support the economy adopted in response to the pandemic crisis, namely public guarantee schemes and the moratoria regime.
- ❑ On the liability side, and in a context of a high level of savings, **deposits continued to rise significantly**.
- ❑ As a result of the attractive monetary policy measures, reinforced in this period of crisis, **funding from the Eurosystem increased significantly, with the system's liquidity remaining at extremely comfortable levels**.
- ❑ **In the first half of 2021, the profitability of the banking system increased significantly on a year-on-year basis**, which is mostly explained by an increase in total operating income and a decrease in the flow of provisions and impairments, as a result of lower restrictions related to the pandemic crisis and the economic recovery. However, profitability remains below the cost of equity and is one of the biggest challenges facing the sector.
- ❑ **In terms of solvency**, the system is well capitalised, with the capacity to accommodate a possible deterioration in credit risk and an increase in non-performing assets.
- ❑ **The COVID-19 pandemic and the uncertainty regarding its potential effects pose critical challenges for the banking sector, which already faced significant pressure before the pandemic shock**. Among these challenges, the following stand out: the deep economic recession; the high level of uncertainty regarding the recovery; the maintenance of a low interest rate environment; the high indebtedness level of the non-financial sector; and the potential increase in defaults.

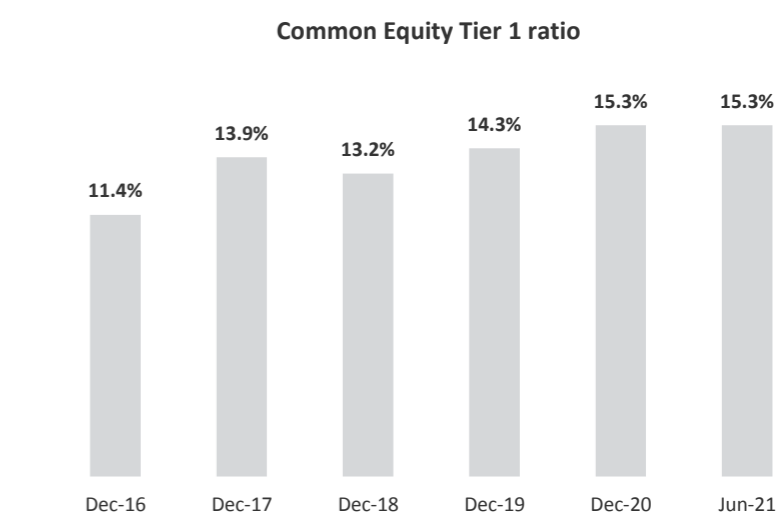
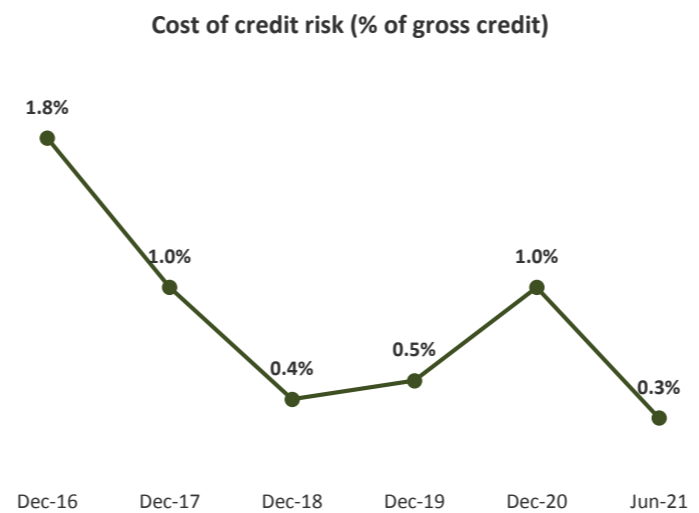
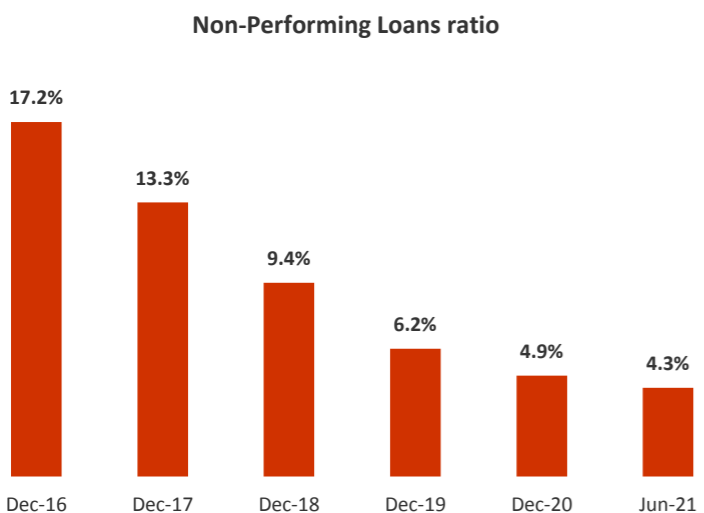
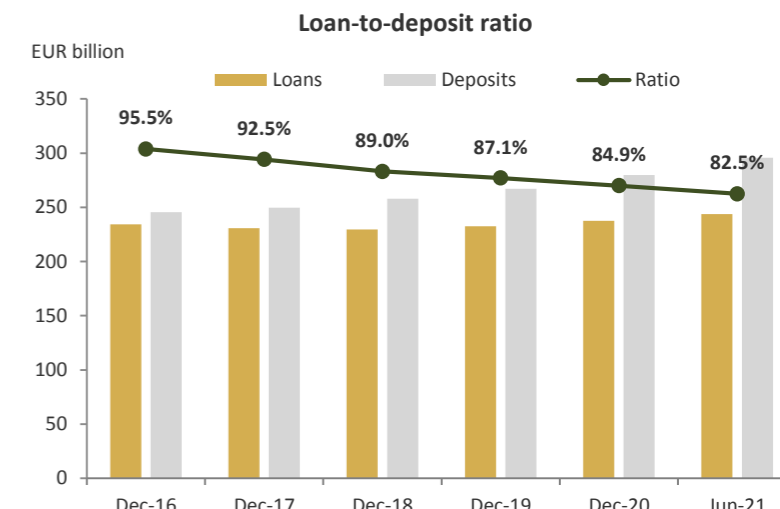
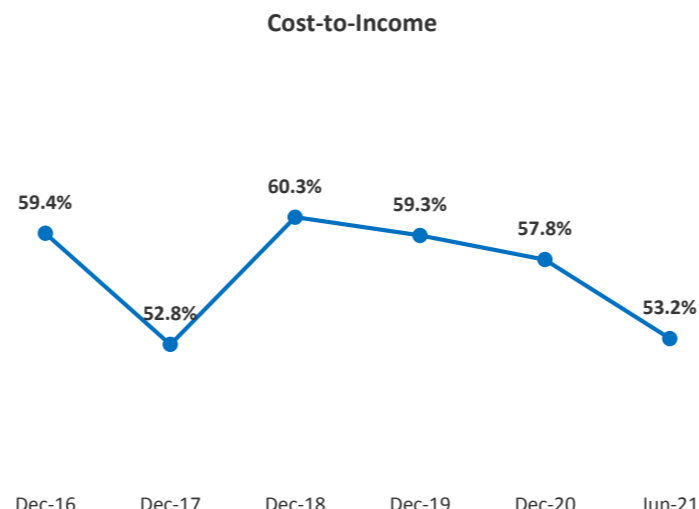
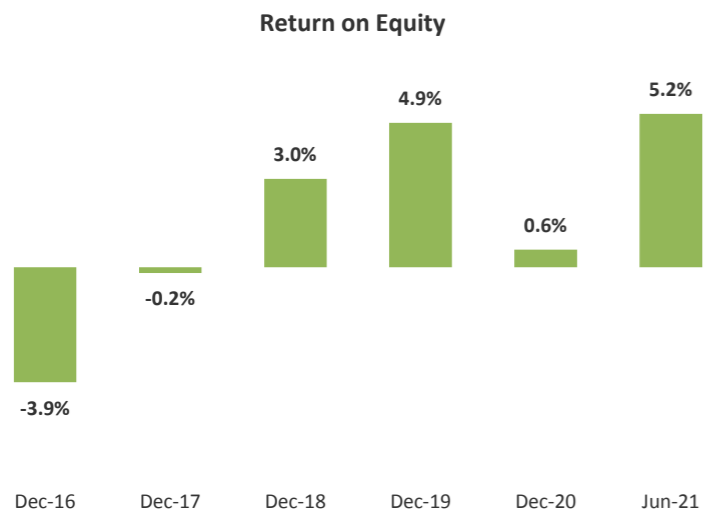
I. RECENT EVOLUTION AND MAIN INDICATORS



Source: APB's associates (branches, employees, and payment systems) and Banco de Portugal (credit institutions).

I. RECENT EVOLUTION AND MAIN INDICATORS

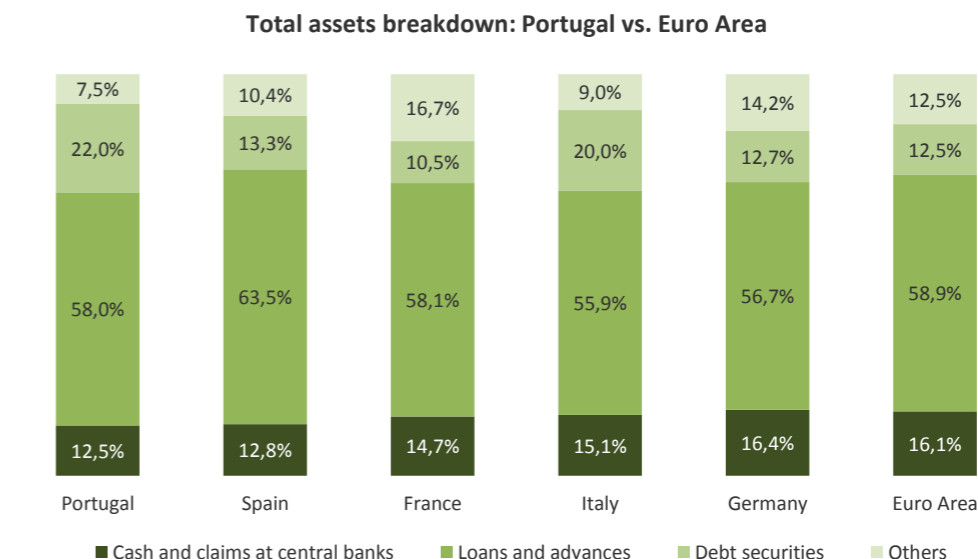
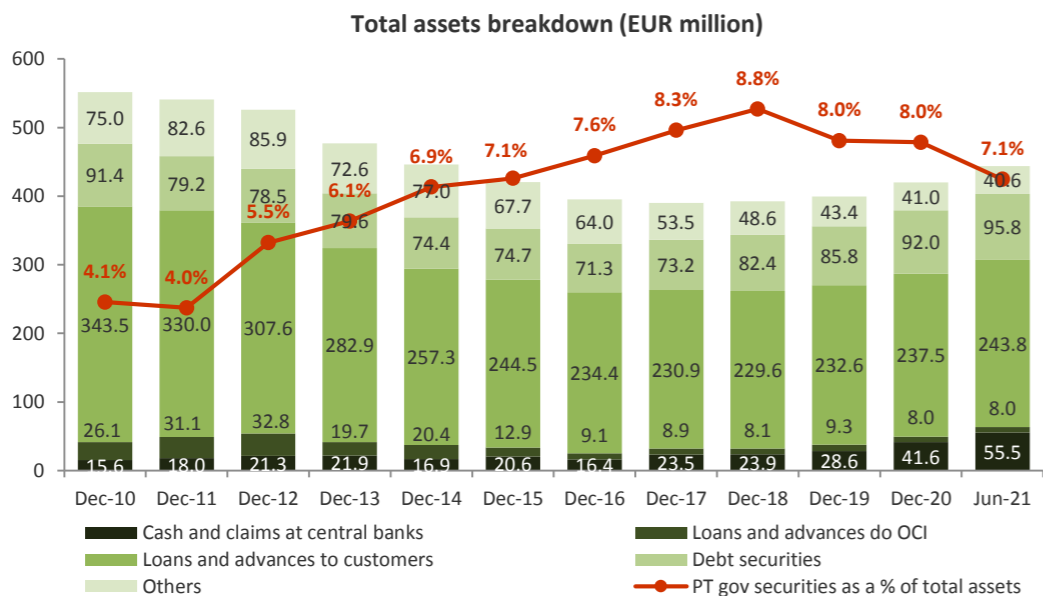
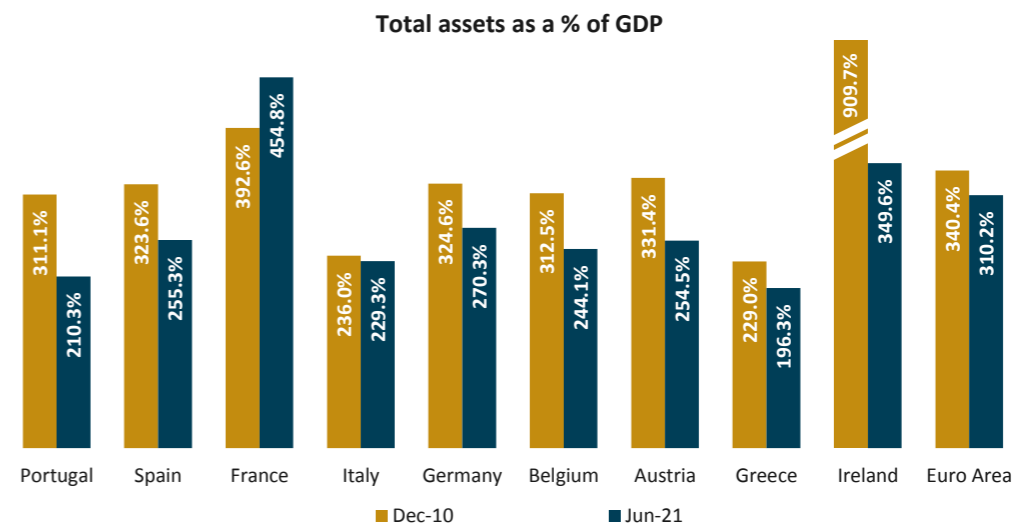
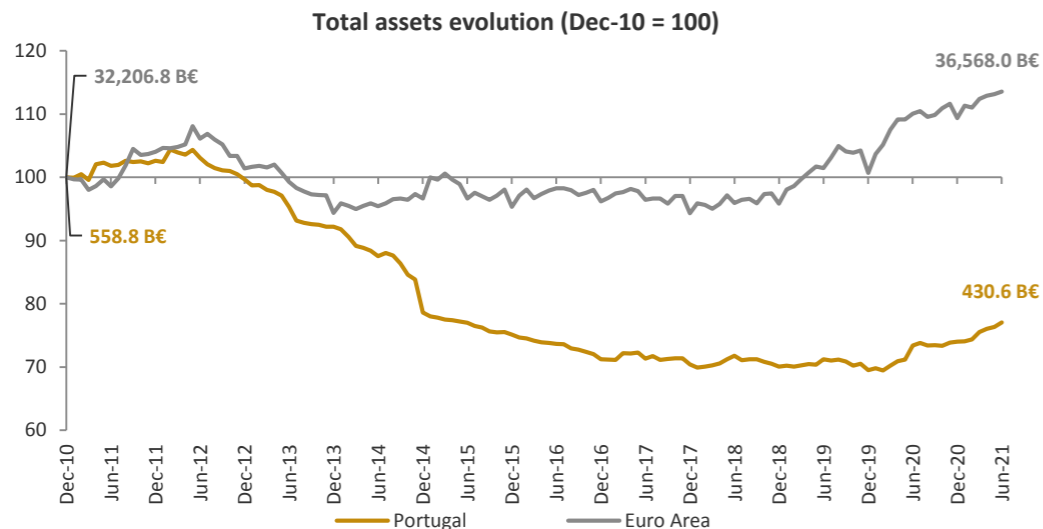
The Portuguese banking sector has shown to be resilient and well prepared to face the shock caused by the COVID-19 pandemic, particularly in terms of liquidity and solvency.



Source: Banco de Portugal (consolidated data). Return on Equity calculated based on net income after tax and before minority interests and on equity (average).

II. FINANCIAL POSITION

Total assets of the Portuguese banking sector rose 5.6% over December 2020, as a result of the increase in cash balances at central banks, loans to customers, and public debt securities. Despite this evolution, the banking sector's share of GDP remains at significantly lower levels than before the sovereign debt crisis due to the economy's deleveraging process registered in subsequent years.

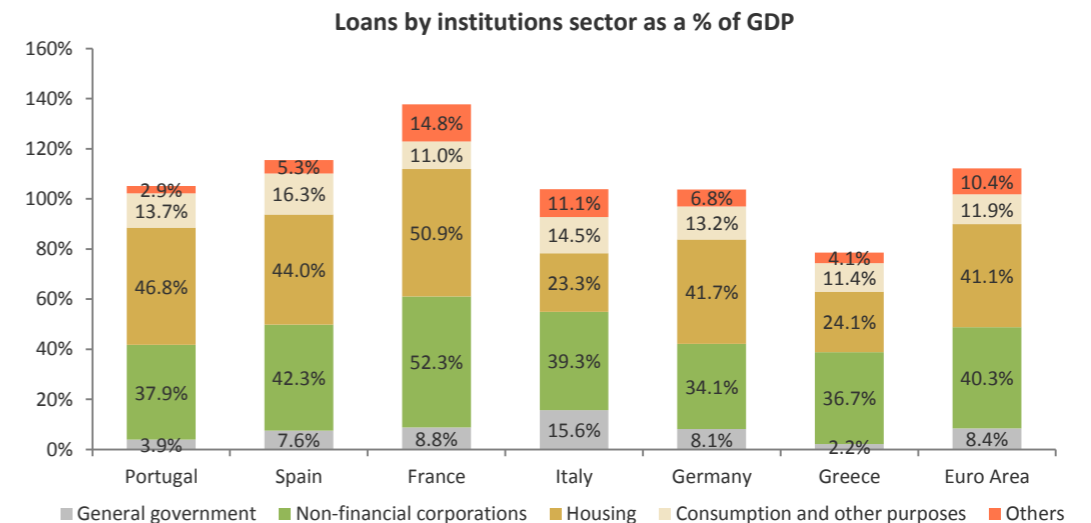
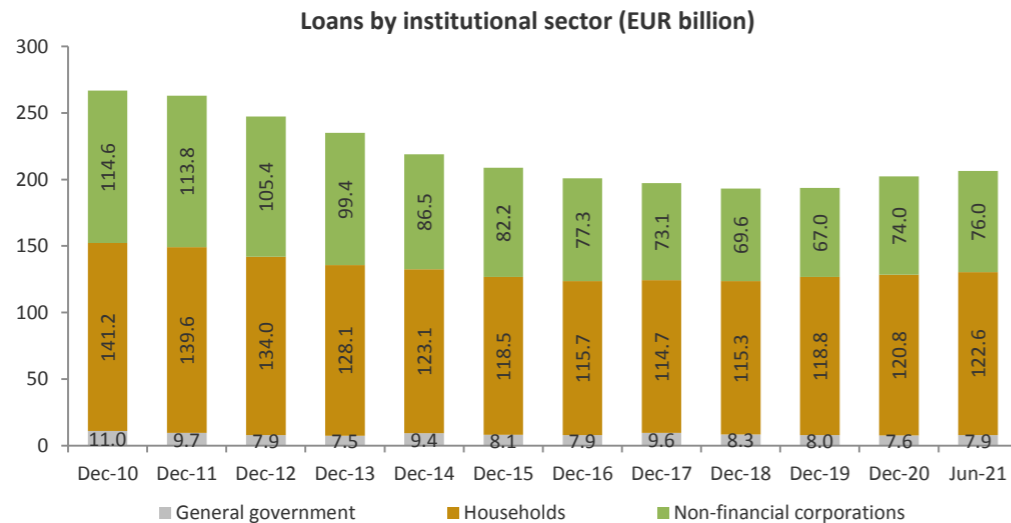
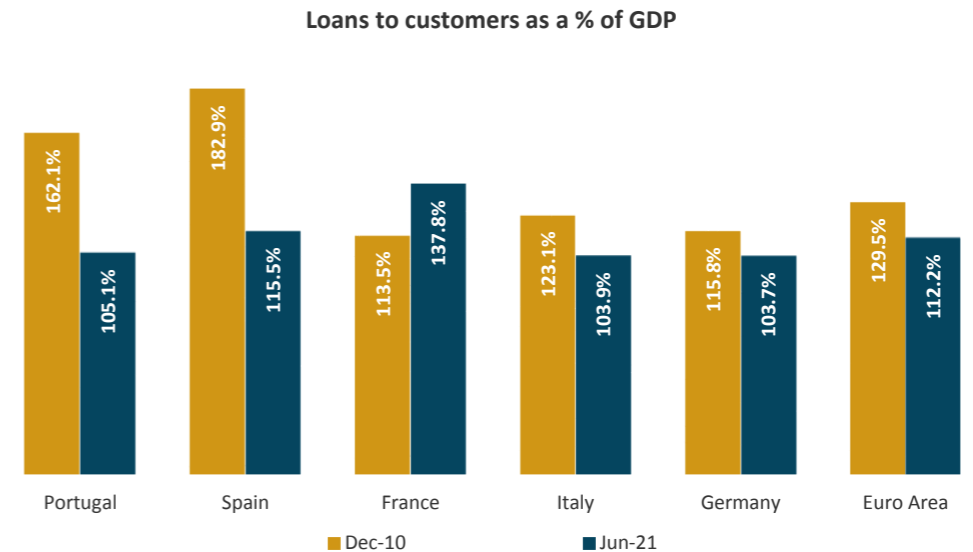
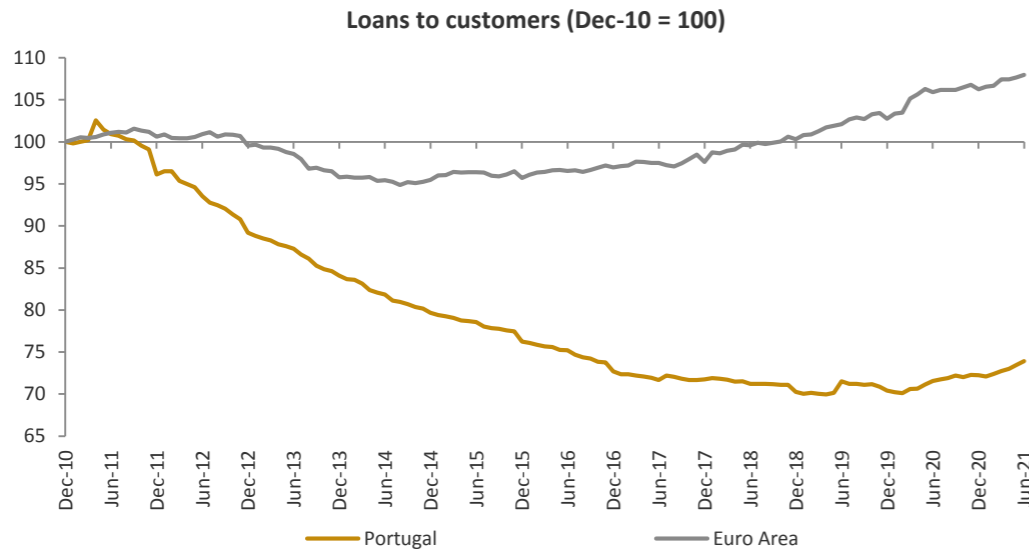


Source: ECB – MFI Balance Sheet Items (Monetary and Financial Statistics) and Banco de Portugal (consolidated data).

Source: ECB – MFI Balance Sheet Items (Monetary and Financial Statistics) and Consolidated Banking Data and Eurostat.

II. LENDING

The increase in the stock of loans to customers since the end of 2019 is largely explained by the measures to support the economy adopted in response to the pandemic crisis, namely public guarantee schemes and the moratoria regime.

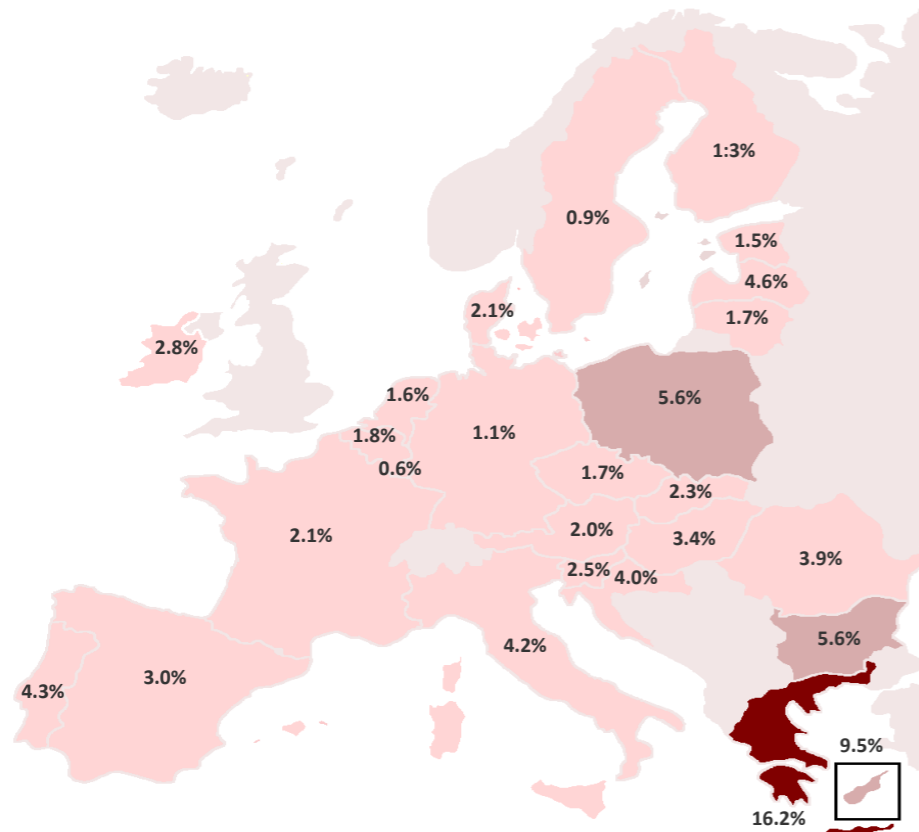


Source: Banco de Portugal (Monetary and Financial Statistics), ECB – MFI Balance Sheet Items (Monetary and Financial Statistics) and Eurostat. Loans to customers are equivalent to loans granted to the non-monetary sector (gross end of period balances). Others included Non-Monetary Financial Institutions: Other Financial Intermediaries, Financial Auxiliaries, Insurance Corporations and Pension Funds.

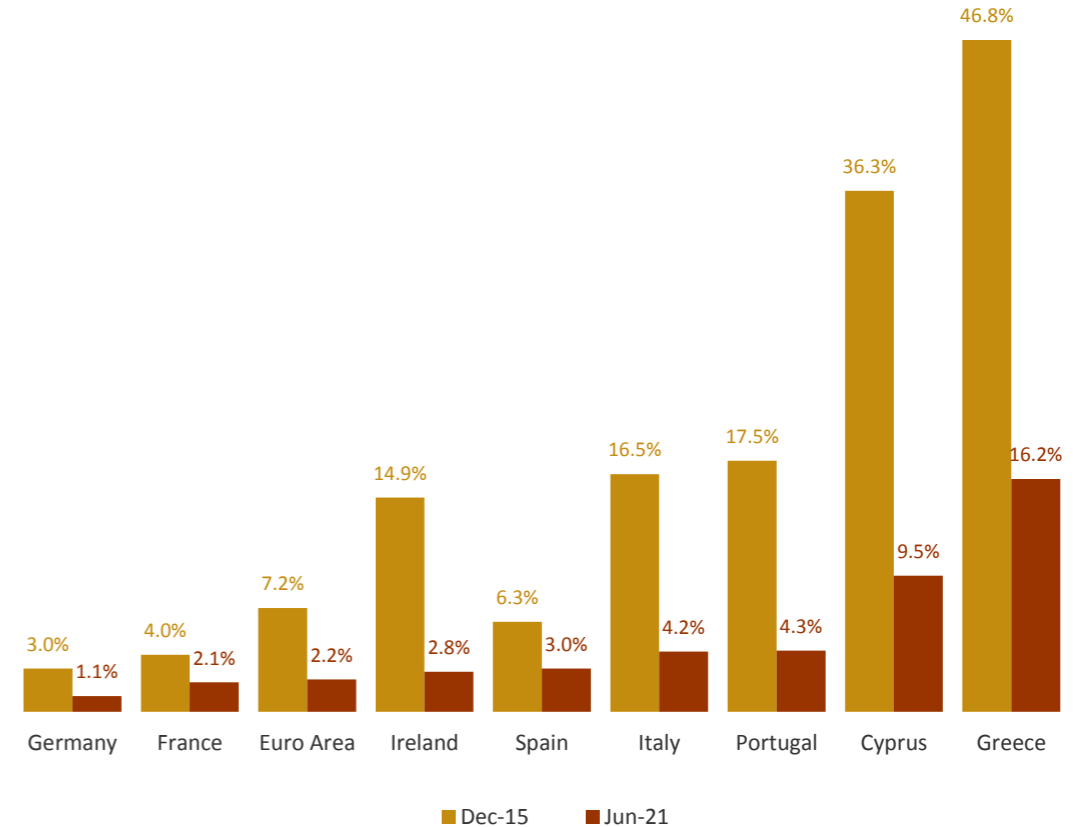
II. LENDING

Despite an extremely challenging macroeconomic environment, the Portuguese banking sector continued to deliver progresses in the reduction of the NPL stock. Since December 2015, this reduction amounted to around 36 billion euros.

NPL ratio in the EU



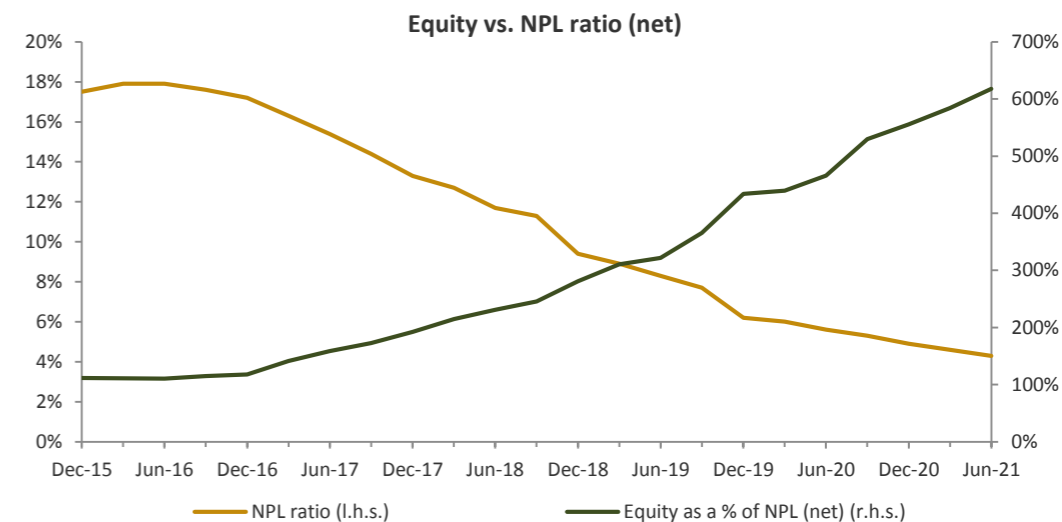
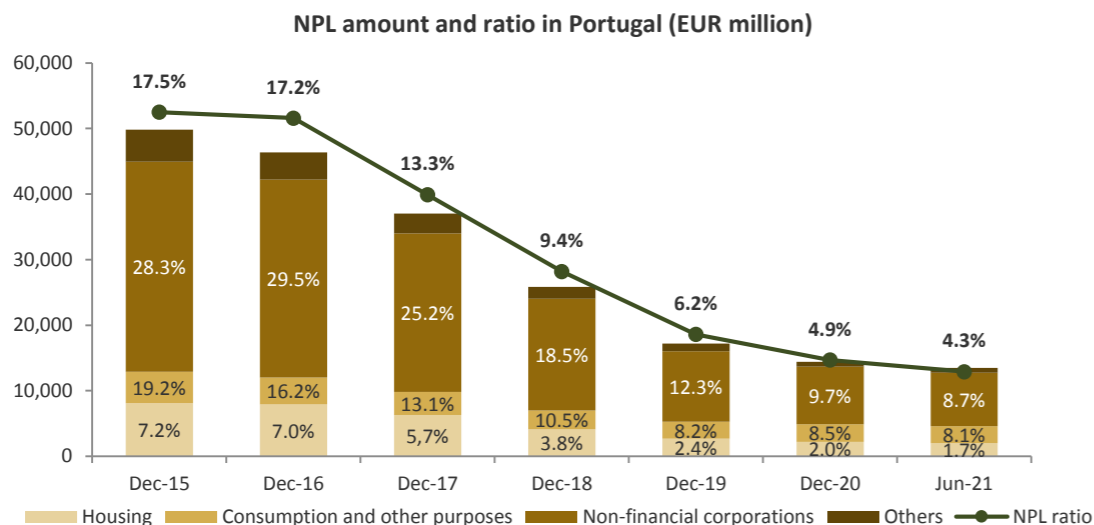
Evolution of the NPL ratio in the EU



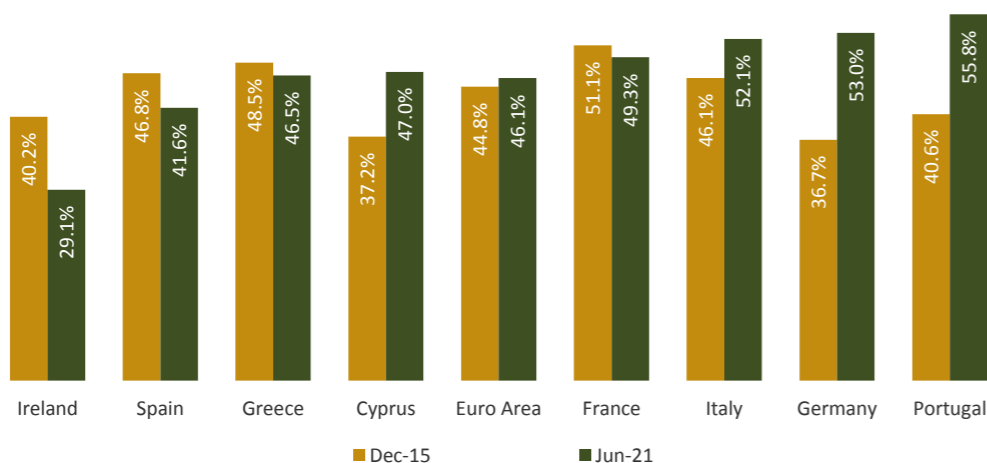
Source: ECB – Consolidated Banking Data.

II. LENDING

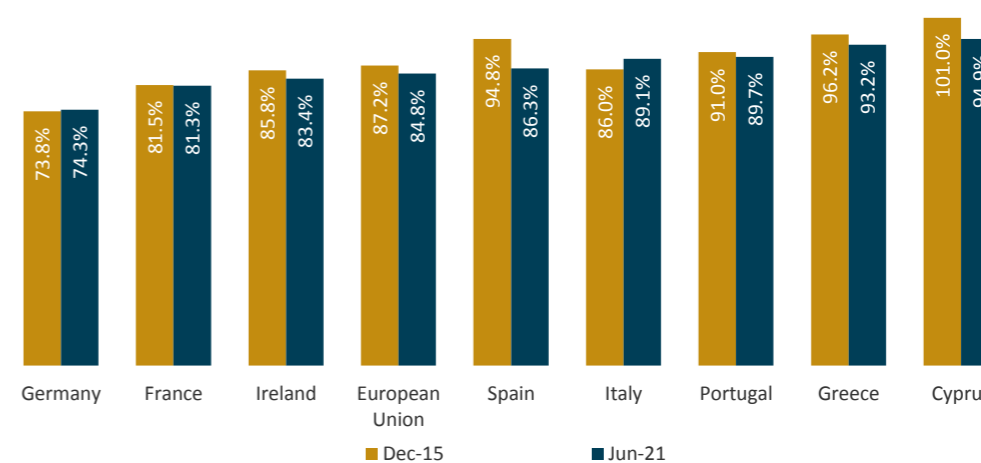
In the first half of 2021, the NPL ratio decreased to 4.3% on the back of the reduction of non-performing loans and the increase of performing loans. The NPL ratio net of impairments stood at 1.9%, vis-à-vis 2.2% in 2020. The increase in the coverage ratio was stronger in the loans to companies that operate in sectors more affected by the pandemic.



Impairment coverage ratio



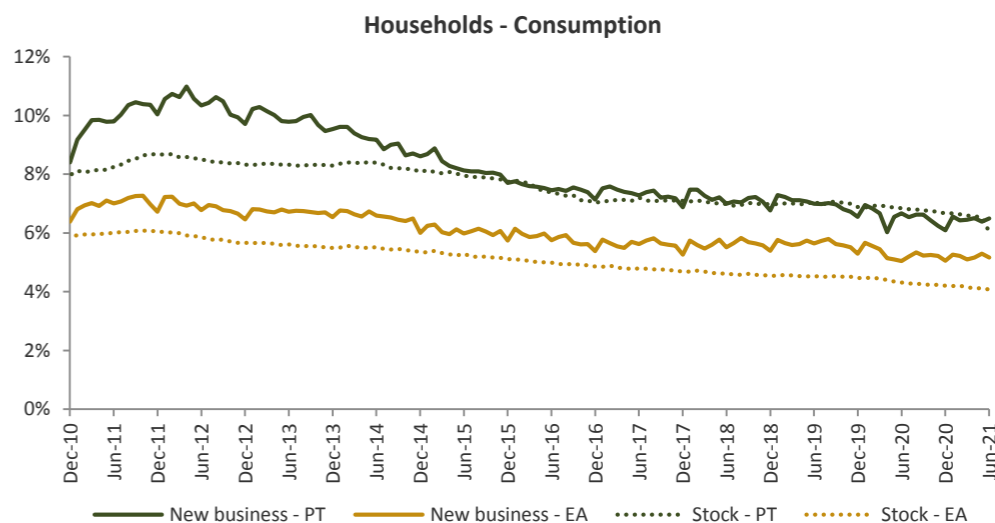
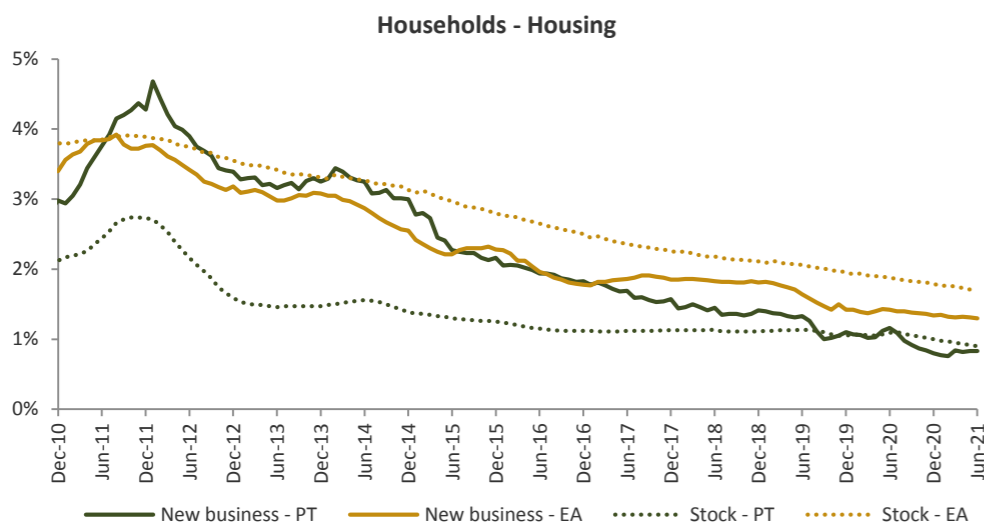
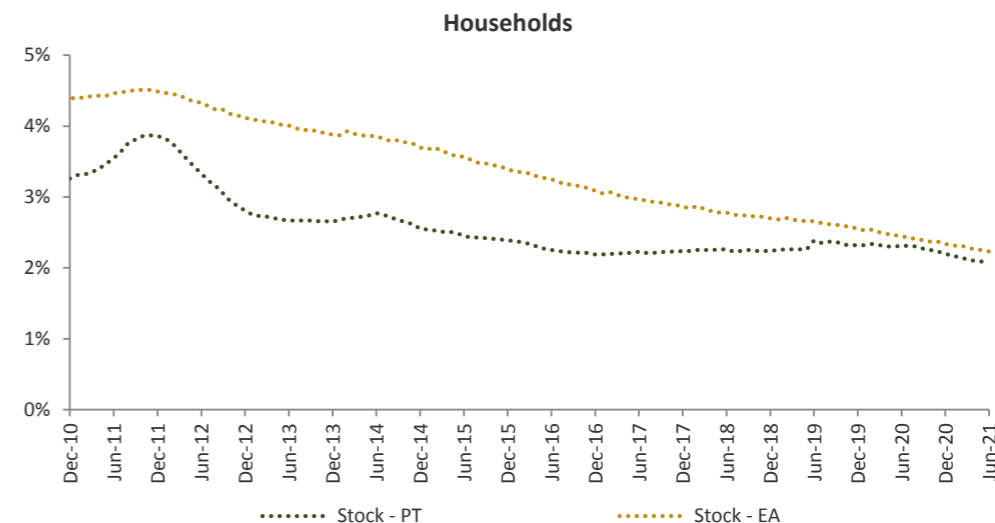
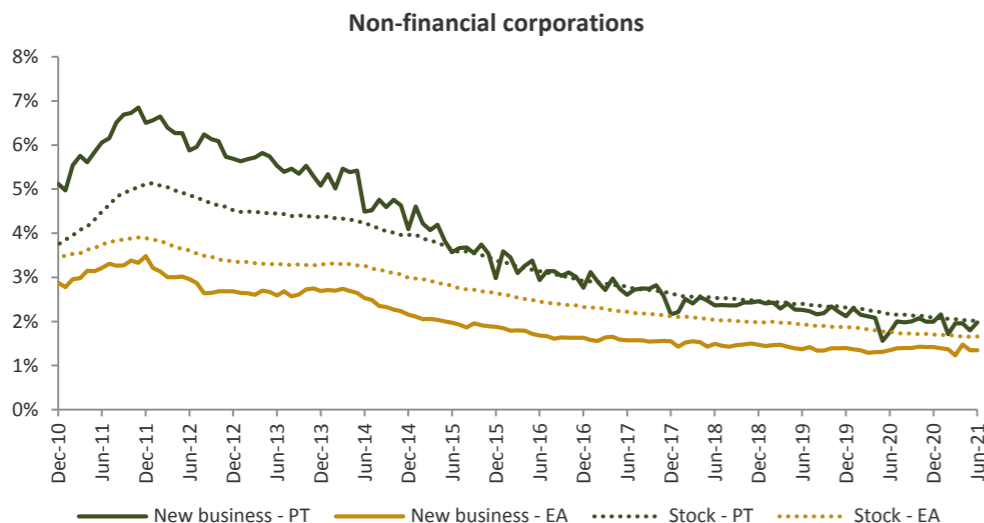
NPL total coverage ratio



Source: Banco de Portugal (consolidated data), ECB – Consolidated Banking Data, and EBA – EU-wide transparency exercise (NPL total coverage ratio). The Impairment coverage ratio refers to non-performing loans and debt securities. NPL total coverage ratio includes cumulative impairments, collateral, and financial guarantees associated with non-performing loans. The EBA sample includes, as of Jun-21, 120 banks at the highest level of consolidation (Portugal: BCP, CGD, and LSF Nani Investments).

II. LENDING | LOAN CONDITIONS | INTEREST RATES

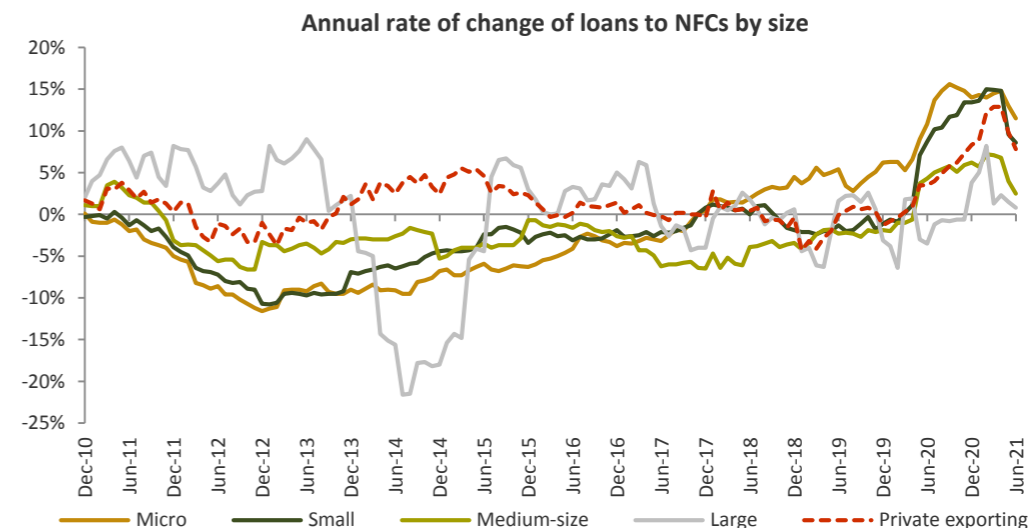
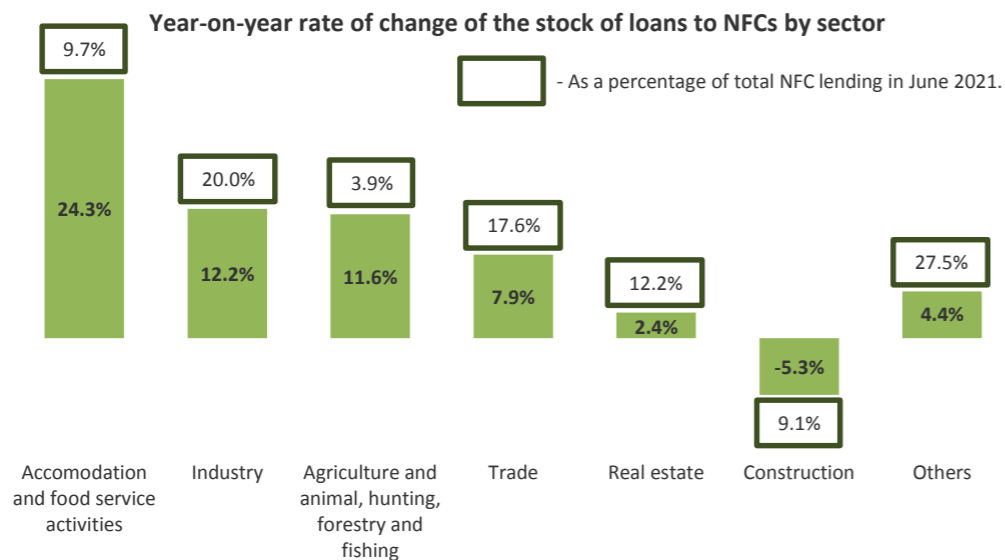
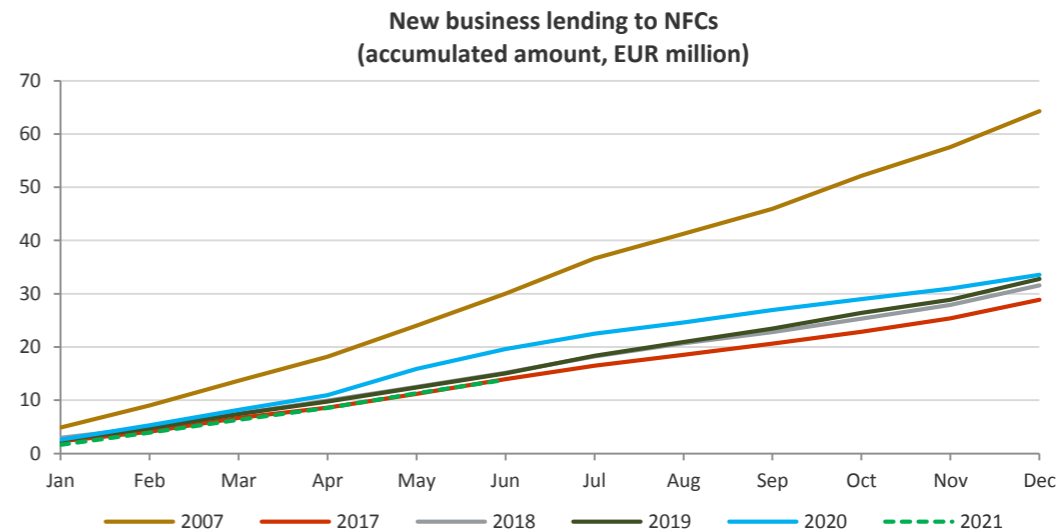
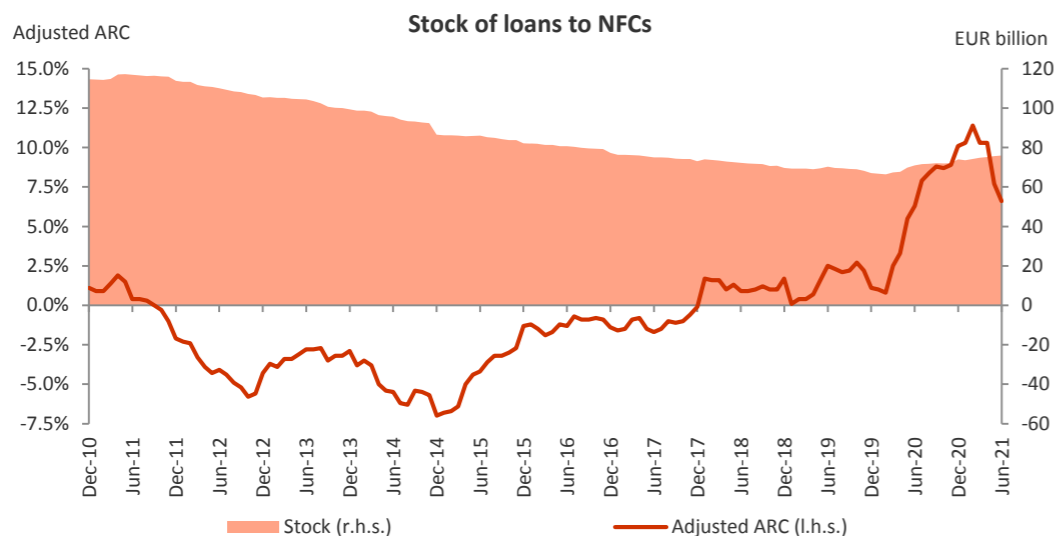
Interest rates on loans have been in a downward path and converging towards the Euro Area average, especially in what concerns interest rates on new lending to non-financial corporations (NFC). The interest rates on households in Portugal remain below the EU average level.



Source: ECB – MFI Interest Rate Statistics.

II. LENDING | NFC

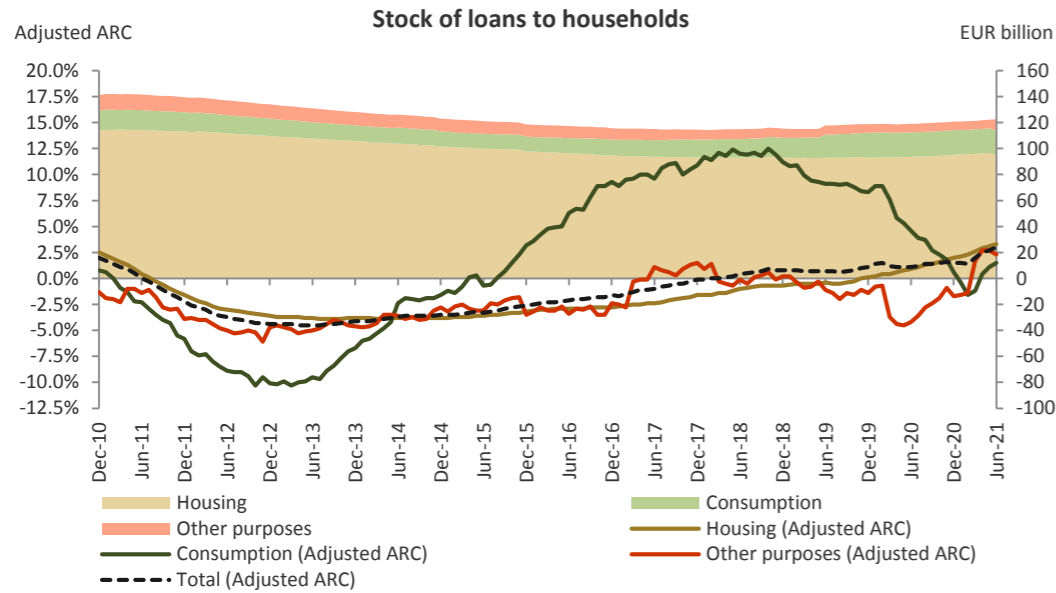
The evolution of the stock of loans to non-financial corporations has been penalized by the effort to reduce non-performing loans. However, since 2020, there was an increase in new loans to non-financial corporations due to public guarantee schemes and the moratoria regime in place as a response to the pandemic crisis. By sector of activity, the largest increase occurred in Accommodation and food service activities, and by size, in the SME segment.



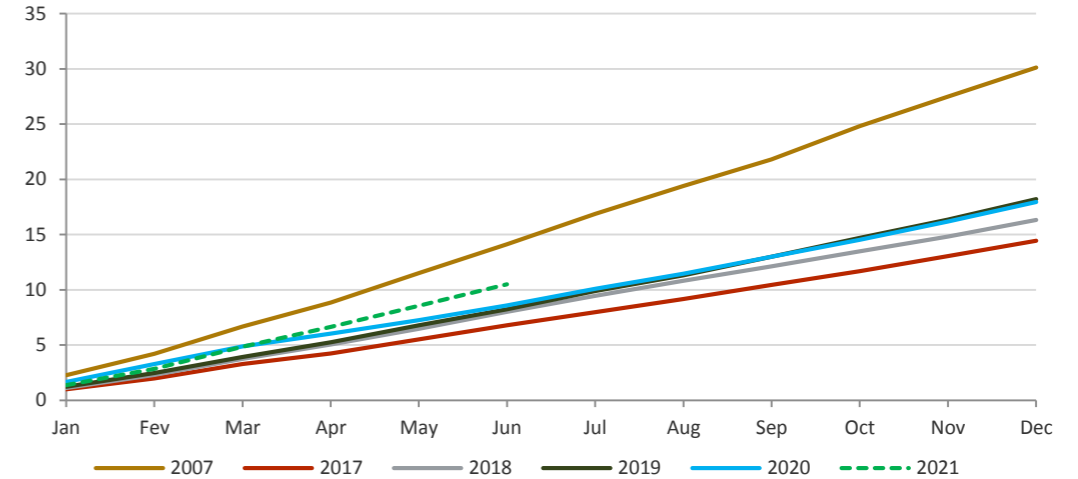
Source: Banco de Portugal (Monetary and Financial Statistics). Adjusted ARC = Annual rate of change (ARC) adjusted for securitisation and liquidity-providing operations.

II. LENDING | HOUSEHOLDS

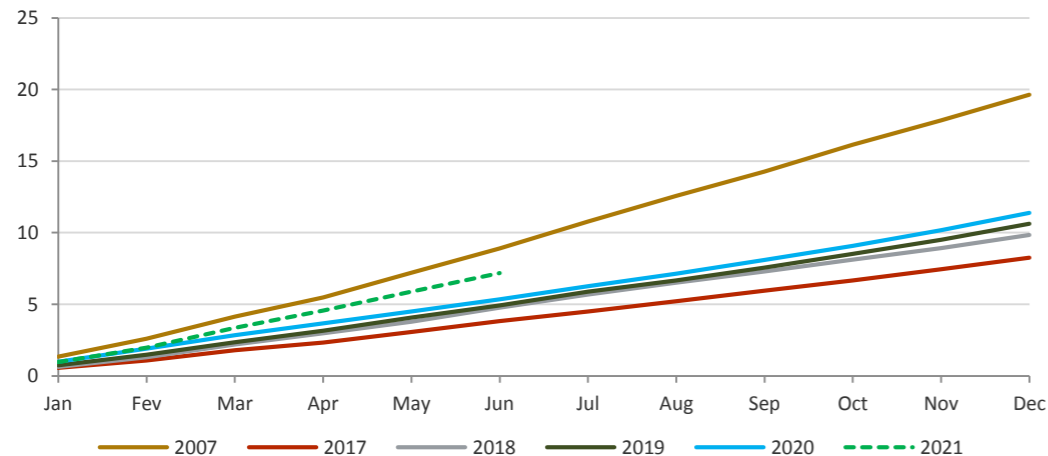
In the first half of 2021, the stock of loans for house purchase maintained the path of recovery started in 2019, essentially due to the growth of new loans and the reduction in repayments, reflecting the effects of the moratoria regimes.



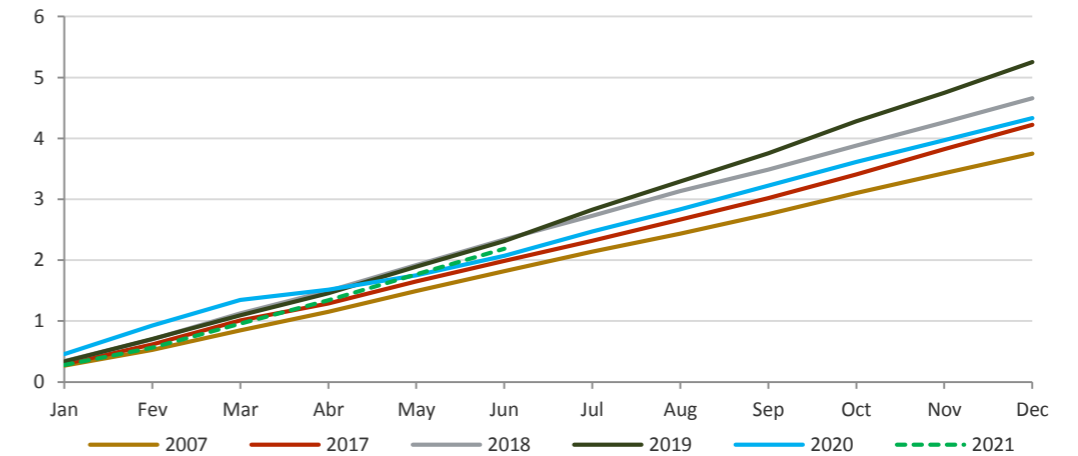
New business lending to households (accumulated amounts, EUR million)



New business lending to households - Housing (accumulated amounts, EUR million)



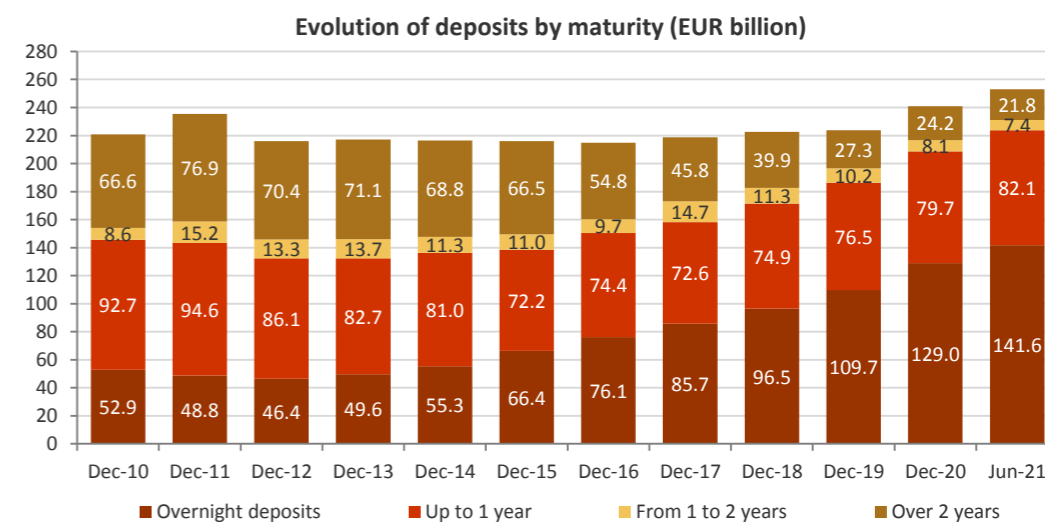
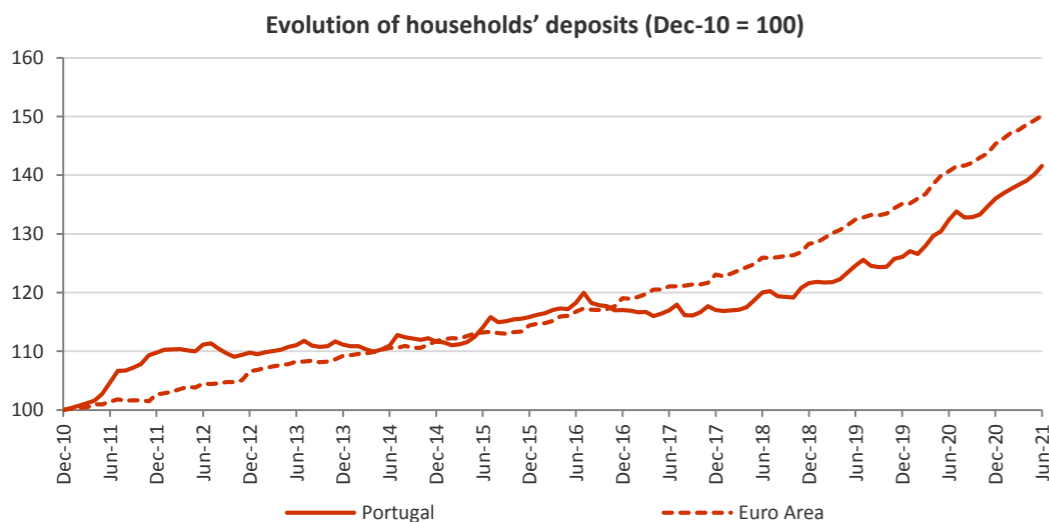
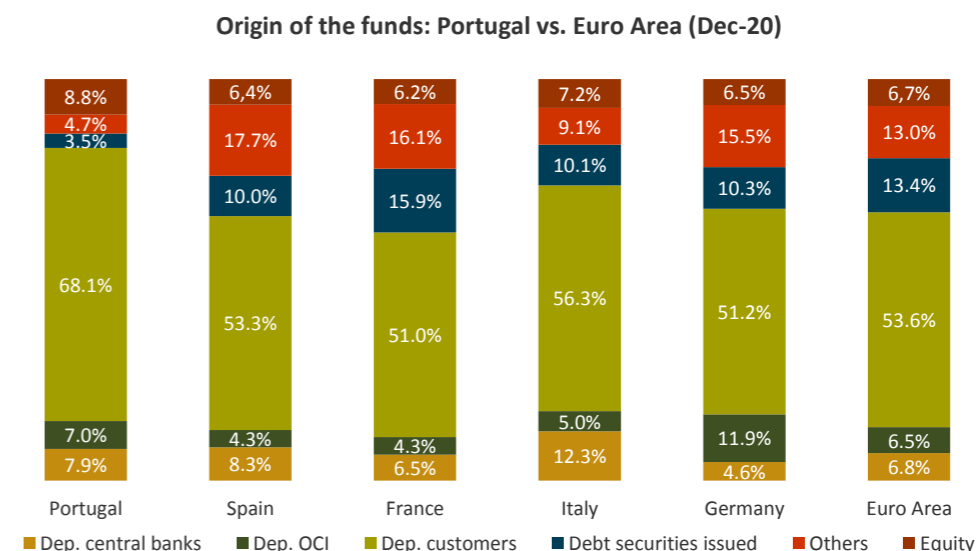
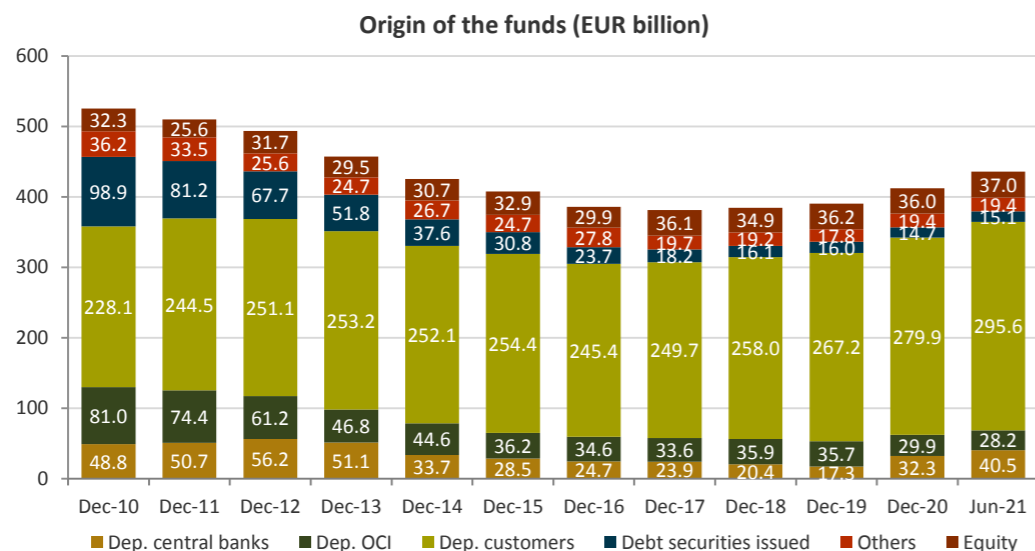
New business lending to households - Consumption (accumulated amounts, EUR million)



Source: Banco de Portugal (Monetary and Financial Statistics). Adjusted ARC = Annual rate of change (ARC) adjusted for securitisation and liquidity-providing operations.

III. ORIGIN OF THE FUNDS AND LIQUIDITY

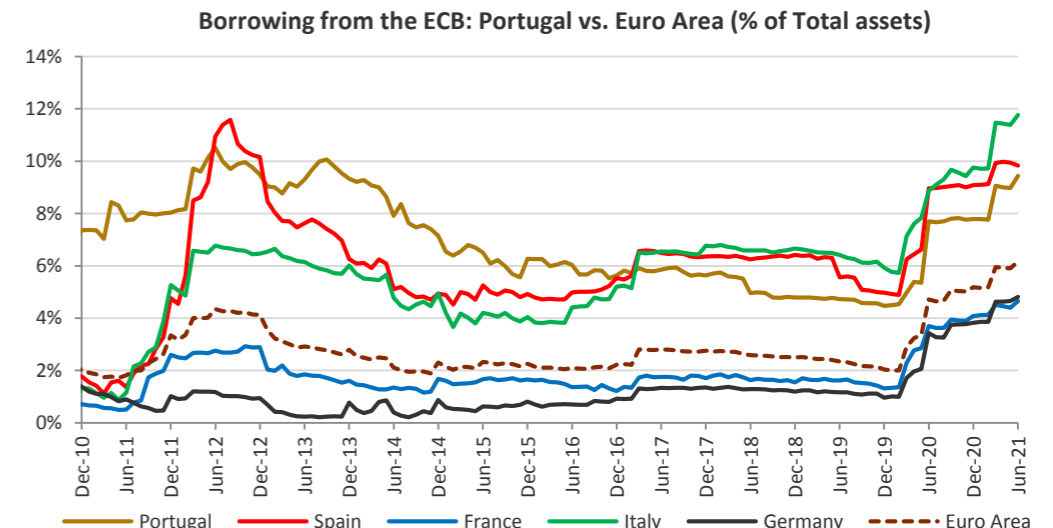
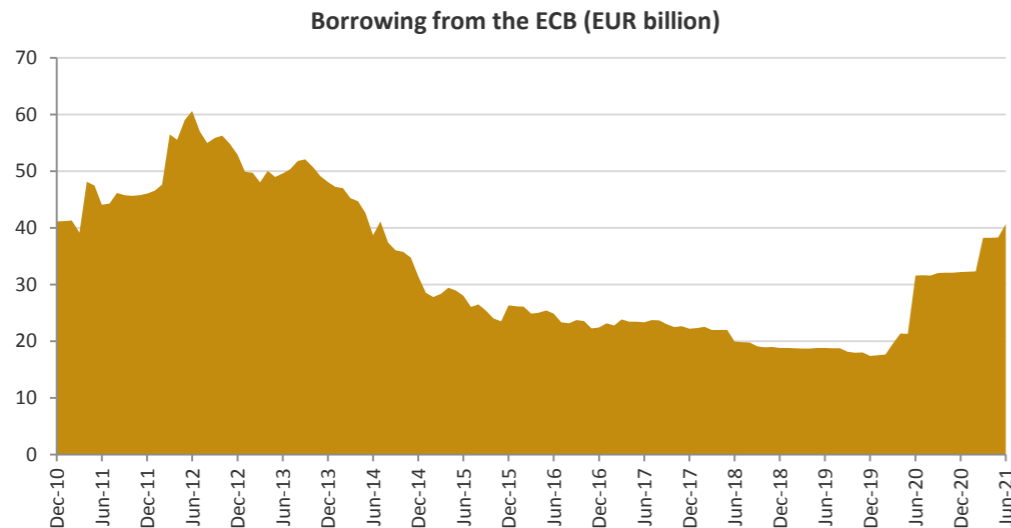
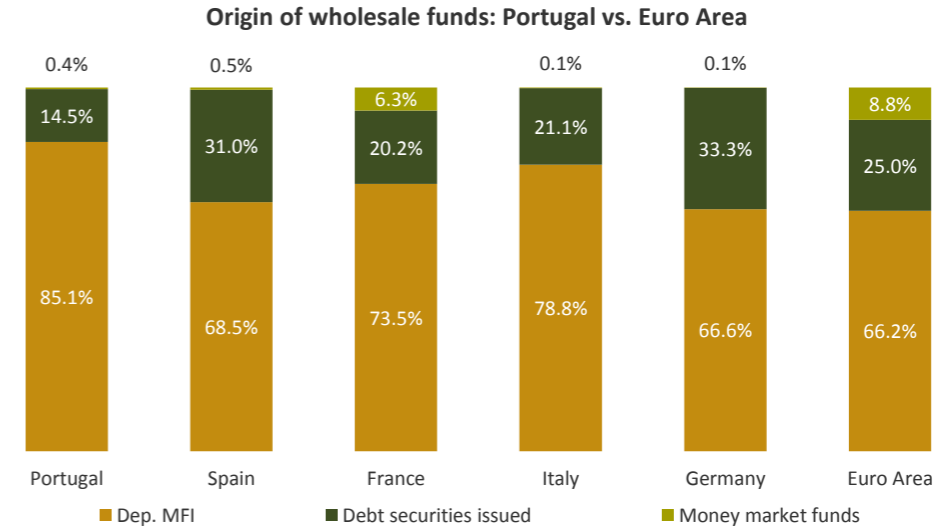
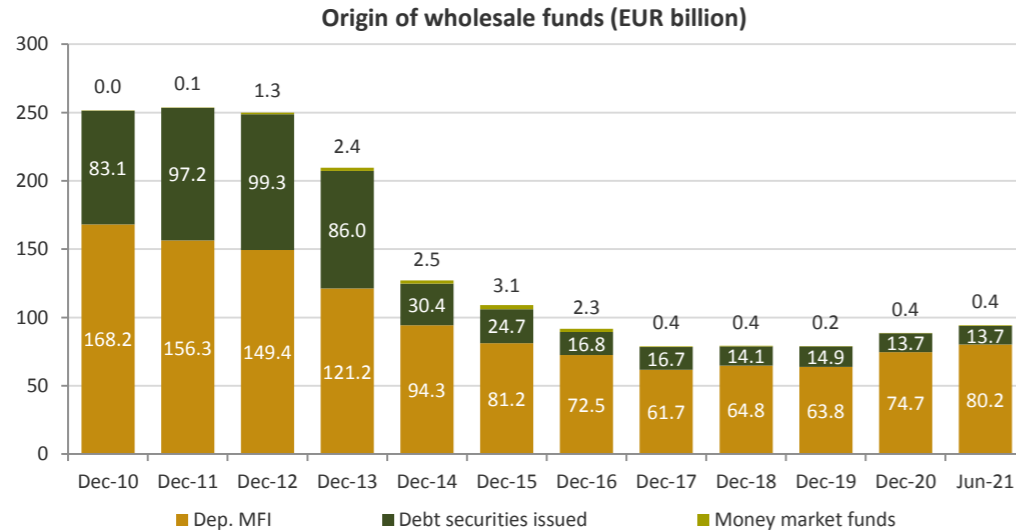
Due to the high level of savings, customer deposits continued to increase significantly in the first half of 2021. In a very low interest rates environment, due to the ECB's accommodative monetary policy, there has been a decrease in the weight of term deposits and an increase in the weight of overnight deposits.



Source: Banco de Portugal (consolidated data and Monetary and Financial Statistics) and ECB – Consolidated Banking Data (consolidated data reported in FINREP format) and MFI Balance Sheet Items (Monetary and Financial Statistics). OCI = Other Credit Institutions. Households' deposits include emigrants. Deposits from the non-monetary sector (end-of-period balances).

III. ORIGIN OF THE FUNDS AND LIQUIDITY

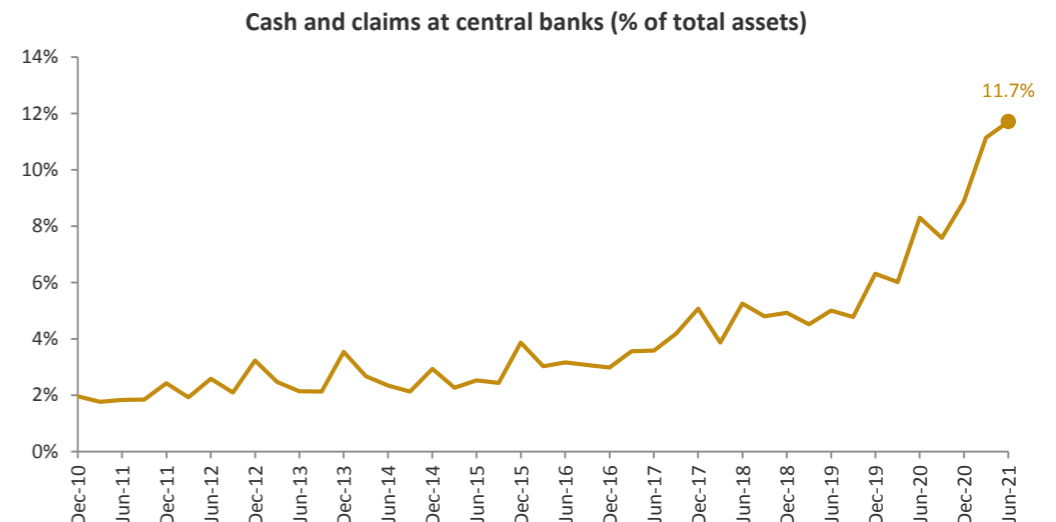
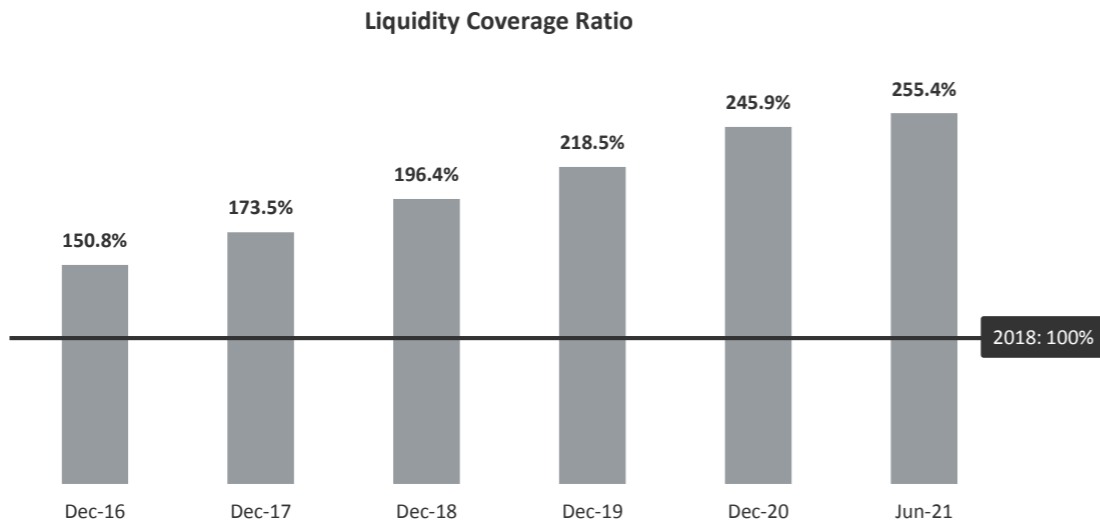
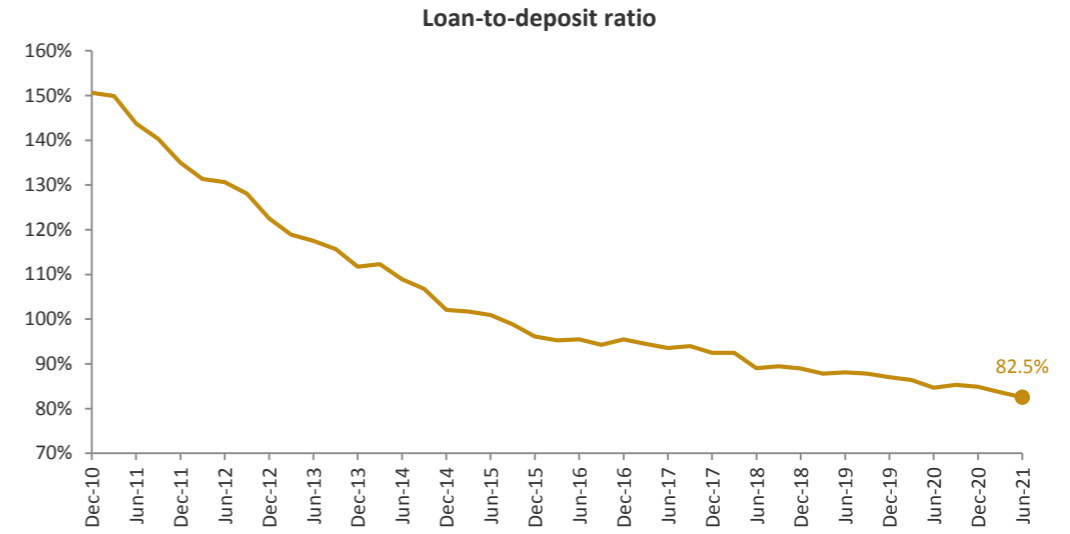
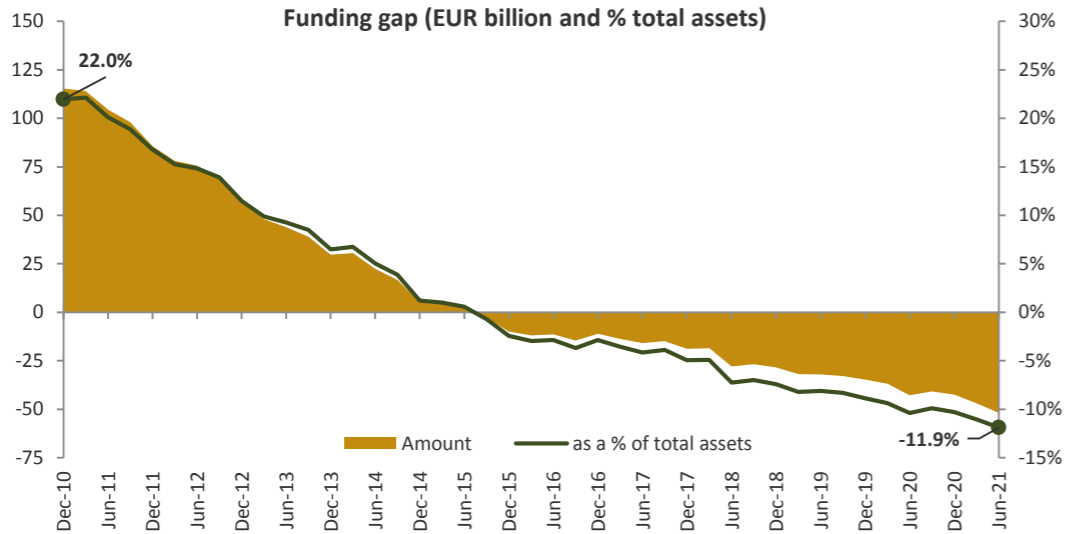
Recourse to wholesale funding has been decreasing its weight and currently is not very significant in the funding of the Portuguese banking sector. In turn, funding from the Eurosystem increased 1.5 pp vis-à-vis 2020, representing 9.3% of total assets, due to the attractive monetary policy measures that have been significantly strengthened in the current pandemic context.



Source: ECB – MFI Balance Sheet Items (Monetary and Financial Statistics). Monetary Financial Institutions (MFI) include the Central Bank and Other Monetary and Financial Institutions (OMFI).

III. ORIGIN OF THE FUNDS AND LIQUIDITY

Liquidity indicators have registered a very positive evolution. This extremely comfortable position of the Portuguese banking system in terms of liquidity has allowed it to play an essential role in mitigating the impacts of the COVID-19 crisis on companies and families.

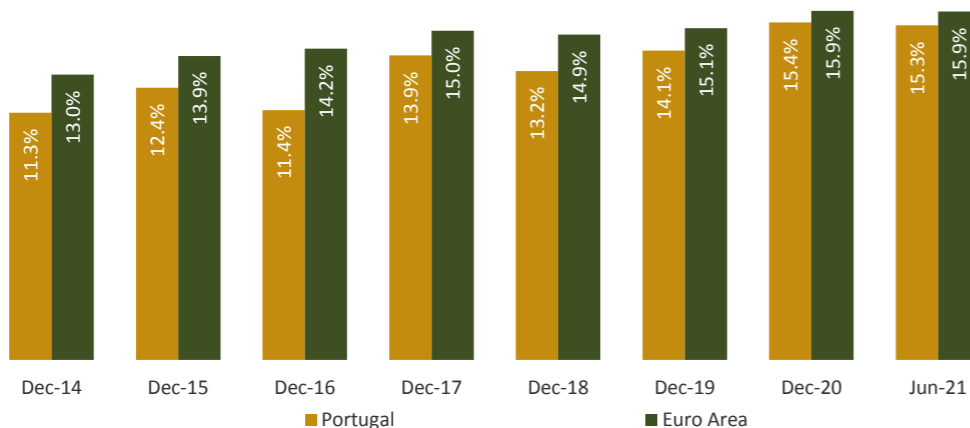


Source: Banco de Portugal (consolidated data).

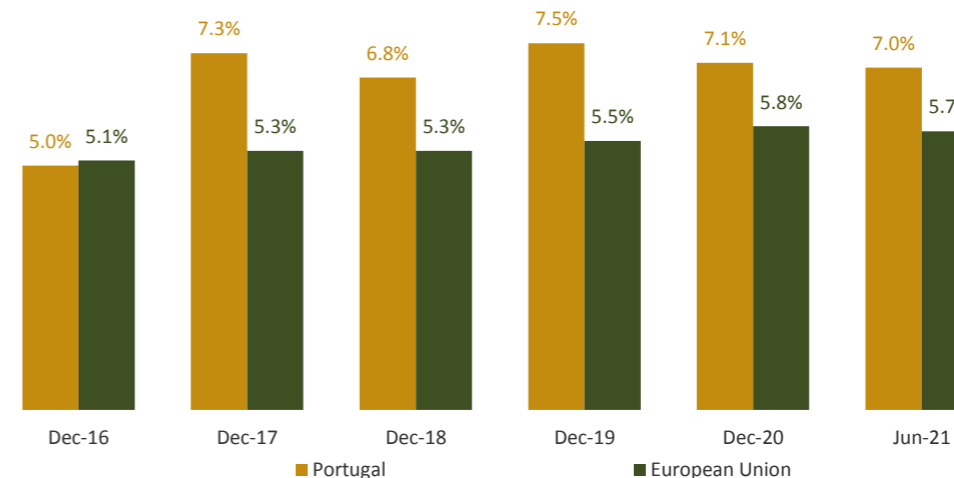
IV. SOLVENCY

In the last years, solvency has been improving, reflecting the reinforcement of own funds, with the CET1 ratio reaching 15,3% by the end of the first half of 2021. The leverage ratio is considerably higher than the EU average and the minimum reference (3%). Together with the favourable liquidity position, the system's solvency levels allow it to respond effectively to the economy's financing needs in the current context and accommodate a possible deterioration in credit risk and an increase in NPL.

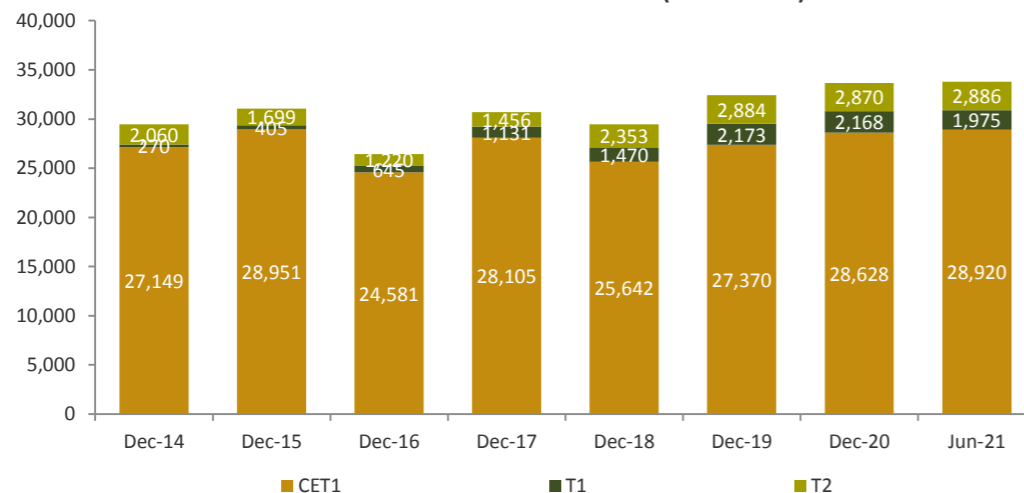
Common Equity Tier 1 (CET1) ratio



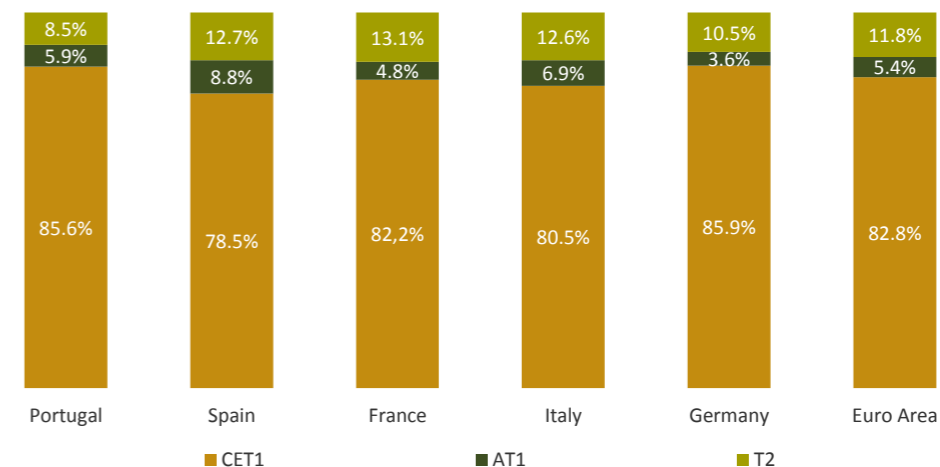
Leverage ratio



Evolution a structure of own funds (EUR million)



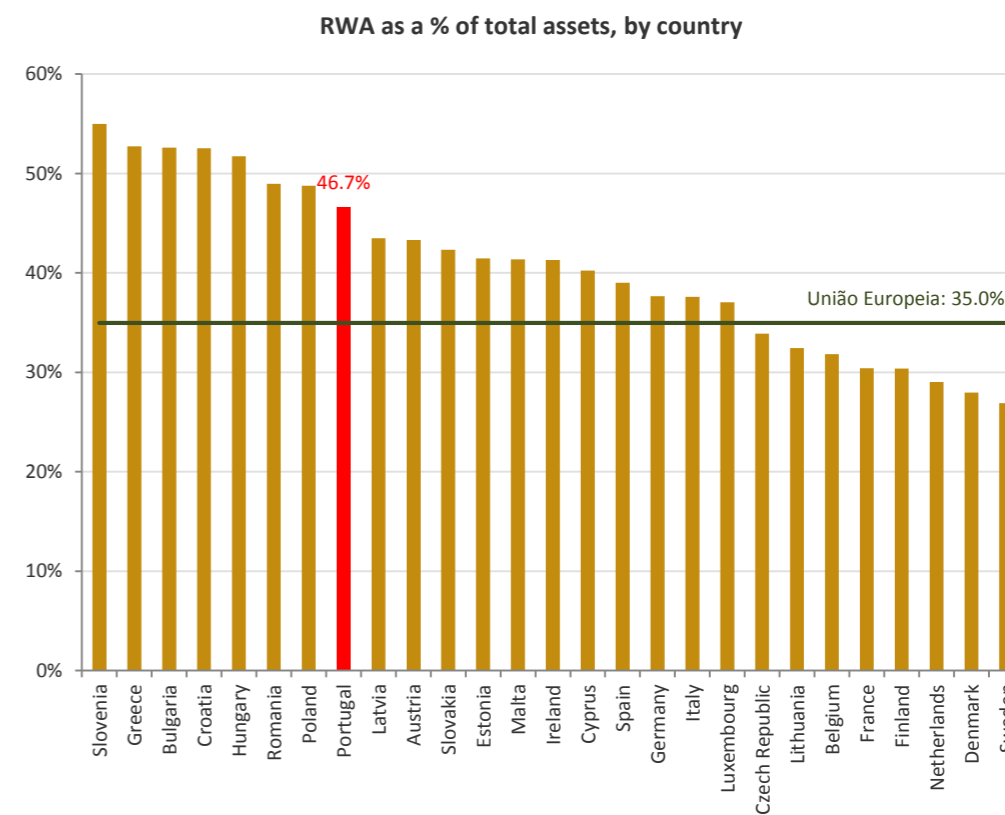
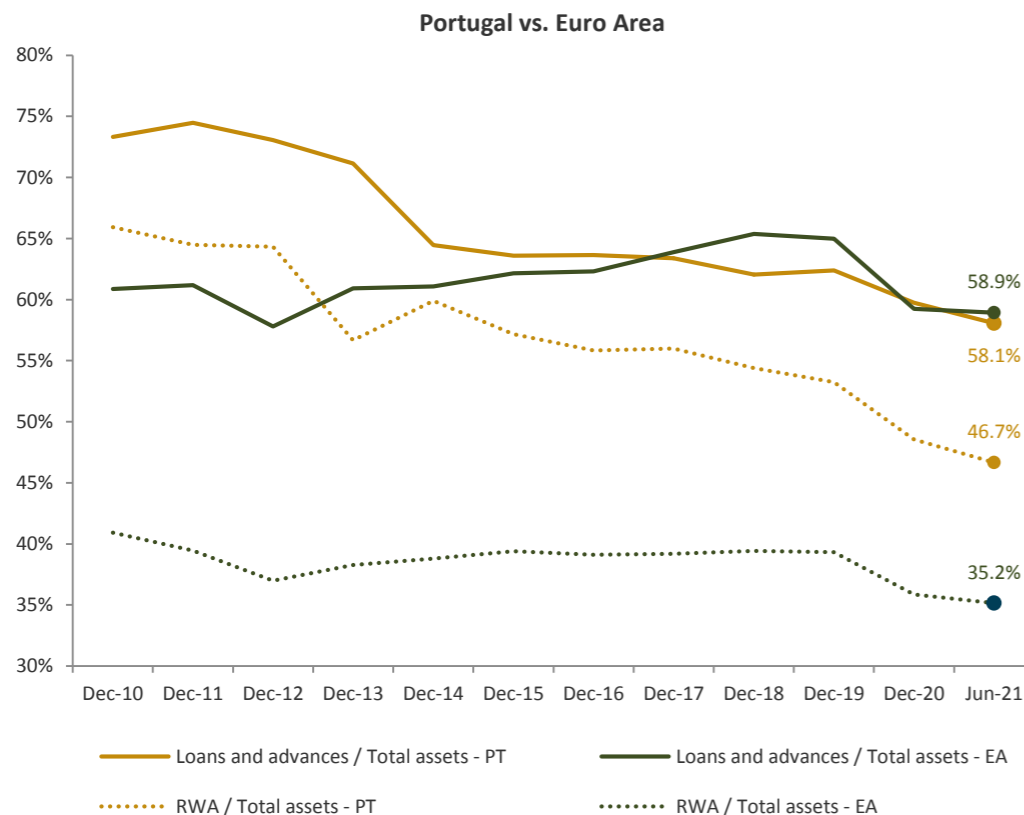
Structure of own funds: Portugal vs. Euro Area



Source: ECB – Consolidated Banking Data and EBA – Risk Dashboard (leverage ratio – fully phased-in definition of Tier 1).

IV. SOLVENCY

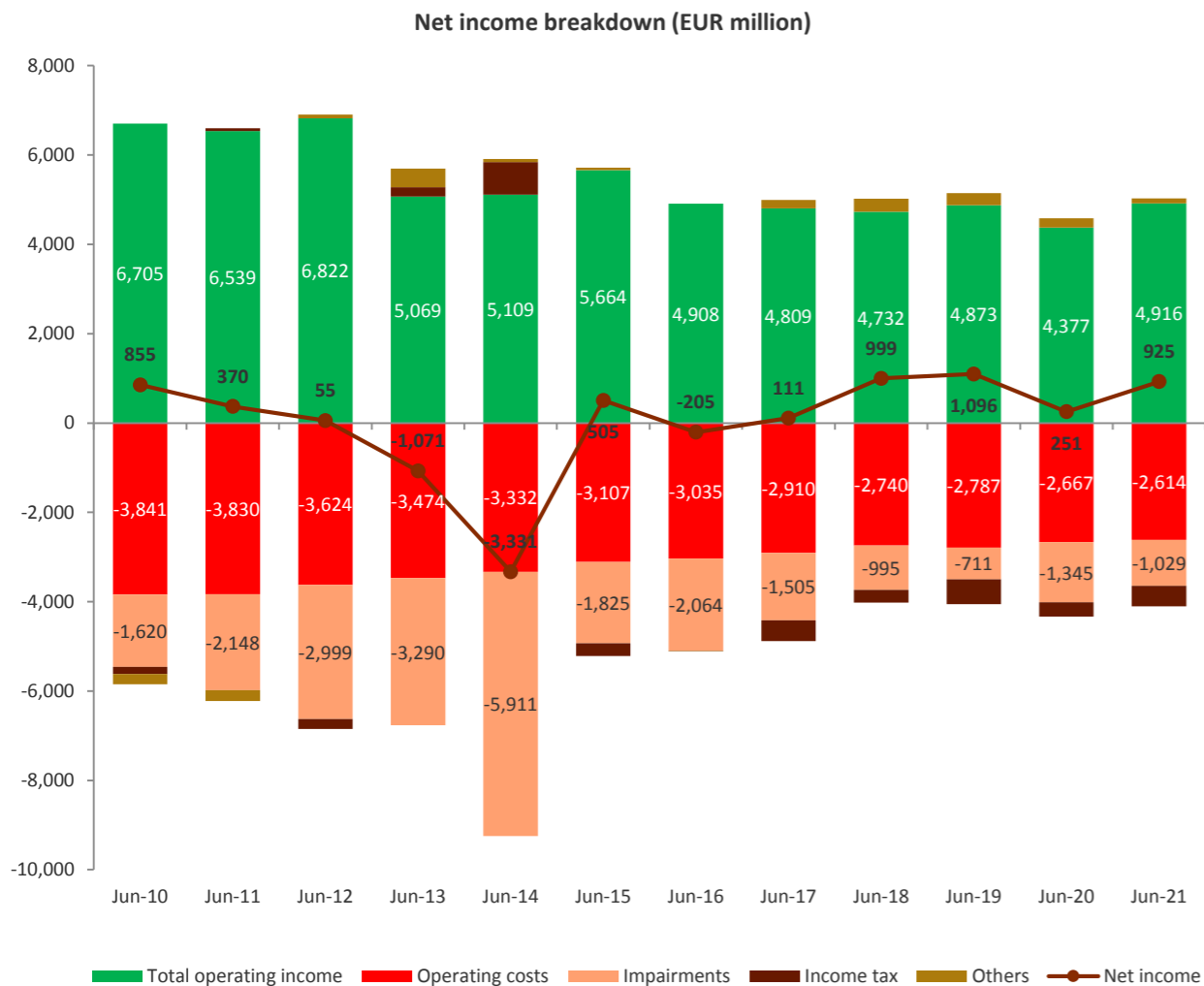
The lower use of internal models for calculation of capital requirements, together with a higher level of defaults and losses from a historical perspective, justifies that the ratio of risk-weighted assets (RWA) per unit of assets for the Portuguese sector continues to compare unfavourably to the European Union, despite the reduction experienced in the last years. This implies a higher level of capital requirements for the majority of Portuguese banks than for the majority of European Union banks.



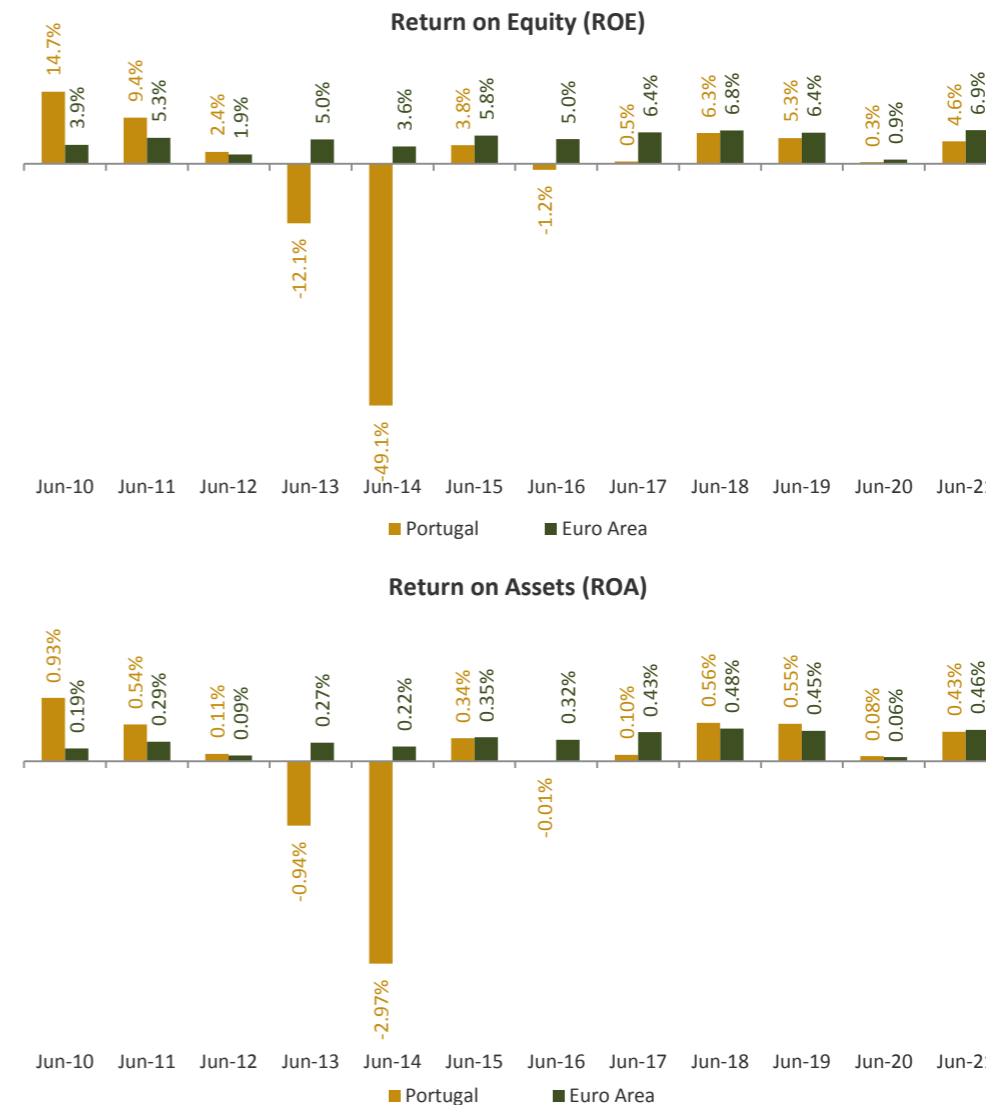
Source: ECB – Consolidated Banking Data.

V. PROFITABILITY

In the first half of 2021, the profitability of the banking system increased significantly on a year-on-year basis, mostly due to an increase in total operating income and a decrease in the flow of provisions and impairments, as a result of lower restrictions related to the pandemic crisis and the economic recovery. However, profitability remains one of the biggest challenges facing the sector.



Source: Banco de Portugal (consolidated data).

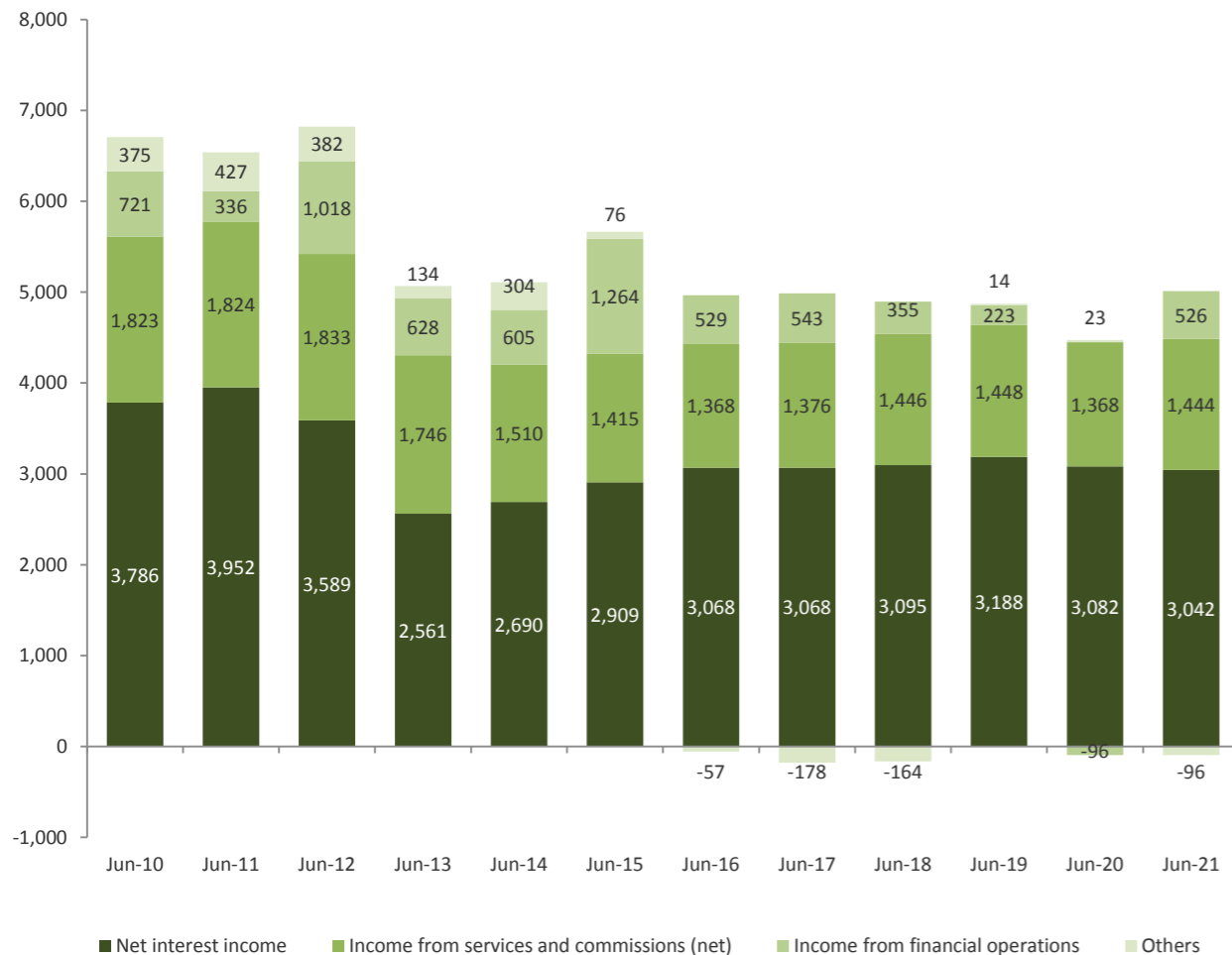


Source: ECB – Consolidated Banking Data. Calculated based on net income after tax and before minority interests and on end-of-period equity and total assets. Return on Equity excludes branches of foreign banks. Annualised values.

V. PROFITABILITY

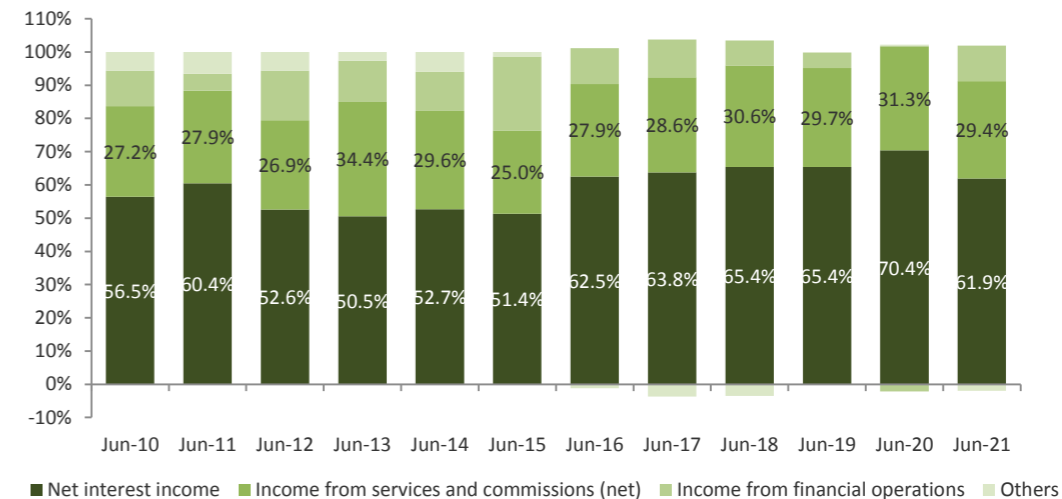
The positive evolution in total operating income was explained mainly by the increase in income from financial operations.

Total operating income breakdown (EUR million)

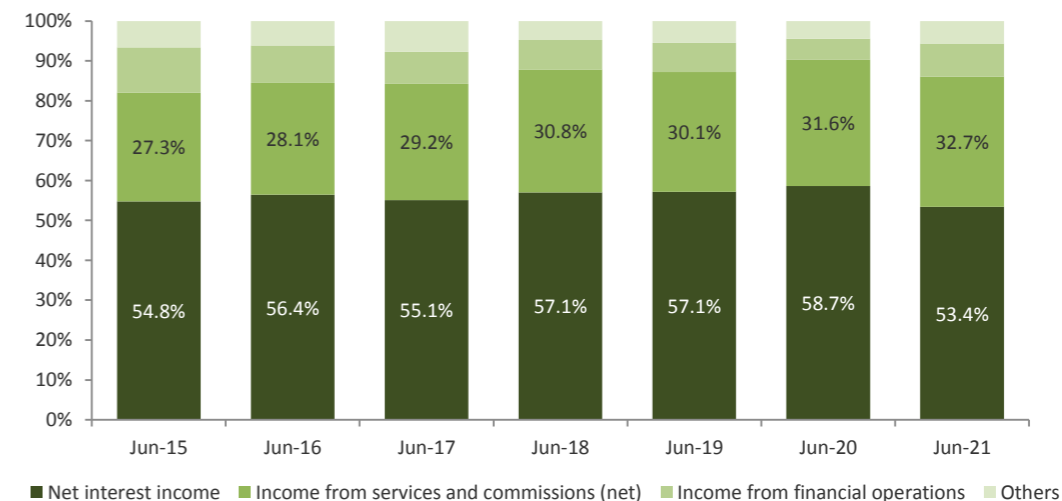


Source: Banco de Portugal (consolidated data).

Total operating income breakdown (Portugal)



Total operating income breakdown (Euro Area)

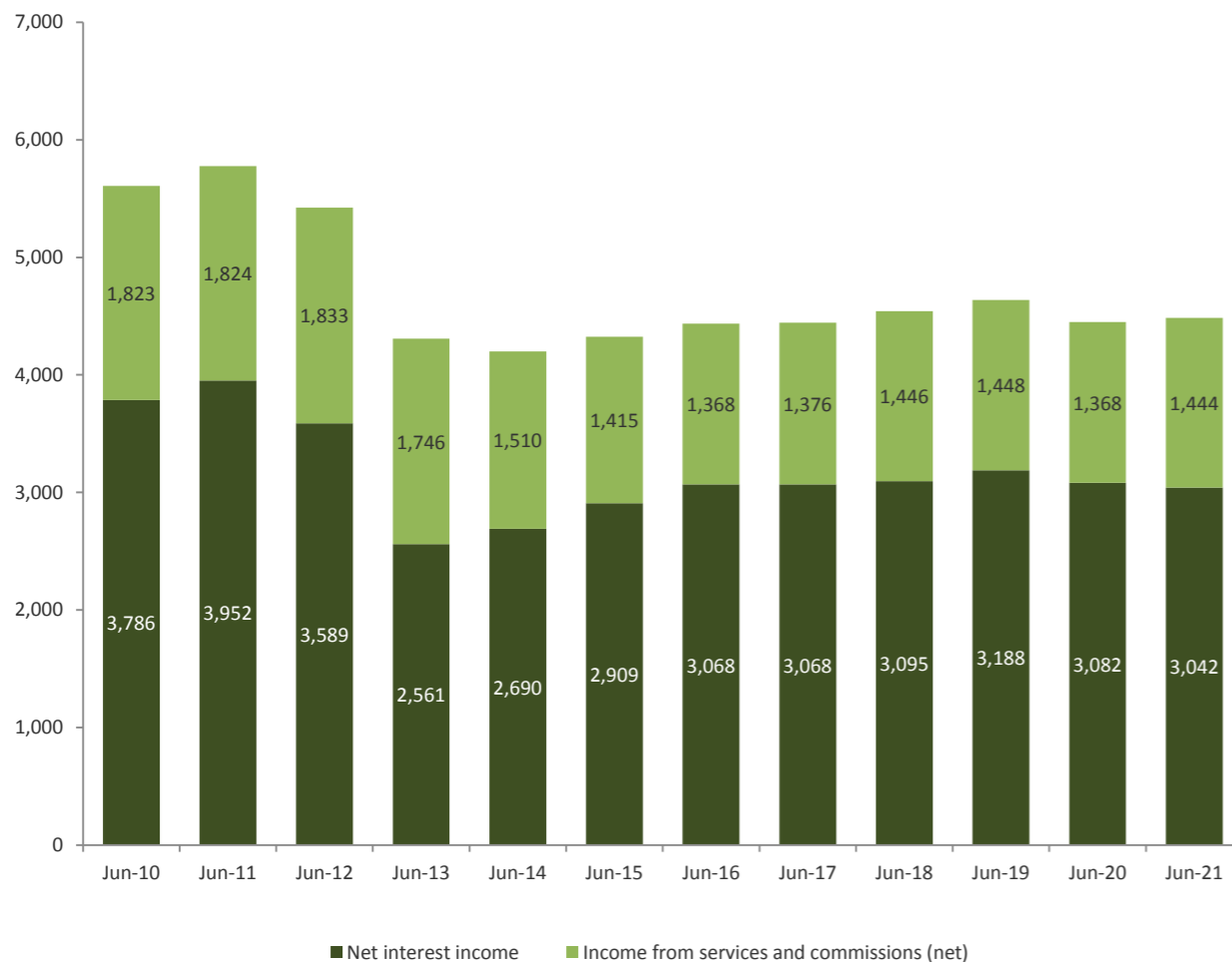


Source: Banco de Portugal (consolidated data) and ECB – Consolidated Banking Data (Euro Area). Total operating income breakdown starting only on Jun-15 due to unavailability of older data on Commissions and Income from financial operations for the Euro Area. Annualised values.

V. PROFITABILITY

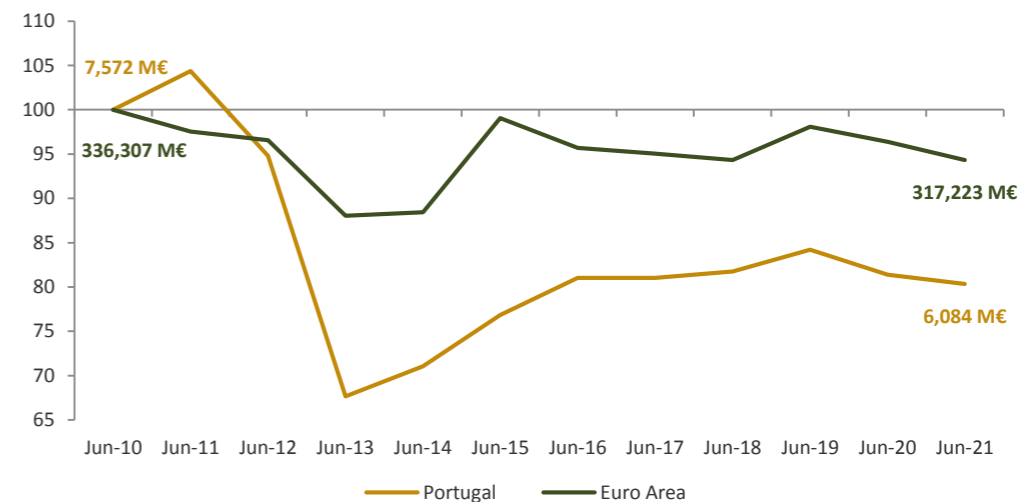
The decrease in net interest income, compared to the first half of 2020, was due to a decrease in interest received, which was greater than the decrease in interest paid. However, this decline was mitigated by the reduction in the cost of funding from central banks (net of cash and investments). Concerning net fee and commission income, the recovery of economic activity and the consequent increase in transactions led to an increase in this item, which recovered to pre-pandemic levels.

Net interest income and Commissions (EUR million)

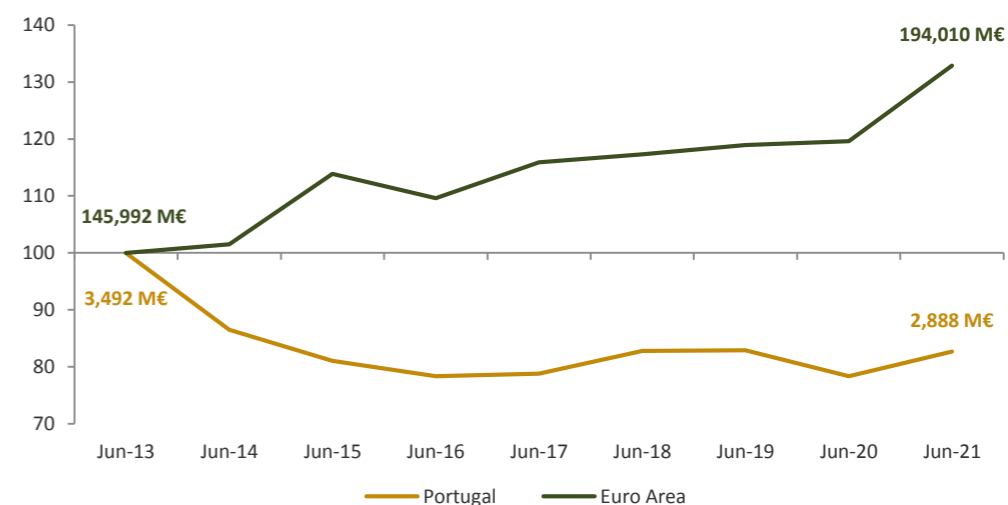


Source: Banco de Portugal (consolidated data).

Net interest income (Jun-10 = 100)



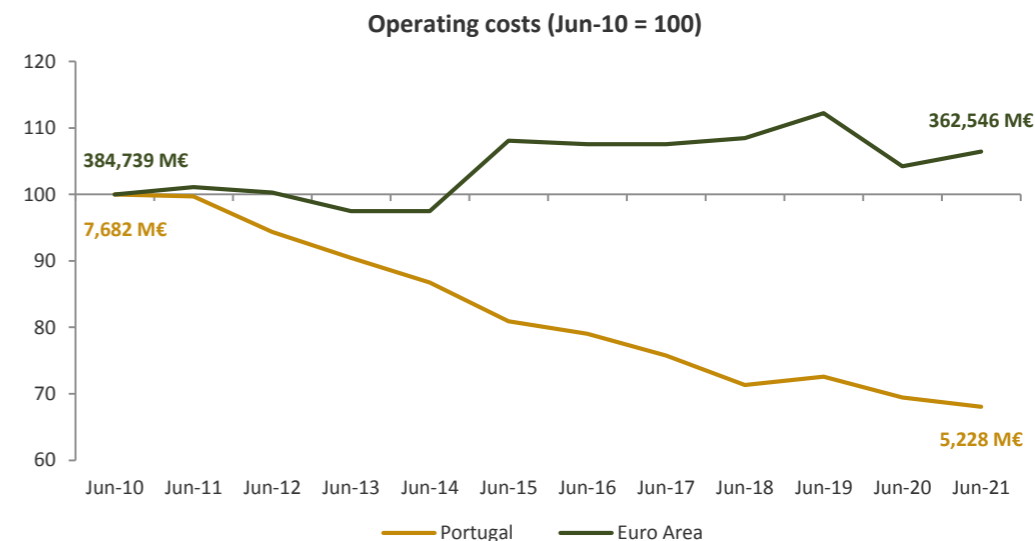
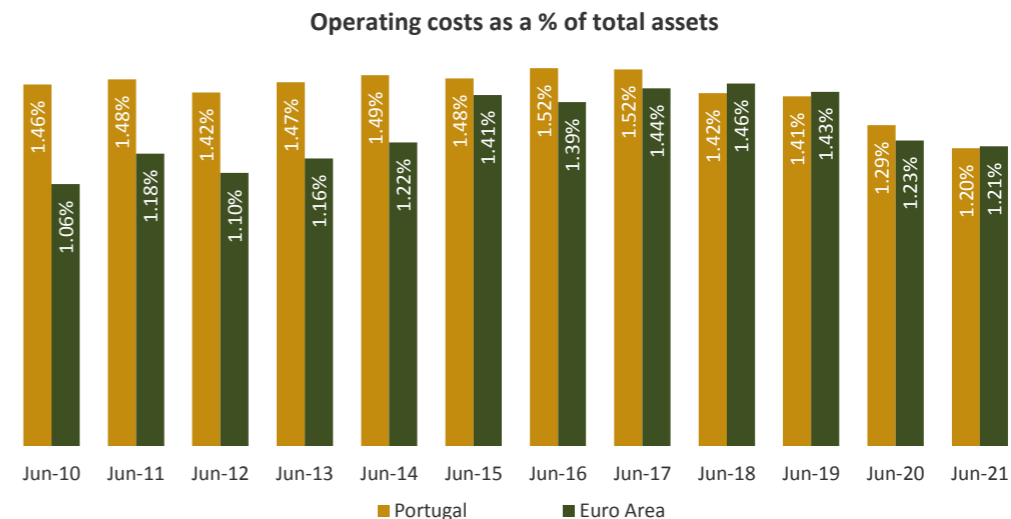
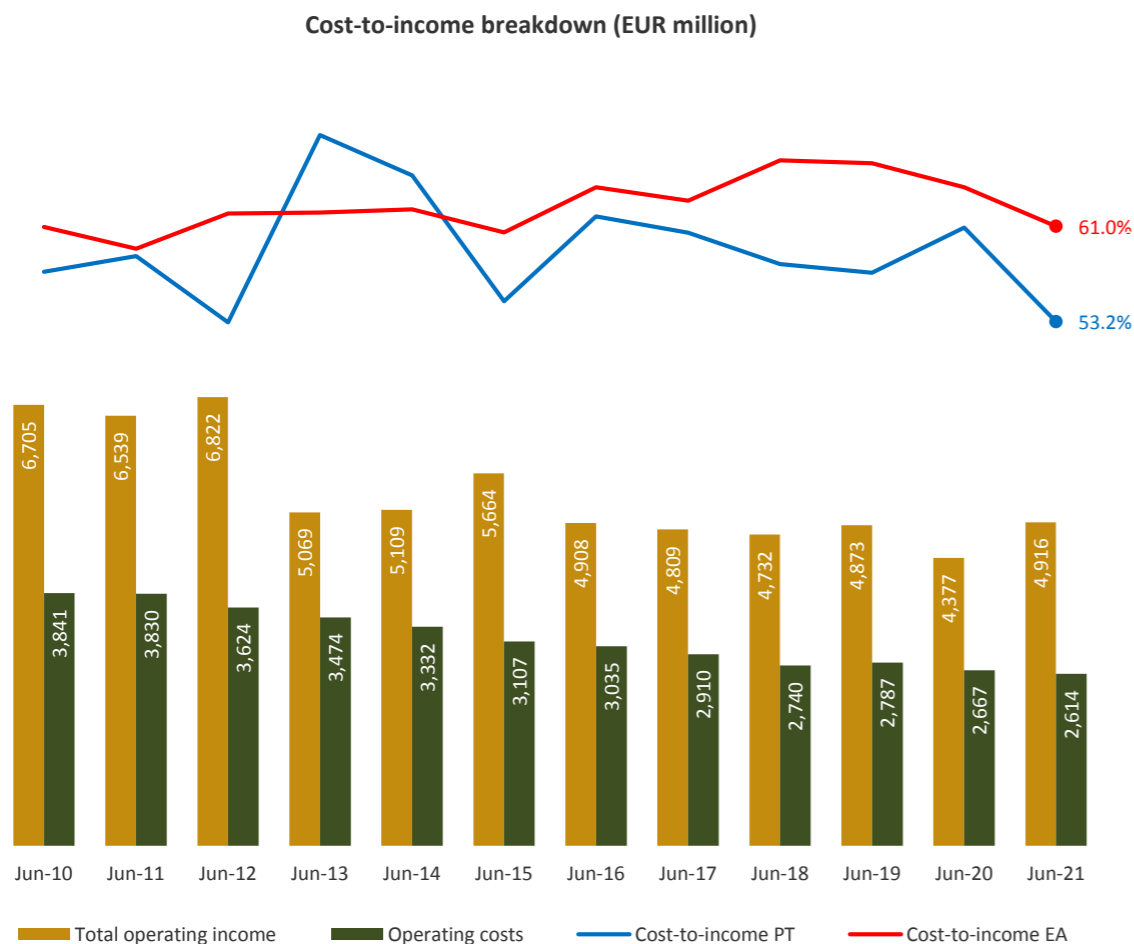
Income from services and commissions (Jun-13 = 100)



Source: Banco de Portugal (consolidated data) and ECB – Consolidated Banking Data (Euro Area). Data on Commissions starting only on Jun-13 due to unavailability of older data for the Euro Area. Annualised values.

V. PROFITABILITY

In the first half of 2021, the decrease in operating costs and the increase in total operating income resulted in an improvement in the efficiency of the banking sector.

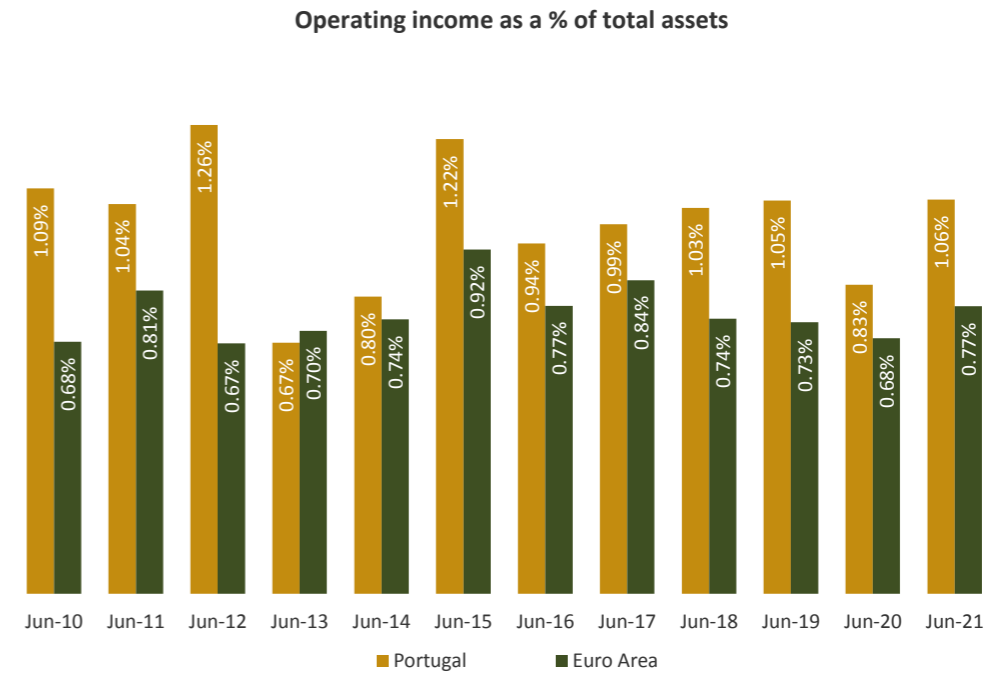
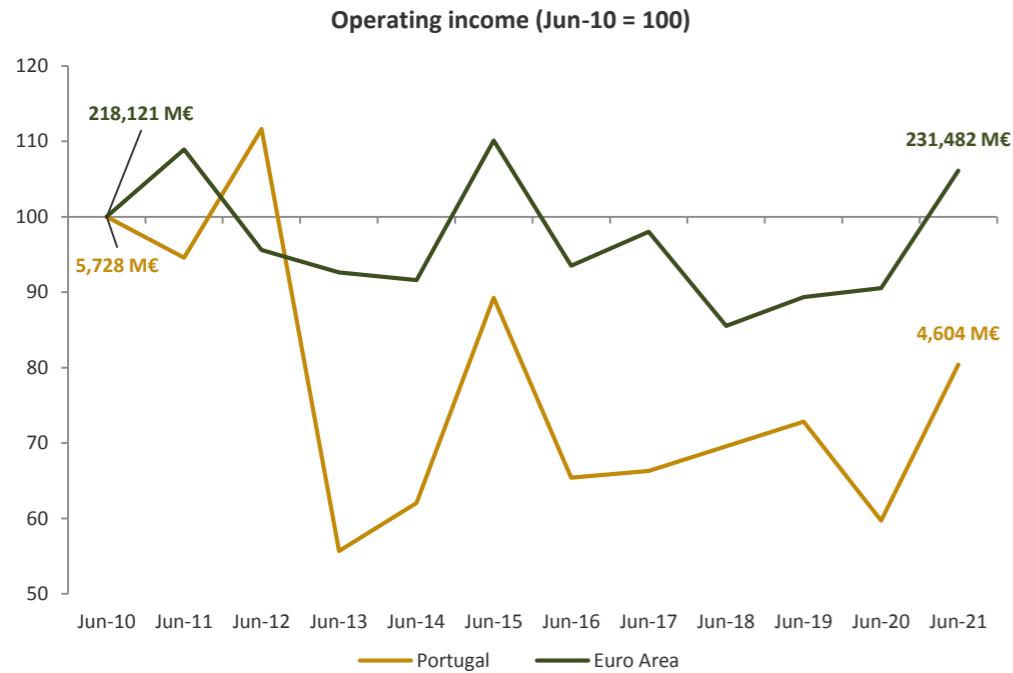


Source: Banco de Portugal (consolidated data) and ECB – Consolidated Banking Data (Euro Area).

Source: Banco de Portugal (consolidated data) and ECB – Consolidated Banking Data (Euro Area). Annualised values.

V. PROFITABILITY

The improvement in the operating result was due to an increase in total operating income and a decrease in operating costs. The decline in the cost of credit risk reflects the significant decrease in net provisions and impairments when compared to the strong reinforcement that occurred in 2020, which is explained by improving prospects of economic recovery.



Source: Banco de Portugal (consolidated data) and ECB – Consolidated Banking Data (Euro Area).

Cost of credit risk				
	Jun-18	Jun-19	Jun-20	Jun-21
Portugal	0.72%	0.75%	1.09%	0.66%
EU	0.48%	0.47%	0.86%	0.51%

Source: EBA – Risk Dashboard.

- The information provided by Banco de Portugal and the ECB regarding monetary statistics differ from that provided in the context of consolidated data of the banking system. The main differences derive fundamentally from non-coincidence in the universes surveyed and from different consolidation procedures. This information is available on the Banco de Portugal and the ECB websites. Among others, the following documents may be consulted: Suplemento ao Boletim Estatístico n.º1/2001, de agosto; Instrução n.º 25/2014, de 15 de dezembro, e Sistema Bancário Português: desenvolvimentos recentes – 4.º trimestre de 2016.
- This document was published with updated information as of 3 December 2021.

PORTUGUESE BANKING SECTOR OVERVIEW