



BANCO DE PORTUGAL
EUROSISTEMA

Portuguese Banking System

Recent Developments

Updated: 2Q 2014

Prepared with data available up to 16 September 2014



- Portuguese Banking System at a Glance
- Recent Financial Stability Measures
- Macroeconomic and Financial Indicators
- Portuguese Banking System
 - Balance Sheet
 - Liquidity & Funding
 - Asset Quality
 - Profitability
 - Solvency



- I. Balance Sheet
 - The reduction in credit portfolio was the main contribution to the decrease in assets
- II. Liquidity & Funding
 - The loan-to-deposits ratio decreased
 - The recourse to the Eurosystem decreased considerably
- III. Asset/Credit Quality
 - The credit at risk ratio increased, despite the slowdown in the flow of new overdue and other doubtful loans
- IV. Profitability
 - Excluding BES, the banking system profitability was positive, although at a low level
 - The flow of credit impairments decreased but remains high
- V. Solvency
 - Solvency levels remained broadly robust in most Portuguese banks. Excluding BES, there was a slight increase in average solvency ratios.

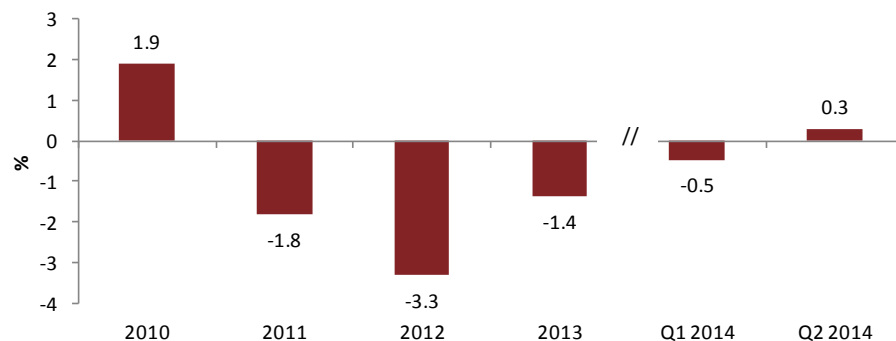
Note: The data for the banking system include the institution ESFG until March 2014 and BES, on a consolidated basis, for June 2014, which results from the change in the entity subject to supervision by Banco de Portugal. This event, together with the substantial impairments that motivated the adoption of the resolution measure by Banco de Portugal in the 3rd of August, has a non-negligible impact on banking system aggregate numbers. For this reason, whenever relevant, it is presented, for the benefit of the analysis, the evolution of indicators excluding the group's relevant institution (ESFG until March 2014 and BES, on a consolidated basis, for June) from the aggregate, referred in the text as "excluding BES".



Topic	Institution	Latest measures (Q2 2014)
Liquidity	ECB	<p>On 5 June 2014 the Governing Council of the ECB decided to adopt further non-standard measures, notably:</p> <ul style="list-style-type: none">▪ To conduct a series of targeted longer-term refinancing operations (TLTROs) maturing in September with an interest rate fixed over the life of each operation at the rate on the Eurosystem's main refinancing operations prevailing at the time of take-up, plus a fixed spread of 10 basis points;▪ To continue conducting the Eurosystem's main and three-month longer-term refinancing operations as fixed rate tender procedures with full allotment for as long as necessary, and at least until the end of the Eurosystem's reserve maintenance period ending in December 2016;▪ To discontinue the Eurosystem's special-term refinancing operations with a maturity of one maintenance period, following the operation to be allotted on 10 June 2014;▪ To suspend the weekly fine-tuning operation sterilising the liquidity injected under the Securities Markets Programme, following the operation to be allotted on 10 June 2014;▪ To extend the existing eligibility of additional assets as collateral, notably under the additional credit claims framework, at least until September 2018, in order to ensure sufficient collateral is available for banks to participate in TLTROs.
		<p>On 5 June 2014, when deciding to lower the key ECB interest rates, the Governing Council of the ECB decided to adopt a negative deposit facility interest rate of -0.10%, that also applies to average reserve holdings in excess of the minimum reserve requirements and other deposits held with the Eurosystem.</p> <p>This decision materialized in the adoption of the Decision ECB/2014/23, of June 5, 2014, which comes into effect on 11 June 2014, together with the changes to the key ECB interest rates.</p>
Legal framework	Banco de Portugal	<p>Publication of Notice No 2/2014 which amends Notice No 9/2012 on the information requirements in the field of money laundering and terrorist financing risk management, to be periodically reported to Banco de Portugal by entities subject to its supervision or providing financial services related to matters under its supervision.</p>



GDP growth rate - Volume

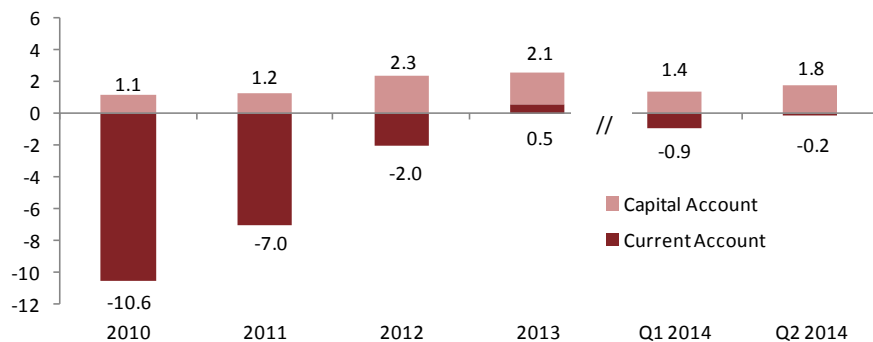


Note: Quarterly figures correspond to q-on-q rates of change.

The series presented is based on the level of GDP calculated in accordance with the new European System of Accounts - ESA 2010. In the remaining series, in which GDP appears as the denominator, the basis remains SEC 1995 for consistency with the basis of the numerators (current and capital account, public debt, fiscal deficit, national financial accounts). These variables that were not reviewed yet by the competent authorities, according to the ESA 2010.

Chart 1

Current account and capital account, %GDP



Note: Quarterly figures are seasonally adjusted.

Chart 2

■ In the second quarter of 2014, GDP recorded a positive quarter-on-quarter rate of change, following a negative change in the first quarter of the year.

■ The current and capital account remained in surplus, at a higher level than the observed in the preceding quarter, while a small deficit was recorded in the current account.



Unemployment rate, % of active population - Average value of period

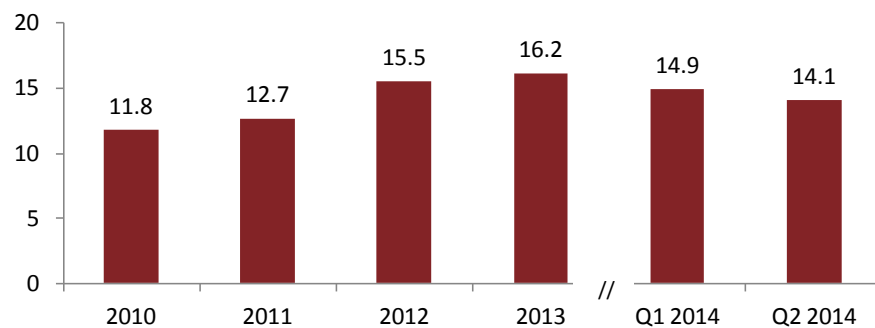


Chart 3

Fiscal deficit, % GDP

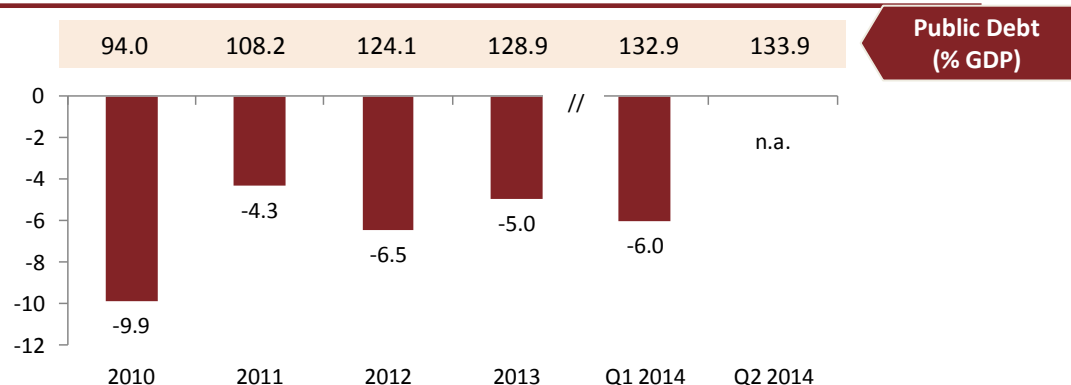


Chart 4

■ In the second quarter of 2014 the unemployment rate kept the downward trend observed since the second quarter of 2013, remaining, nonetheless, at high levels.

■ The fiscal deficit stood at 6% in the first quarter of 2014, which compares to the 10% figure recorded in the first quarter of 2013. The ratio between public debt and GDP slightly increased.



Net lending/borrowing of non-financial corporations, % GDP

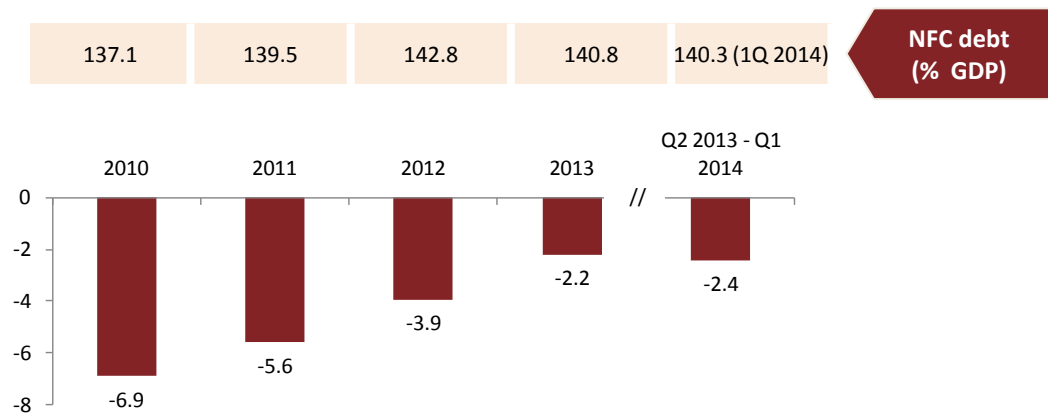


Chart 5

Net lending/borrowing of households, % GDP

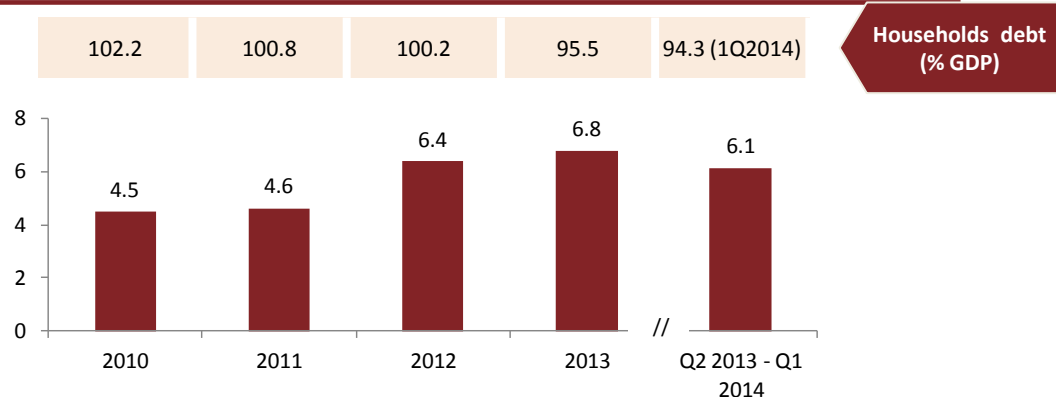


Chart 6

■ Financing needs of non-financial corporations increased slightly in the first quarter of 2014. The indebtedness level decreased slightly, remaining at high levels.

■ Households' financing capacity remained significantly positive in the first quarter of 2014. The households' indebtedness level continued to decline.



Sovereign debt yields 10 Y

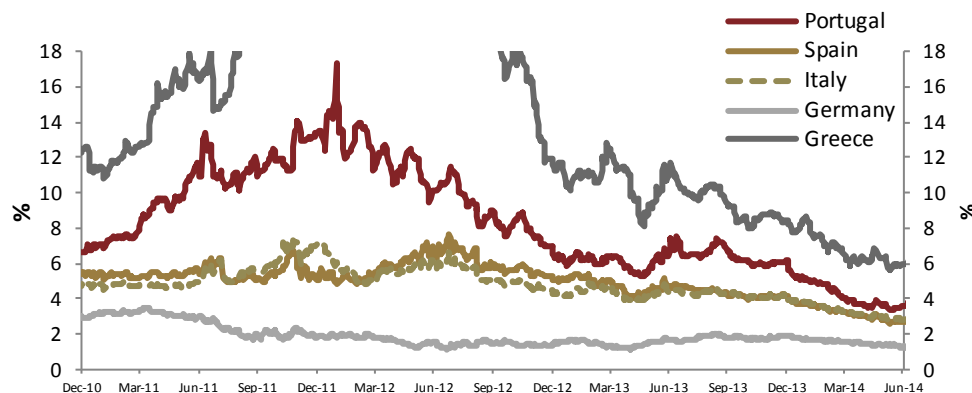


Chart 7

Euribor and ECB main refinancing rate

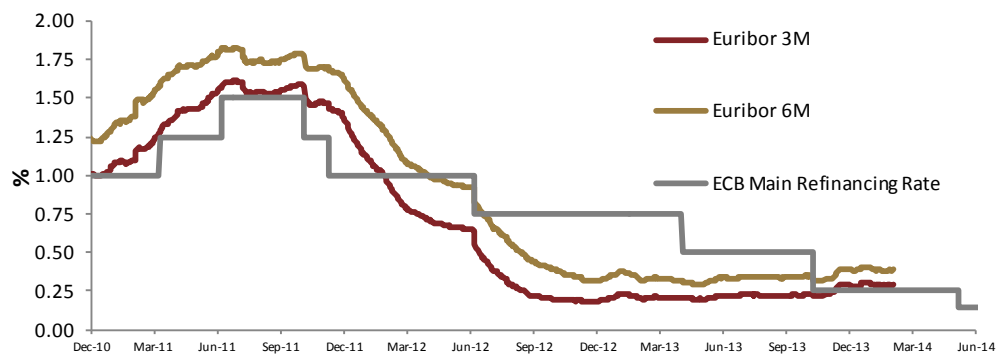


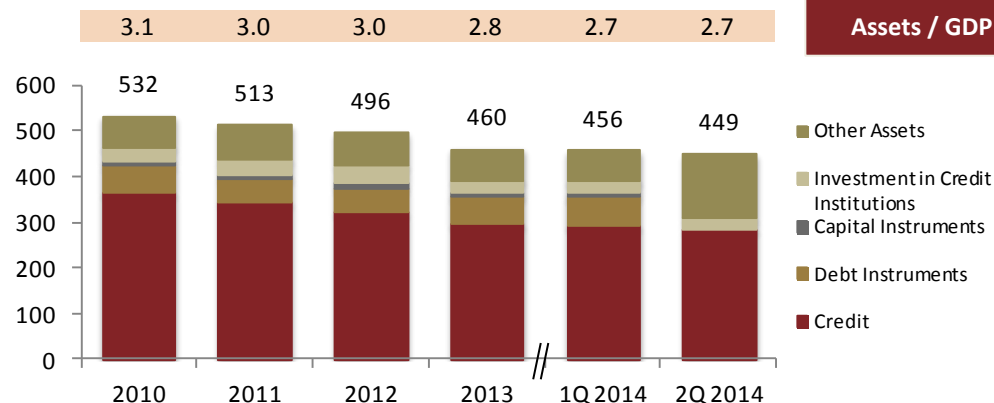
Chart 8

■ The Portuguese sovereign yields kept decreasing in the course of the first semester of 2014, narrowing the spread vis-à-vis comparable German debt.

■ The ECB decreased the rate on main refinancing operations by 10 basis points in the beginning of June to 0.15 per cent, along with a decrease in the rate on the deposit facility of the same magnitude to a negative rate (-0.10 per cent).



Assets (€Bn) - Value at end of period



Note: Data reported by BES, with reference to June 2014, do not allow the usual breakdown of total assets by major accounting headings.

Chart 9

Bank financing structure (€Bn) - Value at end of period

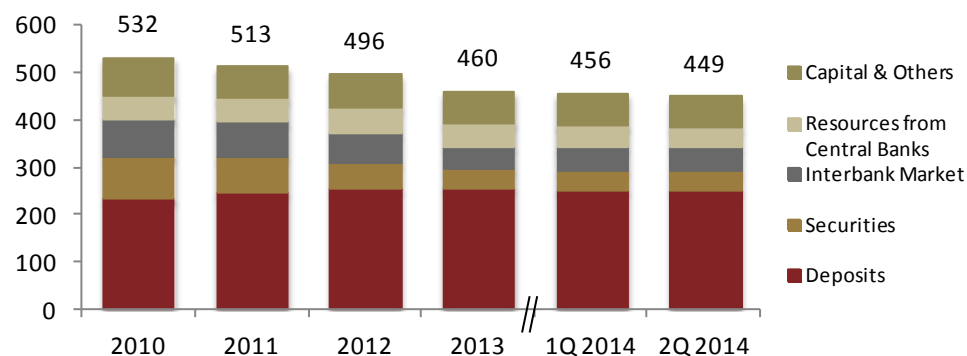


Chart 10

■ Total assets of the Portuguese banking system reduced further in the second quarter of 2014, continuing the downward trajectory observed since the end of 2010. Excluding BES, total assets decreased about 0.7%.

■ The reduction in credit to customers and the reduction in investments in credit institutions were the main drivers of this evolution.

■ Regarding the financing structure, a considerable decrease in the recourse to the Eurosystem was observed. Customers' deposits recorded a slight increase.



Central Banks Financing (€Bn) - Value at end of period

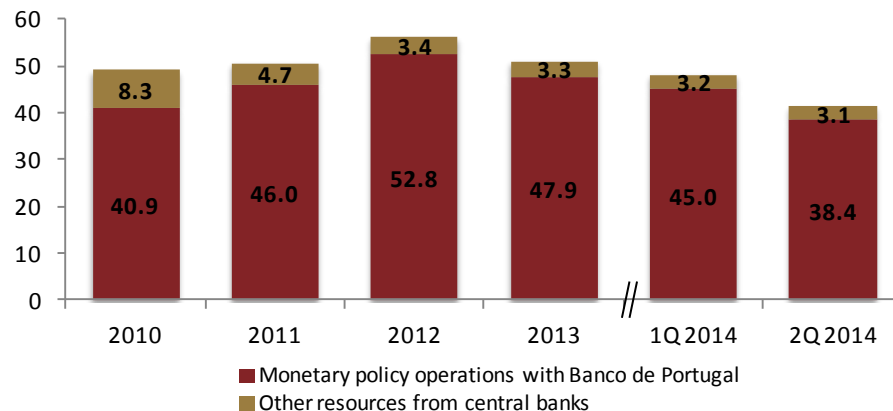


Chart 11

Loan-To-Deposits ratio (%) - Value at end of period

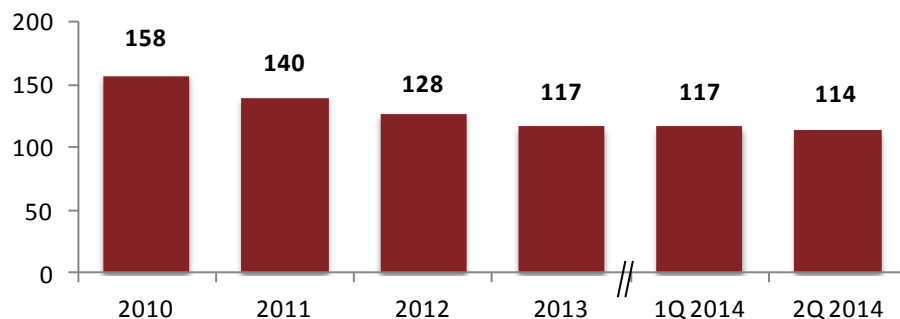


Chart 12

■ In the second quarter of 2014, Central Banks' financing, most through the recourse to the Eurosystem, decreased to minimum levels since the beginning of the Economic and Financial Assistance Programme.

■ The loan-to-deposits ratio resumed the downward trend: roughly 2/3 due to the reduction in the credit portfolio and 1/3 attributable to the increase in customers' deposits.



Commercial gap (€Bn) - Value at end of period

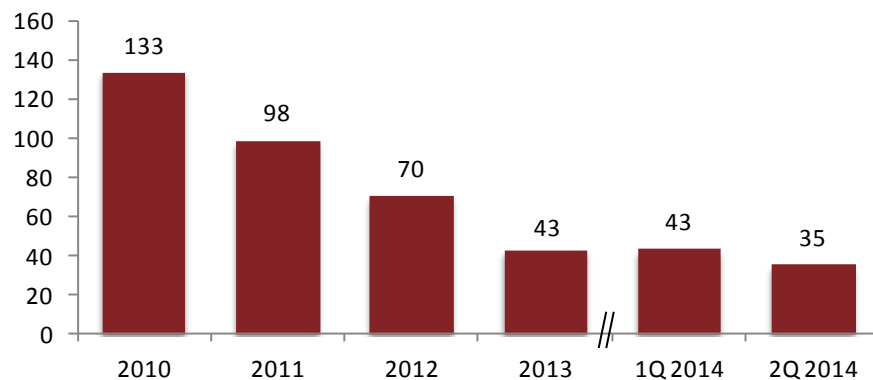


Chart 13

Liquidity gap in cumulative maturity ladders (% stable assets) - Value at end of period

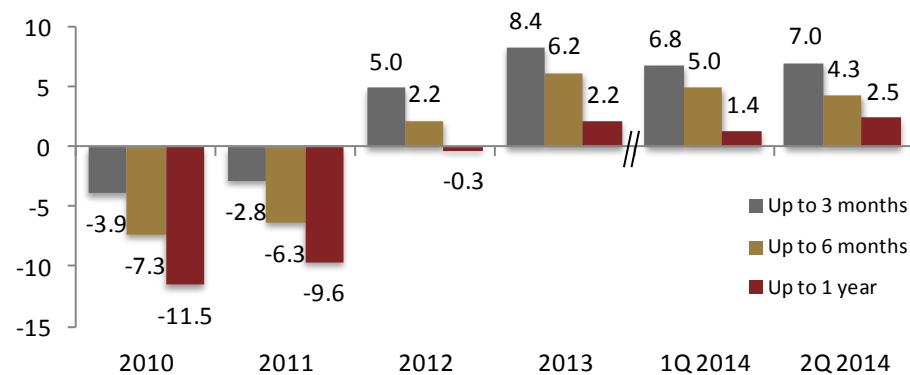


Chart 14

■ In the second quarter of 2014, the commercial gap reduced further, standing at a very low level in historical terms.

■ Liquidity gaps remained broadly unchanged, taking on positive values in all maturities considered.



Credit at Risk ratio (% of gross credit) - Value at end of period

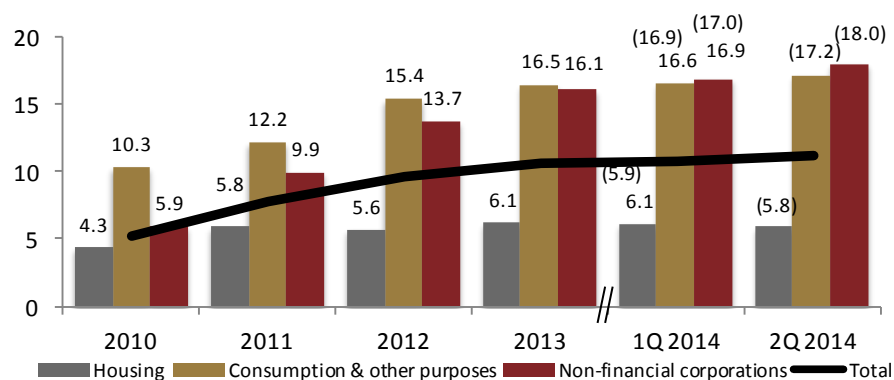


Chart 15

Note: The data for the 2Q2014 do not include BES, therefore appearing in brackets. Moreover, for March 2014, the credit at risk ratios presented in brackets correspond to the aggregate banking system figures excluding ESFG, to allow comparison.

Credit Impairments as % of gross credit - Value at end of period

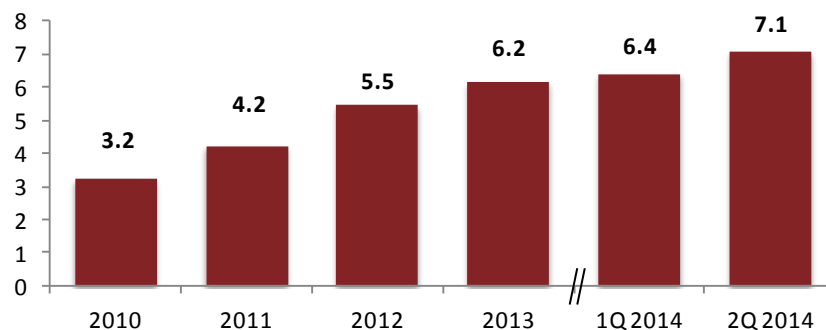


Chart 16

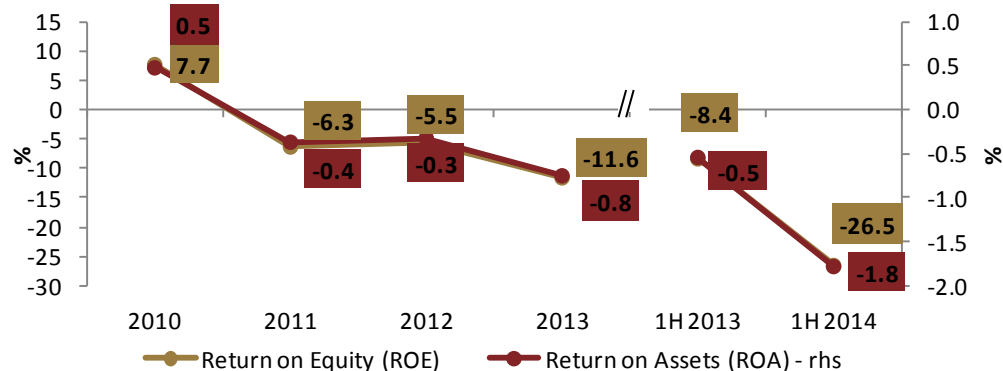
■ The credit at risk ratio kept the upward trajectory in the second quarter of 2014. This development is partially driven by a denominator effect (deleveraging) as the flow of new overdue and other doubtful loans has been decreasing since mid-2012.

■ The worsening of the credit at risk ratio since 2010 resulted mainly from the deterioration of the quality of credit granted to the non-financial corporate sector. The above mentioned denominator effect represents about 50% of the increase in the last semester.

■ The impairment to gross credit ratio has been trending upwards since 2010, following the materialisation of credit risk. The considerable increase observed in 2Q2014 is mainly related to developments in BES. Excluding this institution, the ratio would have increased slightly, from 6.3% to 6.4%.



ROA & ROE - Value in the period



Note: Annualized figures.

Return is measured by earnings before taxes and minority interests.

Chart 17

Income and costs as a % of gross income - Value in the period

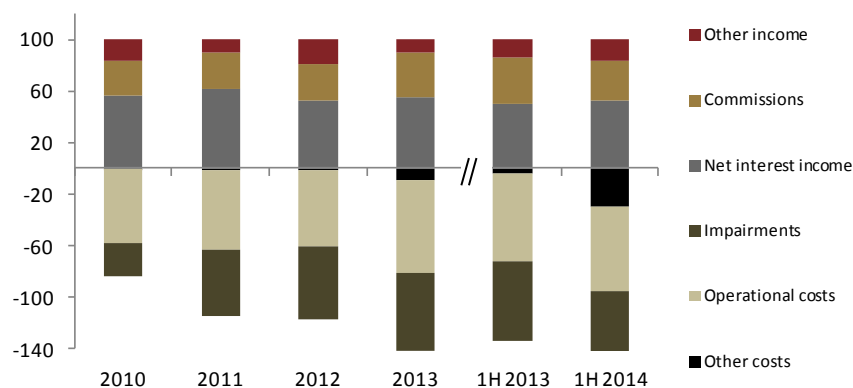


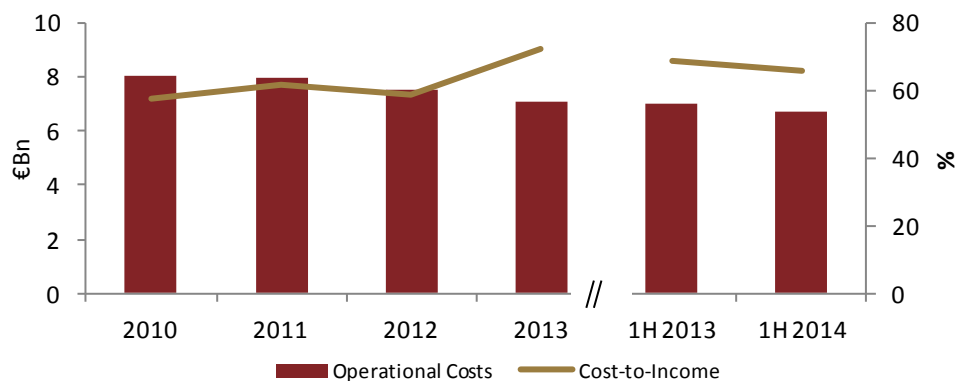
Chart 18

■ In the first half of 2014 the aggregate results of the Portuguese banking system were completely driven by the developments in BES, on the account of significant impairments and other provisions included in the 'Others costs' item.

■ Excluding BES, profitability would be positive (ROA of 0.25% and ROE of 3.8%). In the recent period, reference should be made to the positive dynamics in net interest income, the increase in profits from financial operations and the reduction in operating costs. In turn, a slight decrease of the impairment flow was observed.



Cost-to-Income (%), Operational Costs (€Bn) - Value in the period



Note: Annualized figures.

Chart 19

Banking interest rates (new business) - Average value of period

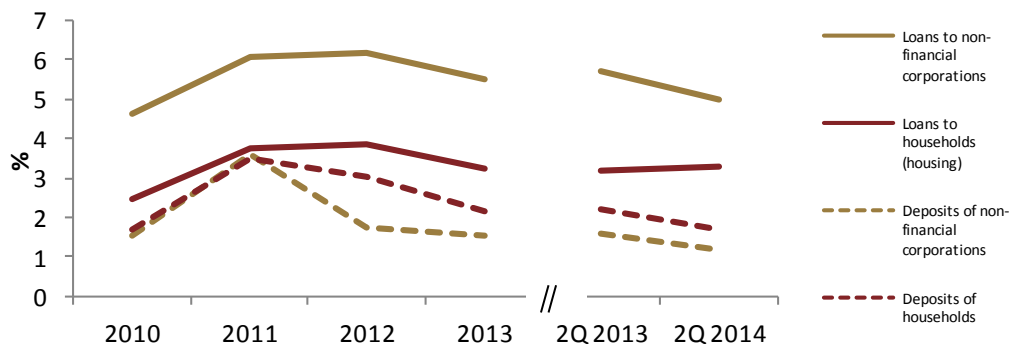


Chart 20

■ The reduction in the cost-to-income ratio (CtI) was mainly due to the increase of gross income. Excluding BES this evolution would have been more pronounced. The CtI ratio, with reference to the first half of 2014, would amount to 55%, about 10 p.p. below the aggregate figure.

■ In the second quarter of 2014, interest rates on new loans to non-financial corporations decreased vis-à-vis the homologous quarter, maintaining the downward trend.

■ Interest rates on new loans to households have been stable since the fourth quarter of 2012.

■ Cost of new deposits continued the decreasing trend. Interest rates are now significantly below the ones offered in 2011/2012, a period of fierce competition for customers resources.



Tier 1 capital to Total Assets ratio - Value at end of period

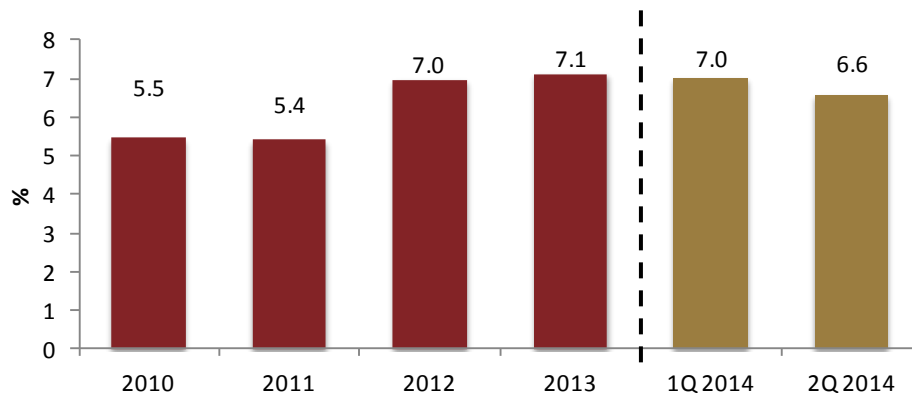


Chart 21

Core Tier 1 ratio (until 2013) and CET 1 ratio (2014) - Value at end of period

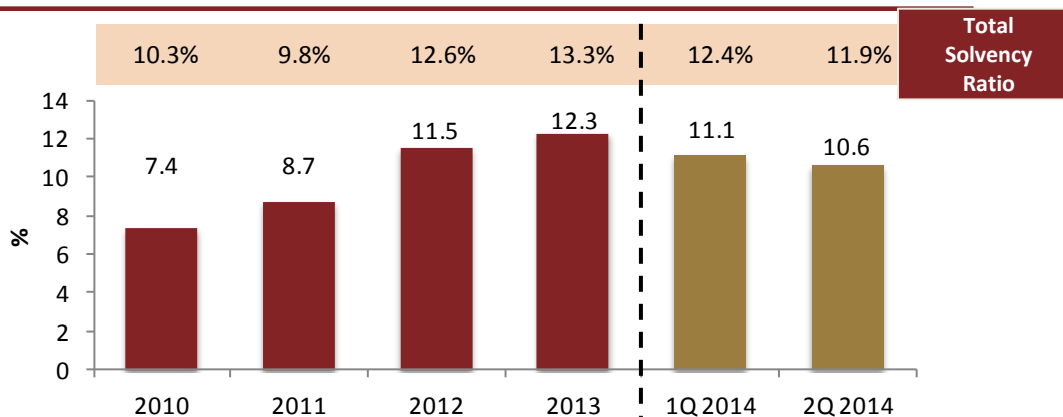


Chart 22

■ As of June 2014, the leverage of the banking system, measured by the ratio between Tier 1 capital and total assets stood at 6.6% (7.1% excluding BES).

■ The CET 1 ratio reached 10.6% for the Portuguese banks aggregate, in the context of a regulatory minimum of 7%*. BES has a considerable impact on the average ratio and on its evolution. Excluding this institution, the average CET 1 ratio of the banking system increased slightly, from 12.2% to 12.3%.

*Since 1 January 2014 is in effect the Notice of Banco de Portugal 6/2013 which establishes a new, transitory, regime of own funds adequacy. The new regime establishes inter alia that credit institutions and investment firms preserve a common equity Tier 1 (CET 1 ratio) not below 7% until the Directive 2013 / 36/UE (or CRD IV - Capital Requirements Directive) is transposed to the Portuguese legal framework.

Portuguese Banking System

Recent Developments – 2nd quarter 2014



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