



BANCO DE PORTUGAL
EUROSISTEMA

Portuguese Banking System

Recent Developments – 3rd quarter 2016

Prepared with data available up to 23rd December of 2016



- Portuguese banking system – Main highlights
- Macroeconomic and financial indicators
- Portuguese banking system
 - Balance sheet
 - Liquidity & funding
 - Asset quality
 - Profitability
 - Solvency



I. Balance Sheet

- Banking system total assets continued to decrease gradually in the third quarter of 2016, reflecting developments in credit.

II. Liquidity & Funding

- Both the Loan-to-Deposits ratio and the commercial gap decreased vis-à-vis the previous quarter, as did the Eurosystem financing.

III. Asset/Credit Quality

- The credit-at-risk ratio diminished slightly during the third quarter of 2016, driven chiefly by developments in the NFC segment.

IV. Profitability

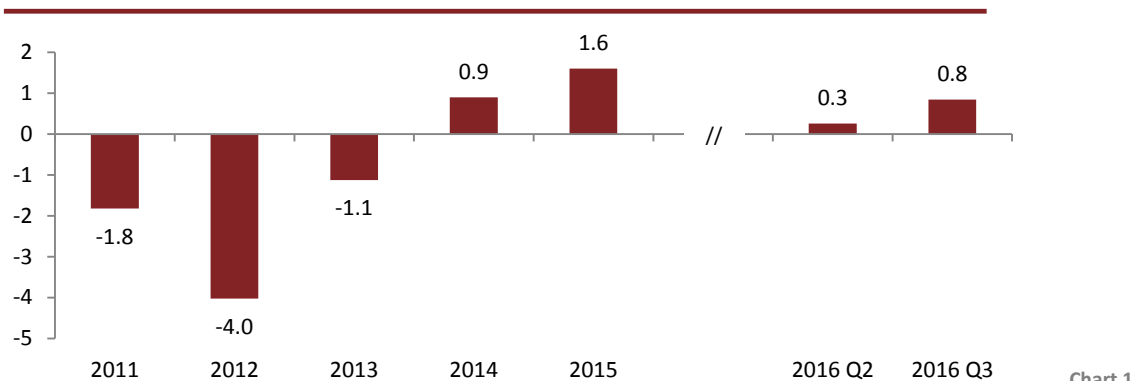
- Although slightly positive, banking system profitability decreased in the first three quarters of 2016 on a year-on-year basis, due mainly to a considerable reduction in income from financial operations, which was substantial in the same period of the previous year.
- Net interest income increased vis-à-vis the set of the first three quarters of 2015, as a result of a sharper reduction in interest expenses than the reduction observed in interest income.

V. Solvency

- The banking system solvency level increased slightly in the third quarter of 2016, due, chiefly, to a reduction in RWA.

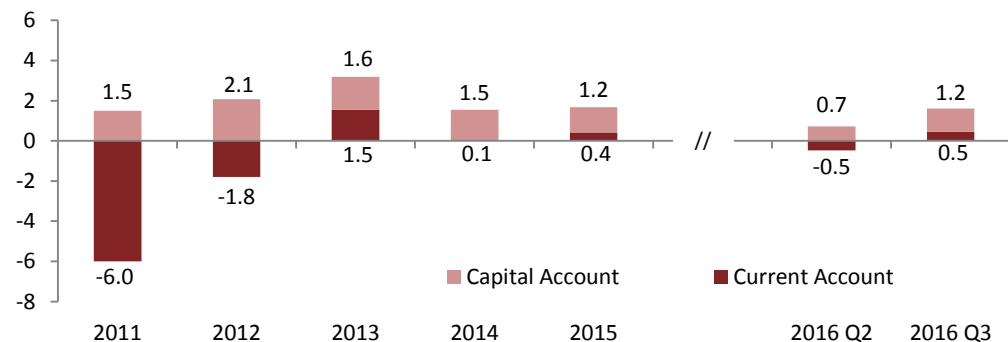


GDP growth rate (%) – Volume



Note: Quarterly figures correspond to q-on-q rates of change. National Accounts and Balance of Payments figures are already presented according to the rules of the European System of National and Regional Accounts (ESA 2010) and Balance of Payments and International Investment Position Manual (BPM6).

Current account and capital account, % of GDP



Note: Quarterly figures are seasonally adjusted.

■ In 2016 Q3, the quarter-on-quarter GDP growth rate was positive (0.8%), significantly higher than in the previous quarters.

■ The year-on-year growth rate stood at 1.6%.

■ In 2016 Q3, the current and capital accounts grew by around 1.4 p.p. of GDP vis-à-vis the second quarter of 2016, mainly due to the increase in the first component. The current and capital accounts decreased by 0.4 p.p. of GDP year-on-year.

■ In the first nine months of 2016, on year-on-year terms, the current and capital accounts balance decreased by 0.6 p.p. of GDP to 1.0% of GDP.



Unemployment rate, % of active population

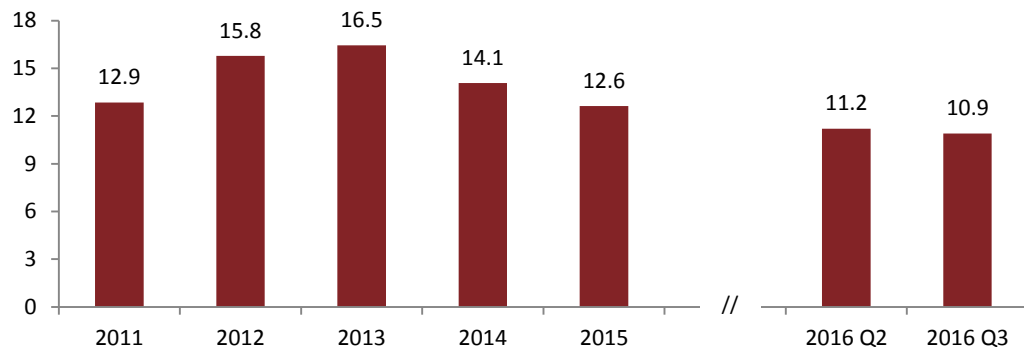


Chart 3

Fiscal Balance, % of GDP

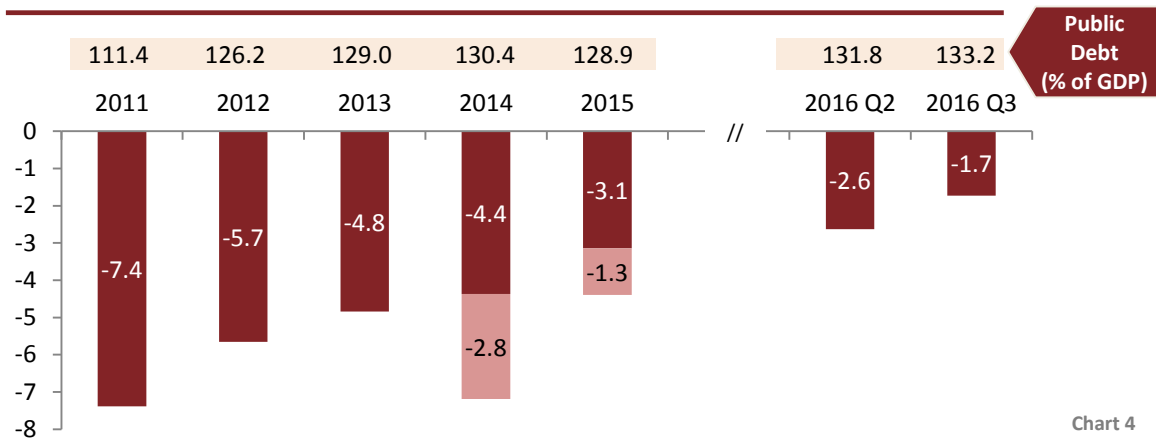


Chart 4

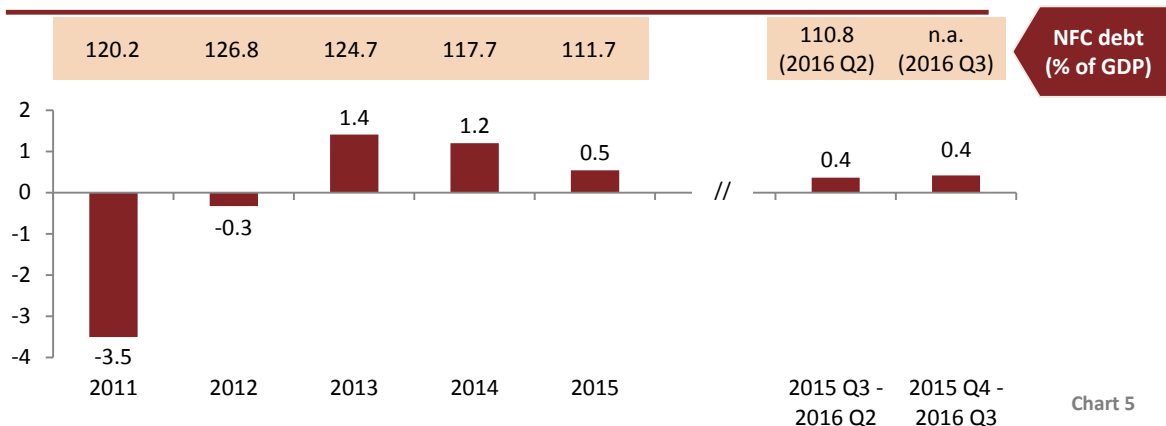
Note: The unemployment rate corresponds to the figure of the central month of each quarter published by the National Statistical Institute. The fiscal deficit of 2014 reflects the inclusion of 4.9 billion Euros related to the capitalization of Novo Banco as a capital transfer (-2.8% of GDP). The fiscal deficit of 2015 reflects the inclusion of 2.3 billion euros as a capital transfer in the context of the Banif resolution in 2015Q4 (-1.3% of GDP).

■ The unemployment rate was 10.9% in 2016 Q3, which corresponds to a decrease of 0.3 p.p. from the previous quarter and to a decrease of 1.4 p.p. year-on-year.

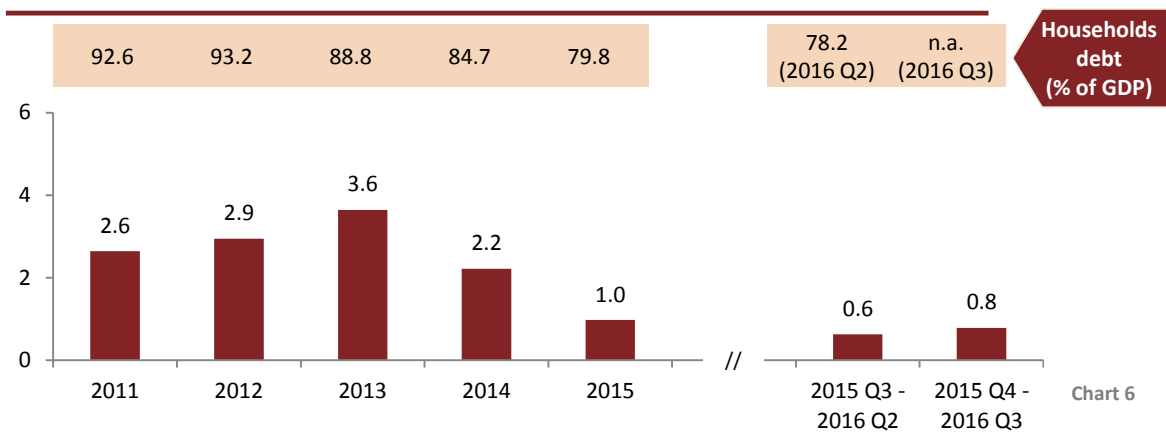
■ Public debt as a percentage of GDP stood at 133.2% in 2016 Q3, an increase of 1.4 p.p. of GDP compared to the previous quarter. This indicator, net of Central Government deposits, stood at 121.6% of GDP.



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



Net lending/borrowing of households, % of GDP



n.a. – not available.

Note: National Sector Accounts were revised when Statistics Portugal released the Accounts for the fourth quarter of 2014. These revisions reflect changes introduced in detailed Annual National Accounts for 2012 (final results), with an impact on subsequent years.

▪ At the end of 2016 Q2, NFC debt amounted to 110.8% of GDP, remaining practically unchanged from the previous quarter (a 4.6 p.p. decline year-on-year).

▪ In the year ended in 2016 Q3, net lending of NFC stood at 0.4% of GDP.

▪ Households' debt continued to decrease in 2016 Q2 to 78.2% of GDP, which represents a decline of roughly 1.5 p.p. of GDP vis-à-vis end-2015.

▪ In the year ended in 2016 Q3, households' net lending amounted to 0.8% of GDP.



Sovereign debt yields 10Y (%)

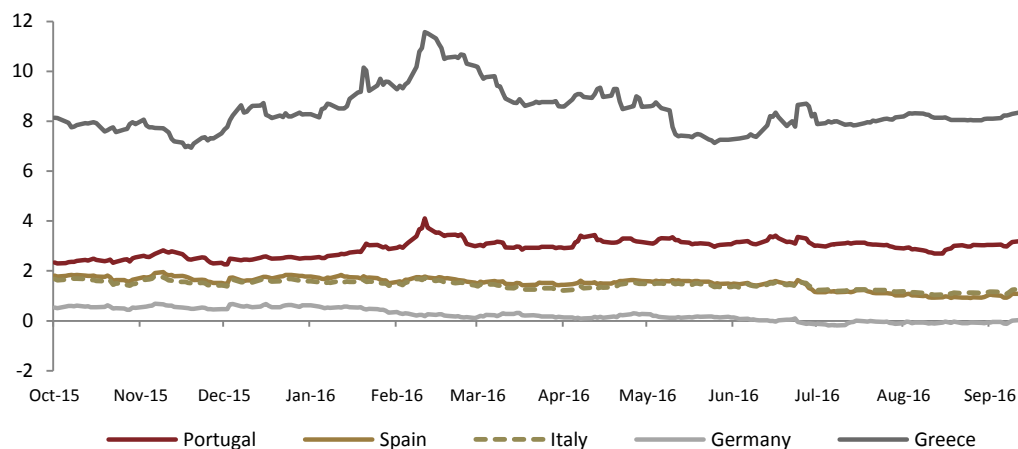


Chart 7

ECB rates (%)

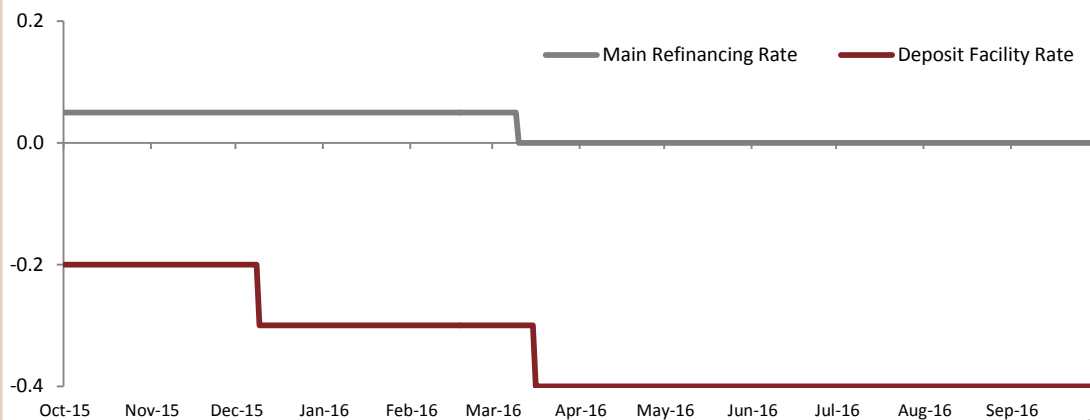


Chart 8

■ The Portuguese 10-year government bond yield increased about 30 b.p. in 2016 Q3.

■ The interbank rates continued to be negative for all maturities, reflecting the accommodating monetary policy pursued by the ECB.

■ ECB rates have been kept unchanged since March 2016: the deposit facility interest rate at -0.40%, the main refinancing operations interest rate at 0%, and the marginal lending facility interest rate at 0.25%.



Comment on accounting and prudential information

The banking system data present the following breaks in time series:

- In the third quarter of 2014, resulting from the resolution measure applied to Banco Espírito Santo (BES). In particular, the break in the time series arises from the fact that the assets/liabilities not transferred to the balance sheet of Novo Banco (NB) are not considered in the aggregate of the banking system from August 2014 onwards.

In the absence of accounting information for BES on a consolidated basis for the period from 30 June 2014 to the day of implementation of the resolution measure (closing balance sheet and statement of profit and loss), the reporting of BES on individual basis, with reference to 31 July 2014, was considered when determining the aggregate results of the banking system for the third quarter of 2014. However, it must be stressed that the adjustments stemming from the resolution measure applied to BES were not considered.

Changes in banking system liabilities represented by debt securities and equity items, in the fourth quarter of 2015, somewhat reflect the re-transfer from NB to BES of five issuances of non-subordinated debt, which had been originally transferred from BES to NB following the Decision of 3 August 2014.

- In the fourth quarter of 2015, resulting from the resolution measure applied to BANIF – Banco Internacional do Funchal (Banif). In particular, the break in the time series arises from the fact that the assets/liabilities transferred to the financial vehicle – Oitante, S.A. – are not considered in the aggregate of the banking system from 20 December 2015 onwards.

In the absence of accounting information for Banif on a consolidated basis for the period from 30 September 2015 to the day of implementation of the resolution measure (statement of profit and loss), the reporting of Banif on individual basis, with reference to 30 November 2015, was considered when determining the aggregate results of the banking system for the fourth quarter of 2015. However, it must be stressed that the adjustments resulting from the resolution measure applied to Banif were not considered.

- In the second quarter of 2016, resulting from the reclassification of some assets/liabilities from the "non-current assets and liabilities held for sale and discontinued operations" category related to the acquisition of the Barclays operation in Portugal by Bankinter. This reclassification did not have an impact on the banking system total assets, but requires careful analysis regarding balance sheet items' rates of change. In addition, the deconsolidation of Banco Millennium Angola, also in the second quarter of 2016, was a non-recurring event with a significant impact on balance sheet items.



Assets (€Bn) – Value at end of period

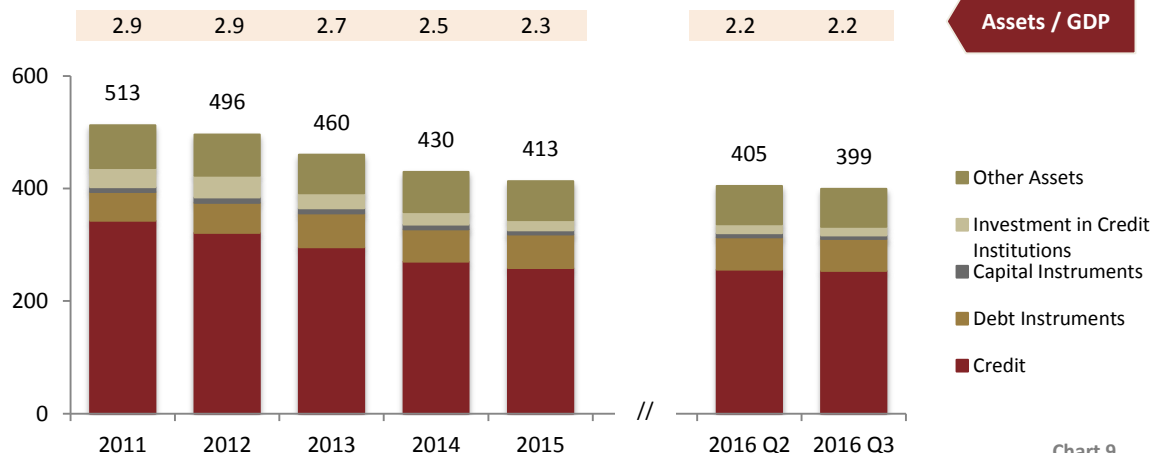


Chart 9

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

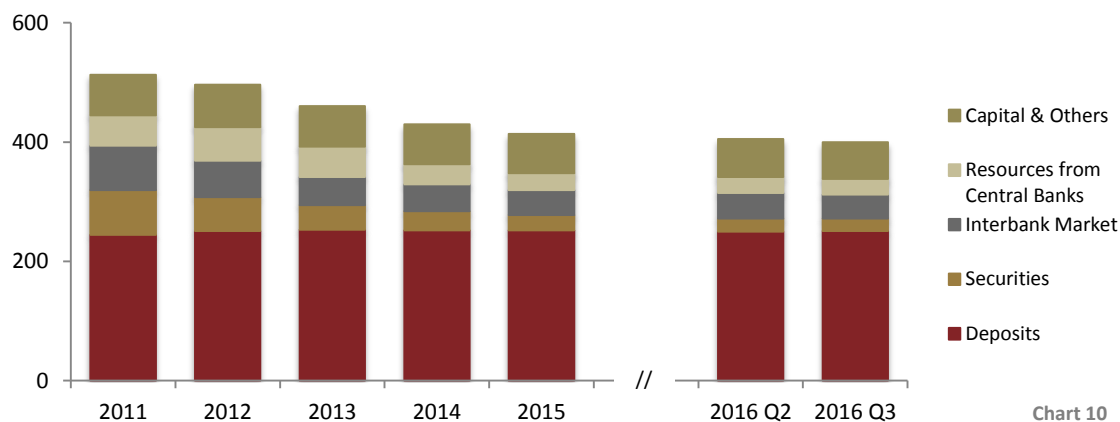


Chart 10

Source: Banco de Portugal

▪ The banking system total assets reduction continued in 2016 Q3, driven mainly by credit. Vis-à-vis end-2015, total assets decreased 3.4% and credit 2.0%.

▪ On a comparable basis (accounting for time series' breaks since the beginning of the year), total assets decreased 2.5% between end-2015 and 2016 Q3, whilst credit decreased 3.0%.

▪ In 2016 Q3, interbank funding decreased and, as in the previous quarter, deposits increased. Comparing to end-2015, interbank funding and total deposits decreased by 4.8% and 0.4% respectively (whilst non-financial resident private sector deposits increased by 3.3%).

▪ On a comparable basis, interbank funding decreased by 2.5% between end-2015 and 2016 Q3, whilst total deposits decreased by 0.7% (non-financial resident private sector deposits increased by 2.1%).



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

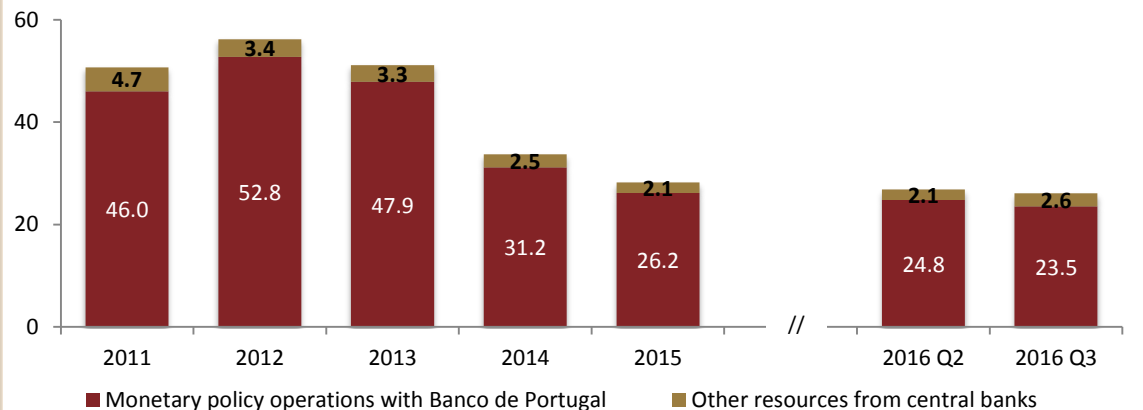


Chart 11

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

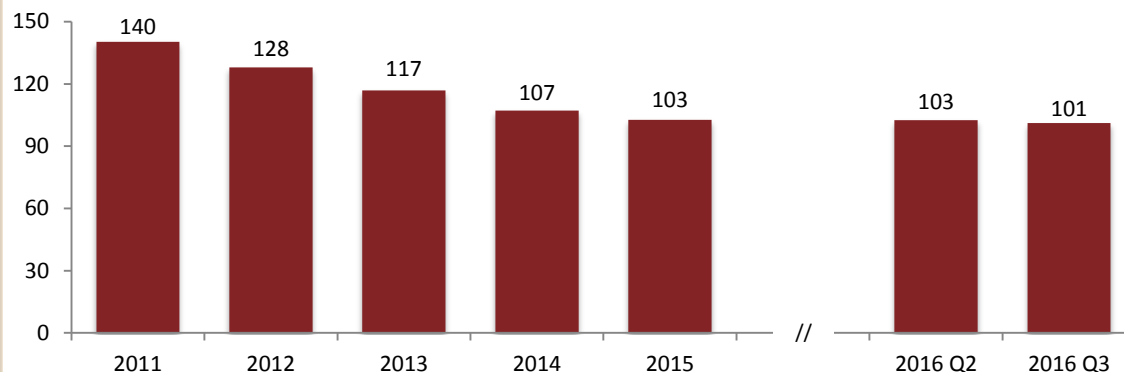


Chart 12

■ In 2016 Q3, central banks funding declined slightly, accounting for 6.5% of the banking system total assets. This is the lowest figure since the beginning of the Economic and Financial Assistance Programme (the highest was recorded in June 2012: €64.1 Bn, 12.5% of total assets).

■ The decrease in credit and, to a less extent, the increase in customer resources vis-à-vis the second quarter led to a reduction of the Loan-to-Deposits ratio in 2016 Q3.



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

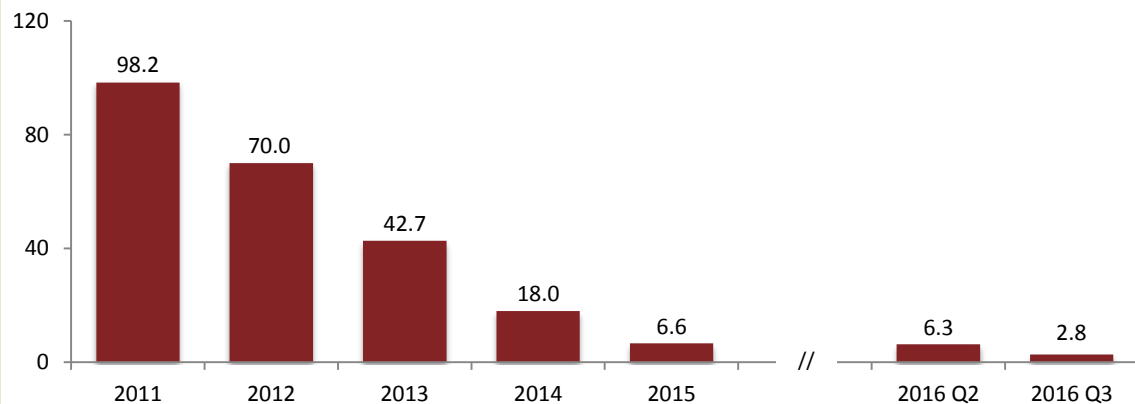
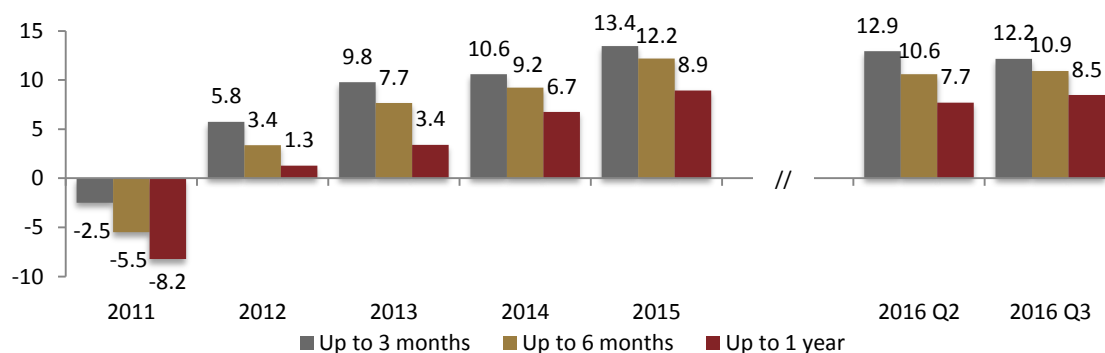


Chart 13

Liquidity gap in cumulative maturity ladders for domestic institutions (% of stable assets) – Value at end of period



Note: The liquidity gap is defined as the difference between liquid assets and volatile liabilities in proportion of the difference between total assets and liquid assets, for each cumulative maturity scale. An increase of this indicator reflects an improvement of banks' liquidity position.

Chart 14

▪ The commercial gap (credit minus deposits) decreased to €2.8 Bn in 2016 Q3.

▪ Liquidity gaps for domestic institutions remained at high levels for all maturities in 2016 Q3.



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

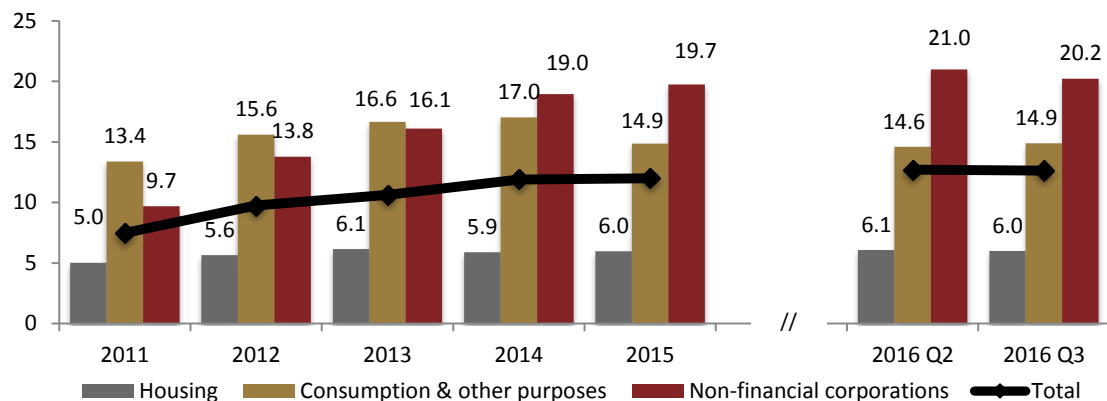


Chart 15

Credit Impairments (% of gross credit) – Value at end of period

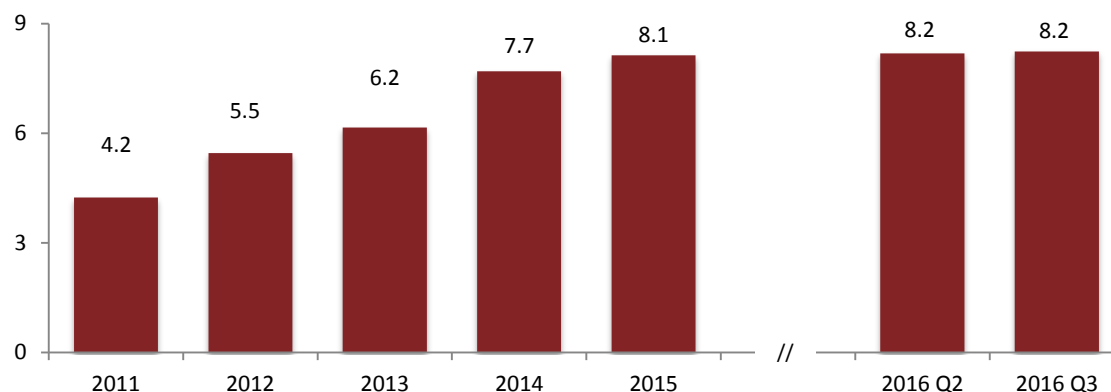


Chart 16

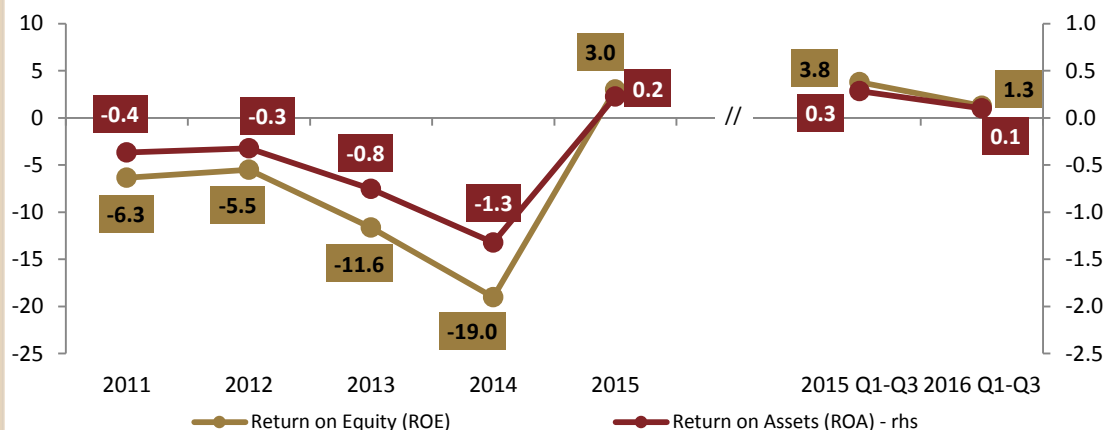
■ In 2016 Q3, the credit-at-risk ratio diminished by 0.1 p.p. vis-à-vis the previous quarter to 12.6%.

■ This fall in the credit-at-risk ratio reflects primarily the developments in the NFC's segment in which occurred a decrease in credit at risk (numerator effect) and an increase in credit (denominator effect).

■ In 2016 Q3, credit impairments stood at 8.2% of gross credit, as in the two previous quarters.



ROA & ROE (%) – Value in the period



Note: Return is measured by earnings before taxes and minority interests. Annualized figures.

Chart 17

Income and costs (% of gross income) – Value in the period

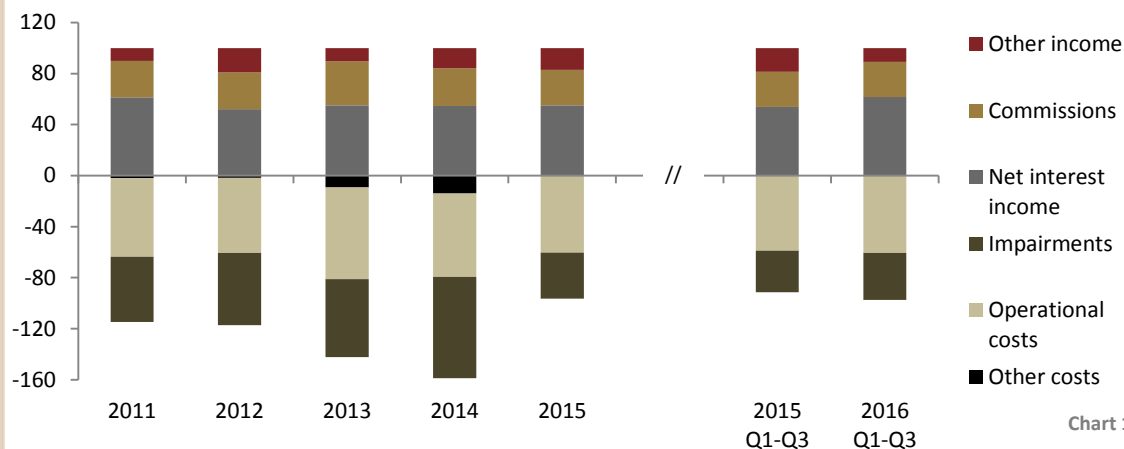


Chart 18

Source: Banco de Portugal

■ In the set of the first three quarters of 2016, the return on equity and the return on assets displayed a substantial reduction on a year-on-year basis. Notwithstanding, both ratios remained positive.

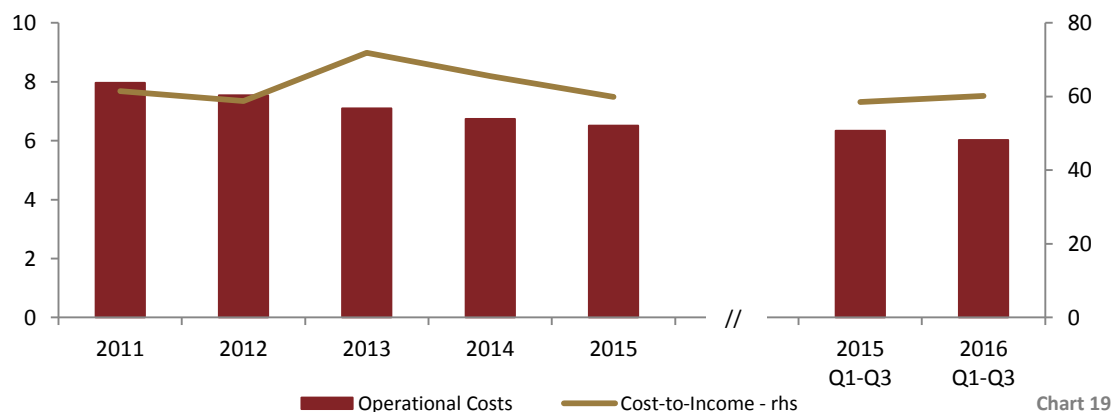
■ This decline in profitability continued to be largely driven by a significant decrease in income from financial operations, which was considerable in 2015.

■ Net interest income increased 5.8% year-on-year in the set of the first three quarters of 2016, following the trend observed since 2014. This increase resulted from a sharper reduction in interest expenses than the reduction registered in interest income.

■ The flow of impairments increased on a year-on-year basis, due exclusively to those associated with financial assets other than credit.



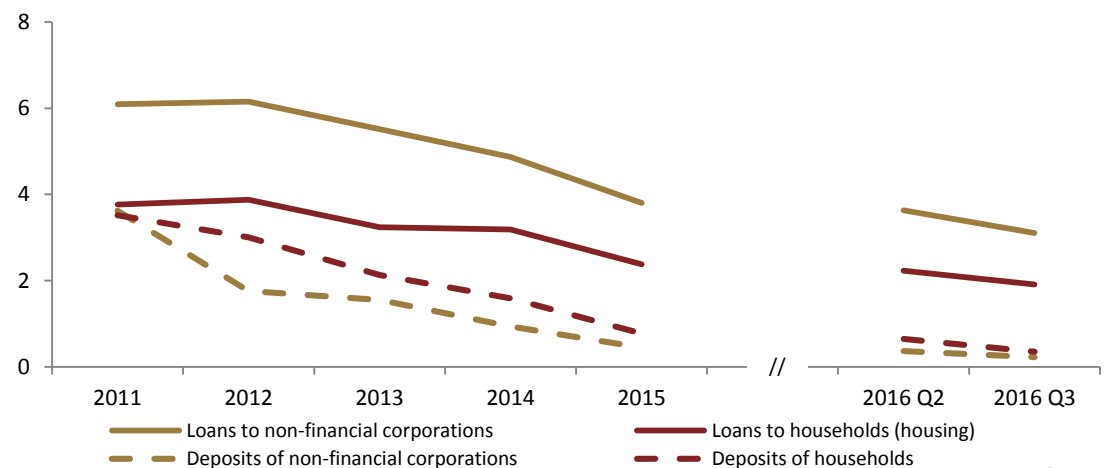
Operational Costs (€Bn), Cost-to-Income (%) – Value in the period



■ Despite a reduction in operational costs over the first three quarters of 2016, the cost-to-income ratio increased vis-à-vis the same period of the previous year, due to a greater reduction in gross income.

■ Interest rates on new operations decreased slightly in 2016 Q3.

Banking interest rates (new business) – Average value of period (%)



■ Compared to 2016 Q2, interest rates on new loans for housing purchase and to NFC fell by 7 b.p. and 9 b.p., respectively.

■ The cost of new deposits decreased by 7 b.p. for the households' segment and by 1 b.p. for the NFC's segment.



Tier 1 capital to Total Assets ratio – Value at end of period (%)

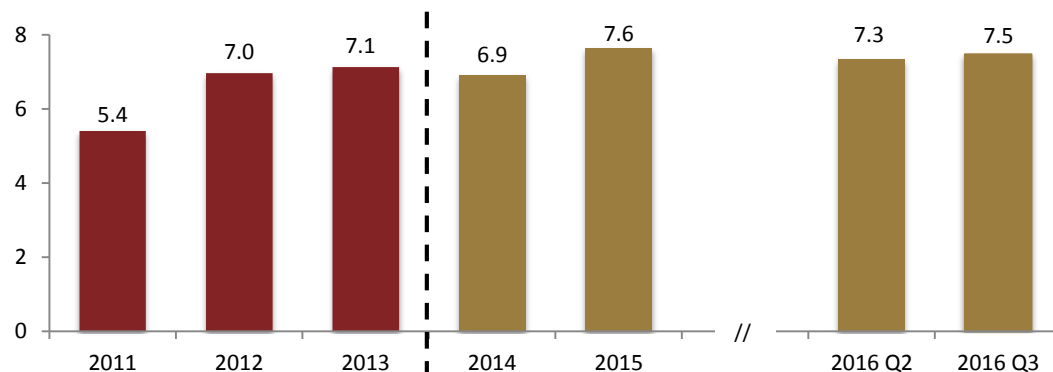


Chart 21

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

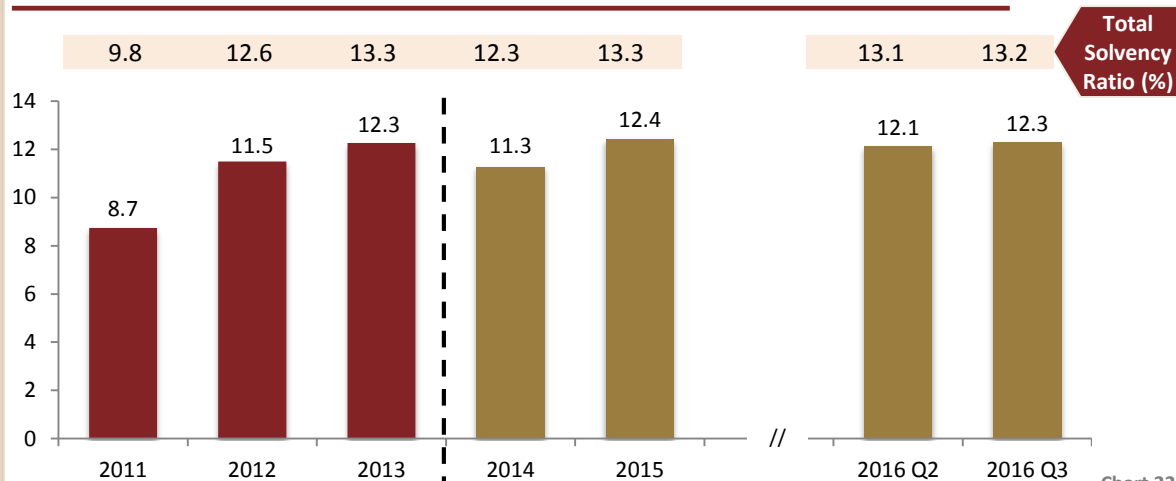


Chart 22

■ The ratio between Tier 1 capital and total assets increased by 0.2 p.p. in 2016 Q3, as a result of a decline in total assets.

■ Both the CET 1 ratio and the Total Solvency ratio increased slightly vis-à-vis 2016 Q2, due primarily to a reduction in RWA.

Note: In 2014, the transition to a new prudential regime determined the existence of breaks in the series of solvency indicators justified by methodological differences in the calculation of own funds components, affecting the comparability of ratios with previous years.

Portuguese Banking System

Recent Developments – 3rd quarter 2016



BANCO DE PORTUGAL
EUROSISTEMA