Portuguese Banking System: latest developments

4th quarter 2018

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Portuguese banking system – 4th quarter of 2018

Balance-sheet structure

The banking system's total assets increased by 0.2% from the third quarter of 2018, due to a rise of 1% in the debt securities portfolio (particularly public debt securities) and of 0.7% in loans to customers, partly offset by a reduction in equity holdings (-0.1 p.p. of assets) and in non-current assets held for sale (-0.3 p.p. of assets).

Central bank funding remained at 5.3% of assets in the fourth quarter, which was the lowest value recorded since the first quarter of 2010.

The banking system's liquidity position remained at comfortable levels, with a loan-to-deposit ratio of 88.9% and the liquidity coverage ratio at 196.5%.

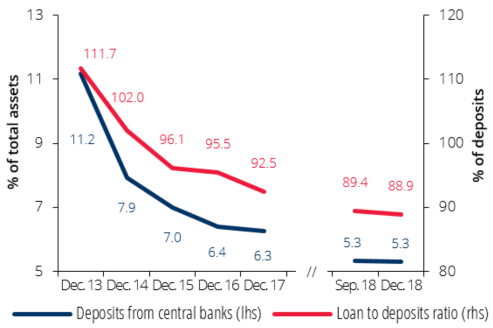
Asset quality

The NPL ratio remained on a downward trend, standing at below 10% (9.4%) at the end of 2018, which meant a quarterly reduction of 1.9 p.p.. These developments vis-à-vis the previous quarter result from a sharp reduction in the stock of non-performing loans of NFCs and Households by €3.8 billion and €1.3 billion respectively, thus leading to an NPL ratio net of impairments of below 5% (4.5%).

Since its historical peak in June 2016, the NPL ratio declined by 8.5 p.p. (NFCs: -11.9 p.p.; Households: -4.1 p.p.). This reflects a reduction of almost 50% of the total NPL stock (NFCs: -49%; Households: -46%), corresponding to a decline of €24.6 billion (NFCs: -€16.1 billion; Households: -€5.9 billion).

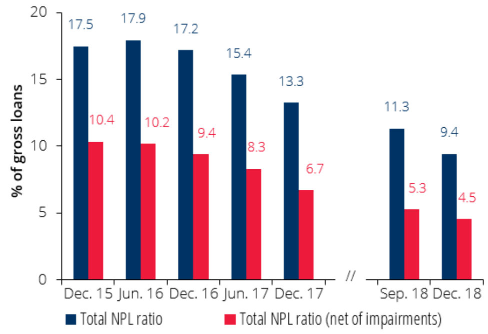
The NPL impairment coverage ratio declined by 1.4 p.p. in the quarter under review, to 51.9%, due to a decline in the NFC's NPL coverage ratio.

Chart 1 • Central bank funding and loan-to-deposit ratio



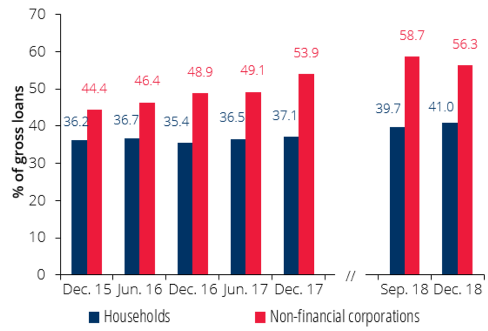
Source: Banco de Portugal.

Chart 2 • NPL ratios



Source: Banco de Portugal.

Chart 3 • NPL coverage ratios



Source: Banco de Portugal.

Profitability

In 2018 bank profitability measured by return on equity (ROE) and return on assets (ROA) increased from the previous year by 3.7 p.p. and 0.3 p.p. respectively, to stand at 7.1% and 0.7%. The rise in ROA was mostly determined by a significant reduction in provisions and impairments (0.6 p.p. of assets), in particular credit impairments. This led to a 0.6 p.p. decline in the loan loss charge, to 0.4%.

Total operating income made a negative contribution to the evolution of ROA (0.4 p.p.). This was due to a decline in profits from financial operations, associated to losses on credit sales and the dissipation of the base effect related to the recording, under other operating income in 2017, of instalments related to the contingent capitalisation scheme envisaged in Novo Banco's sale contracts.

The less marked reduction of operational costs (1.9%), in the context of a fall in total operating income, was reflected on a decrease in the banking system's efficiency, as measured by the cost-to-income ratio, which stood at 60.3% (52.8% in 2017).

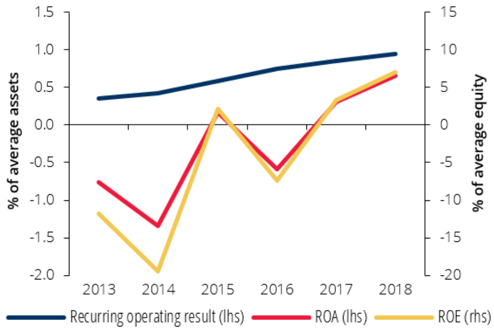
Solvency

In the fourth quarter of 2018 solvency ratios declined slightly, with the total capital ratio and the Common Equity Tier 1 (CET1) ratio standing at 15.1% and 13.2% respectively. This development was in part due to the change of Novo Banco's parent undertaking – for the purposes of prudential supervision – to LSF Nani Investments S.à.r.l.

The decline in risk-weighted assets led to a 0.7 p.p. decrease in the average risk weight, which stood at 54.4% at the end of 2018.

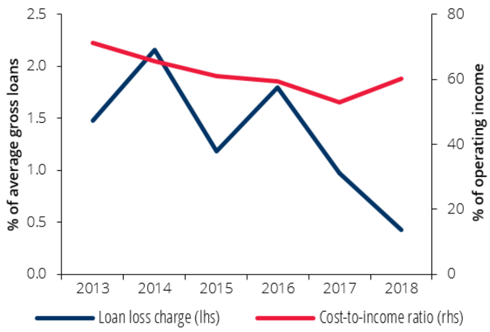
The leverage ratio declined slightly to 7.3%, remaining far above the minimum benchmark defined by the Basel Committee on Banking Supervision (3%).

Chart 4 • Return on equity (ROE), return on assets (ROA) and recurring operating result



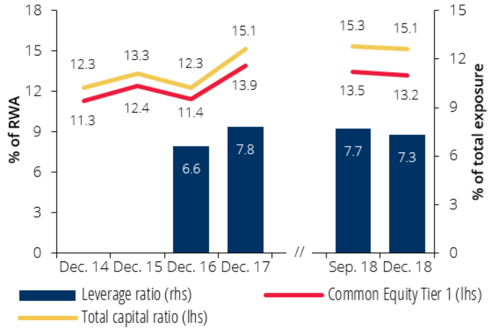
Source: Banco de Portugal.

Chart 5 • Cost-to-income and credit risk cost ratios



Source: Banco de Portugal.

Chart 6 • Own funds ratios and leverage ratio



Source: Banco de Portugal.

Note: RWA means risk-weighted assets. Total exposure includes total assets, derivatives and off-balance sheet positions.

Table 1 • Portuguese banking system indicators [(a)]

	Notes	Unit	Dec. 08	Dec. 14	Dec. 15	Dec. 16	Dec. 17	Sep. 18	Dec. 18
Assets									
Loans to customers (net)	(1)	%	70.2	60.4	60.0	60.7	60.6	59.4	59.7
Debt securities	(1)	%	10.6	17.5	18.3	18.5	19.2	21.3	21.4
Portuguese government debt securities	(2)	%	0.9	6.4	6.6	7.1	8.3	8.8	8.8
Total assets		€ billion	474.6	425.7	407.6	386.1	381.3	383.7	384.5
Total assets (gross) / GDP (nominal)		%	265.3	246.0	226.7	207.0	195.9	191.7	190.8
Liquidity and funding									
Central bank funding	(1)	%	3.0	7.9	7.0	6.4	6.3	5.3	5.3
Interbank financing (net)	(1)	%	9.2	4.9	4.7	5.5	5.6	6.3	6.1
Customer deposits	(1)	%	45.9	59.2	62.4	63.6	65.5	66.4	67.1
Liabilities represented by debt securities	(1)	%	22.3	8.8	7.5	6.1	4.8	4.3	4.2
Equity	(1)	%	5.5	7.2	8.1	7.7	9.5	9.3	9.1
Loan-to-deposit (Ltd) ratio	(3)	%	152.9	102.0	96.1	95.5	92.5	89.4	88.9
Highly liquid assets	(4)	%	n.a.	n.a.	n.a.	11.3	14.8	15.8	17.2
Liquidity coverage ratio (LCR)	(5)	%	n.a.	n.a.	n.a.	150.8	173.5	185.0	196.5
Asset quality									
Non-performing loans (gross value)		€ million	n.a.	n.a.	49,818	46,361	37,001	31,171	25,850
Non-performing loans (net of impairments)		€ million	n.a.	n.a.	29,512	25,364	18,728	14,541	12,428
NPL ratio - Total	(6)	%	n.a.	n.a.	17.5	17.2	13.3	11.3	9.4
NPL ratio - Households	(6)	%	n.a.	n.a.	9.4	8.7	7.1	6.1	5.1
NPL ratio - Non-financial corporations	(6)	%	n.a.	n.a.	28.3	29.5	25.2	22.1	18.5
NPL ratio net of impairments - Total	(7)	%	n.a.	n.a.	10.4	9.4	6.7	5.3	4.5
NPL impairment coverage ratio - Total	(8)	%	n.a.	n.a.	40.8	45.3	49.4	53.4	51.9
Coverage ratio - Households	(8)	%	n.a.	n.a.	36.2	35.4	37.1	39.7	41.0
Coverage ratio - Non-financial corporations	(8)	%	n.a.	n.a.	44.4	48.9	53.9	58.7	56.3
Profitability [(b)]									
Return on assets (ROA)	(9)	%	0.3	-1.3	0.2	-0.6	0.3	0.8	0.7
Recurring operating result	(10)	%	0.9	0.4	0.6	0.7	0.8	0.9	0.9
Return on equity (ROE)	(11)	%	5.7	-19.4	2.2	-7.3	3.3	8.7	7.1
Profit or loss for the year		€ million	970	-5,311	324	-1,249	-88	2,248	1,084
Cost-to-Income	(12)	%	55.6	65.5	60.9	59.4	52.8	56.1	60.3
Loan loss charge	(13)	%	0.7	2.2	1.2	1.8	1.0	0.4	0.4
Solvency									
Common Equity Tier 1 (Core Tier 1 / CET 1)	(14), (15)	%	12.2	11.3	12.4	11.4	13.9	13.5	13.2
Additional Tier 1 (AT 1)	(14)	%	n.a.	0.1	0.2	0.3	0.6	0.7	0.8
Tier 2	(14)	%	n.a.	0.9	0.7	0.6	0.7	1.2	1.2
Leverage ratio	(16)	%	n.a.	6.9	7.6	6.6	7.8	7.7	7.3
Average risk weight	(17)	%	n.a.	60.9	60.6	58.9	56.0	55.2	54.4

Notes:

(a) Banking system data are based on accounting information on a consolidated basis from credit institutions and investment firms, reported to Banco de Portugal for supervisory purposes.

(b) Profitability indicators are calculated with annualised flows accumulated up to the reference period.

(1) As a percentage of total assets.

(2) Monetary and financial statistics. As a percentage of other monetary financial institutions' assets.

(3) Ratio of customer loans to customer deposits.

(4) Corresponds to the amount of liquid assets held by credit institutions that satisfy requirements set in the Commission Delegated Regulation (EU) 2015/61 of 10 October 2014. As a percentage of total assets.

(5) Ratio of available highly liquid assets and net cash outflows calculated under a 30-day stress scenario.

(6) Ratio of the gross value of non-performing loans to the total gross value of loans.

(7) Ratio of non-performing loans net of impairments to the total gross value of loans.

(8) Ratio of impairments for non-performing loans to their gross value.

(9) Profit and loss before taxes as a percentage of average assets.

(10) Net interest income and net commissions less operational costs; as a percentage of average assets.

(11) Profit and loss before taxes as a percentage of average equity.

(12) Ratio of operational costs to total operating income.

(13) Flow of credit impairments as a percentage of total average gross credit granted to customers.

(14) As a percentage of risk-weighted assets.

(15) The transition to a new prudential regime in 2014 led to structural breaks in solvency indicators, accounted for by methodological differences in the calculation of own funds components, affecting the comparability of ratios vis-à-vis previous years.

(16) Up to June 2016 it corresponds to the ratio of Tier 1 capital to total assets. From September 2016 onwards it corresponds to the ratio of Tier 1 capital to total exposure (including on- and off-balance sheet assets and derivatives).

(17) Ratio of risk-weighted assets to total assets.

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