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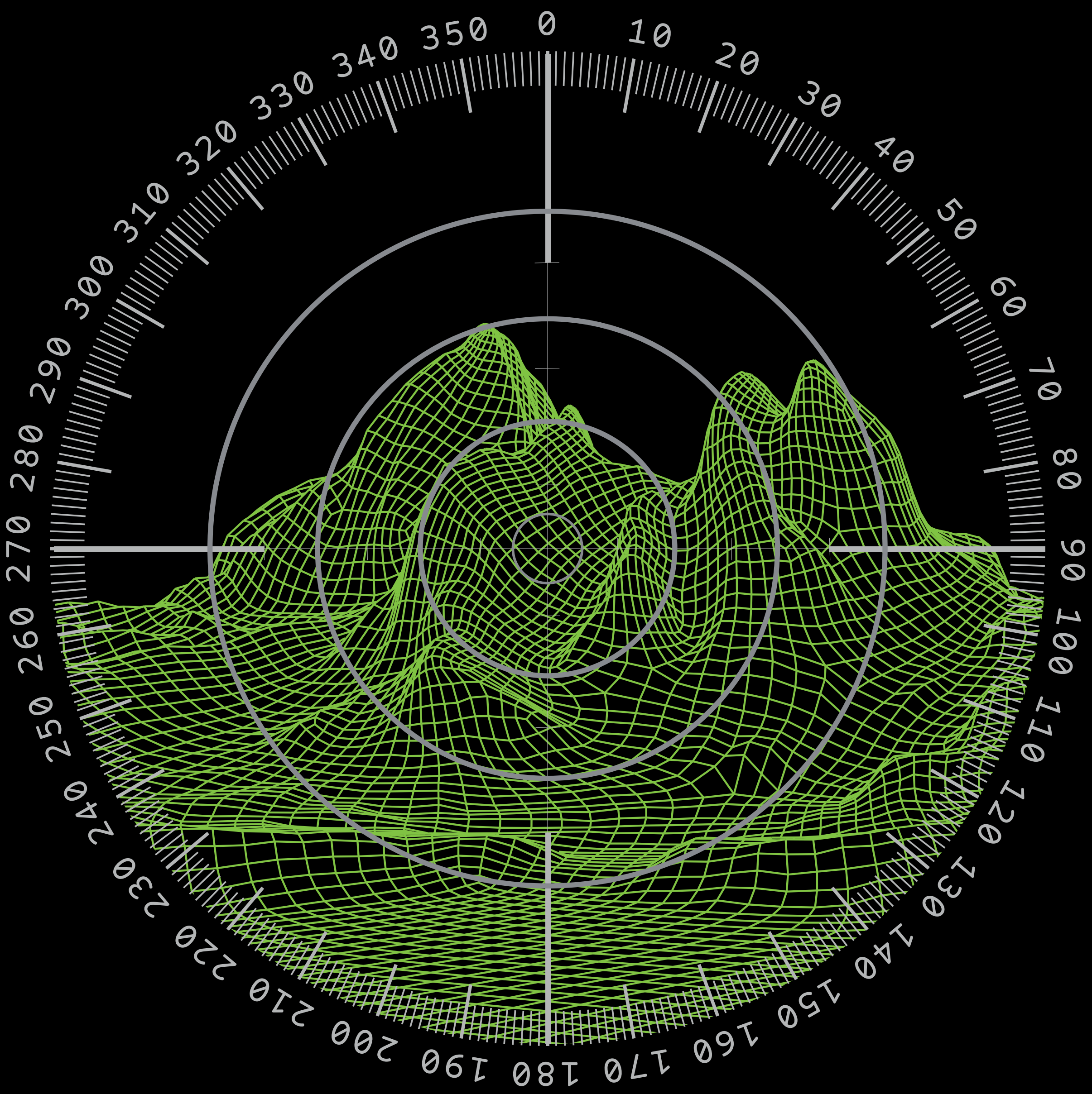


CEE NPL markets on the peak?

Strong dynamics with shifting focus

January 2018

Contents

Foreword

2016 was a record year in terms of non-performing loan portfolio disposals with just over EUR 7bn face value of completed deals in the CEE region, and 2017 also saw strong NPL sales activity. Given that distressed assets in the UK and Irish markets are exhausting and were negatively impacted by the Brexit, NPL investors' focus turned towards the Mediterranean (Italy, Spain and Portugal and also Greece) and CEE regions. As a result, the number of distressed asset transactions increased rapidly in the aforementioned geographies in 2016-17. Besides this, the improving economic environment and property market conditions also gave a considerable impetus to NPL markets.

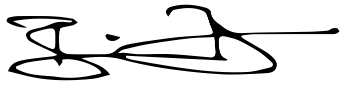
Based on our discussions with banking leaders, three main global trends prevail in the banking industry. Besides the consolidation of the banking sector (non-core exits, economies of scale, acquisitions growth) and the digital transformation triggered mainly by Fintech companies, deleveraging is still on the financial institutions' agenda. The sale of NPL portfolios is still one of the core elements of the deleveraging activity, and despite active portfolio cleaning in the past years, there are still considerable amounts of NPLs in the balance sheets of European banks. The average NPL rate of the CEE region is still above the EU average. Following the disposal of sizeable non-performing corporate portfolios, many investors turned their interest towards retail mortgages.

With a number of corporate NPL transactions being completed in the past years, supply of new corporate NPL portfolios to be sold by banks has visibly decreased recently. As a result, investors turned their interest towards retail mortgages in 2016. Hungary is an outstanding example of the surging retail NPL market, with multiple sizeable deals in 2016 and 2017. The declining supply of unsecured NPLs resulted in increasing prices, the secondary NPL transaction markets are reviving, and activity is expected to further increase in the forthcoming years. Activity of NPL markets in CEE is expected to subside in 1-2 years, as incumbent banks will wind down their existing NPL volumes to sustainable levels, whereas NPL markets of the Mediterranean countries are expected to emerge and attract significant investor focus.

One element that curbed the pace of deals in 2017 was the intensifying regulatory load on potential NPL sellers. Banks need time to internally deal with ECB's new guidelines on NPL recognition and disposal strategy, the forthcoming adoption of IFRS 9 standards as well as the European Banking Authority's 2017 transparency exercise.

As investors are acquiring more and more experience in NPL markets of core CEE countries, their comfort and confidence grow, thus they might also open to new, more challenging markets as well. Therefore, in our 2017 study we cover two additional countries, Ukraine and Bosnia and Herzegovina. Due to the economic and political crisis in 2014-2015 in Ukraine, the banking sector – among other segments – was hit hard by the consequences of the turbulence, thus significant amounts of distressed assets accumulated in the banking system and NPL levels reached their historical maximum last year. Although NPL ratio has been scaling down in Bosnia and Herzegovina in recent years, it is still above the average reported by the countries covered in this study.

In summary, after active portfolio cleaning and numerous deals completed in CEE in the past years, NPL transaction activity is expected to subside in the coming years. However, market of PL transactions and banking entity deals is perking up in alignment with the long-awaited consolidation of the fragmented CEE banking markets, which is expected to drive regional transaction activity in the upcoming years.



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Key findings

The sale of non-performing assets is still the most common deleveraging option among banking industry players in the CEE region. As UK and Irish debt sales markets mature, the focus of investors turned towards the CEE and Mediterranean regions, giving an impetus to distressed asset transactions.

Non-performing loan portfolio disposals picked up in 2016 with just over EUR 7bn face value of completed deals in the CEE region, and enhanced debt sales market activity continued in 2017. The most active CEE markets with the highest volumes of portfolios sold in recent years were Romania, Hungary, Croatia as well as Slovenia.

While activity in geographies where corporate NPL volumes are still relatively high is expected to rise in 2018, mature markets in terms of corporate NPLs are likely to shift towards mixed and retail mortgage debt sales.

Secondary NPL trade activity is reviving and activity is expected to increase in the forthcoming years. The Romanian NPL market was the first to see secondary trade of NPL portfolios.

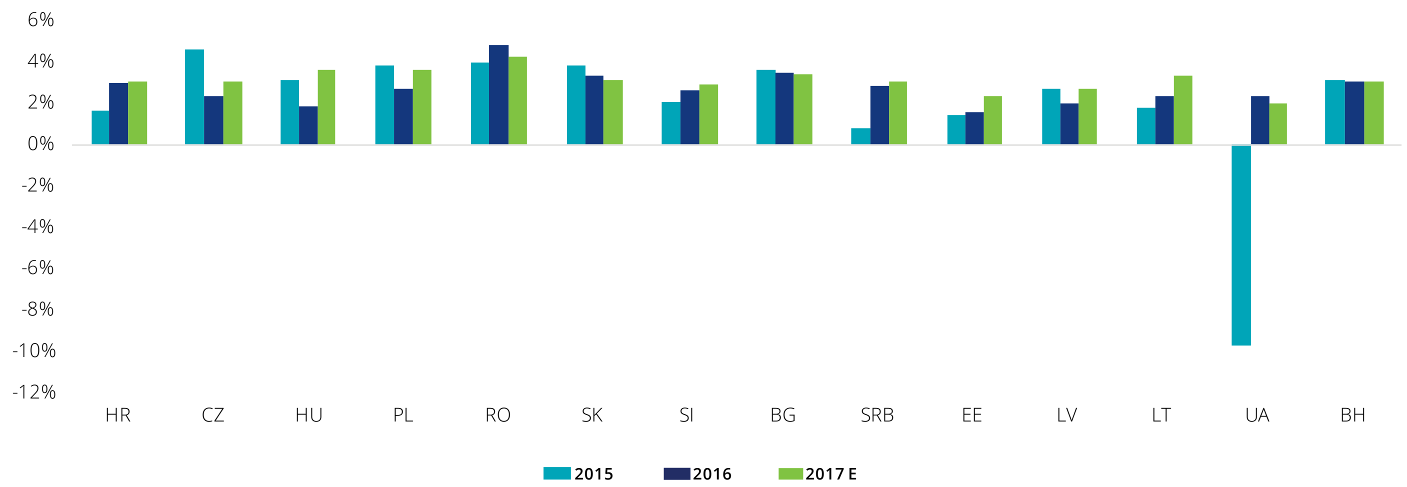
Following the disposal of sizable corporate NPL portfolios, supply of new corporate NPL portfolios to be sold by banks has visibly decreased recently in many countries. Although, corporate NPLs are still the most actively traded loan portfolios, some investors turned their interest towards retail mortgages on the back of improving macroeconomic environment and residential real estate markets, notwithstanding some potential political and reputation risks.

Activity of NPL markets in CEE is likely to gradually subside in the forthcoming years and NPL markets of the Mediterranean countries are expected to emerge and attract more significant investor focus. However, loan portfolio markets in the CEE region that have not seen much activity in recent years are likely to emerge in the forthcoming years, potentially Ukraine and Bosnia and Herzegovina.

In parallel with the slowdown of a few regional NPL markets, performing loan transactions and banking entity deals are likely to perk up on the back of the ongoing consolidation of the fragmented CEE banking markets.

Macroeconomic overview

Figure 1. Changes in real GDP, 2015-2017 (Estimation)



Source: Local national banks, EIU

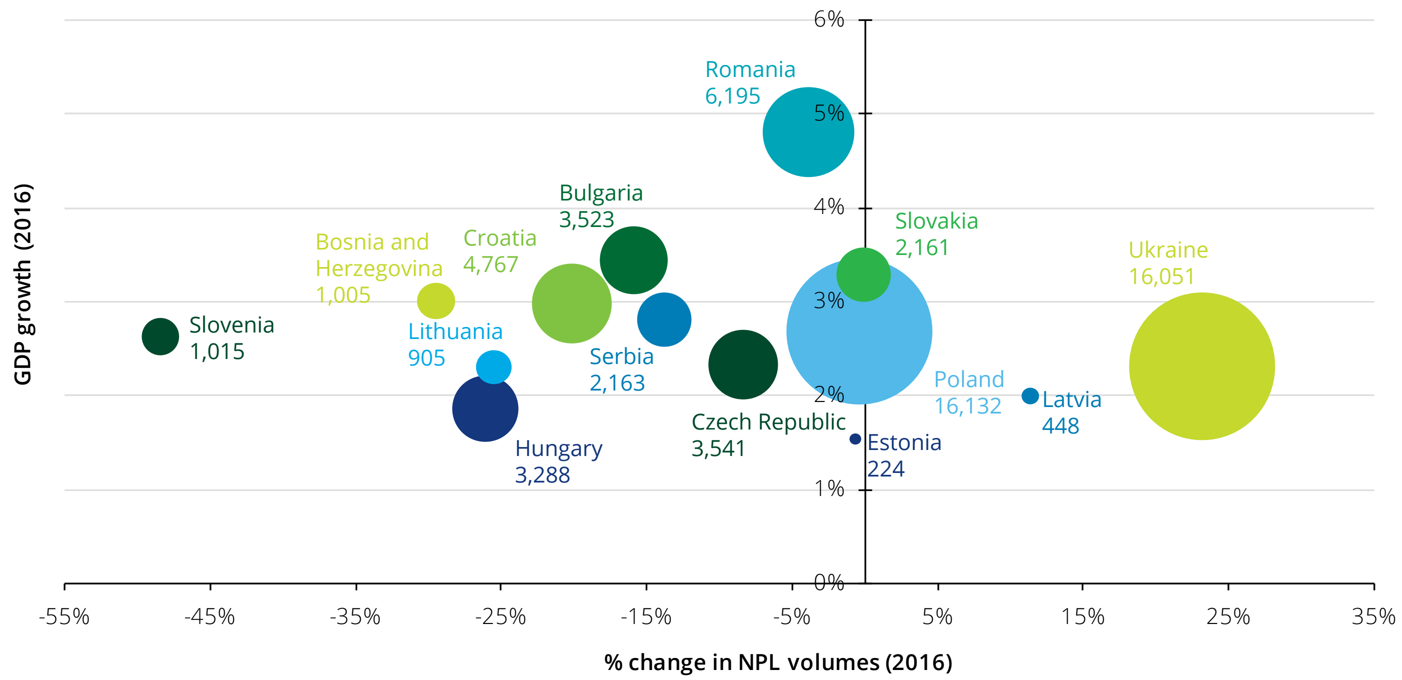
All countries covered in the study had positive GDP growth in 2016. The average GDP growth of the 14 countries improved by 0.8% point to 2.7% in 2016 compared to the previous year, and expected to further increase to 3.1% in 2017. This economic improvement was particularly driven by the increasing domestic demand owing to the tightening labour markets and the wage growth in the majority of the examined countries. Specific country related factors also boosted the upward trend in 2016 like the record tourism year in Croatia or the end of a political and social conflict in Ukraine. In some countries, the decreasing level of EU funds posted a negative effect on the GDP growth for instance in Hungary, in the Czech Republic or in Bulgaria.

Similarly to the previous year, owing to the improved economic conditions, the NPL investors remained active in the CEE region. The continuous investor interest was still matched by the willingness of banks to sell their non-performing portfolios. Judging from the current transaction pipeline, we expect that NPL transaction activity will level off in the CEE region in 2018. It should be noted though that investors' attention can also be shifted to the Mediterranean region due to the massive supply of distressed assets available for sale.

NPL metrics summary

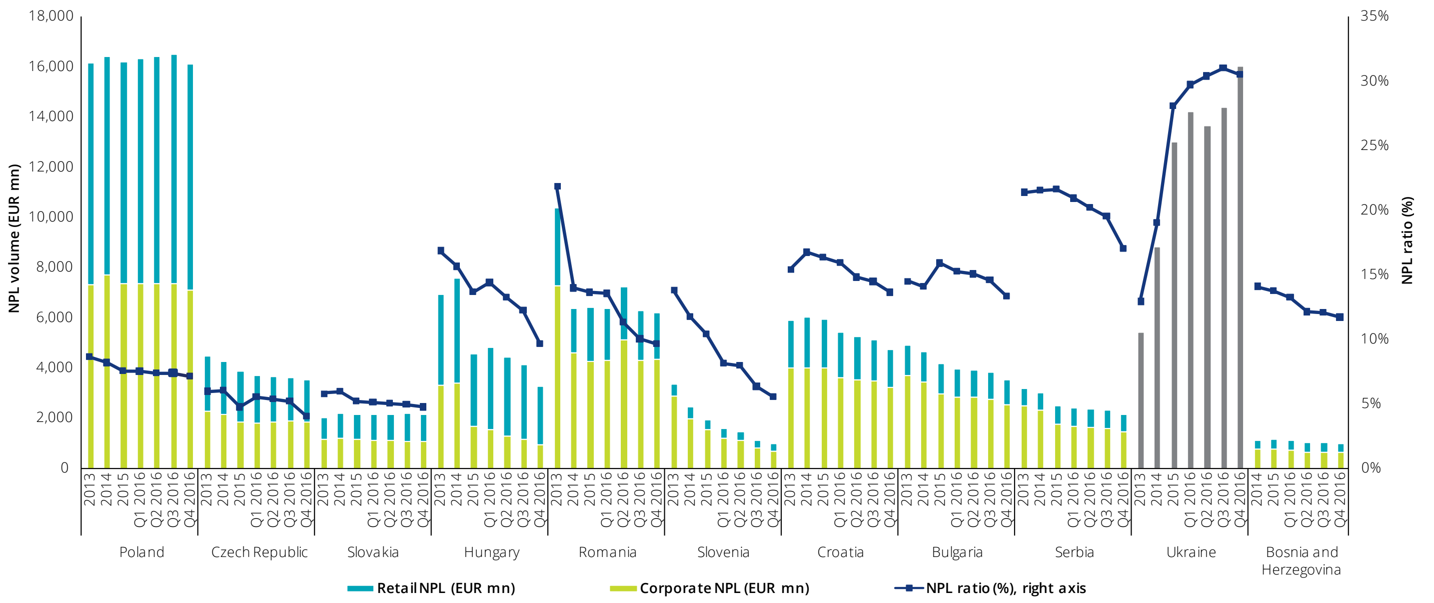
The lending volume tendencies depict a mixed picture among the examined countries, but there are some common factors. Lending activity is boosted by the increasing demand for housing loans in almost all countries. This upward trend in retail lending is the result of the improving labour market conditions as well as the low interest rate environment. Corporate lending was primarily affected by the investment activity of selected countries, such as Croatia, Bosnia and Herzegovina as well as Serbia. The continuously improving asset quality in the CEE region positively contributed to the profitability of the banking sector on the back of the generally recovering credit profiles of both corporate and retail client segments, fueled by the economic upturn. Banks improved their provisioning for NPLs in 2014-2015 and reached a healthy level of provisioning coverage for bad loans in 2016 and managed to even release provisions in 2017. Only three out of the fourteen examined countries reported a decreasing ROE in 2016 compared to 2015.

Figure 2. Evolution of NPL volumes and GDP, Q4 2015 - Q4 2016



Source: Local national banks, EIU
Notes: Bubble size: Q4 2016 NPL volume (EURmn)

Figure 3. Evolution of key NPL metrics, 2013 - Q4 2016



Source: National Banks, Deloitte analysis
Note: Disclosure of NPL volumes and ratios by segments (retail / corporate) is not available until February 2017 in Ukraine. Therefore, total NPL volume is presented.

Table 1. NPL volumes and ratios, Q4 2016

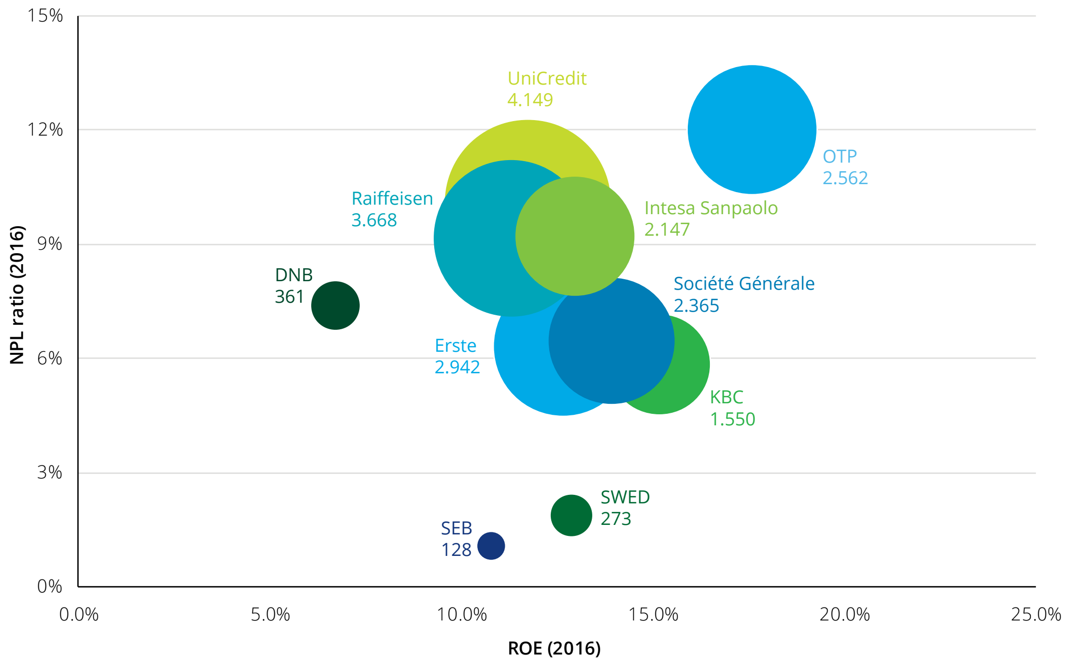
Country	Corporate (EUR mn)	Corporate NPL ratio (%)	Retail (EUR mn)	Retail NPL ratio (%)	Total (EUR mn)	Total NPL ratio (%)
Poland	7,126	9.1%	9,006	6.1%	16,132	7.1%
Czech Republic	1,860	5.2%	1,681	3.2%	3,541	4.0%
Slovakia	1,077	6.5%	1,084	3.7%	2,161	4.7%
Hungary	948	5.3%	2,340	14.3%	3,288	9.6%
Romania	4,350	19.0%	1,845	7.4%	6,195	9.6%
Slovenia	694	7.5%	320	3.5%	1,015	5.5%
Croatia	3,220	25.1%	1,547	10.3%	4,767	13.6%
Bulgaria	2,569	15.1%	954	10.0%	3,523	13.3%
Serbia	1,458	17.2%	705	10.0%	2,163	17.0%
Estonia	119	1.6%	53	0.7%	172	0.9%
Latvia	172	2.2%	275	4.9%	448	4.4%
Lithuania	505	6.2%	400	4.8%	905	3.7%
Ukraine	n/a	n/a	n/a	n/a	16,051	30.5%
Bosnia and Herzegovina	653	15.3%	352	8.6%	1,005	11.7%
Total	**24,099**		**20,210**		**61,366**	

Source: National banks, Deloitte analysis
Note: Estonia NPL ratio is based on DPD 60
Disclosure of NPL volumes and ratios by segments (retail / corporate) in Ukraine is not available until February 2017.

Following the massive reduction of NPL stocks in 2015, Slovenia's banking sector managed to further improve credit quality in 2016. Increased restructuring activity, acceleration of write offs and the sale of non-performing portfolios all contributed to a healthy level of NPL ratio (5.5%). Slovenia's NPL volume almost halved from EUR 2bn to EUR 1bn from 2015 to 2016. Besides Slovenia, Hungary also reported a decrease in NPL volumes of around 25% in 2016 mostly due to active NPL portfolio sales. Total NPL volume of the Ukrainian banking sector increased by 23% in 2016 compared to 2015 and is expected to further increase in 2017, primarily due to the introduction of a new definition of NPLs which was adopted in June 2016 and came into full effect as of January 2017. The new regulation aimed to measure and mitigate credit risk associated with non-performing exposures and bring Ukraine close to the common global standard for the definition on NPLs. The Ukrainian banking sector is heavily contaminated with distressed assets accumulated since the economic and political crisis.

Although the North-South CEE divergence remained in 2016 in terms of NPL volumes and ratios, signs of recovery are undisputedly visible in case of many countries belonging to the South region. Particularly NPL ratios of Hungary, Romania and Slovenia have been inching down at an accelerated pace. All of the three countries reported NPL ratios under 10% at the end of 2016 while Slovenia's former outstandingly high NPL ratio decreased to 5.5%. NPL ratios of Poland, the Czech Republic and Slovakia are rather stagnating on a relatively low level. The banking sectors of Croatia, Bulgaria and Serbia still have to look for adequate measures to mitigate the NPL problem, as their NPL ratios still exceeded 10% as at end-2016. Ukraine posted the highest NPL ratio among the countries covered in this study in 2016, which is the consequence of the already mentioned political and social turbulence in 2014-2015.

Figure 4. NPL ratio, ROE and NPL volumes of leading banking groups in CEE and Baltic (EUR mn)



Source: Banks' data disclosure, ECB CBD, ISI Emerging Markets, Deloitte analysis
Notes: Bubble size: Q4 2016, NPL volume (EUR mn)
SWED, SEB, DNB metrics are based on impaired loans as no NPL metrics are available

Considering the twelve countries covered in last year's edition of the study, total NPL volume experienced a considerable decrease from EUR 51bn in 2015 to EUR 44.3bn in 2016 excluding Ukraine and Bosnia and Herzegovina. The decrease was mainly driven by Hungary, Slovenia and Croatia but Bulgaria and Serbia also contributed to the downward trend. Hungary, Romania and Slovenia recorded the highest decrease with regards to the corporate NPL ratio. Hungary also reduced its retail NPL ratio from 17.7% in 2015 to 14.3% in 2016 mainly due to accelerated retail mortgage portfolio disposals.

Figure 4. shows the connection between ROE and NPL ratio for the ten leading banking groups in the CEE and Baltic region. Banking groups reported improving ROE indicators in 2016 as ROEs of the majority of the banking groups stood under 10% in 2015, while in 2016 almost all banks reported ROE above 10%. With regards to portfolio quality, banking groups saw a slight improvement, with NPL ratios being in the range of 6% and 12%. The decrease of the NPL volume of Unicredit group was principally attributable to the sale of the majority stake in the Polish Pekao. The NPL volume of the Polish bank amounted to EUR 1.3bn in 2016.

ROE of OTP group improved considerably in 2016 compared to 2015, posting the highest ROE indicator among the examined banking groups at 17.6%. At the same time, OTP reported a relatively high NPL ratio of 12%, massively affected by the poor portfolio quality of the Ukrainian subsidiary. KBC group managed to preserve its position among the banks with high ROE and low NPL ratio.

Table 2. NPL ratios and volumes in subsidiaries of major banking groups in CEE and the Baltic region

UniCredit subsidiaries in CEE (2016, EUR mn)

	Bank name	Loans	NPL %	NPL vol.
CZ	UniCredit CZ & SK	13,964	3.6%	506
HR	Zagrebacka Banka	8,244	13.8%	1,138
BG	UniCredit Bulbank	5,438	14.0%	761
HU	UniCredit Bank Hungary	3,776	12.7%	479
RO	Unicredit Tiriac	4,457	13.7%	611
SI	UniCredit Banka	1,460	16.4%	239
SRB	UniCredit Banka	1,772	11.6%	205
BH	UniCredit Bank d.d. Sarajevo	1,576	10.7%	168
BH	UniCredit Banka a.d. Banja Luka	474	8.5%	40
	Total	41,160	10.1%	4,149

Erste Group subsidiaries in CEE (2016, EUR mn)

	Bank name	Loans	NPL %	NPL vol.
CZ	Ceska Sporitelna	18,752	3.2%	600
SK	Slovenska Sporitelna	10,395	4.5%	468
RO	BCR	6,541	11.7%	765
HR	Erste & Steiermarkische	6,285	11.2%	704
HU	Erste Bank Hungary	3,435	9.9%	339
SRB	Erste Bank	731	7.1%	52
BH	Sparkasse Bank d.d. BiH	477	9.8%	14
	Total	46,616	6.3%	2,942

KBC subsidiaries in CEE (2016, EUR mn)

	Bank name	Loans	NPL %	NPL vol.
CZ	CSOB	10,005	2.5%	252
HU	K&H	3,945	9.8%	387
SK	Ceskoslovenska Obchodna	5,002	2.4%	119
CZ	Hypotechni Banka	n/a	n/a	n/a
CZ	Českomoravská Stavební	4,326	2.1%	93
BG	CIBANK	913	11.2%	102
BG	United Bulgarian Bank	2,312	25.8%	598
	Total	26,504	5.8%	1,550

Raiffeisen subsidiaries in CEE (2016, EUR mn)

	Bank name	Loans	NPL %	NPL vol.
PL	Raiffeisen Bank Polska	7,286	8.3%	605
SK	Tatra Banka	8,543	3.5%	299
CZ	Raiffeisen Bank	7,872	2.5%	197
HU	Raiffeisen Bank	2,992	13.8%	412
RO	Raiffeisen Bank	4,489	8.3%	373
HR	Raiffeisenbank Austria	2,484	15.7%	390
BG	Raiffeisen Bank	2,161	6.5%	140
SRB	Raiffeisen Banka	1,151	9.7%	112
BH	Raiffeisen BANK d.d. BiH	1,174	12.1%	142
UA	Raiffeisen Bank Aval	1,906	52.4%	998
	Total	40,058	9.2%	3,668

Société Générale subsidiaries in CEE (2016, EUR mn)

	Bank name	Loans	NPL %	NPL vol.
CZ	Komercní Banka	19,831	2.5%	496
RO	BRD	6,804	12.9%	878
HR	Splitska Banka	2,359	15.0%	354
SI	SKB Banka	1,748	8.9%	156
BG	Soc. Gén. Expressbank	1,999	5.7%	114
SRB	Société Générale Banka	1,291	12.5%	161
PL	Eurobank	2,584	8.0%	207
	Total	36,617	6.5%	2,365

OTP Group subsidiaries in CEE (2016, EUR mn)

	Bank name	Loans	NPL %	NPL vol.
HU	OTP Hungary	8,425	9.8%	826
BG	DSK Bank	3,716	11.5%	426
HU	OTP Jelzálogbank Zrt.	3,134	1.9%	60
HR	OTP Banka Hrvatska	1,521	12.1%	184
SK	OTP Banka Slovensko	1,255	11.2%	140
RO	OTP Bank Romania	1,693	17.4%	295
SRB	OTP Bank Srbja	351	32.7%	115
UA	OTP Ukraine	1,232	41.9%	516
	Total	21,327	12.0%	2,562

Intesa Sanpaolo subsidiaries in CEE (2016, EUR mn)

	Bank name	Loans	NPL %	NPL vol.
SK	VUB	10,081	5.3%	535
HR	Privredna Banka Zagreb	5,026	15.9%	799
HU	CIB	2,828	10.3%	290
SRB	Banca Intesa	2,452	12.5%	305
RO	Intesa Sanpaolo Romania	623	8.2%	51
SI	Banka Koper	1,625	6.8%	111
BH	Intesa Sanpaolo Banka, d.d. BiH	653	8.4%	54
	Total	23,288	9.2%	2,147

Swedbank subsidiaries in Baltic (2016, EUR mn)

	Bank name	Loans	NPL %	Imp. loan vol.
EE	SWED	6,822	1.8%	120
LV	Swedbank	3,189	2.2%	70
LT	Swedbank, AB	4,607	1.8%	84
	Total	14,618	1.9%	273

DNB subsidiaries in Baltic (2016, EUR mn)

	Bank name	Loans	NPL %	NPL vol.
EE	DNB	534	3.7%	20
LV	DNB banka	1,497	8.6%	129
LT	AB DNB bankas	2,844	7.4%	212
	Total	4,875	7.4%	361

SEB subsidiaries in Baltic (2016, EUR mn)

	Bank name	Loans	NPL %	NPL vol.
EE	SEB	4,225	0.6%	25
LV	AB SEB bankas	2,534	1.3%	32
LT	AB SEB bankas	4,941	1.4%	71
	Total	11,699	1.1%	128

Source: Banks' data disclosure, ECB CBD, ISI Emerging Markets, Deloitte analysis
Note: NPL % and NPL volume for Swedbank, DNB and Skandinaviska Enskilda Banken subsidiaries are based on impaired loans

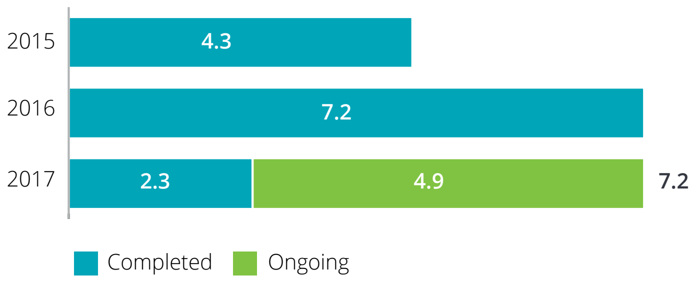
Recent transactions

NPL market activity gained momentum in 2015 and further increased in 2016 as the face value of selected completed deals, based on publicly available deal information[1], amounted to EUR 7.2bn in 2016. Figure 5. shows that only a few transactions reached the completion phase in 2017 and the volume of ongoing transactions as of October 2017 amounted to a massive EUR 4.9bn with a main focus on Romania where large-scale portfolios are offered for sale.

Many corporate NPL portfolios were transacted in 2015 and 2016 but this type of distressed assets are expected to subside within 1-2 years. Consequently, regional and certain international investors started to show interest towards retail mortgage portfolios in certain countries in 2016 and 2017. Transacted residential real estate backed portfolios amounted to EUR 0.8bn in 2016 and EUR 0.4bn up to October 2017, with many already ongoing transactions and more expecting to be launched soon.

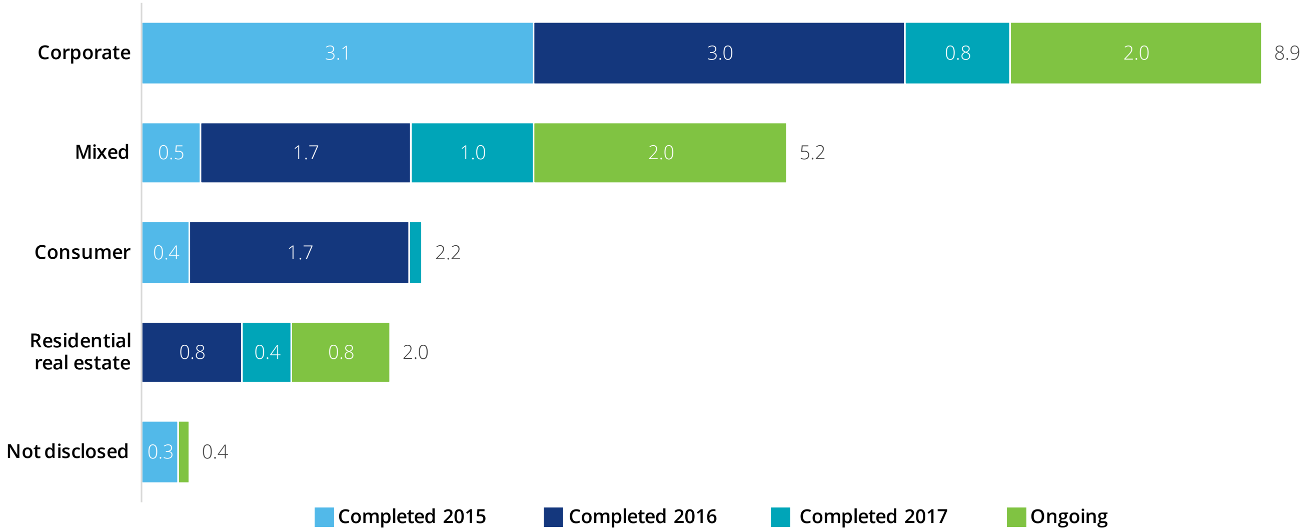
The busiest markets in the CEE region by October 2017 in terms of deal face value were Romania, Hungary, Croatia as well as Slovenia. Romania has seen EUR 4.1bn of deals completed by October 2017 from 2015, meanwhile completed deals amounted to EUR 2.7bn in Hungary by October 2017. In 2017, the most active market for distressed debt was Croatia with EUR 1.0bn of completed deals where dominantly corporate portfolios have been transacted.

Figure 5. Activity by year - CEE (EUR bn)



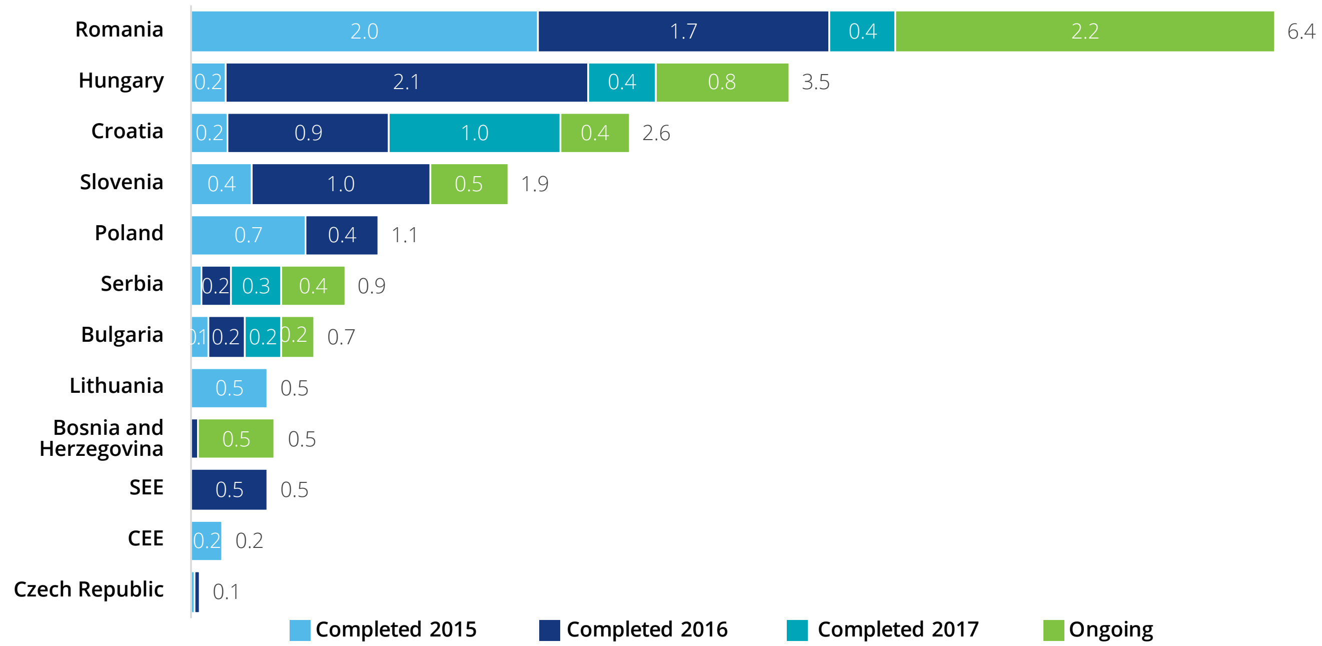
Source: Deloitte Intelligence, October 2017

Figure 6. Activity by asset class - CEE, 2015 - 2017 (EUR bn)



Source: Deloitte Intelligence, October 2017

Figure 7. Activity by country - CEE, 2015 - 2017 (EUR bn)



Source: Deloitte Intelligence, October 2017

The scale of completed and ongoing sales activity reflects that most of the countries are committed to tackle the challenges related to the distressed debts in the CEE region. Judging from the recent pipeline, we expect that further portfolios will be offered for sale in 2018. In our opinion, 2018 is going to be an active year in the regional NPL market with the closure of several ongoing deals and a few new transactions.

1: Please note that all figures and charts are based on publicly available deal information, therefore the actual market activity might differ.

NPL market outlook – shifting investor focus

There are some typical aspects an international investor interested in distressed assets takes into account when considering to enter a new market. The typical ticket size / equity cheque is between EUR 25-50mn for an international investor. Future deal flow is also key for them investing time and money to perform diligence on the country. As for the regional players, smaller packages can be of interest as well (with c. EUR 100-150mn gross book value consisting of around 3,000-4,000 loans). Nevertheless, none of the investors prefer small pilot packages aiming to pre-test market appetite as they search for real, efficient processes given the heavy resources they have to use for such transactions.

As investors commit significant resources, they are seeking solid and real transaction processes managed by reputable advisors in a transparent and professional manner with regards to all the timeline, coordination of due diligence process as well as the transaction execution. Based on feedback from investors, a committed seller is also of high importance to them limiting the execution risk of the transaction.

Portfolio composition is a very important aspect for every potential investor as erroneously packaged portfolios (e.g. consisting of different types of assets or multi-country portfolios) is likely to have negative effects on pricing and transaction efficiency. They are keen on understanding the portfolio selection methodology so they can see based on what principles the cases were selected.

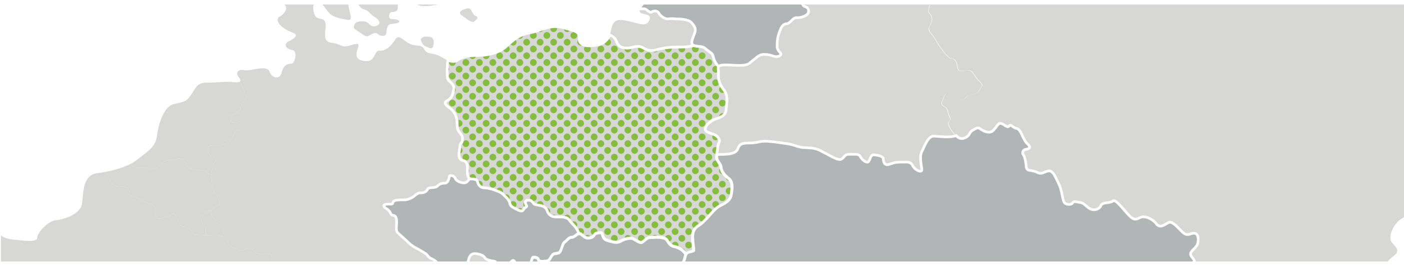
International investors typically prefer concentrated corporate secured portfolios as they are easy to diligence (therefore lower risk) and also enables a focused servicing thanks to the limited number of assets underlying the portfolio.

The improving macroeconomic environment in the CEE region increased the disposable income of the households and also had a positive impact on the growth of employment rate in the past few years. The residential real estate market is prosperous, prices increased back to pre-crisis levels. Due to the aforementioned market conditions as well as the fact that corporate NPL portfolio pipeline is narrowing down in the CEE region, residential real estate backed portfolios recently became attractive and caught the attention of NPL investors.

However, retail mortgage portfolios are generally highly granular and have a geographically diverse collateral base. Inherent reputational risks are also among the reasons that made this segment less attractive for NPL investors before 2017. NPL investors also may face some more challenges when buying a real estate mortgage portfolio compared to a corporate portfolio. They require a suitable servicing partner to manage the portfolio post acquisition. When considering retail mortgage portfolios, investors need to be more mindful of the local regulatory and political environment, as well as consumer protection considerations, including debtor rescue schemes, eviction related regulations and similar government and regulatory measures, which could have a significant impact on the portfolio as well as the potential future recovery.

Nevertheless, there are investors on the market who have already developed cooperation with a debt servicing partner and grouped in a consortium. Although the number of debt servicers with an appropriate track record of dealing with retail mortgages is still limited. Some of the former unsecured portfolio servicers and/or investors also shifted towards retail mortgages as the pipeline of unsecured consumer loans is gradually narrowing down. As a result, they are likely to reallocate their resources, retrain their employees or expand their existing profile. Competitive landscape is quite intense in certain countries, like in Hungary with many completed retail mortgage transactions and deals currently under negotiation.

So while activity in geographies where non-performing corporate loan volumes are still relatively high (e.g. Adriatic region) is expected to rise in 2018, mature markets in terms of corporate NPLs are likely to shift towards mixed and retail mortgage debt sales. New markets in the CEE region that have not seen much activity in recent years are likely to emerge in the forthcoming years, potentially Ukraine and Bosnia and Herzegovina. Secondary market transactions are also expected to emerge in 2018, especially in countries that saw an early debt sales market development (e.g. Romania).



Poland

Total NPL ratio of the Polish banking sector stood at 7.1% as of year-end 2016 which was a reduction of 0.4% point compared to 2015. “Repolonization” of the banking sector continued in 2016, the market share of foreign-owned banks decreased to 55%.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	3.3%	3.8%	2.7%	-1.1%
Consumer prices (% change pa)	0.1%	-0.9%	-0.7%	0.2%
Recorded unemployment (%)	12.3%	10.5%	9.0%	-1.5%
Budget balance (% of GDP)	-1.7%	-2.4%	-2.5%	-0.1%
Public debt (% of GDP)	43.9%	44.7%	48.4%	3.7%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	132,856	141,614	148,836	5.1%
Corporate loans (EUR mn)	68,223	73,909	78,196	5.8%
Interest rates				
Lending (%)	6.3%	4.9%	4.7%	-0.2%
Deposit (%)	2.5%	1.9%	1.6%	-0.3%
NPL volumes				
Retail NPLs (EUR mn)	8,686	8,822	9,006	2.1%
Corporate NPLs (EUR mn)	7,727	7,373	7,126	-3.3%
NPL ratios				
Retail NPL ratio (%)	6.5%	6.2%	6.1%	-0.2%
Corporate NPL ratio (%)	11.3%	10.0%	9.1%	-0.9%
Key ratios				
CAR (%)	15.0%	15.6%	17.5%	1.9%
ROE (%)	9.5%	7.7%	7.5%	-0.2%
ROA (%)	1.0%	0.8%	0.8%	0.0%
CIR (%)	52.9%	60.2%	57.6%	-2.6%
L/D (%)	104.8%	102.5%	98.0%	-4.5%
FX share of lending (%)	31.0%	29.0%	27.0%	-2.0%
Coverage ratio (%)	n/a	n/a	n/a	n/a

Source: EIU, NBP, ECB CBD

Slowing growth with deflationary environment

After real GDP growth of 3.8% in 2015, the growth decelerated to 2.7% in 2016 due to falls in construction and investment activity. The main driver of the GDP growth was the higher consumer spending in the persistent deflationary environment. Despite growing domestic demand, deflation started in 2015 continued, consumer prices decreased by 0.7% in 2016. Recorded unemployment also decreased from 10.5% to 9.0% in 2016.

Increasing retail and decreasing corporate NPL volume

Both retail and corporate lending posted substantial growth in 2015 and this upward trend continued in 2016, however at a slower pace. The strong growth of credit demand was still mainly driven by low interest rates, steady economic growth and improvements in the labour market.

The volume of retail non-performing loans increased by 2.1% in 2016, however in the corporate segment NPL volumes decreased by 3.3%. Retail and corporate NPL ratios decreased slightly by 0.2% point and 0.9% point respectively, following previous years’ trends. According to NBP, the improvement and relatively low loan losses were supported by the development of the real sector’s financial situation (increasing incomes and lower unemployment, increasing profitability and liquidity of the enterprises).

According to NBP’s Financial Stability Report, quality of loans to households improved somewhat and the improvement was mainly seen at commercial banks. Despite this trend, quality of loans to households remained on average better at cooperative banks (except for large cooperative banks) than commercial banks.

After excluding one-off effects, the profitability of banks declined in 2016

The capital position of the Polish banking system is sufficient, CAR of the Polish banking sector further improved by 1.9% point to 17.5% in 2016. The profitability of the financial sector was positive in 2016, although ROE decreased by 0.2% point to 7.5%, whilst ROA stagnated at 0.8%. According to NBP, besides the decline of the profitability (excluding one-off effects), the major determinants of bank’s profitability were the tax on assets, an increase in net interest margin, a fall of non-interest margin and a reduction of personnel costs (associated with employment reductions in the banking sector). The burden of credit risk costs on banks’ earnings has not changed substantially compared to the previous year. CIR decreased from 60.2% to 57.6% in 2016, largely because of the overall increase in non-interest margins, although there was a rise in operating costs due to the introduction of tax on certain financial institutions.

"Repolonization" continued with the PZU's acquisition of 32.8% share in Pekao from Unicredit

Total NPL ratio of the Polish banking sector slightly improved in 2016, from 7.5% (2015) to 7.1%.

The lowest NPL ratio was posted by ING BSK with a level of 2.2%, followed by Alior Bank S.A. with 3.3%. In 2016, none of the top 10 banks were loss-making, with the majority having ROE around 10% other than Getin, BGZ and Raiffeisen (similarly to 2015).

The major change in ownership structure among the Polish banks related to Pekao. After selling 10% from its stake, UniCredit sold another 32.8% share in Pekao to the state-owned Polish insurance group PZU (20%) and to the Polish Development Fund (12.8%) in December 2016. The agreed purchase price was PLN 123 per share (total transaction value amounted to approx. EUR 2.5 bn). The aim of the sale was to boost UniCredit's tier 1 capital ratio by about 55 basis points, according to the bank. UniCredit also plans to sell its remaining 7.3% stake in the open market.

In November 2016, Alior Bank completed the transaction to acquire Bank BPH SA's core business from GE Capital Corporation. The acquisition excludes the entire mortgage portfolio, which remained with GE. With this transaction, Alior strengthened its position in the market, and increased its customer base to 3.3mn. The sale is also in line with the strategy of GE to focus on its core industrial businesses.

In April 2016, PZU acquired 25.26% stake in Alior Bank. Owing to the transaction, the state-owned PZU managed to create a platform to consolidate the domestic banking sector and to attain a leading position. PZU also intended to buy Raiffeisen Bank Polska, but in the end the deal was not agreed. Raiffeisen Bank Polska is going to debut on the WSE with an IPO of 15% of shares.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	**PKO**	61,699	43,104	7,367	653	1.1%	8.9%	6.0%	2,594	State
2	**Pekao**	38,650	21,929	5,037	515	1.3%	10.2%	6.0%	1,316	PZU (State)
3	**BZ WBK**	29,706	24,476	4,302	471	1.6%	10.9%	6.6%	1,611	Santander
4	**mBank**	28,982	19,178	2,944	276	1.0%	9.4%	5.4%	1,036	Commerzbank
5	**ING BSK**	25,662	17,089	2,327	273	1.1%	11.7%	2.2%	382	ING
6	**BGŻ BNP Paribas S.A.**	15,909	10,567	1,384	11	0.1%	0.8%	6.4%	681	BNP Paribas
7	**Millennium**	15,460	9,445	1,524	148	1.0%	9.7%	4.5%	425	BCP
8	**Getin Noble**	15,117	11,361	1,159	25	0.2%	2.2%	9.0%	1,022	Leszek Czarnecki
9	**Alior Bank S.A.**	13,836	10,493	1,407	143	1.0%	10.2%	3.3%	343	PZU (State)
10	**Raiffeisen Bank Polska**	12,040	7,286	1,440	37	0.3%	2.6%	8.3%	605	Raiffeisen
	Banking sector total	**387,517**	**227,032**	**41,372**	**3,100**	**0.8%**	**7.5%**	**7.1%**	**16,132**	

Source: Banks' data disclosure, NBP, ECB CBD, ISI Emerging Markets

Czech Republic

Already enviable NPL ratio improved further in 2016, mostly due to a substantial increase of corporate and retail loans.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	2.0%	4.6%	2.3%	-2.3%
Consumer prices (% change pa)	0.4%	0.3%	0.7%	0.4%
Recorded unemployment (%)	7.7%	6.2%	5.2%	-1.0%
Budget balance (% of GDP)	-1.9%	-0.6%	0.6%	1.2%
Public debt (% of GDP)	43.3%	40.3%	36.7%	-3.6%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	45,452	48,986	52,531	7.2%
Corporate loans (EUR mn)	32,377	32,712	36,123	10.4%
Interest rates				
Lending (%)	4.6%	4.3%	3.9%	-0.4%
Deposit (%)	0.7%	0.5%	0.4%	-0.1%
NPL volumes				
Retail NPLs (EUR mn)	2,151	1,994	1,681	-15.7%
Corporate NPLs (EUR mn)	2,142	1,871	1,860	-0.6%
NPL ratios				
Retail NPL ratio (%)	4.7%	4.1%	3.2%	-0.9%
Corporate NPL ratio (%)	6.6%	5.7%	5.2%	-0.5%
Key ratios				
CAR (%)	17.8%	18.4%	18.5%	0.1%
ROE (%)	16.6%	16.3%	17.5%	1.2%
ROA (%)	1.7%	1.7%	1.7%	0.0%
CIR (%)	47.7%	48.6%	48.2%	-0.4%
L/D (%)	76.7%	79.0%	78.0%	-1.0%
FX share of lending (%)	19.0%	19.0%	20.0%	1.0%
Coverage ratio (%)	55.9%	54.8%	56.3%	1.5%

Source: EIU, CNB, ECB CBD

GDP growth halved in 2016, but budget balance turned positive

The Czech economy grew by 2.3% in 2016 following an outstanding real GDP growth of 4.6% in 2015. This is mainly attributable to the decreasing investment activities and the transition of EU funding periods. As in 2015, domestic consumption and foreign trade remained the main economic drivers in 2016. Recorded unemployment rate decreased from previous year's 6.2% to 5.2% in 2016. Budget balance in 2016 resulted in a positive ratio of 0.6%, and public debt also decreased significantly by 3.6% points to 36.7%.

Significant increase in lending volume with remarkable retail NPL reduction

Similar to previous years, retail and corporate loans increased steadily by 7.2% and 10.4% respectively in 2016, triggered mainly by the low interest rate environment and improving economic conditions. NPL volumes declined significantly by 15.7% in the retail segment and by 0.6% in the corporate sector partially resulted from write-offs. As a result of the increasing loan base, NPL ratios decreased further in 2016, with corporate NPL ratio melting from 5.7% to 5.2%, and retail NPL ratio from 4.1% to 3.2%. Although economic and lending conditions are favorable, the Czech National Bank is examining possible threats and has already introduced regulations and recommendations with the aim of mitigating potential risks stemming from accelerated lending. A countercyclical capital buffer (CCB) was introduced in 2017, and will be effective from 1st January 2018 at a level of 0.5% of total risk exposures of all banks operating in the Czech Republic. Both retail and corporate lending increased in 2016 as banks are operating in a relatively low interest rate environment and they are focusing more on increasing volumes to offset the effect of low interest margins. This upward trend in lending might lead to a rise in NPL metrics in the long/mid-term future.

Profitability of the banking sector remained high

The Czech banking industry is in a strong position to withstand external shocks with a CAR stabilizing at 18.5% in 2016.

The ROE indicator increased by 1.2% point and stood at 17.5% at the end of 2016, which is the highest ROE among CEE countries. Increasing profitability was affected by the one-off effect of the sale of the selected banks' stake in VISA Europe (accounting for 4% points of the net profit growth). According to the Czech National Bank, profitability growth was mainly flat among large banks, the growth mostly came from the medium-sized banks. Despite the profit growth, there is a downward trend both in interest and commission income in the Czech banking sector, but banks managed to offset it with cost-cutting.

Cost/income ratio decreased slightly to 48.2%. Although volume of outstanding loans increased significantly, L/D ratio decreased slightly by 1.0 % point due to the continuous increase of deposits.

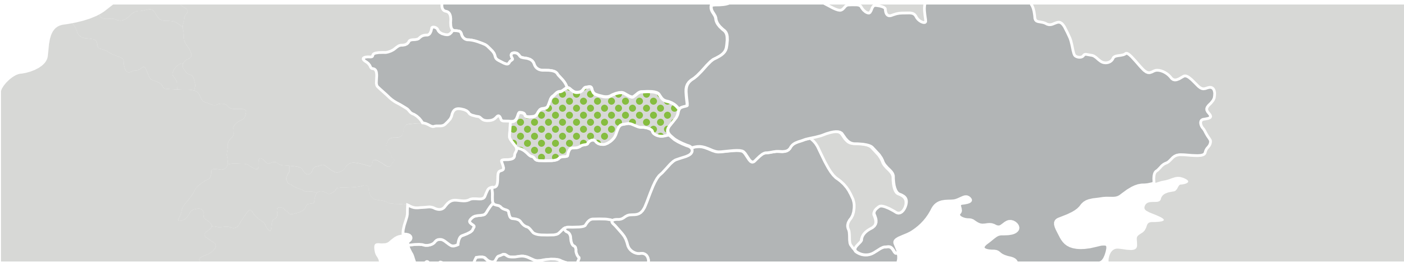
Only one bank out of the top ten banks in the Czech Republic has NPL ratio over 5%

Starting from 1st May 2016, GE Money Bank operates under the name MONETA Money Bank in the Czech Republic. With this rebranding they aimed to have a more clearly recognizable identity as a Czech banking institution. Asset quality is outstanding in regional comparison, with NPL ratios in the top ten under 5%, the only exception being MONETA Money Bank with 6.3%. There is a significant gap between the first three market players compared to the remaining banks with regards to their market share: CSOB has 17.5%, Ceska Sporitelna has 16.6%, and Komercní Banka has 14.4%, whereas the fourth largest UniCredit has 8.2% of the total market. Nine out of the top ten banks have foreign owners, only the tenth largest PPF Banka is in domestic control.

In March 2016, Raiffeisen completed acquisition of the consumer banking business of Citibank Europe plc in the Czech Republic. The transaction included Citibank's retail banking and card businesses.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	CSOB	38,992	10,005	3,011	575	1.5%	19.1%	2.5%	252	KBC
2	Ceska Sporitelna	36,972	18,752	4,291	537	1.5%	12.5%	3.2%	600	Erste
3	Komercní Banka	32,126	19,831	3,443	523	1.6%	15.2%	2.5%	496	Société Générale
4	UniCredit Bank CZ & SK	18,284	13,964	1,926	174	1.0%	9.0%	3.6%	506	UniCredit
5	Raiffeisen Bank	11,779	7,872	928	59	0.5%	6.4%	2.5%	197	Raiffeisen
6	Hypotechni Banka	9,715	n/a	1,265	119	1.2%	9.4%	n/a	n/a	KBC
7	ING Bank	5,840	n/a	FB	25	0.4%	n/a	n/a	n/a	ING
8	MONETA Money Bank	5,561	4,342	1,059	269	4.8%	25.4%	6.3%	277	GE Capital
9	Českomoravská Stavební	5,534	4,326	360	44	0.8%	12.2%	2.1%	93	KBC
10	PPF banka	5,056	1,077	324	45	0.9%	13.9%	4.8%	52	PPF Group N.V.
	Banking sector total	222,521	88,654	21,708	3,799	1.7%	17.5%	4.0%	3,541	

Source: Banks' data disclosure, CNB, ECB CBD, ISI Emerging Markets
FB: foreign branch



Slovakia

Growth in retail (13.4%) and corporate (5.3%) lending in the Slovakian banking sector remained one of the highest among the countries covered by the study. The banking sector is healthy, NPL ratios are low, and profitability is high.

Macro	2014	2015	2016	Change 2015-16 (% point)	
GDP (% real change pa)	2.4%	3.8%	3.3%	-0.5%	
Consumer prices (% change pa)	-0.1%	-0.3%	-0.5%	-0.2%	
Recorded unemployment (%)	12.8%	11.5%	9.5%	-2.0%	
Budget balance (% of GDP)	-2.9%	-2.7%	-1.7%	1.0%	
Public debt (% of GDP)	57.0%	52.5%	51.9%	-0.6%	

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)	
Retail loans (EUR mn)	23,036	25,893	29,361	13.4%	
Corporate loans (EUR mn)	14,389	15,685	16,514	5.3%	
Interest rates					
Lending (%)	3.2%	2.8%	2.6%	-0.2%	
Deposit (%)	0.7%	0.4%	0.3%	-0.1%	
NPL volumes					
Retail NPLs (EUR mn)	995	1,007	1,084	7.7%	
Corporate NPLs (EUR mn)	1,230	1,155	1,077	-6.8%	
NPL ratios					
Retail NPL ratio (%)	4.3%	3.9%	3.7%	-0.2%	
Corporate NPL ratio (%)	8.5%	7.4%	6.5%	-0.9%	
Key ratios					
CAR (%)	17.4%	17.7%	18.2%	0.5%	
ROE (%)	10.3%	11.4%	13.1%	1.7%	
ROA (%)	1.2%	1.3%	1.4%	0.1%	
CIR (%)	56.6%	55.0%	54.9%	-0.1%	
L/D (%)	91.1%	90.9%	95.0%	4.1%	
FX share of lending (%)	0.9%	0.6%	0.6%	0.0%	
Coverage ratio (%)	54.1%	55.7%	n/a	n/a	–

Source: EIU, NBS, ECB CBD

The domestic economy remained strong after the end of the EU funding period in 2016

Although the drawdown of EU funds in 2015 contributed to a solid GDP growth, economic growth slightly dropped to 3.3% in 2016. Owing to the increasing domestic demand through rising employment and increasing nominal wages, GDP is expected to grow further in 2017 by 3.2%.

Household indebtedness doubled in recent years although retail NPL ratio has been decreasing steadily

Similar to previous years, lending volume increased dynamically in 2016, especially in the retail sector by 13.4%. According to the National Bank of Slovakia, household indebtedness has doubled in recent years and became the highest in the region. Due to falling interest rates and improving labour market situation the average stock of loans grew faster than the average wage. Moreover, Slovak households have relatively low savings compared to their debts, which developments are to be monitored cautiously in the coming years.

Both retail and corporate NPL ratios decreased further in 2016 by 0.2% and 0.9% point respectively, and stood at 3.7% and 6.5% as of year-end 2016, posting one of the lowest ratios in the region. According to the NBS, the net default rate of housing loans was around nil, indicating the high quality of this loan segment.

Increased net profit in spite of the significant fall in interest income

ROE of the Slovak banking sector increased by 1.7% point and peaked at 13.1% in 2016. According to the NBS, the profit of the banking sector would have fallen by 15% without the sale of the VISA stake and the extraordinary dividend income of VUB Banka from its leasing subsidiary. The Slovak banks' profitability traditionally relies on the interest income, and there is a significant downward trend in interest income (5.2% decrease compared to 2015), especially in the housing loans segment.

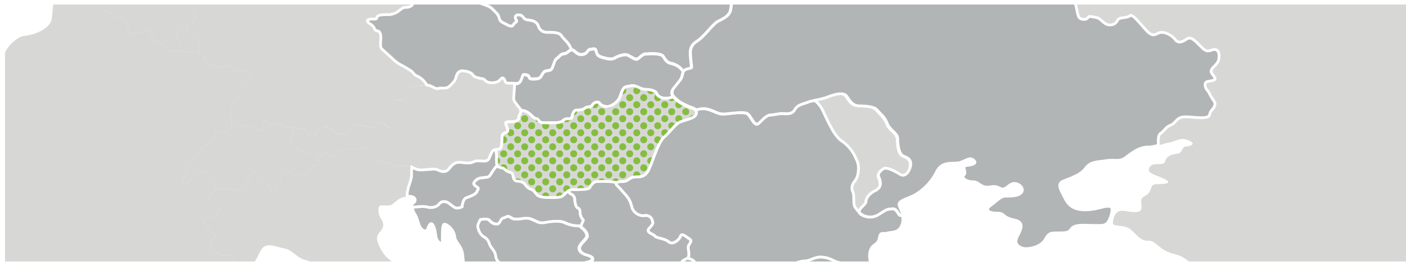
CAR increased by 0.5% point reaching a robust level of 18.2% in 2016. According to the NBS, Slovakian banks have been using excess capital to pay dividends, which resulted in the sector's capital adequacy inching down below the EU median.

The loss-making Sberbank Slovensko merged with Prima Banka in July 2017

All the top 3 banks reported an increasing loan volume and net profit in 2016. As in the previous year, Sberbank Slovensko was loss-making in 2016 too and announced to merge with Prima Banka in 2017, the legal successor is going to be Prima Banka. Based on announcements the merge was mainly driven by the inefficient internal processes and the lack of sufficient client base of Sberbank.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	**Slovenska Sporitelna**	14,801	10,395	1,533	212	1.4%	13.8%	4.5%	468	Erste
2	**VUB**	13,509	10,081	1,444	265	2.0%	18.4%	5.3%	535	Intesa Sanpaolo
3	**Tatra Banka**	11,165	8,543	948	127	1.1%	13.4%	3.5%	299	Raiffeisen
4	**Ceskoslovenska Obchodna**	7,499	5,002	666	78	1.0%	11.7%	2.4%	119	KBC
5	**UniCredit CZ & SK**	5,217	n/a	550	50	1.0%	9.1%	n/a	n/a	UniCredit
6	**Postova Banka**	4,256	2,186	607	49	1.2%	8.1%	13.0%	284	J&T FINANCE
7	**Prva Stavebna Sporitelna**	2,848	2,132	240	20	0.7%	8.3%	4.6%	98	Schwäbisch Hall
8	**Prima Banka Slovensko**	2,150	1,559	146	10	0.5%	6.8%	n/a	n/a	Penta Investments
9	**Sberbank Slovensko**	1,549	n/a	152	-37	-2.4%	-24.3%	n/a	n/a	Sberbank
10	**OTP Banka Slovensko**	1,456	1,255	108	-3	-0.2%	-2.8%	11.2%	140	OTP
	Banking sector total	**73 051**	**45 875**	**7,979**	**1,045**	**1.4%**	**13.1%**	**4.7%**	**2,161**	

Source: Banks' data disclosure, NBS, ECB CBD, ISI Emerging Markets



Hungary

In 2016, Hungary reported one of the highest NPL reductions in the region, retail NPL volume decreased substantially by 19.0% whereas corporate NPL volume decreased by 43.2%, mainly attributable to the significant portfolio cleaning performed in both segments as well as the steadily improving economic conditions.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	3.6%	3.1%	1.9%	-1.2%
Consumer prices (% change pa)	-0.2%	-0.1%	0.4%	0.5%
Recorded unemployment (%)	7.9%	6.8%	5.1%	-1.7%
Budget balance (% of GDP)	-2.8%	-1.6%	-1.9%	-0.3%
Public debt (% of GDP)	76.9%	74.8%	74.1%	-0.7%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	21,704	16,343	16,400	0.4%
Corporate loans (EUR mn)	21,819	17,111	17,797	4.0%
Interest rates				
Lending (%)	4.4%	2.9%	2.1%	-0.8%
Deposit (%)	1.8%	1.1%	0.6%	-0.5%
NPL volumes				
Retail NPLs (EUR mn)	4,162	2,888	2,340	-19.0%
Corporate NPLs (EUR mn)	3,409	1,671	948	-43.2%
NPL ratios				
Retail NPL ratio (%)	19.2%	17.7%	14.3%	-3.4%
Corporate NPL ratio (%)	15.6%	9.8%	5.3%	-4.4%
Key ratios				
CAR (%)	17.0%	19.9%	20.1%	0.2%
ROE (%)	-17.5%	0.3%	12.1%	11.9%
ROA (%)	-1.6%	0.0%	1.2%	1.2%
CIR (%)	65.7%	83.9%	64.9%	-19.1%
L/D (%)	107.0%	87.5%	80.0%	-7.5%
FX share of lending (%)	51.0%	23.0%	22.0%	-1.0%
Coverage ratio (%)	62.6%	69.2%	71.4%	2.2%

Source: EIU, NBH, ECB CBD

Declining EU transfers pushed back GDP growth

After two years of GDP growth over 3%, the Hungarian economy slowed down in 2016, with a GDP growth of 1.9% as a result of the declining level of EU transfers. However, GDP growth is forecasted to accelerate to around 3% in 2017 as the economy is expected to be stimulated by fiscal loosening ahead of the 2018 election. Recorded unemployment rate decreased further by 1.7% point to 5.1% in 2016.

Slight increase in lending with significant NPL volume reduction both in the retail and corporate segments

Corporate lending expanded in 2016, rising by 4% compared to the previous year. According to the National Bank of Hungary, this growth was mainly driven by SME lending; the volume of outstanding loans of the SME sector increased by 8% on an annual basis, while the volume of outstanding loans of the SME sector including sole proprietors rose by 12%. The uplift in lending was reflected not only in loans disbursed under the Funding for Growth Scheme (which was phased out in March 2017), but also in the expansion of the market-based HUF loans, which was significantly supported by the Market-based Lending Scheme. The volume of retail loans saw a moderate increase of 0.4% in 2016. On the other hand, volume of newly disbursed retail loans reached EUR 3.4bn in 2016, which was nearly 50% higher compared to 2015.

Both corporate and retail NPL ratios decreased substantially in 2016. In case of the corporate sector, the cleaning of the non-performing claims was performed at a relatively fast pace in the past 2-3 years. As a result, distressed assets in the corporate segment are decreasing, only a few portfolios might be brought to the market in the forthcoming years. The disposal of distressed household loan portfolios – particularly the mortgage loan portfolios – was less intense compared to the corporate receivables in the recent past. Although up to October 2017 the market has seen significant non-performing mortgage portfolio sales by major Hungarian banks, the banking sector still may face significant challenges in terms of non-performing retail loans. The sale of Project Ulysses was the first significant retail mortgage transaction at the end of 2016 with a face value exceeding EUR 300mn. The portfolio was sold by Erste Bank Hungary followed by two other residential real estate backed portfolios (Project Taurus and Project Lara) sold in 2017 with a total face value of close to EUR 400mn. Secured retail portfolios almost entirely accounted for the yet completed deals in Hungary in 2017, meanwhile loan sale market was dominated by corporate portfolios in 2016.

The profitability of the Hungarian banking sector improved significantly mostly due to one-off items

Profitability of the banking sector improved significantly compared to 2015 as the aggregated profit increased from EUR 29mn to EUR 1.3bn in 2016. As a result of the highest profit in recent years, the average return on equity in the sector rose to 12.1%. According to the NBH, improvement of the profitability was mostly driven by one-off, unsustainable items (e.g. revenues from the VISA transaction, decreasing credit losses and even loan loss provision write-backs). Profitability of the banking sector is expected to remain under pressure due to the low interest rate environment, especially after the maturity of the outstanding portfolio issued in high interest rate environment.

The National Bank of Hungary introduced certified consumer-friendly housing loans in 2017, with the aim of fostering competition among banks, which is expected to result in a decline in spreads.

Besides the privatization of MKB Bank in 2016, major market consolidation is still awaited

In June 2016, an international investor consortium, Blue Robin Investments S.C.A. (Luxembourg-based investment firm), METIS Private Capital Fund (Hungary-based private equity fund) and Pannonia Pension Fund (Hungary-based pension fund) acquired 45%, 45% and 10% stake respectively in MKB Bank Zrt. from the Hungarian Government. Subsequently, 15% ownership from Blue Robin Investments was transferred to the Employee Shareholder Program of MKB Bank.

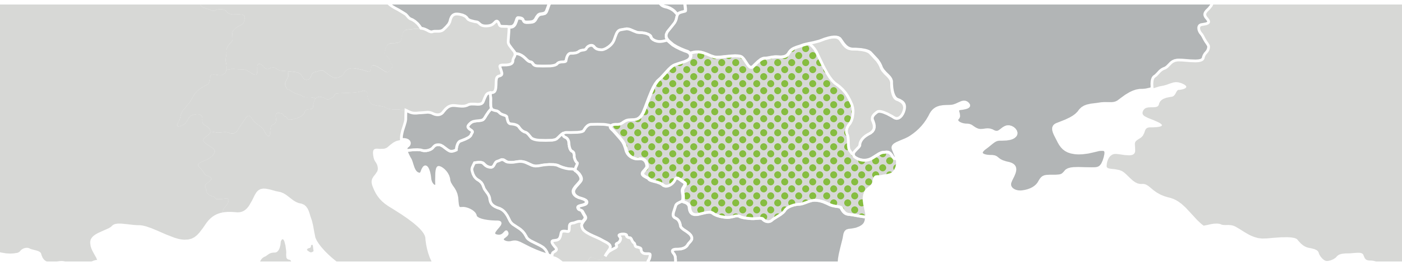
In August 2016, Corvinus Nemzetkozi Befektetesi Zrt. and the European Bank for Reconstruction and Development acquired 15%-15% respectively in Erste Bank Hungary Zrt, from Erste Group Bank AG.

In November 2016, OTP Bank Plc has completed the acquisition of AXA Bank Hungary from AXA Bank Europe S.A. OTP took over the retail credit and saving portfolio, and a small part of the corporate portfolio and the employees of AXA Bank Hungary.

Privatization of Budapest Bank is also being prepared by the state, with both trade sale and IPO being potential alternatives. In Hungary, the savings cooperation integration is also on the agenda, with the mergers there will be 12 savings cooperation instead of 52.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	**OTP Hungary**	22,947	8,425	3,584	651	2.8%	18.2%	9.8%	826	OTP
2	**UniCredit Bank Hungary**	9,818	3,776	966	173	1.8%	17.9%	12.7%	479	UniCredit
3	**K&H**	9,241	3,945	837	152	1.6%	18.2%	9.8%	387	KBC
4	**MKB**	6,775	3,130	438	29	0.4%	6.6%	n/a	n/a	PE/VC
5	**Erste Bank Hungary**	6,579	3,435	901	114	1.7%	12.7%	9.9%	339	Erste
6	**Raiffeisen Bank**	6,459	2,992	539	58	0.9%	10.8%	13.8%	412	Raiffeisen
7	**CIB**	5,261	2,828	688	39	0.7%	5.7%	10.3%	290	Intesa Sanpaolo
8	**MFB Magyar Fejlesztési Bank Zrt.**	4,179	1,816	647	1	0.0%	0.2%	n/a	n/a	State
9	**BUDAPEST Hitel- és Fejlesztési Bank Zrt.**	3,193	2,074	412	34	1.1%	8.3%	11.4%	237	State
10	**OTP Jelzálogbank Zrt.**	3,142	3,134	210	66	2.1%	31.4%	1.9%	60	OTP
	Banking sector total	**108,193**	**34,197**	**10,972**	**1,331**	**1.2%**	**12.1%**	**9.6%**	**3,288**	

Source: Banks' data disclosure, NBH, ECB CBD, ISI Emerging Markets



Romania

The Romanian banking sector remained profitable in 2016 with ROE of 10.5% and continued the disposal of distressed assets decreasing total NPL ratio below 10%.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	3.0%	3.9%	4.8%	0.9%
Consumer prices (% change pa)	1.1%	-0.6%	-1.6%	-1.0%
Recorded unemployment (%)	6.6%	6.8%	5.6%	-1.2%
Budget balance (% of GDP)	-1.9%	-1.5%	-2.4%	-0.9%
Public debt (% of GDP)	39.8%	38.0%	37.6%	-0.4%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	22,498	23,783	24,934	4.8%
Corporate loans (EUR mn)	23,236	23,557	22,893	-2.8%
Interest rates				
Lending (%)	8.5%	6.8%	5.7%	-1.1%
Deposit (%)	3.0%	1.9%	1.1%	-0.8%
NPL volumes				
Retail NPLs (EUR mn)	1,745	2,164	1,845	-14.7%
Corporate NPLs (EUR mn)	4,339	6,162	4,350	-29.4%
NPL ratios				
Retail NPL ratio (%)	7.8%	9.1%	7.4%	-1.7%
Corporate NPL ratio (%)	18.7%	26.2%	19.0%	-7.2%
Key ratios				
CAR (%)	17.6%	19.2%	19.7%	0.5%
ROE (%)	-12.5%	11.4%	10.5%	-0.9%
ROA (%)	-1.3%	1.2%	1.1%	-0.1%
CIR (%)	54.9%	57.9%	52.4%	-5.4%
L/D (%)	91.3%	85.4%	79.1%	-6.3%
FX share of lending (%)	58.0%	49.0%	43.0%	-6.0%
Coverage ratio (%)	55.6%	57.7%	56.2%	-1.5%

2014 and 2015 levels of NPL ratios and volumes are not comparable since ratios for 2014 were calculated based on the previous methodology used by the NBR.
Source: EIU, NBR, ECB CBD

Outstanding economic performance driven by domestic demand

In 2016, real GDP growth accelerated to 4.8% from 3.9% in 2015. Growth was mainly driven by consumer demand arising from the increased consumer purchasing power. Since mid-2015, tightening of the labour market, strong wage growth as well as consumer price deflation contributed to the economic growth and the increasing purchasing power.

Intense activity of portfolio sales reduced NPL volumes greatly

In 2016, the stock of retail loans increased by 4.8% boosted solely by the lei-dominated housing loans. At the same time, volume of corporate loans slightly decreased by 2.8% in 2016. Asset quality improved among Romanian banks, as a result of intense activity of non-performing portfolio sales with over EUR 2bn completed deals in 2016 and up to October 2017 based on publicly available market intelligence. The Romanian loan sale market is one of the most active loan sale markets in the CEE region in recent years. Up to October in 2017, the largest completed deal was the sale of a mixed portfolio by the third largest market player, BRD with a face value of EUR 280mn (Project Iris). In 2016, the market has seen large portfolio sales from Bancpost (Project Metro) and BCR (Project Blue Lake) with face values amounting to c. EUR 600mn and EUR 370mn respectively. Given the remarkable amount of ongoing deals, transaction volume can even exceed EUR 2bn in 2018. NPL ratios decreased both in the retail and corporate sectors by 1.7% and 7.2% points respectively. Despite significant NPL reductions, overall NPL ratio of the banking sector stood at 9.6% as of year-end 2016, which is still above EBA's red threshold of 8% and the EU-wide average. Judging from the current transaction pipeline, a further improvement of the NPL ratio is forecasted in 2018.

The Romanian banks remained profitable and well-capitalized in 2016

Profitability of the Romanian banking sector slightly decreased in 2016. According to the National Bank of Romania, the main drivers of the profitability were the growing operating profit, the low funding costs, favourable domestic macroeconomic conditions as well as the revival of domestic currency lending. Although, interest income of the banking sector declined in 2016, interest expenses decreased at a faster pace so overall net interest income increased in 2016.

The banking sector of Romania is well-capitalized with CAR at 19.7% in 2016, well above the capital requirements. Although this solid capital base is expected to somewhat diminish due to the gradual increase of the capital conservation buffer from 2016 imposing a buffer of 1.25% of total risk exposure of the Romanian credit institutions. L/D ratio fell further to 79.1% in 2016, strengthening the self-financing position of the Romanian banking sector.

There was no major change among the top banks as the M&A market was rather passive in 2016

Similarly to 2015, Banca Transilvania remained the most profitable bank in Romania with a ROE of 20.6% in 2016. The profit of the Romanian banking sector is extremely concentrated, the net profit of the seven largest banks accounted for 93% of the overall profit.

There was no significant change among the top ten banks. Banca Transilvania overtook BRD becoming the second largest bank by asset volume. NPL ratios of the top ten banks are in the range of 8-14%.

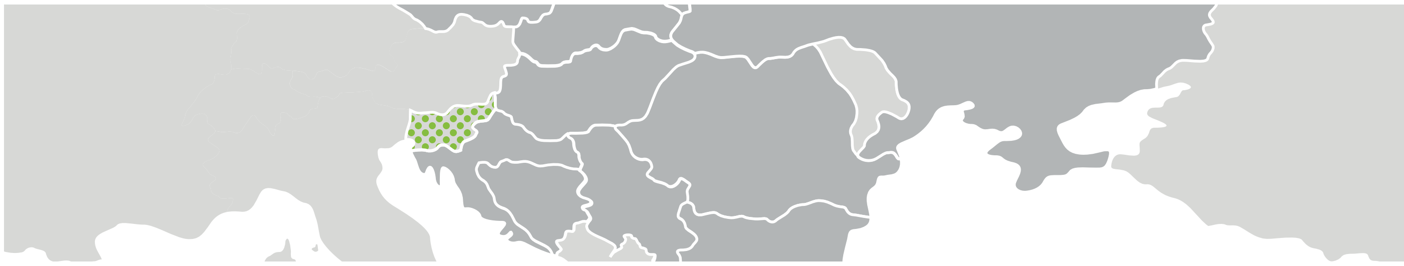
Patria Bank acquired majority stake of 54.79% in Banca Comerciala Carpatica S.A in January 2016. Growth of Banca Carpatica is expected to be supported with capital and know-how of Patria Bank.

In July 2017, OTP Bank Romania S.A. agreed to acquire a 99.28% stake in Banca Romaneasca SA from National Bank of Greece SA. Subject to the approval of the transaction, OTP will increase its market share to approximately 4%, becoming the 8th largest bank in Romania.

The presence of Greek-based banks (Alpha Bank, Eurobank, Piraeus) is strong among the top ten players. Given the NPL-related problems of these banks, Greek-owned banks might drive M&A activity in 2018. As per the Eurobank-owned Bancpost, Banca Transilvania is reported to be close to sign an agreement on the acquisition by December 2017.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	**BCR**	14,115	6,541	1,518	195	1.4%	12.8%	11.7%	765	Erste
2	**Banca Transilvania**	11,406	6,494	1,318	271	2.4%	20.6%	9.5%	614	Private
3	**BRD**	11,161	6,804	1,403	160	1.4%	11.4%	12.9%	878	Société Générale
4	**Raiffeisen Bank**	7,363	4,489	710	100	1.4%	14.1%	8.3%	373	Raiffeisen
5	**Unicredit Tiriac**	7,201	4,457	718	59	0.8%	8.2%	13.7%	611	UniCredit
6	**CEC Bank**	6,212	3,429	415	2	0.0%	0.5%	10.0%	344	State
7	**ING**	6,140	n/a	FB	104	1.7%	n/a	n/a	n/a	ING
8	**Alpha Bank**	3,246	2,771	417	3	0.1%	0.7%	14.0%	388	Alpha Bank
9	**Bancpost**	2,568	n/a	290	1	0.0%	0.3%	9.1%	n/a	Eurobank Ergasias
10	**Garanti Bank**	1,974	n/a	243	9	0.5%	3.7%	n/a	n/a	Garanti Bank
	Banking sector total	**88,202**	**47,827**	**9,013**	**944**	**1.1%**	**10.5%**	**9.6%**	**6,195**	

Source: Banks' data disclosure, NBR, ECB CBD, ISI Emerging Markets
FB: foreign branch



Slovenia

Backed by continued active portfolio cleaning of the Slovenian banking sector, NPL volumes plummeted, especially in the corporate segment where NPL volume decreased by 55.2% in 2016. Banks expanded the sale of non-performing exposures in both the corporate and household segments, increased write-offs and the role of restructuring, while collateral liquidation also attributed to asset quality improvement.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	2.4%	2.0%	2.6%	0.6%
Consumer prices (% change pa)	0.4%	-0.7%	-0.2%	0.6%
Recorded unemployment (%)	9.6%	9.0%	7.9%	-1.1%
Budget balance (% of GDP)	-4.9%	-2.7%	-1.8%	0.9%
Public debt (% of GDP)	80.9%	83.5%	79.7%	-3.8%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	8,762	8,856	9,154	3.4%
Corporate loans (EUR mn)	11,191	10,068	9,259	-8.0%
Interest rates				
Lending (%)	5.0%	3.5%	2.8%	-0.7%
Deposit (%)	0.8%	0.2%	0.1%	-0.1%
NPL volumes				
Retail NPLs (EUR mn)	464	416	320	-23.0%
Corporate NPLs (EUR mn)	1,981	1,550	694	-55.2%
NPL ratios				
Retail NPL ratio (%)	5.3%	4.7%	3.5%	-1.2%
Corporate NPL ratio (%)	17.7%	15.4%	7.5%	-7.9%
Key ratios				
CAR (%)	15.8%	18.8%	19.3%	0.5%
ROE (%)	-2.7%	3.5%	7.8%	4.3%
ROA (%)	-0.3%	0.4%	0.9%	0.5%
CIR (%)	58.2%	61.0%	61.4%	0.4%
L/D (%)	107.0%	94.4%	87.0%	-7.4%
FX share of lending (%)	0.0%	0.0%	0.0%	0.0%
Coverage ratio (%)	60.8%	65.0%	68.0%	3.0%

Source: EIU, BSI, ECB CBD

Increasing GDP growth with tightening labour market

Slovenia's real GDP grew by 2.6% in 2016, which is 0.6% point higher than the rate in 2015. The main driver of growth was still export and foreign demand, but domestic private demand also expanded owing to improving labour market conditions and increasing disposable income of households. Following the decrease of unemployment rate in 2015, recorded unemployment decreased further in 2016 to 7.9%. Investment activity was weak in 2016 due to the lower disbursement of EU funds. The largest increase in growth was posted in the manufacturing segment, whilst the largest decline occurred in the construction sector.

Increasing credit quality with significant NPL volume reduction

Lending to the corporate sector declined further in 2016 by 8%. In spite of improving economic conditions and loose monetary policy that have been reflected in high surplus reserves at banks, banks in Slovenia are not strengthening their corporate lending activity. This decline is the result both of the supply side and the demand side. In case of the demand side, the structure of the economy is changing by increasing the use of internal and non-bank resources in financing corporates. With regards to the supply side, the major limiting factor is the commitments made to the European Commission regarding the minimum return on new corporate lending that have received state aid. On the other hand, retail lending increased slightly by 3.4% mostly driven by the housing loans.

Thanks to banks' intention to improve portfolio quality, both retail and corporate NPL rates decreased by 1.2% point and 7.9% points respectively. The more successful restructuring activity, the acceleration of write offs and sale of non-performing portfolios also contributed to improving credit quality. In 2016, the amount of disposed NPL portfolios in Slovenia amounted to c. EUR 1bn based on publicly available market intelligence. Almost entirely corporate portfolios dominated the loan sale market with the exception of one transaction when the largest market player sold a retail mortgage portfolio with a face value of EUR 100mn. No completed deals were reported in 2017 until October, but two ongoing transactions are on the market based on publicly available information. Heta, NLB and UniCredit were the top sellers in 2016. The improvement in portfolio quality has been manifested particularly in construction, wholesale and retail trade segments.

Profitability improvement through declining credit risk and increasing profit margins

The banking sector's profitability improved further in 2016. ROE stood at 7.8%, posting a 4.3% point increase compared to 2015. Although profitability trended upwards, the decline of interest income was due to the contraction of the overall loan volume and falling lending rates. According to the BSI, main drivers of the improvement were the decline in operating costs, the sharp reduction in impairment and provisioning costs under the influence of the improved economic situation, as well as banks' increased activity to resolve non-performing claims, which together offset the effect of decreasing net interest margin.

CAR of the Slovenian banking sector increased moderately in 2016 by 0.5% point, arriving to a solid 19.3%. In Slovenia, there are significant differences among banks in terms of capital adequacy. Backed by higher profitability, large domestic banks have the highest capital ratios. On the contrary, small domestic banks and savings banks remained more vulnerable in terms of capitalization.

Restructuring process continued with the privatization of Nova KBM and the sale of state-owned NLB is also in progress

Similarly to other countries in the region, consolidation of the banking sector in Slovenia is in progress. Smaller banks with a minor market share might either take steps to achieve economies of scale or consider possible exit.

In September 2016, Nova KBM acquired Poštna banka Slovenije. The new bank operates under the name Nova KBM d.d., with its head office being in Maribor. The merger made it possible for Nova KBM to strengthen its market presence and to regain its position as the second largest bank in Slovenia in terms of total assets.

Apollo Global Management, LLC and the EBRD completed the transaction to acquire Nova KBM from Government of the Republic of Slovenia in April 2016. According to the agreement Apollo Global acquired 80% and EBRD acquired 20% stake in Nova KBM.

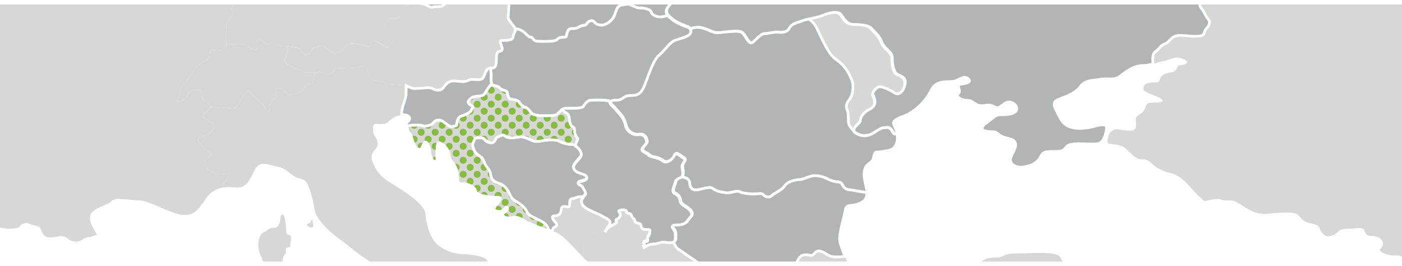
In January 2017, Nova KBM completed the transaction to acquire KBS banka d.d. from Raiffeisen Bank International AG.

In addition, the Serbia-based AIK Banka a.d. and Apollo Global Management are in the race to acquire control over Gorenjska banka d.d. AIK Banka already has 19.4% stake in the Bank, but showed interest in November 2016 to raise its stake above 50%.

The Government of Slovenia agreed to the sale of its 50% stake in NLB, but eventually cancelled the transaction in June 2017 with the reasoning that the suggested price was too low.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	**NLB d.d.**	8,778	4,759	1,265	64	0.7%	5.1%	11.9%	753	State
2	**Nova KBM d.d.**	4,832	2,067	671	33	0.7%	4.9%	12.4%	257	Apollo Global, EBRD
3	**Abanka d.d.**	3,612	1,826	614	77	2.1%	12.5%	15.9%	291	State
4	**SKB Banka**	2,803	1,748	353	62	2.2%	17.6%	8.9%	156	Société Générale
5	**UniCredit Banka**	2,571	1,460	246	14	0.5%	5.7%	16.4%	239	UniCredit
6	**SID bankad.d. Ljubljana**	2,548	788	394	21	0.8%	5.3%	11.8%	93	State
7	**Banka Koper**	2,326	1,625	290	20	0.9%	6.9%	6.8%	111	Intesa Sanpaolo
8	**Sberbank Banka**	1,779	1,230	147	1	0.1%	0.7%	14.6%	180	Sberbank
9	**Gorenjska Banka**	1,513	945	201	6	0.4%	3.0%	11.3%	107	Sava d.d.
10	**Addiko Bank d.d.**	1,414	n/a	122	13	0.9%	10.7%	n/a	n/a	PE Advent
	Banking sector total	**40,587**	**18,413**	**4,870**	**382**	**0.9%**	**7.8%**	**5.5%**	**1,015**	

Source: Banks' data disclosure, BSI, ECB CBD, ISI Emerging Markets



Croatia

Having peaked in 2014-2015, both retail and corporate NPL ratios decreased gradually in 2016 backed by the increased willingness of banks to sell their NPL portfolios.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	-0.4%	1.6%	3.0%	1.4%
Consumer prices (% change pa)	-0.2%	-0.5%	-1.1%	-0.7%
Recorded unemployment (%)	17.3%	17.1%	13.4%	-3.7%
Budget balance (% of GDP)	-5.7%	-3.4%	-0.8%	2.6%
Public debt (% of GDP)	85.1%	86.3%	83.8%	-2.6%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	16,727	15,930	14,980	-6.0%
Corporate loans (EUR mn)	13,017	13,363	12,825	-4.0%
Interest rates				
Lending (%)	6.3%	5.8%	4.9%	-0.9%
Deposit (%)	3.5%	3.2%	2.7%	-0.5%
NPL volumes				
Retail NPLs (EUR mn)	2,024	1,940	1,547	-20.2%
Corporate NPLs (EUR mn)	3,996	4,024	3,220	-20.0%
NPL ratios				
Retail NPL ratio (%)	12.1%	12.2%	10.3%	-1.9%
Corporate NPL ratio (%)	30.7%	30.1%	25.1%	-5.0%
Key ratios				
CAR (%)	21.4%	21.0%	22.5%	1.5%
ROE (%)	3.6%	-6.8%	8.9%	15.7%
ROA (%)	0.5%	-0.9%	1.2%	2.1%
CIR (%)	53.2%	57.6%	52.8%	-4.7%
L/D (%)	98.7%	92.9%	89.0%	-3.9%
FX share of lending (%)	74.0%	71.0%	66.0%	-5.0%
Coverage ratio (%)	51.3%	56.9%	63.3%	6.4%

Source: EIU, HNB, ECB CBD

Stable economic growth driven by record tourism season

Following the economic recovery in 2015, real GDP growth accelerated to 3% in 2016. The main drivers were private consumption and investment, benefited from the record tourism season in 2016. The outstanding economic performance had a positive impact on the labour market with an unemployment rate decrease of 3.7% points in 2016.

Decreasing lending with NPL volume reduction by over 20% both in retail and corporate segment

Both retail and corporate loan stock decreased in 2016 by 6% and 4% respectively. In the retail sector total loan amount was falling continuously due to the statutory conversion of loans indexed to the Swiss franc, write-offs and sale of claims, although credit demand started to recover in 2016. According to the Croatian National Bank, new long-term household borrowing was spurred by positive signals from the labour market, and growing consumer confidence, while relaxed credit standards might boost further acceleration in credit activity in 2017. In the corporate segment the situation is similar as growth in newly-granted loans to corporates was insufficient to offset the dominant impact of write-offs and sales of claims, thus the overall loan volume decreased further. Croatia was one of the most active markets for distressed debt in the CEE region with transactions amounting to almost EUR 2.0bn in 2016 and up to October 2017. Corporate portfolios dominated the loan sale market in 2016 and 2017 as well Project Taurus being the largest portfolio disposed with a face value of EUR 700mn. The largest deal in 2016 was the sale of a corporate portfolio of NPLs by HETA with a face value of c. EUR 330mn.

Improved profitability owing to the reduction in value adjustments and provisions, and one-off revenue

As a result of the intense balance sheet clean-up process of the banks, both the retail and corporate NPL ratio decreased by 1.9% point and 5% point respectively. According to the HNB, the improvement of credit portfolio quality can be strongly influenced by the inflow of fully or partially irrecoverable placements to the Agrokor Group and its economically related entities.

The Croatian banking sector reported a robust CAR of 22.5% in spite of the statutory conversion of CHF-denominated loans to euros in 2015, which affected profitability negatively through one-off impairments. Having booked losses related to the mandatory conversion already in 2015, ROE of the Croatian banking sector increased significantly by 15.7% points in 2016, reaching a level of 8.9%. The slight increase in NIM also contributed to the improvement, due to the faster decrease of interest expenses than interest incomes.

Significant profitability improvement in 2016 with the phasing out of mandatory CHF conversion, in tandem with substantial NPL volume decrease

Following the deterioration of profitability in 2015 due to the mandatory conversion, all of the top ten banks reported a positive ROE in 2016, main drivers of the improvement were mostly the considerable one-off revenues (sale of the shares of Visa Europe Ltd. and other smaller divestments) associated with a bank's equity investment into a subsidiary and sales of non-performing claims at a price over book value. Although NPL ratios were still above 10% as of year-end 2016, the top ten banks saw a substantial asset quality improvement, having decreased their aggregate NPL volume from EUR 5.9bn to EUR 4.7bn from 2015 to 2016.

Hungary-based OTP Bank announced to purchase the 100% stake of Splitska Banka in December 2016. With this merge, the new bank will be the fourth largest Croatian bank with a market share over 10%. The Croatian banking sector was concentrated already, and the merge of OTP and Splitska Banka will further increase this concentration.

In addition, as per recent market intelligence, the state-owned Hrvatska Postanska Banka is mulling a potential acquisition of local peer, Jadranska Banka.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	**Zagrebacka Banka**	13,907	8,244	1,885	281	2.0%	14.9%	13.8%	1,138	UniCredit
2	**Privredna Banka Zagreb**	9,582	5,026	1,597	262	2.7%	16.4%	15.9%	799	Intesa Sanpaolo
3	**Erste & Steiermarkische**	7,423	6,285	972	110	1.5%	11.3%	11.2%	704	Erste
4	**Raiffeisenbank Austria**	4,157	2,484	587	77	1.9%	13.1%	15.7%	390	Raiffeisen
5	**Splitska Banka**	3,577	2,359	428	62	1.7%	14.5%	15.0%	354	Société Générale
6	**Addiko Bank d.d.**	2,791	n/a	489	11	0.4%	2.2%	n/a	n/a	PE Advent
7	**Hrvatska Postanska Banka**	2,561	1,157	201	21	0.8%	10.4%	16.1%	187	State
8	**OTP Banka Hrvatska**	2,089	1,521	222	20	1.0%	9.0%	12.1%	184	OTP
9	**Sberbank**	1,226	n/a	152	9	0.7%	5.9%	n/a	n/a	Sberbank
10	**Kreditna banka Zagreb d.d.**	470	230	41	2	0.4%	4.4%	19.3%	44	Croatian citizens
	Banking sector total	**58,082**	**27,806**	**8,026**	**714**	**1.2%**	**8.9%**	**13.6%**	**4,767**	

Source: Banks' data disclosure, HNB, ECB CBD, ISI Emerging Markets

Bulgaria

NPL volumes decreased in both retail and corporate segments with 21.4% and 13.6% respectively. However, corporate NPL ratio at 15.1% still belongs to the higher ratios among the countries involved in the study.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	1.7%	3.6%	3.4%	-0.2%
Consumer prices (% change pa)	-1.4%	-0.1%	-0.8%	-0.7%
Recorded unemployment (%)	11.2%	10.1%	8.7%	-1.4%
Budget balance (% of GDP)	-3.7%	-2.8%	1.6%	4.4%
Public debt (% of GDP)	27.4%	26.0%	29.5%	3.5%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	9,145	9,363	9,498	1.4%
Corporate loans (EUR mn)	17,160	17,019	16,965	-0.3%
Interest rates				
Lending (%)	8.3%	7.5%	6.4%	-1.1%
Deposit (%)	1.7%	0.6%	0.2%	-0.4%
NPL volumes				
Retail NPLs (EUR mn)	1,211	1,215	954	-21.4%
Corporate NPLs (EUR mn)	3,438	2,972	2,569	-13.6%
NPL ratios				
Retail NPL ratio (%)	13.2%	13.0%	10.0%	-3.0%
Corporate NPL ratio (%)	20.0%	17.5%	15.1%	-2.4%
Key ratios				
CAR (%)	21.9%	22.2%	22.2%	0.0%
ROE (%)	7.2%	8.0%	10.4%	2.4%
ROA (%)	0.9%	1.0%	1.4%	0.3%
CIR (%)	48.8%	47.5%	42.6%	-4.9%
L/D (%)	87.3%	78.1%	73.0%	-5.1%
FX share of lending (%)	57.0%	51.0%	45.0%	-6.0%
Coverage ratio (%)	59.1%	51.5%	51.0%	-0.5%

Source: EIU, BNB, ECB CBD

Continuing economic recovery driven by increasing external and domestic demand

Bulgaria's real GDP grew by 3.4% in 2016. After a slow recovery period from the crisis, in 2014 the Bulgarian economy started to grow again. In 2016, in tandem with the deceleration of EU inflows, economic growth also slowed down but owing to the improving labour market and the increasing domestic and external demand, growth decreased only by 0.2% point. In 2017, a further growth is expected because of the stronger employment rate, wage growth and increasing private consumption.

Practically stagnating lending and significant NPL volume decrease

There was a slight increase of 1.4% in the volume of retail loans in 2016, mainly driven by consumer loans similarly to 2015, whereas demand for mortgage loans is relatively low, since only 5% of households have a housing loan. The volume of corporate loans slightly contracted by 0.3% due to less investment activity, although recovery of corporate lending is expected in 2017, driven by GDP growth.

Both retail and corporate NPL volumes decreased substantially by 21.4% and 13.6% respectively, mostly due to NPL disposals from balance sheets and write-offs of fully impaired exposures. The two main completed Bulgarian NPL portfolio deals in 2016 related to Postbank and National Bank of Greece, the first was an unsecured retail portfolio of EUR 145mn. The second portfolio was also a consumer portfolio with a face value of EUR 70mn. Up to October 2017, no major completed NPL deal were reported, only the sale of Project Taurus with a face value of c. EUR 90mn. In 2015 and early 2016, banks focused on cleaning up their balance sheets in preparation for the asset-quality review and stress test conducted by the Bulgarian National Bank. The Bulgarian National Bank aimed to stabilize the banking system and improve asset quality, hence they conducted such asset quality review and stress test. The impact of the adjustments required by the BNB did not have a significant negative effect on the capitalization and profitability of the banking system.

Lower impairment losses and decreased administrative expenses boosted banks' profitability

Capital adequacy of the Bulgarian banking sector stagnated at a robust level of 22.2% in 2016, being significantly higher than the minimum requirements. According to the BNB, the amount of Tier 1 capital was sufficient in all banks to meet the requirements for capital conservation and systemic risk buffers as of year-end 2016.

Aggregated ROE of the banking sector also increased by 2.4% points and stood at 10.4% at the end of 2016, the highest level since 2008. Lower impairment loss on loans and decreasing administrative expenses were the main drivers of profitability improvement. Furthermore, credit institutions have so far managed to adjust to the environment of low and decreasing interest rates without serious decreases in net interest income.

Consolidation in the bank sector with the reduction of the Greek banks' market share

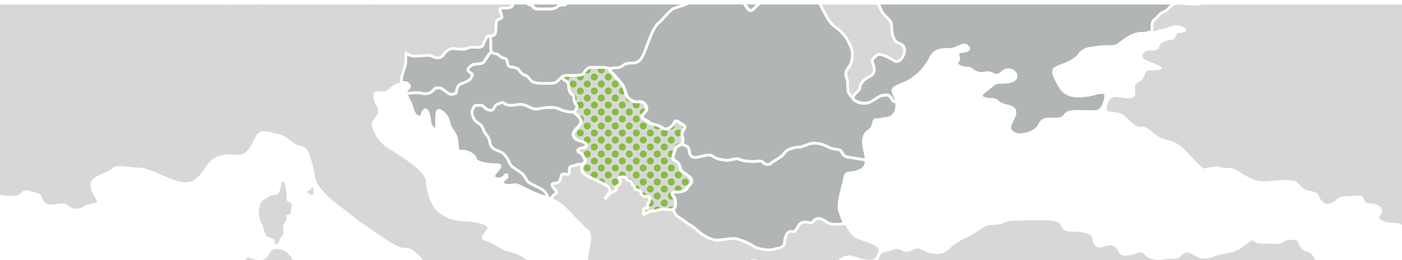
The renewed Greek crisis in mid-2015 posed a particular risk through the subsidiaries of Greek banks in the Bulgarian bank sector. However due to mergers and sales, the relatively significant market share of Greek-owned banks decreased from 23% (2015) to around 10% in 2017. Similarly to 2015, only Piraeus Bank remained heavily loss-making in 2016 among the top 10.

In March 2016, the Bulgaria-based Postbank (subsidiary of Eurobank Ergasias) acquired Alpha Bank Bulgaria from Alpha Bank SA. The sale is in line with Alpha Bank's strategy of divesting from non-core markets. With the transaction Postbank strengthened its position in the Bulgarian banking market and expanded its corporate and retail customer base.

In June 2017, the Belgian KBC Groep NV acquired 99.1% stake in United Bulgarian Bank AD, from National Bank of Greece SA. After the transaction, UBB will be combined with KBC's Bulgarian subsidiary, CIBANK, and the new bank is going to be the third largest bank in Bulgaria in terms of assets, with approximately 11% market share.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	**UniCredit Bulbank**	9,523	5,438	1,386	149	1.6%	10.8%	14.0%	761	UniCredit
2	**DSK Bank**	5,953	3,716	786	145	2.4%	18.4%	11.5%	426	OTP
3	**First Investment Bank**	4,526	3,006	430	46	1.0%	10.7%	12.8%	386	Private
4	**United Bulgarian Bank**	3,493	2,312	554	57	1.6%	10.3%	25.8%	598	KBC
5	**Eurobank Bulgaria Postbank**	3,486	2,366	587	61	1.7%	10.4%	15.3%	363	Eurobank Ergasias
6	**Raiffeisen Bank**	3,233	2,161	465	68	2.1%	14.6%	6.5%	140	Raiffeisen
7	**Soc. Gén. Expressbank**	3,034	1,999	346	46	1.5%	13.3%	5.7%	114	Société Générale
8	**Central Cooperative Bank**	2,541	1,151	214	14	0.6%	6.5%	9.8%	113	CCB Group
9	**CIBANK**	1,586	913	170	17	1.1%	10.0%	11.2%	102	KBC
10	**Piraeus Bank Bulgaria**	1,487	935	186	-35	-2.4%	-18.8%	25.7%	240	Piraeus Bank
	Banking sector total	**48,034**	**26,463**	**6,278**	**653**	**1.4%**	**10.4%**	**13.3%**	**3,523**	

Source: Banks' data disclosure, BNB, ECB CBD, ISI Emerging Markets



Serbia

Having peaked in 2015, total NPL ratio decreased to 17.0% in 2016 with an improving asset quality both in the retail and corporate segment.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	-1.8%	0.8%	2.8%	2.0%
Consumer prices (% change pa)	3.6%	1.4%	1.2%	-0.2%
Recorded unemployment (%)	22.8%	17.7%	15.3%	-2.4%
Budget balance (% of GDP)	-6.6%	-3.7%	-1.4%	2.3%
Public debt (% of GDP)	71.0%	75.9%	74.0%	-1.9%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	6,037	6,264	7,047	12.5%
Corporate loans (EUR mn)	8,085	8,189	8,479	3.5%
Interest rates				
Lending (%)	14.8%	8.8%	8.5%	-0.3%
Deposit (%)	6.8%	3.2%	2.9%	-0.3%
NPL volumes				
Retail NPLs (EUR mn)	692	731	705	-3.6%
Corporate NPLs (EUR mn)	2,344	1,778	1,458	-18.0%
NPL ratios				
Retail NPL ratio (%)	11.5%	11.7%	10.0%	-1.6%
Corporate NPL ratio (%)	29.0%	21.7%	17.2%	-4.4%
Key ratios				
CAR (%)	20.4%	20.9%	21.2%	0.3%
ROE (%)	0.6%	1.6%	3.4%	1.8%
ROA (%)	0.1%	0.3%	0.7%	0.3%
CIR (%)	64.3%	62.2%	64.8%	2.6%
L/D (%)	110.8%	107.5%	100.0%	-7.5%
FX share of lending (%)	69.0%	71.0%	67.0%	-4.0%
Coverage ratio (%)	54.9%	62.3%	67.8%	5.5%

Source: EIU, NBS, ECB CBD

Accelerated GDP growth with low, stable inflation and decreasing unemployment

Serbia's macroeconomic outlook improved in 2016. GDP grew by 2.8%, 2% points higher compared to the previous year. The outstanding GDP growth – since 2008 – was mainly driven by the acceleration of investments and exports as well, owing to the positive effects of the fiscal consolidation and the structural reforms. Increasing remittances from abroad also contributed to growth. Decrease of unemployment rate continued, arriving to 15.3% in 2016.

Expanding retail lending and growing share of local currency loans

Both corporate and retail lending expanded in 2016. Corporate loan stock increased by 3.5% in 2016, driven by the companies' need to finance their assets (according to the National Bank of Serbia, current asset loans amounted to 53% of the newly granted loans) and to restructure debt. The corporate loan market is expected to grow further in 2017 due to improving economic activity and the low interest rate environment. There was an upswing in retail lending in 2016 as well, total loan amount increased by 12.5%. The key driver of expansion was the low interest rate environment triggered by monetary policy easing, as well as enhanced pricing competition among banks. Growth was mainly fueled by cash loans, but housing and investment loans also contributed to loan expansion. Loans denominated in local currency dominated new retail lending.

Both the retail and corporate NPL ratios dropped in 2016 by 1.6% point and 4.4% points respectively, owing to the successful implementation of the NPL Resolution Strategy of the Serbian Government in August 2015, fostering write-offs and the sale of NPL portfolios. The NBS reported that amount of write-offs of non-performing portfolios was six times higher in 2016 than in 2015. The largest NPL deal up to October 2017 was the sale of a corporate portfolio by HETA (Project Onyx) with a face value of EUR 300mn.

Well-capitalized banking sector with improving profitability

The banking sector of Serbia remained well-capitalized, capital adequacy ratio increased slightly by 0.3% point, reaching 21.2% at the end of 2016, significantly exceeding the regulatory minimum.

Profitability of the banking sector continued in an upward path, reaching 3.4% return on equity in 2016. It should be noted though that this figure is the second worst among the countries covered in the study, behind the heavily loss making Ukrainian banking sector. Improved profitability is the result of the asset quality improvement and the reduction in net credit losses.

Heterogeneous profitability distribution in the Serbian banking sector

Among the top 10 banks, there were two heavily loss-making banks in 2016. Both state-owned Komercijalna Banka and Vojvodjanska Banka reported ROE of negative 14.5% and negative 53.7% respectively.

Direktna Banka acquired Piraeus Bank AD Beograd for EUR 58 mn in October 2017. Direktna Banka AD also performed another acquisition, having acquired Findomestic Banka a.d. Beograd from BNP Paribas in November 2016.

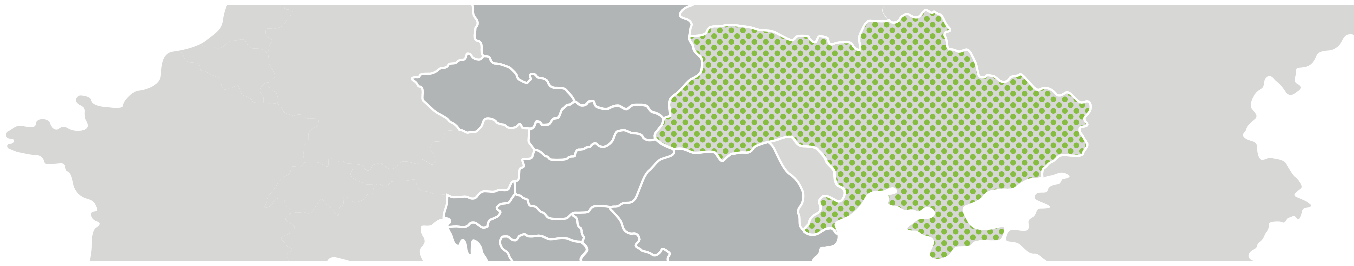
In August 2017, the Serbian subsidiary of OTP Bank Plc, OTP banka Srbija a.d. Novi Sad agreed to acquire Vojvodjanska banka a.d from from National Bank of Greece SA. With this transaction, the market share of OTP banka will rise to c. 5.7% and it will become the 7th largest bank in the country.

Also in August 2017, 85% of Telenor Banka was acquired by River Styxx Capital, a Bulgaria-based investment fund, for an undisclosed consideration.

In January 2017, MK Group owned by Miodrag Kostić acquired Alpha Bank Srbija AD for an undisclosed consideration. MK Group already possesses AIK Banka, thus further increased its market share with the acquisition of Alpha Bank Srbija.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	**Banca Intesa**	4,466	2,452	1,005	80	1.8%	8.0%	12.5%	305	Intesa Sanpaolo
2	**Komercijalna Banka**	3 240	1,597	449	-65	-2.0%	-14.5%	15.4%	246	State
3	**UniCredit Banka**	2,691	1,772	520	50	1.9%	9.6%	11.6%	205	UniCredit
4	**Raiffeisen Banka**	2,057	1,151	455	44	2.1%	9.7%	9.7%	112	Raiffeisen
5	**Société Générale Banka**	1,910	1,291	327	30	1.6%	9.2%	12.5%	161	Société Générale
6	**AIK Banka**	1,488	743	429	35	2.4%	8.2%	22.0%	163	MK Group
7	**Eurobank a.d. Beograd**	1,220	933	397	17	1.4%	4.3%	29.2%	272	Eurobank Ergasias
8	**Erste Bank**	1,157	731	147	17	1.5%	11.6%	7.1%	52	Erste
9	**Banka Poštanska**	1,078	n/a	95	-51	-4.7%	-53.7%	n/a	n/a	State
10	**Vojvođanska Banka**	1,020	657	162	2	0.2%	1.2%	18.5%	121	NBG
	Banking sector total	**26,336**	**15,526**	**5,139**	**175**	**0.7%**	**3.4%**	**17.0%**	**2,163**	

Source: Banks' data disclosure, NBS, ECB CBD, ISI Emerging Markets



Ukraine

Ukraine's financial industry has been hit hard by the political turmoil of the past several years. Owing to the crisis, the new NPL rule – introduced by NBU in 2017 – and PrivatBank's recognition of its assets' real quality, the Ukrainian banking sector reported the highest NPL ratios among the countries covered by the study.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	-6.6%	-9.8%	2.3%	12.1%
Consumer prices (% change pa)	12.1%	48.7%	13.9%	-34.8%
Recorded unemployment (%)	9.3%	9.1%	9.3%	0.2%
Budget balance (% of GDP)	-4.2%	-1.4%	-2.2%	-0.8%
Public debt (% of GDP)	69.4%	79.1%	81.0%	1.9%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	7,439	6,127	5,537	-9.6%
Corporate loans (EUR mn)	29,955	28,869	29,803	3.2%
Interest rates				
Lending (%)	17.7%	21.8%	19.2%	-2.6%
Deposit (%)	12.1%	13.0%	11.5%	-1.5%
NPL volume				
Total NPLs (EUR mn)	8,824	13,026	16,051	23.2%
NPL ratio				
Total NPL ratio (%)	19.0%	28.0%	30.5%	2.4%
Key ratios				
CAR (%)	15.6%	12.3%	12.7%	0.4%
ROE (%)	-35.4%	-82.1%	-128.8%	-46.7%
ROA (%)	-4.0%	-6.2%	-12.6%	-6.4%
CIR (%)	66.0%	74.4%	65.9%	-8.5%
L/D (%)	148.0%	134.8%	120.3%	-14.5%
FX share of lending (%)	46.4%	51.8%	47.7%	-4.1%
Coverage ratio (%)	75.5%	80.2%	99.5%	19.2%

Note: Disclosure of NPL volumes and ratios by segments (retail / corporate) is not available until February 2017.
Source: EIU, NBU, ECB CBD

Economic setback due to the political conflict of Crimea

Ukraine's real GDP fell significantly in 2015 by 9.8% because of the disruption of the Crimea conflict. A structural change occurred in the Ukrainian economy, moving away from heavy industry towards agriculture. In 2016, economic growth accelerated to 2.3% after a period of long recession. This recovery was driven by the intense revival of private investment and consumption. In 2017, a similar growth is forecasted, with the same main drivers as in 2016. Potential growth is shaded by the uncertainty caused by the military hostilities in the east of Ukraine. Inflation was extremely high in 2015 with 48.7% increase in consumer prices, which declined to a still high level of 13.9% in 2016. Recorded unemployment slightly increased by 0.2% point to 9.3% in 2016.

Extreme level of NPLs due to the recognition of non-performing loans and entailing disastrous profitability in 2016

Different movements characterized lending of the Ukrainian banking sector in 2016. Owing to the large-scale restructuring, UAH-denominated corporate loans increased, while the volume of corporate FX-loans fell progressively. The explanation for the expansion of hryvnia loans is that banks set these loans' interest rates closer to the FX, especially USD rates rather than hryvnia rates. The newly issued loans are mainly provided to the agricultural sector. On the other hand, the retail loan portfolio declined further mainly due to the high interest rates and the poor solvency of households. The main obstacle to the recovery of lending is the accumulated volume of distressed loans. Disclosure of NPL volumes and ratios by segments is not available until February 2017 but based on available data both corporate and retail NPL ratio exceeded 50% as of end March 2017. One-off effects impacted NPL volumes early 2017 like the recognition of non-performing corporate loans by Privatbank after its nationalization, exclusion of off-balance sheet items of the highest quality and the changes in the definition of NPLs in June 2016. The unexampled banking sector stimulus has made a massive supply of corporate NPLs for sale. The Ukrainian corporate NPL market size is estimated to amount to c. EUR 21bn. Besides that nearly EUR 15bn of failed bank assets have been accumulated in the Deposit Guarantee Fund which is the Ukrainian government agency responsible for winding down insolvent banks via asset auctions.

In 2016, the National Bank of Ukraine performed a study and revealed problems of the Ukrainian banks, for instance inadequate reporting of asset quality and a significant level of hidden credit risk. According to the NBU, after the issue of the study covering the top 20 banks, estimated NPL ratio increased from 19% as reported by banks up to 53%. Following the results of the study, the NBU introduced a new regulation in the beginning of 2017 of credit risk assessment in order to foster banks to provide realistic data. According to NBU's decision, effective from March 2017, NPL figures should be disclosed on a monthly basis by credit institutions.

Poor asset quality and heavily loss-making banking sector

The banking sector was heavily loss-making in 2016 mainly due to poor asset quality. Owing to the recognition of non-performing loans, NPL ratios among the top 10 banks are monstrous, especially the NPL ratio of the largest bank in Ukraine, PrivatBank stood at 90.6% as of year-end 2016. The bank was nationalized in December 2016 because of its systemic importance. After its nationalization, the Ministry of Finance and the National Bank of Ukraine invested EUR 4.1bn during December 2016 – January 2017. Reflecting the distressful asset quality of the largest bank in Ukraine, 90% of NPLs belonging to related parties are more than 1 year overdue.

Systemically important banks needed to be recapitalized in 2016

The second largest Oschadbank suffered huge losses in 2014-15 after the revolutionary wars in Ukraine, but reported positive net income in 2016. The Bank has repaid about 90% of NBU`s refinancing loans, and also this bank has the lowest impaired loan ratio of 19.2% among the top 10 banks.

The third largest Ukreximbank was also recapitalized with the amount of EUR 0.3bn by the Government in 2016. The Bank has an impaired loan ratio of 78.4%, corporate non-performing loans accounted for 98% of total distressed assets of the bank.

According to the NBU, the banking sector is expected to become profitable in 2017 since the provisioning by the largest banks has almost been completed, so majority of the negative impacts of the current crisis has already been reflected in the financial statements.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	Impaired loan ratio	Impaired loan vol.	Major owner
1	**PrivatBank**	7,741	8,019	446	-4,779	-61.7%	-1072.6%	90.6%	7,265	State
2	**Oschadbank**	7,392	4,100	525	17	0.2%	3.1%	19.2%	789	State
3	**Ukreximbank**	5,640	2,946	185	-36	-0.6%	-19.3%	78.4%	2,310	State
4	**Raiffeisen Bank Aval**	1,970	1,906	354	135	6.8%	38.1%	52.4%	998	Raiffeisen Bank International AG
5	**Ukrgazbank**	1,889	988	176	10	0.5%	5.9%	28.8%	272	State
6	**Sberbank**	1,701	2,187	131	-100	-5.9%	-76.0%	53.8%	1,176	Norvik Banka
7	**UkrSibbank**	1,596	967	144	-35	-2.2%	-24.3%	31.3%	n/a	Paribas Group
8	**First Ukrainian International Bank**	1,568	1,239	142	13	0.8%	9.1%	41.0%	508	Renat Akhmetov
9	**Ukrsotsbank**	1,471	1,780	451	-366	-24.9%	-81.2%	68.8%	1,224	ABH Holdings S.A.
10	**Alfa Bank Ukraine**	1,371	1,233	117	-145	-10.6%	-124.1%	29.8%	367	ABH Holdings S.A.
	Banking sector total	**44,849**	**35,341**	**4,386**	**-5,648**	**-12.6%**	**-128.8%**	**30.5%**	**16,051**	

Source: Banks' data disclosure, NBU, ECB CBD, ISI Emerging Markets
Note: Individual banks' loan volumes and ratios are impaired, banking sector total loan volume and ratio are 90 days past due

Bosnia and Herzegovina

In Bosnia and Herzegovina, both the NPL volume and the NPL ratio decreased owing to the expanding lending activity and the permanent write-offs. There were significant changes in the banking sector but the overall strength of the sector has been improved.

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	1.1%	3.1%	3.0%	-0.1%
Consumer prices (% change pa)	-0.9%	-1.0%	-1.1%	-0.1%
Recorded unemployment (%)	27.5%	27.7%	25.4%	-2.3%
Budget balance (% of GDP)	-2.2%	0.7%	1.2%	0.5%
Public debt (% of GDP)	30.9%	30.3%	29.2%	-1.1%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	3,790	3,972	4,121	3.8%
Corporate loans (EUR mn)	3,785	3,785	3,930	3.8%
Interest rates				
Lending (%)	5.8%	5.5%	4.5%	-1.0%
Deposit (%)	1.5%	0.9%	0.7%	-0.3%
NPL volumes				
Retail NPLs (EUR mn)	382	383	352	-8.0%
Corporate NPLs (EUR mn)	764	769	653	-15.0%
NPL ratios				
Retail NPL ratio (%)	10.2%	9.7%	8.6%	-1.1%
Corporate NPL ratio (%)	17.6%	17.2%	15.3%	-1.9%
Key ratios				
CAR (%)	15.6%	14.9%	15.8%	0.9%
ROE (%)	4.7%	5.0%	6.8%	1.8%
ROA (%)	0.7%	0.7%	0.9%	0.2%
CIR (%)	n/a	n/a	n/a	n/a
L/D (%)	103.6%	99.5%	95.0%	-4.5%
FX share of lending (%)	1.4%	1.3%	1.2%	-0.1%
Coverage ratio (%)	n/a	n/a	n/a	n/a

Source: EIU, CBBH, ECB CBD

Stable GDP growth, high unemployment

GDP growth inched down by 0.1% point to 3.0% in 2016. Rising external demand and low oil prices could not fully offset the effect of depressed government expenditure caused by the failure of securing external financing. In the second half of 2016, both the industrial and financial sectors' performance improved, so GDP growth is expected to accelerate moderately in 2017. Unemployment rate decreased by 2.3% points in 2016 but due to structural problems it is still the highest among the countries covered by the study at 25.4%.

Increasing lending, NPL metrics gravitating south mainly due to one-off effect

Both the retail and corporate lending increased by 3.8% in 2016. Among retail loans the general consumption loans have the highest share (c. 77%), and the volume posted an increase of the highest rate of 5.5% in 2016. Despite the downward trend of housing loans' interest rate, volume decreased for the fourth consecutive year. Increasing loan demand of the corporate sector arose from stronger economic activity and decline of non-performing portfolios. Agriculture and manufacturing loans attributed mostly to such increase. Total NPL volume in the retail sector decreased by 8.0%, while retail NPL ratio saw a decrease from 9.7% to 8.6% in 2016. According to the CBBH, this improvement was mainly driven by the permanent write offs of non-performing portfolios and the withdrawal of the operating license of Banka Srpske a.d. Banja Luka, reporting an extremely high level of non-performing loans. Corporate NPL ratio also fell from 17.2% to 15.3% in 2016 mainly driven by the exclusion of Banka Srpske a.d. Banja Luka from the reported figures.

The Bosnian banking sector strengthened in 2016 owing to decrease of impairment costs

The stability of the Bosnian banking sector definitely strengthened in 2016 owing to the modernization and adjustment of the local regulations to the European Union regulations.

Capital adequacy of the banking sector was adequate in 2016, CAR improved slightly by 0.9% point to 15.8%. Recovery of the banking sector was driven by the positive effect of a considerable decrease of impairment costs and the increase of operative income. Significant growth of the fee based income also contributed to profitability growth. Profit is reasonably concentrated among several systemically important banks.

Significant changes in the banking sector with two mergers and two liquidations

There were significant changes in the banking sector in Bosnia in 2016. Moja Banka d.d. Sarajevo merged into Investiciono-komercijalna banka d.d. Zenica and Investiciono-komercijalna banka took over all the rights and liabilities of Moja banka d.d. Sarajevo. The new bank has been operating under the name ASA Banka d.d. Sarajevo since the beginning of 2017.

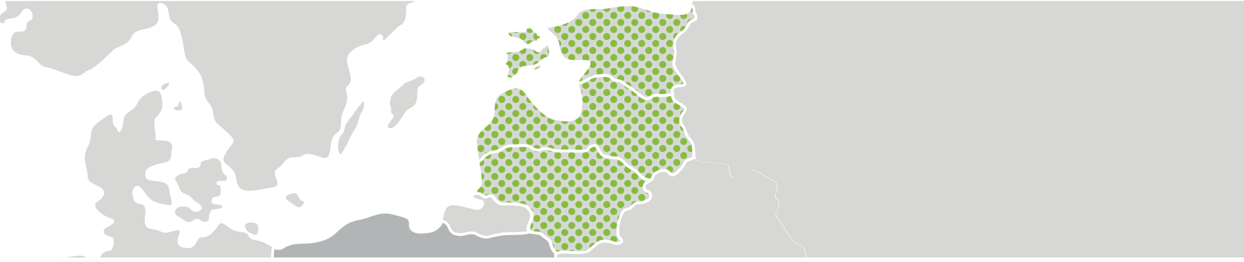
At the end of 2016, Privredna banka Sarajevo d.d. Sarajevo merged with BOR banka d.d. Sarajevo, and the new bank operates under the name Privredna banka Sarajevo d.d. Sarajevo.

Beside the mergers, Bobar Banka and Banka Srpske a.d. Banja Luka were liquidated in 2016. The liquidation of Banka Srpske contributed highly to the improvement of the asset quality, because Banka Srpske owned 7.2% of the banking sector's total non-performing loans.

Total NPL ratio of the banking sector is 11.7%, which is not disconcertingly high. Most banks in the top 10 are materially in line with this, only Addiko Banks have substantially worse portfolio quality.

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	NPL ratio	NPL vol.	Major owner
1	**UniCredit Bank d.d. Sarajevo**	2,410	1,576	364	42	1.7%	11.5%	10.7%	168	UniCredit
2	**Raiffeisen BANK d.d. BiH**	2,020	1,174	266	27	1.3%	10.2%	12.1%	142	Raiffeisen
3	**Intesa Sanpaolo Banka, d.d. BiH**	915	653	133	14	1.5%	10.5%	8.4%	54	Intesa Sanpaolo
4	**Nova Banka a.d. Banja Luka**	873	444	76	7	0.8%	9.2%	7.4%	33	State
5	**UniCredit Banka a.d. Banja Luka**	716	474	96	11	1.5%	11.5%	8.5%	40	UniCredit
6	**NLB Razvojna banka a.d.**	634	374	76	15	2.3%	19.3%	8.1%	30	Nova Ljubljanska Bank
7	**Sparkasse Bank d.d. BiH**	605	477	80	11	1.7%	13.2%	9.8%	14	Erste Group Austria
8	**Sberbank BH d.d. Sarajevo**	593	493	86	5	0.8%	5.7%	6.6%	32	Sberbank Europe AG
9	**Addiko Bank d.d. Sarajevo**	433	285	105	-19	-4.4%	-18.1%	44.0%	133	Addiko Invest d.o.o. Mostar
10	**Addiko Bank a.d. Banja Luka**	366	307	75	-5	-1.4%	-6.7%	26.7%	82	Addiko Bank AG
	Banking sector total	**13,284**	**8,051**	**1,831**	**125**	**0.9%**	**6.8%**	**11.7%**	**1,005**	

Source: Banks' data disclosure, CBBH, ECB CBD, ISI Emerging Markets



Baltic Region (Estonia, Latvia, Lithuania)

The Baltic states namely Estonia, Latvia and Lithuania are quite similar in terms of economic situation and NPL metrics, therefore we are analyzing the trends consolidated in this section.

Estonia

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	2.9%	1.4%	1.6%	0.1%
Consumer prices (% change pa)	-0.1%	-0.5%	0.1%	0.6%
Recorded unemployment (%)	7.3%	6.2%	6.8%	0.6%
Budget balance (% of GDP)	0.8%	0.1%	0.4%	0.3%
Public debt (% of GDP)	10.4%	10.1%	9.3%	-0.8%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	7,055	7,331	7,711	5.2%
Corporate loans (EUR mn)	6,560	6,933	7,499	8.2%
Interest rates				
Lending (%)	4.8%	4.5%	4.2%	-0.3%
Deposit (%)	0.5%	0.5%	0.4%	-0.1%
NPL volumes				
Retail NPLs (EUR mn)	96	66	53	-20.6%
Corporate NPLs (EUR mn)	127	106	119	11.8%
NPL ratios				
Retail NPL ratio (%)	1.4%	0.9%	0.7%	-0.1%
Corporate NPL ratio (%)	1.9%	1.5%	1.6%	0.2%
Key ratios				
CAR (%)	42.0%	35.0%	34.0%	-1.0%
ROE (%)	10.2%	6.6%	11.1%	4.5%
ROA (%)	1.3%	0.8%	1.4%	0.7%
CIR (%)	n/a	44.6%	44.5%	-0.2%
L/D (%)	100.0%	104.0%	n/a	n/a
FX share of lending (%)	1.0%	0.7%	0.0%	-0.7%
Coverage ratio (%)	76.0%	74.0%	n/a	n/a

Source: EIU, Eesti Pank, ECB CBD
Note: NPL volumes and ratios are based on 60 days past due basis

Stable economic growth with improving labour market conditions

All of the three countries posted a positive GDP growth in 2016 driven mainly by the private consumption boosted by the real wage growth. The growth decelerated only in case of Lithuania, mostly due to the slowdown of investment activity in 2016. A further economic growth is expected in all of the three countries in 2017 owing to the recovery of one of their main trade partners, Russia. All the Baltic countries reported an inflation below 1%, but all of them managed to avoid deflation in 2016.

Latvia

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	2.4%	2.7%	2.0%	-0.8%
Consumer prices (% change pa)	0.6%	0.2%	0.2%	0.0%
Recorded unemployment (%)	10.9%	9.9%	9.6%	-0.3%
Budget balance (% of GDP)	-1.6%	-1.3%	0.0%	1.3%
Public debt (% of GDP)	40.8%	36.5%	40.1%	3.6%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	5,794	5,594	5,581	-0.2%
Corporate loans (EUR mn)	7,873	7,874	7,943	0.9%
Interest rates				
Lending (%)	4.6%	4.5%	4.5%	0.0%
Deposit (%)	0.1%	0.0%	0.0%	0.0%
NPL volumes				
Retail NPLs (EUR mn)	527	405	275	-32.0%
Corporate NPLs (EUR mn)	374	278	172	-37.9%
NPL ratios				
Retail NPL ratio (%)	9.5%	7.6%	4.9%	-2.6%
Corporate NPL ratio (%)	5.4%	4.0%	2.2%	-1.7%
Key ratios				
CAR (%)	20.9%	22.4%	21.4%	-1.0%
ROE (%)	11.1%	12.5%	14.3%	1.8%
ROA (%)	1.1%	1.3%	1.4%	0.1%
CIR (%)	49.7%	47.5%	47.8%	0.3%
L/D (%)	66.1%	63.1%	70.8%	7.7%
FX share of lending (%)	13.0%	13.8%	12.5%	-1.3%
Coverage ratio (%)	77.0%	77.8%	89.3%	11.5%

Source: EIU, Bank of Latvia, ECB CBD

Increasing lending activity driven by new household loans and construction loans

Latvia's new household loans have been increasing rapidly, but the early-repayments of existing loans offset the effect resulting in a shrinking loan volume. In Estonia, there was a moderate increase mostly driven by the corporate loan segment in which particularly the trade, real estate and construction sector contributed to the uptrend. In Lithuania, both the retail and corporate lending activity increased driven by housing loans and large individual corporate loans respectively.

The overall loan portfolio quality of the Baltic region is outstanding compared to the other countries analyzed in the study. The aggregated NPL volume (retail and corporate together) of the three states amounted to around EUR 1bn as at end 2016, thus the non-performing loans did not pose serious risks to the Baltic banking sector. Besides the good asset quality, the low NPL volumes posted a further decrease in 2017 especially in Lithuania and Latvia where the year over year fall of distressed assets exceeded 30%. This trend was mainly driven by the improving financial position of the households and the write-down of bad loans.

Lithuania

Macro	2014	2015	2016	Change 2015-16 (% point)
GDP (% real change pa)	3.0%	1.8%	2.3%	0.5%
Consumer prices (% change pa)	0.2%	-0.7%	0.7%	1.4%
Recorded unemployment (%)	10.7%	9.1%	7.9%	-1.3%
Budget balance (% of GDP)	-0.7%	-0.2%	0.3%	0.5%
Public debt (% of GDP)	42.5%	42.7%	40.2%	-2.5%

Banking sector	2014	2015	2016	Change 2015-16 (% or % point)
Retail loans (EUR mn)	7,381	7,751	8,327	7.4%
Corporate loans (EUR mn)	7,390	7,625	8,148	6.9%
Interest rates				
Lending (%)	3.5%	3.0%	2.8%	-0.2%
Deposit (%)	0.5%	0.3%	0.2%	-0.1%
NPL volumes				
Retail NPLs (EUR mn)	664	574	400	-30.3%
Corporate NPLs (EUR mn)	761	640	505	-21.1%
NPL ratios				
Retail NPL ratio (%)	9.0%	7.4%	4.8%	-2.6%
Corporate NPL ratio (%)	10.3%	8.4%	6.2%	-2.1%
Key ratios				
CAR (%)	21.3%	24.9%	19.4%	-5.5%
ROE (%)	8.1%	9.0%	11.9%	2.9%
ROA (%)	0.8%	1.0%	1.0%	0.0%
CIR (%)	53.5%	52.7%	47.7%	-5.0%
L/D (%)	96.7%	94.0%	100.7%	6.7%
FX share of lending (%)	72.8%	0.9%	0.6%	-0.3%
Coverage ratio (%)	n/a	n/a	n/a	n/a

Source: EIU, Bank of Lithuania, ECB CBD

Profitability of the Baltic banking sectors has been supported by strong demand for loans, favourable financing conditions, and low loan loss rates

The banking sectors reported ROE above 10% in all of the three countries in 2016. The sale of Visa Europe Ltd. shares posted a significant one-off effect on the overall profit of the credit institutions in 2016.

In Estonia, the profitability of banks was boosted by the increasing net interest income driven by the low interest expenses and the growth of loan portfolio. According to the Bank of Latvia, net interest margins remained relatively high on both the outstanding loan amounts (3.0%) and on new businesses (2.9%) in spite of low interest rate environment in Latvia. The increase of the Lithuanian banking sector's profit also came from the net interest income improvement. The Lithuanian banks also managed to cut their interest expenses as residents reduced their fixed-term deposits significantly.

The capital adequacy slightly decreased in all of the three Baltic countries compared to the previous year but the banking system remained well capitalized in 2016.

The banking sector of the Baltic region is majorly owned by financial groups located mainly in the Nordic and Baltic countries

Estonia

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	Impaired loan ratio	Impaired loan vol.	Major owner
1	SWED	9,716	6,822	1,627	212	2.2%	13.0%	1.8%	120	Swedbank AB
2	SEB	5,582	4,225	782	71	1.3%	9.1%	0.6%	25	Skandinaviska Enskilda Banken AB
3	Nordea	3,628	3,490	FB	24	0.7%	FB	FB	FB	Nordea Bank AB
4	Danske	1,699	898	FB	16	0.9%	FB	1.1%	10	Danske Bank Group
5	LHV	895	543	75	10	1.1%	13.3%	2.5%	14	LHV Group
6	DNB	831	534	109	6	0.7%	5.5%	3.7%	20	DNB Bank ASA
7	Bigbank	394	61	101	12	3.0%	11.6%	7.3%	4	Private Individuals
8	Krediidipank	290	155	30	2	0.6%	5.9%	4.0%	6	Coop Investeeringud OÜ
9	Versobank	200	43	19	1	0.6%	6.8%	4.6%	2	Ukrselhosprom
10	Pohjola	FB	FB	FB	FB	FB	FB	FB	FB	OP Financial Group
	Banking sector total	24,808	15,210	3,225	358	1.4%	11.1%	0.9%	172	

Source: Banks' data disclosure, Eesti Pank, ECB CBD, ISI Emerging
Note: Individual banks' loan volumes and ratios are impaired, banking sector total loan volume and ratio are 60 days past due
FB: foreign branch

Latvia

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	Impaired loan ratio	Impaired loan vol.	Major owner
1	Swedbank	5,315	3,189	716	93	1.7%	13.0%	2.2%	70	Swedbank AB
2	ABLV Bank	3,877	814	322	79	2.0%	24.5%	4.3%	35	Ojegs Fijs
3	Rietumu Banka	3,594	1,224	477	86	2.4%	18.0%	17.2%	211	Private
4	AB SEB bankas	3,574	2,534	425	51	1.4%	12.0%	1.3%	32	Skandinaviska Ensklida Banken AB
5	Nordea Bank AB Latvijas filiāle	3,220	2,630	FB	39	1.2%	FB	FB	FB	Nordea Bank AB
6	Citadele banka	2,760	1,316	238	36	1.3%	15.1%	3.7%	48	EBRD
7	DNB banka	2,114	1,497	298	30	1.4%	10.1%	8.6%	129	DNB Bank ASA
8	Norvik Banka	926	213	105	11	1.2%	10.5%	50.9%	108	Private Individuals
9	Baltikums Bank	672	116	58	7	1.0%	12.1%	25.5%	29	Private Individuals
10	Reģionālā investīciju banka	502	135	37	3	0.5%	7.1%	39.3%	53	SKY Investment Holding LLC
	Banking sector total	29,676	7,943	2,993	429	1.4%	14.3%	4.4%	448	

Source: Banks' data disclosure, Bank of Latvia, ECB CBD, ISI Emerging
Note: Individual banks' loan volumes and ratios are impaired, banking sector total loan volume and ratio are 90 days past due
FB: foreign branch

Lithuania

#	Bank (2016, EUR mn)	Assets	Loans	Equity	Net Profit	ROA	ROE	Impaired loan ratio	Impaired loan vol.	Major owner
1	AB SEB bankas	7,524	4,941	793	94	1.2%	11.9%	1.4%	71	Skandinaviska Ensklida Banken AB
2	Swedbank, AB	7,327	4,607	721	90	1.2%	12.5%	1.8%	84	Swedbank AB
3	AB DNB bankas	3,995	2,844	471	23	0.6%	4.9%	7.4%	212	DNB Bank ASA
4	Nordea	3,160	FB	FB	22	0.7%	FB	FB	FB	Nordea Bank AB
5	AB Šiaulių bankas	1,824	1,045	173	42	2.3%	24.3%	1.5%	16	EBRD
6	Danske Bank	1,160	735	FB	9	0.8%	FB	FB	FB	Danske Bank
7	AB Citadele bankas	504	228	50	2	0.5%	5.0%	2.7%	6	Citadele Banka AS
8	UAB Medicinos bankas	236	145	27	6	2.6%	22.7%	13.0%	19	Saulius Karosas
	Banking sector total	25,754	16,475	2,222	264	1.0%	11.9%	3.7%	905	

Source: Banks' data disclosure, Bank of Lithuania, ECB CBD, ISI Emerging Markets
Note: Individual banks' loan volumes and ratios are impaired, banking sector total loan volume and ratio are 90 days past due
FB: foreign branch

List of abbreviations

bn Billion

BNB Bulgarian National Bank

BSI Bank of Slovenia

CAR Capital Adequacy Ratio

CBBH Central Bank of Bosnia and Herzegovina

CCB Countercyclical Capital Buffer

CEE Central and Eastern Europe

CHF Swiss Franc

CIR Costtoincome ratio

CNB Czech National Bank

EBA European Banking Authority

EBRD European Bank for Reconstruction and Development

ECB European Central Bank

ECB CBD European Central Bank Consolidated banking data

EIU Economist Intelligence Unit

EUR Euro

FX Foreign exchange

GDP Gross Domestic Product

HNB Croatian National Bank

HUF Hungarian forint

IPO Initial Public Offering

L/D ratio (L/D) Loantodeposit ratio

mn Million

M&A Mergers and Acquisitions

NBR National Bank of Romania

NBH National Bank of Hungary

NBP National Bank of Poland

NBS National Bank of Slovakia/National Bank of Serbia

NBU National Bank of Ukraine

NIM Net interest margin

NPL Nonperforming loan

PLN Polish zloty

ROA Return on Assets

ROE Return on Equity

SME Small and mediumsized enterprises

UAH Ukraine Hryvnia

USD United States Dollars

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