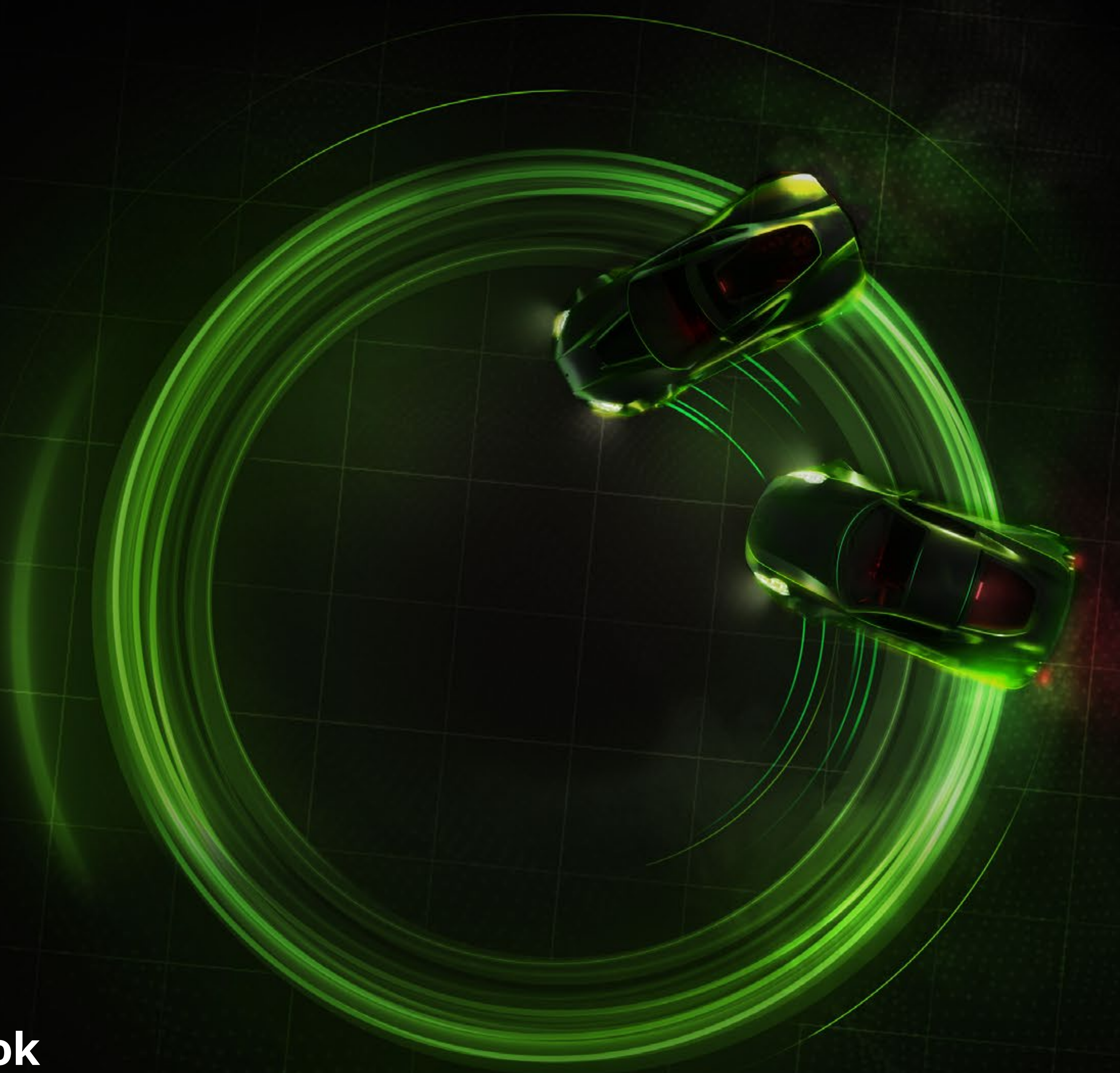

# CE Banking Outlook

## Winning in the Digital Arms Race

October 2016

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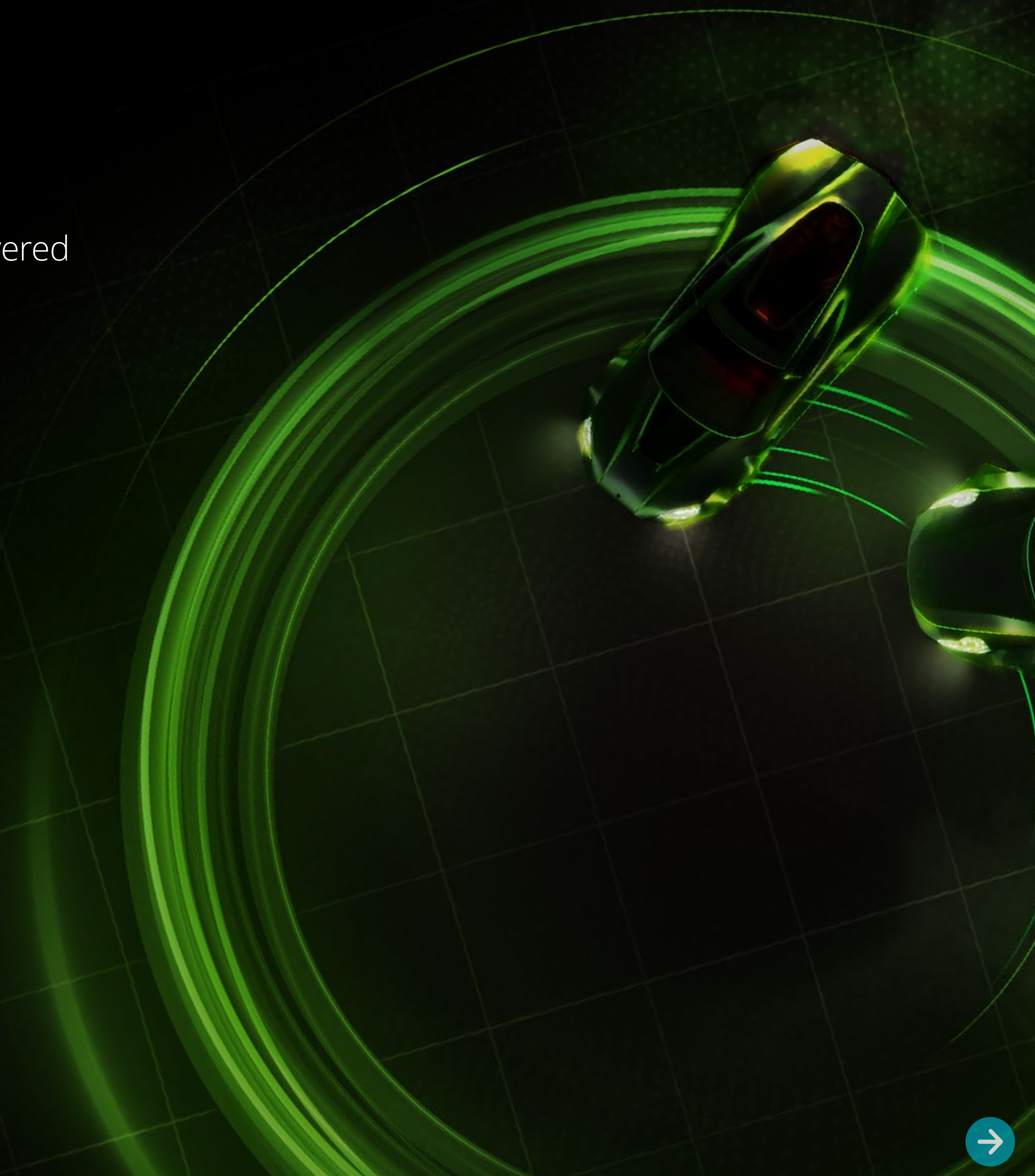

# Foreword

**Although the performance of the banking sector in Central Europe (CE) is shifting up a gear as lending growth accelerates and asset quality improves, profitability is still well below pre-crisis levels. With low interest rates driving margin compression and a rising regulatory burden, banks need to improve operating efficiency.**

The digital maturity of banks in CE countries varies greatly but digitalization is a strategic priority for all. It can not only provide a key avenue for banks to reduce their cost to serve, it is also an imperative that enables them to keep pace with the expectations of customers who are increasingly online and mobile. M&A activity has picked up visibly in CE in recent years, with growing activity in Southern markets (Hungary, Slovenia and Romania), supported by stabilizing asset quality and often involving non-bank buyers (such as private equity funds and insurers). Uneven profit distribution in the banking sector and the advantages of scale will drive further consolidation.

While Europe's economic recovery is expected to slow in 2016 and 2017, and the UK's Brexit vote has increased uncertainty, conditions are expected to remain relatively favourable for CE banks. The Economist Intelligence Unit (EIU) is forecasting GDP growth for the CE region to be 2.8% for the whole of 2016, and 2.7-3.0% in 2017-18 (1.3-1.5 percentage points above the eurozone). This relatively healthy economy has led a faster recovery of loan growth in CE to 3.4% y/y in 2015 (3 p.p. above Euro area) and should allow a further pick up to 5.0% y/y in 2018.

Asset quality has also been improving, with the non-performing loan (NPL) ratio in CE down from a peak of 11.0% in 2013 to 8.8% in 2015 and is expected to fall to a level of 7.0% in 2018. As the region's recovery progresses, the disparities between the leading countries in the north (Poland, the Czech Republic and Slovakia) and those in the south (Hungary, Romania, Bulgaria, Croatia and Slovenia) are expected narrow.

The Return on Equity (ROE) of CE banks rose to 6.7% in 2015 from 4.5% in 2014, maintaining a gap of nearly 2 percentage points over banks in the eurozone. Falling costs of risk, a pick-up in lending to support revenue growth and cost containment are all expected to help drive a further improvement in ROE to 7.8% by 2018. However, ROE will remain far below the pre-crisis double-digit level and even the 8-9% level of 2009-10. Limiting factors are margin pressure, with interest rates in CE at record lows, and higher regulatory burdens (such as Poland's bank levy and rising capital requirements). CE banks have a much higher net interest margin (2.4% in 2015) than those in the euro area (1.3%), but they also rely more on net interest income (which represents 67% of their net revenues). Already down from 2.7% in 2012, the net interest margin of CE banks is expected to fall further to 2.2% in 2018 (even while Poland's banks should buck the trend as the costs of the bank levy are passed on to customers). Improving cost efficiency will therefore be a key priority for CE banks, a factor that will help drive both consolidation and digitalization.

M&A in the region has picked up in recent years. The number of transactions per annum involving a target with at least EUR 0.7 bn of assets has steadily grown, from 1-2 in 2011-12 to 5-7 in 2014-15. This increase in activity has been driven largely by markets in the south (Hungary, Slovenia and Romania), which between them accounted for 11 of 17 transactions in 2014-16. This was accompanied by increased buying by non-banks (organizations such as private equity funds and insurers), which accounted for 8 of 17 transactions in 2014-16. This suggests that further growth in M&A activity lies ahead, as many new PE owners will seek to build the value of their holdings through consolidation and restructuring before eventually exiting in years to come.

Consolidation will also be driven by the advantages of scale. The distribution of net profits in the CE banking sector is skewed towards banks with larger market share: those in the top quartile achieved an average ROE of 10% in 2015, while those in the bottom quartile on average only broke even.

More than 95% of the banks surveyed in Deloitte's CE Top 500 have put a digital strategy in place. However, the 76 banks included in our digital maturity analysis show a wide variation in their approach and level of development, leaving only a narrow set of core digital functionalities. Only 13% of features were present in more than 80% of the banks we analyzed. With such diversity, there are clear leaders and laggards. Poland (48.1% of identified best practices) and Slovakia (47.5%) lead CE in terms of digitalization, followed by the Czech Republic (40%), Romania (37%) and Bulgaria (37%). Hungary (32%), Croatia (32%) and Slovenia (29%) lag behind.

Development efforts have so far focused primarily on customer acquisition and day-to-day banking, but banks are already taking the first steps towards the full digitalization of their sales processes. Mobile banking functionality in CE still has a long way to go to converge with what is already available via the internet. However, in countries that have lagged behind in developing internet platforms,

there is now a strong argument to focus first on mobile.
This report examines the outlook for performance, consolidation and digitalization in the CE banking sector. It seeks to identify key drivers of profitability and balance sheet growth over the next three years, while examining competition in each CE market. The report analyzes the advantages of scale and trends in M&A activity and, explores in detail the digital development of CE banks. We hope the study will help readers better understand the challenges and opportunities facing the region.

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# Executive Summary

**Despite a backdrop of slower expansion in the eurozone, economic conditions for Central Europe's banks are relatively favourable.** GDP growth expectations for CE are above those of the eurozone by around 1.3-1.5 percentage points, standing at 2.8% in 2016 and 2.7-3.0% in 2017-18.

**Asset quality is improving. While there are significant variations in asset quality, non-performing loan (NPL) ratios have been falling in every CE country.** The costs of risk across the region fell from 1.7% of average gross loans in 2012 to 1.2% in 2015, and appear set to decline to 0.9% in 2018.

**Net interest margin is declining in an environment of low interest rates. After falling from 2.7% in 2012 to 2.4% in 2015, a further decline to 2.2% is expected in 2018.** All CE countries face a declining margin except for Poland, which is expected to buck the trend following the introduction of a bank levy.

**Interest rates are at record lows in both Europe as a whole and the CE region, and no significant increase is expected in 2016-18.** Easy monetary policy will help spur on the economy and stimulate lending growth, it is putting bank margins under pressure.

**Loan growth is picking up. After rising from 2.3% in 2014 to 3.4% in 2015, a further acceleration in lending is expected to reach 5% in 2018.** The weakest markets (Slovenia, Croatia, Bulgaria, Romania and Hungary) will benefit from recovery while the current leaders (Poland and Slovakia) face more moderate growth.

**The profitability of CE banks is on a trend of improvement. The Return on Equity (ROE) of CE banks improved to 6.7% in 2015 (up from 4.5% in 2014) and it is expected to rise again to 7.8% in 2018.** While facing pressure on their margins and high regulatory costs, CE banks will benefit from the falling costs of risk.

**Profitability is below pre-crisis levels and distribution is uneven, skewed towards those players with higher market share.** Smaller banks in the bottom quartile are at breakeven, while those in the top quartile have an average ROE of 10%.

**CE banks are investing in digital now to enable future transformation.** While necessary to satisfy customer expectations, digitalization will also drive down branch numbers, reduce cost to serve and lead to better efficiency in the medium term.

**Digital banking maturity is highly differentiated among CE countries with clearly visible pioneers and laggards.** Benchmarked against the best practices of the 5 leading banks in CE, most digitally mature markets are Poland (48,1%) and Slovakia (47,5%) followed by the Czech Republic (40%), Romania, (37%), Bulgaria (36,9%), while Hungary (32,3%), Croatia (31,9%) and Slovenia (28,8%) lag behind.

**Consolidation in the sector has accelerated in recent years and is ongoing.** While transactions are continuing to shape the Polish market (the region's largest), stabilizing asset quality and a return to profitability are helping to drive an increase in transactions in the Southern markets of Romania, Hungary and Slovenia.

**Approaches to digitalization in CE region vary greatly.** Among the 76 analyzed banks, only 13% of internet functionalities were present in more than 80% of institutions. Functionalities in digital channels are focused around day-to-day banking and customer acquisition but many banks have yet to begin to digitalize sales processes.

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## Despite the backdrop of a slower expansion in the Euro area, economic conditions are expected to be relatively favorable for CE banks

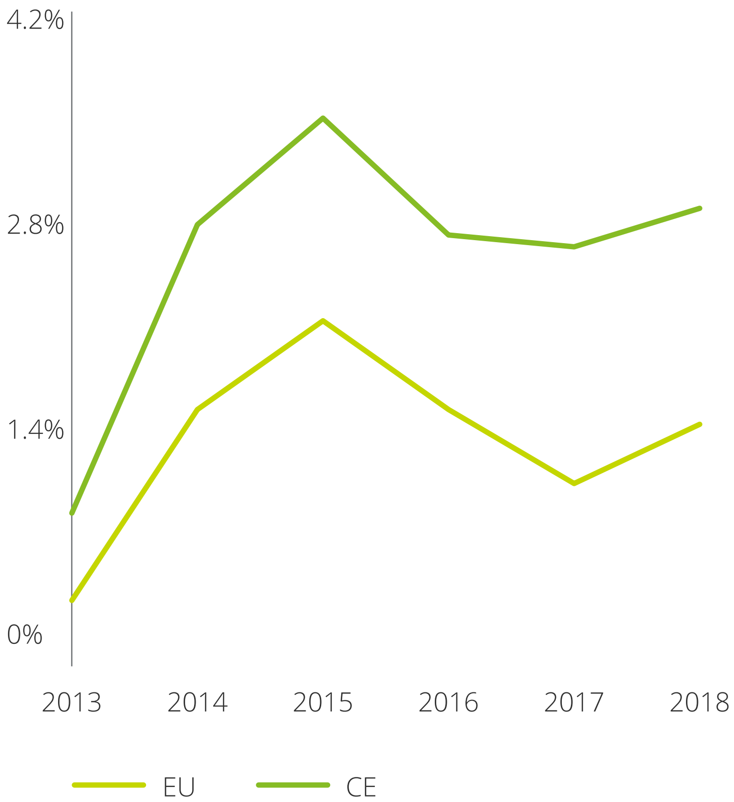
Although the economic recovery in Europe is expected to slow this year and next, conditions are expected to remain relatively favorable for CE banks. The growth expectations of EIU for the CE region in 2016-18 are 1.3-1.5 p.p. above those for the Euro area, mainly reflecting stronger growth of domestic demand and particularly of private consumption.

The Brexit vote has increased uncertainty and triggered a downgrade of growth forecasts for both the UK and the Euro area. While there has been a limited economic impact so far, the base scenario of the EIU remains for a recession in the UK next year. With questions about the future of the EU weighing on confidence and investment, Euro area GDP growth is also forecast, by the EIU, to slow from 2.0% in 2015 to 1.5% in 2016 and 1.3% in 2017 before picking up to 1.5% in 2018.

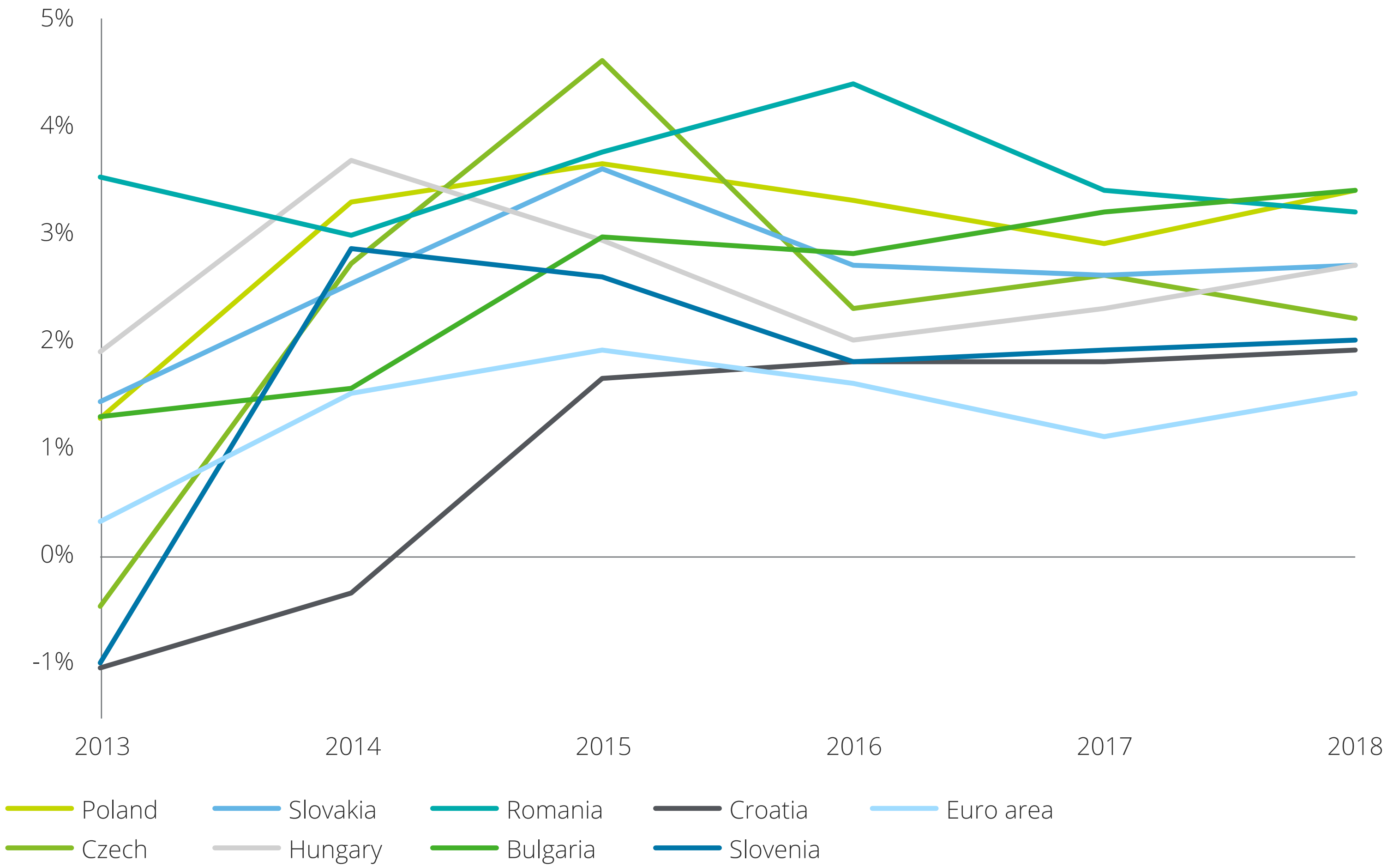
The GDP growth of CE[1] is expected to slow in comparison to 2015 (3.6%) but remain relatively robust at 2.8% in 2016 and 2.7-3.0% in 2017-18. The main driver of growth will be private consumption, gaining pace on the back of improving labor markets. Investment growth is slowing this year, affected by lower EU funds absorption due to the transition between programming periods, but should pick up in 2017-18. Some CE countries lag the region's GDP growth but all are expected to outpace the Euro area.

1 Estimated based on EIU country forecasts for Poland, the Czech Republic, Hungary, Romania, and Bulgaria, Slovenia and Croatia

**GDP growth in CE will outpace the Euro area in 2016-18 by 1.3 – 1.5 p.p. per annum**




**All CE countries will outpace Euro area in 2016-18**



## Interest rates in Europe are at record lows and little increase is expected in 2016-18, spurring loan growth but putting pressure on bank margins

Interest rates in Europe and CE are at record lows and are likely to remain very low in 2016-18. To help spur economic growth, the ECB has adopted an increasingly expansionary monetary policy, cutting its deposit rate to -0.4% this year, while also encouraging growth through quantitative easing and long-term refinancing operations. Euribor 3M has fallen to -0.3% and interbank rates across CE have also fallen to record lows, albeit remaining in positive territory (apart from Euro area members Slovenia and Slovakia). The highest interest rates in CE are in Poland, 1.7% on average in 2016, while all others are 1.0% or lower. The EIU does not expect any increase of the ECB's benchmark rate in 2016-18. Interest rates are assumed by Deloitte to remain depressed in CE as well, though an eventual pick-up in inflation could lead to a rise in some countries by 2018. While persistently low interest rates should encourage an acceleration of loan growth and help lower risk costs, they are also expected to drive margin pressure.



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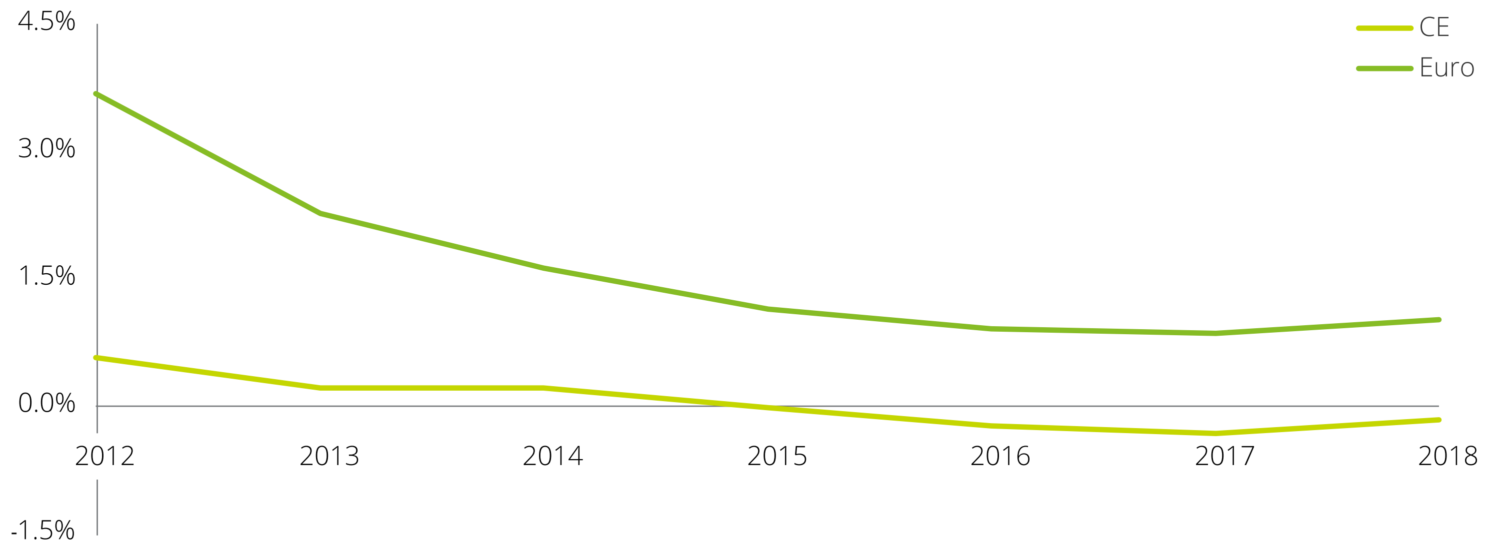
**Chart: CE interest rates (average, range) versus Euro area rates**




| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|
| MAX | 7.0 | 4.3 | 2.5 | 1.8 | 1.7 | 1.7 | 1.8 |
| MIN | 0.6 | 0.2 | 0.2 | -0.02 | -0.3 | -0.4 | -0.2 |

No increase in ECB policy rates is forecast in 2016-18

**Note:** CE line is a weighted average of interest rates with total assets as weights, minimal value of interest rates are Euro rates because of the presence of Slovakia and Slovenia
*Source: Bloomberg*

## Euro area banks are finally seeing loan growth but low profitability indicates a need to improve operating effi-ciency

Euro area banks are seeing modest loan growth again but their still low profitability indicates a need to improve operating efficiency. Return on equity among Euro area banks improved to 4.8% in 2015, from 3.2% in 2014, but it remains well below banks' cost of equity of 7-8%[2] in 2015. Meanwhile, the bar is being raised as banks continue to build higher capital ratios (tier 1 of 14.6% in 2015).

Loan growth (non-financial sector, excl. government) in the Euro area, after declining in 2012-14, turned positive in 2015 (+0.4% y/y) but the recovery has been very gradual (+1.1% y/y in 1H16). While low interest rates should encourage a further pick up in lending, they are also a driver of margin pressure, which is likely to be a drag on revenue growth. Euro area risk costs have trended lower since 2012 but there are large differences in loan quality and NPLs are still very high on many markets (e.g. Greece, Italy, Portugal), which limits the room for further improvement.

To sustainably grow profitability, Euro area banks need to improve operating efficiency and reduce their cost/income ratio (63% in 2015). Banks are in a process of retrenchment, redefining and focusing more on their core markets and reducing branches and employment. Digitalization is changing the banking sector landscape, bringing opportunity for banks to further reduce costs but also making transformation an imperative.

2 Source: ECB, estimated range of expected return for EuroSTOXX Banks index in 2015

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## Increasing access to broadband and mobile internet supports rising penetration of digital banking services in EU, while CE countries are converging towards Western standards

European countries are constantly increasing access to broadband and mobile internet and banks are seizing this opportunity. In 2011-2015, the share of individuals in the EU which used internet services at least once in the last 3 months increased from 71% to 79%, out of which 58% used the internet to access banking services (versus 51% in 2011). Similar trends are expected to influence mobile banking, as penetration of mobile internet in EU increased by 33 p.p. from 19% in 2011 to 52% in 2015%. Given this strong growth trend, Western European banks have focused on digital competencies, developing them internally or acquiring leading players in this area – for example, Spanish BBVA acquired American Simple in 2014 and Finnish Holvi in 2016. Although access to internet services in CE markets lags behind Western European countries (internet penetration in 2015: 70%, mobile: 41%),[3] CE banks are already strongly focusing on digital channels, expecting that their local markets will follow the same direction. Among 76 analyzed banks from 8 European markets, all of them were present in the internet channel and 88% had a native mobile banking application. Given that simple presence in digital channels is no longer a competitive advantage, banks have started a digital arms race to offer constantly new functionalities. In our analysis measuring the digital banking maturity of banks in CE, we have identified and analyzed more than 350 functionalities.

3 Source: Eurostat

## Profitability of CE banks is above that of Euro area banks thanks to their wider margin, but they are also more reliant on net interest income

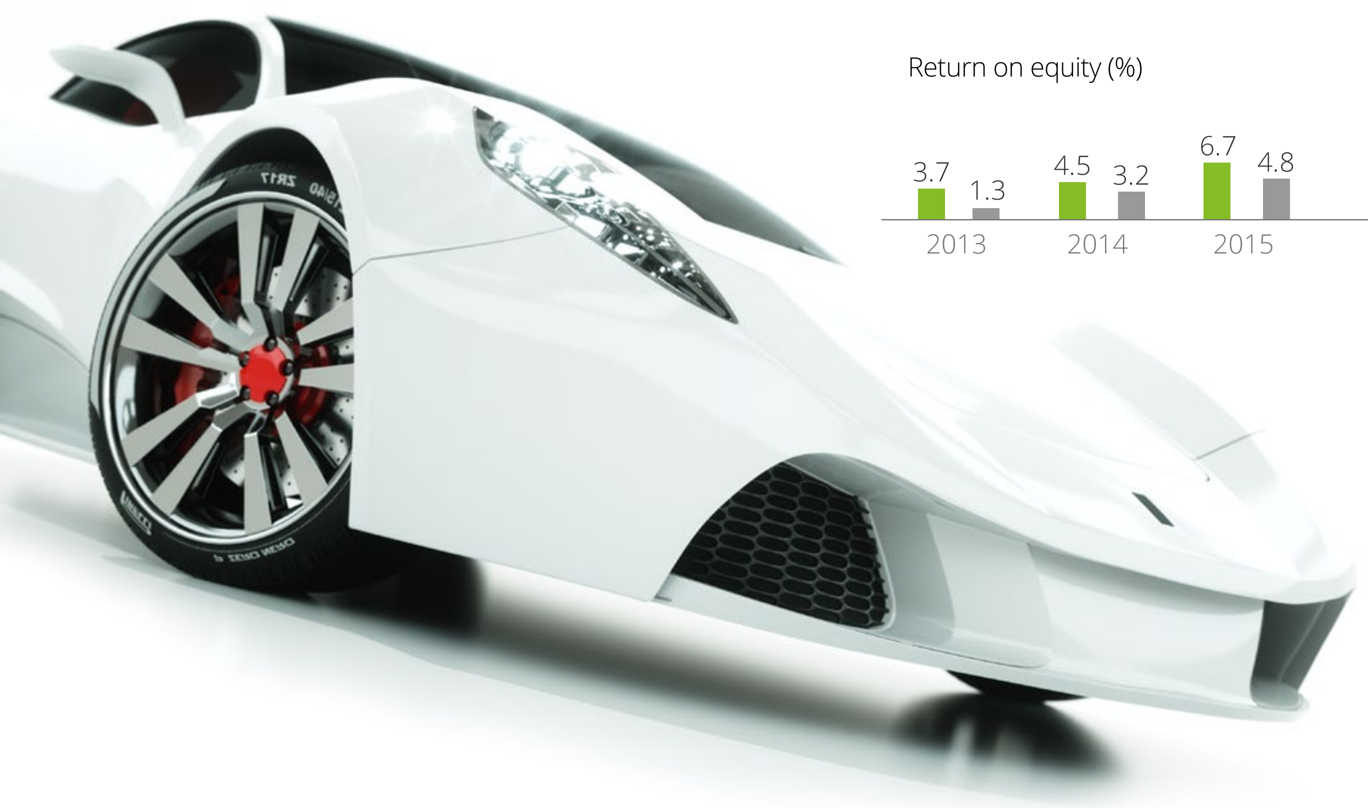
The profitability of CE banks is above that of Euro area banks, mainly due to their wider net interest margin, but they are also more reliant on net interest income as a source of revenue. The ROE of CE banks was 6.7% in 2015, up from 4.5% in 2014. This is still far from the pre-crisis double-digit level (16-18% in 2007-08) or even the 8-9% level of 2009-10. However, CE banks' ROE has maintained a gap of nearly 2 p.p. on average over Euro area banks in recent years.

This is mainly thanks to the higher net interest margin of CE banks at 2.4% in 2015 versus Euro area banks at 1.3%, while net fee income (as a % of average assets) is also better (0.9% versus 0.6%).

This advantage on revenue more than offsets the higher risk costs and higher capital held by CE banks. Risk costs for CE banks at 1.2% (of average assets) are 0.7 p.p. higher than for Euro area banks, while their equity/assets ratio of 10.6% is 4.2 p.p. higher.

CE banks have a lower cost/income ratio (56.6%) than Euro area banks but this reflects the revenue side of the equation and the region's wide margin. CE banks rely more on net interest income (67% of net revenues) than Euro area banks (57%), which presents a challenge going forward, as the low interest rate environment puts ongoing pressure on bank margins. Hence, improving cost efficiency will be no less important for CE banks than for those in the Euro area.

## Profitability of CE banks is higher than in Euro Area mainly thanks to higher net interest margin




*Source: ECB, Central Banks, Deloitte estimates*

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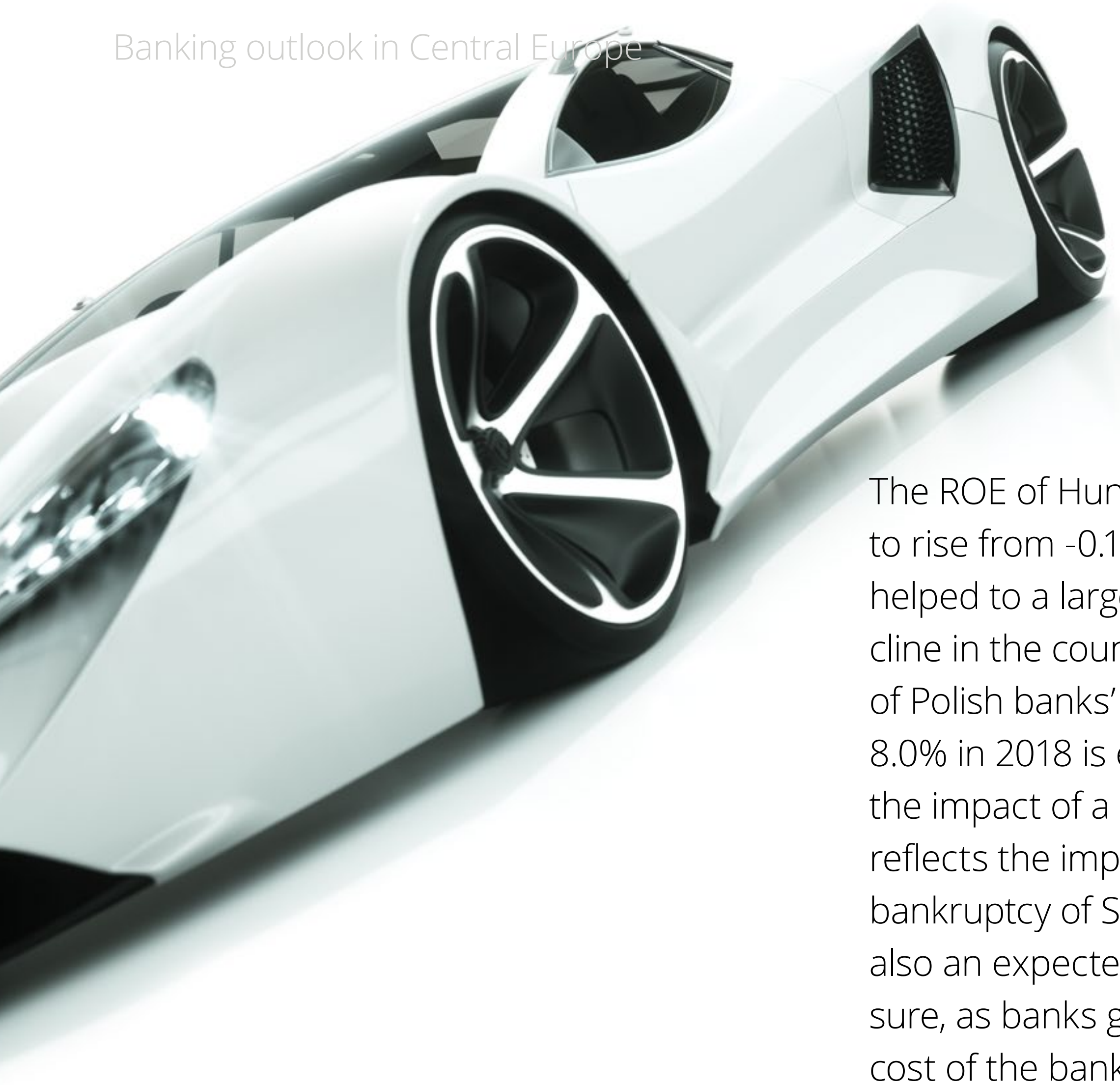
## Profitability of CE banks is expected to remain on an improving trend...

The profitability of CE banks is expected to remain on an improving trend, with ROE rising from 6.7% in 2015 to 7.8% in 2018. This will be underpinned by improving asset quality (declining risk costs), a pick-up in lending (growing revenue), and efforts by banks to improve efficiency (containment of costs), including via digitalization. At the same time, however, banks will be facing headwinds from a declining net interest margin in most of the region and from higher industry taxes in Poland. A peak ROE of 9.1% is expected for CE banks in 2016 but this will not be sustainable as non-recurring gains (Visa transaction) and abnormally low risk costs (as provisions created in prior years are released) in some countries (i.e. Slovenia, Hungary) more than offset one-off losses from CHF loan conversion in Romania.

**...driven by a recovery in countries with the weakest profitability...**

The expected improvement in the ROE of CE banks through 2018 will be driven by a recovery of the weakest markets in 2015 (Croatia, Hungary, Slovenia, and Poland). The key drivers of this recovery differ in each market. Due to a deep loss on CHF mortgage conversion, the ROE of Croatia's banks sunk to -8.1% in 2015 but falling risk costs are expected to support a rebound to 5.0% in 2018. Falling risk costs are also the main driver for Slovenia's banks, expected to lift ROE from 2.7% in 2015 to 3.9% in 2018, though pressure on what is already the region's lowest margin will limit upside.



The ROE of Hungary's banks is expected to rise from -0.1% in 2015 to 5.6% in 2018, helped to a large extent (+2-3 p.p.) by a decline in the country's bank levy. The recovery of Polish banks' ROE from 6.6% in 2015 to 8.0% in 2018 is expected to come despite the impact of a new bank levy (-2 p.p.). This reflects the impact of one-off costs from the bankruptcy of SK Bank (-1 p.p.) in 2015 but also an expected absence of margin pressure, as banks gradually pass through the cost of the bank levy to customers.

## ...while those with the strongest ROEs in 2015 face erosion of profitability

Markets with the highest ROE in 2015 (the Czech Republic, Slovakia, Romania, and Bulgaria) will face an erosion of profitability, with margin pressure a common factor. Facing both margin pressure and a bottoming out of risk costs which are at the lowest levels in the region, the ROE is expected to fall for Czech banks from 12.9% to 10.3% and for Slovak banks from 8.4% to 6.3%. There will be no relief for Slovakian banks from the previously planned reduction of the country's bank levy in 2017, as this has now been extended. An improvement in risk costs will provide an offset to margin pressure for Bulgarian banks but their ROE nonetheless is expected to decline from 8.0% in 2015 to 6.7% in 2018. Romanian banks should also see risk costs offset margin pressure but ROE is expected to fall back to 9.2% in 2018 from 11.8% in 2015, a result that was inflated by a one-off revaluation gain (~4 p.p.) on Banca Transilvania's bargain purchase of Volksbank Romania.

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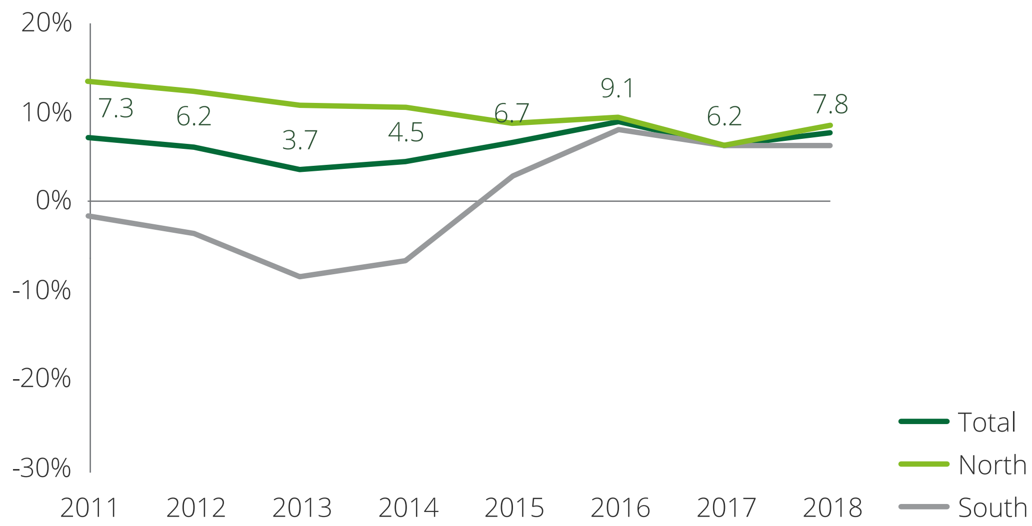
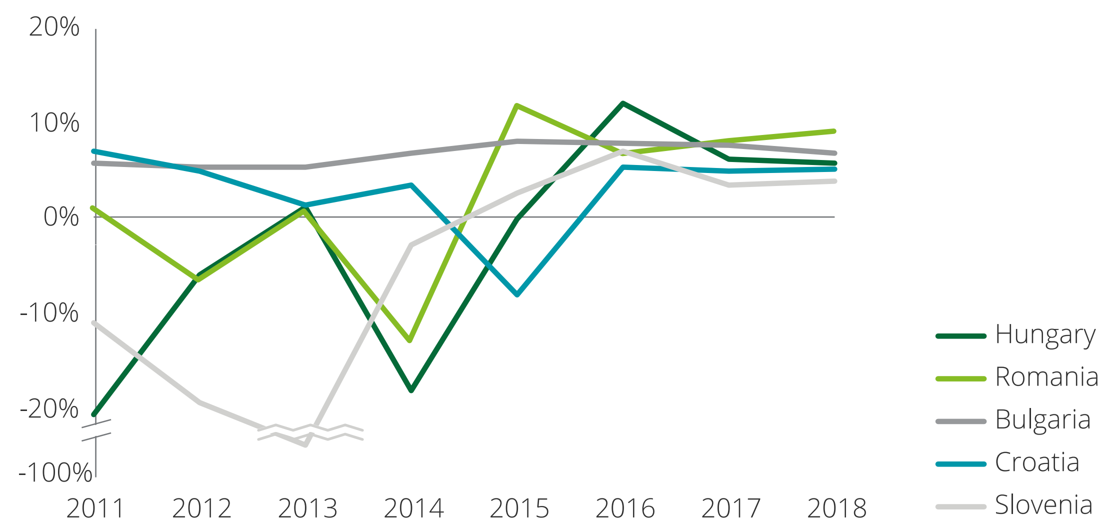
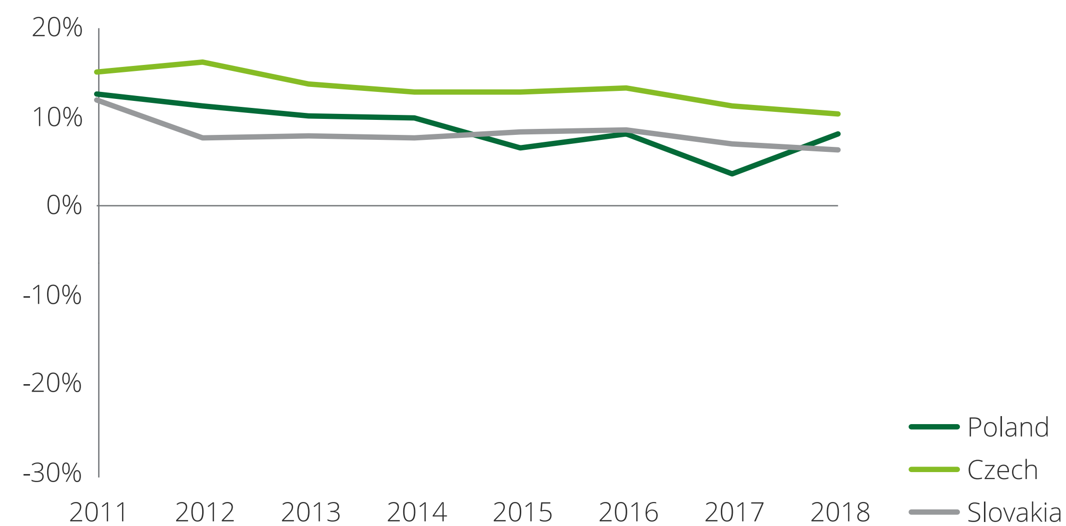
**ROE is expected to rise moderately between 2015 and 2018 led by recovery in Croatia and Hungary**



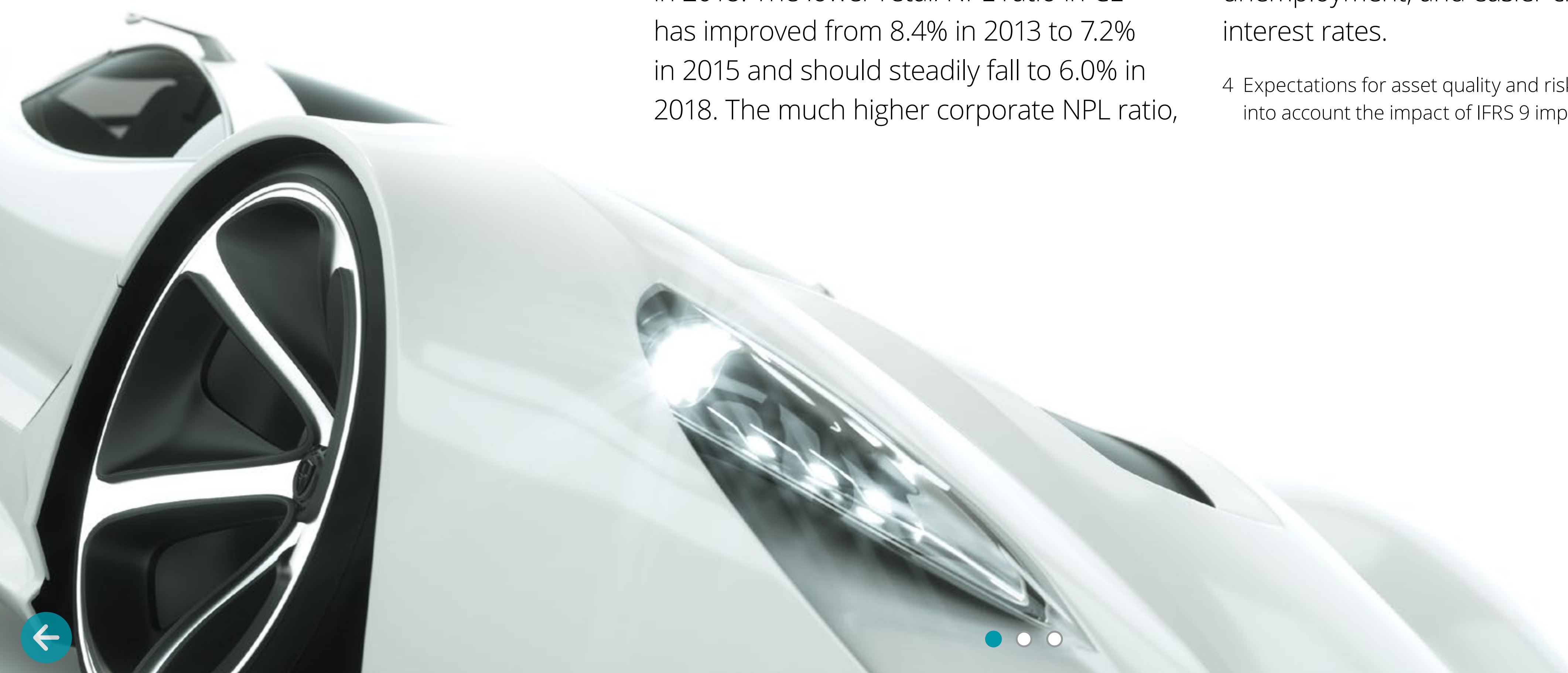




*Source: Central Banks, Deloitte estimates*

## Asset quality is improving across the board...

Although there are still large differences between markets, asset quality in CE is improving across the board, in all countries and in both retail and corporate segments. The NPL ratio in CE has fallen from a peak of 11.0% in 2013 to 8.8% in 2015 and a further decline is expected to a level of 7.0%[4] in 2018. The lower retail NPL ratio in CE has improved from 8.4% in 2013 to 7.2% in 2015 and should steadily fall to 6.0% in 2018. The much higher corporate NPL ratio, which dropped from 15.7% in 2013 to 13.2% in 2015, is expected to fall more steeply to 10.0% in 2018. Drivers behind the improvement include increasing balance sheet cleaning and NPL sales in many CE countries, but also the healthier economic environment of the region in recent years, with falling unemployment, and easier credit, with lower interest rates.

4 Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.



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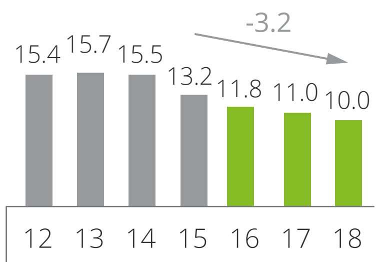
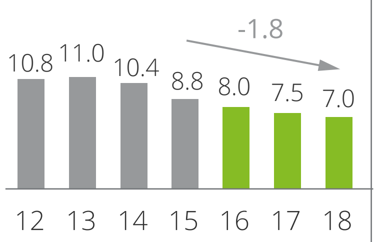
**Asset quality is improving in the retail segment, in the corporate segment and overall**

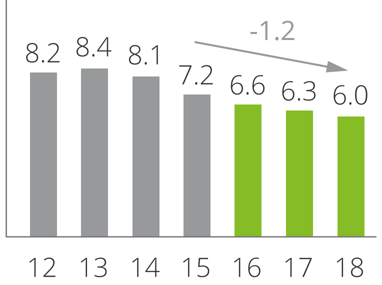
NPL ratio for corporates (%)




NPL ratio for non-financial sector (%)




NPL ratio for households (%)




## ... countries in the South where NPL ratios peaked later are expected to see the biggest gains...

CE countries in the South, where post-crisis NPL ratios peaked later at much higher levels and where the need for balance sheet cleaning is greater, are expected to see the most improvement. Due to its long recession, Croatia's NPL ratio was the last in the region to peak at 17.4% in 2014 and fell only to 17.0% in 2015 but an acceleration of balance sheet cleaning and NPL sales should help lower it below 13% by 2018. While the NPL ratio of Slovenia's banks peaked at 19.9% during 2013, it has since fallen to 10.8% in 2015, helped in large part by EUR 4.8bn of transfers to its Bad Asset Management Company (BAMC). Spurred by another EUR 0.7bn (2 p.p. of gross loans) transfer to the BAMC this year, Slovenia's NPL ratio is expected to fall below 7% in 2018. Although the decline of NPLs in Hungary from a peak of 16.0% in 2013 to 12.3% in 2015 also benefited from transfers to its National Resolution Asset Manager, it is mainly NPL sales that are expected to help drive a further decline to 9.0% in 2018. Bulgaria's NPL ratio has fallen from a peak of 17.2% in 2013 to 15.7% in 2015 but its recently completed asset quality review (AQR) is expected to drive an increase this year before a downward trend resumes towards 13% in 2018. Once the highest in the region, Romania's NPL ratio has declined sharply from 21.9% in 2013 to 13.5% in 2015 and further to 11.3% in 1H16. While balance sheet cleaning will continue, an asset quality review (AQR) in Romania is expected to slow the decline to 10% in 2018.

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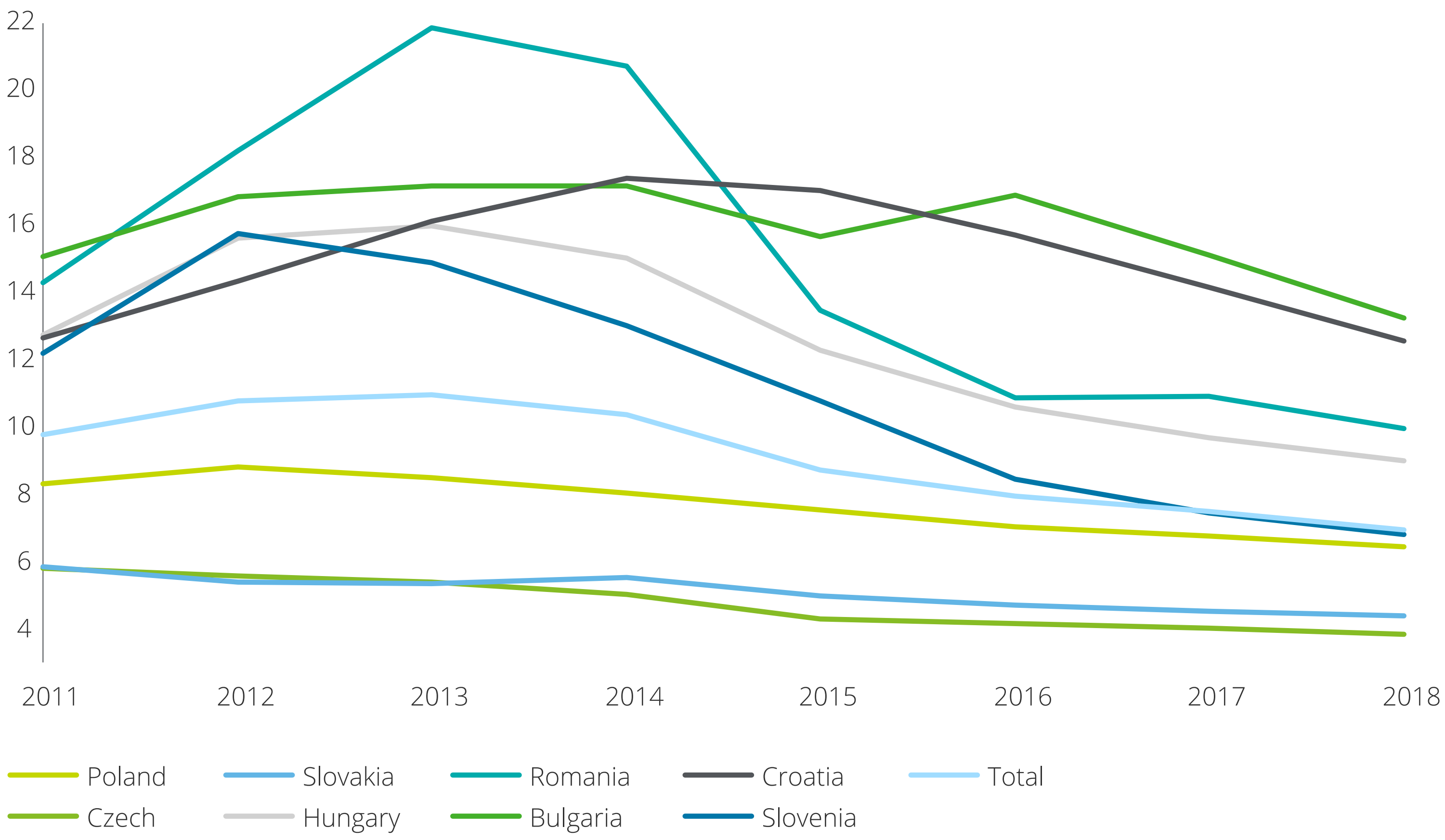
**NPL ratio is falling in all CE countries, although Bulgaria and Romania face speed bumps in 2016-17 due to AQR**




*Source: Central Banks, Deloitte estimates*

## ...countries in the North with relatively low NPL rates are expected to see moderate improvement

With NPL ratios that peaked earlier at lower levels, further asset quality improvement among CE countries in the North will be moderate. While the Czech Republic has the lowest NPL ratio in CE, down from 5.5% in 2013 to 4.4% in 2015, leaving little room for improvement, a benign economic environment is expected to enable a further drop to below 4% in 2018. Asset quality in Slovakia runs a close second behind the Czech Republic, with the NPL ratio down from 5.4% in 2013 to 5.0% in 2015, and it is expected to move lower at a similar pace to 4.4% in 2018. While Poland's NPL ratio is somewhat higher than its northern peers, at 7.6% in 2015 down from 8.5% in 2013, it should also come down more quickly to 6.5% in 2018, supported by banks' sale of NPLs which has broadened to include mortgages and is reaching new highs (1.5 p.p. of gross loans in 2015).

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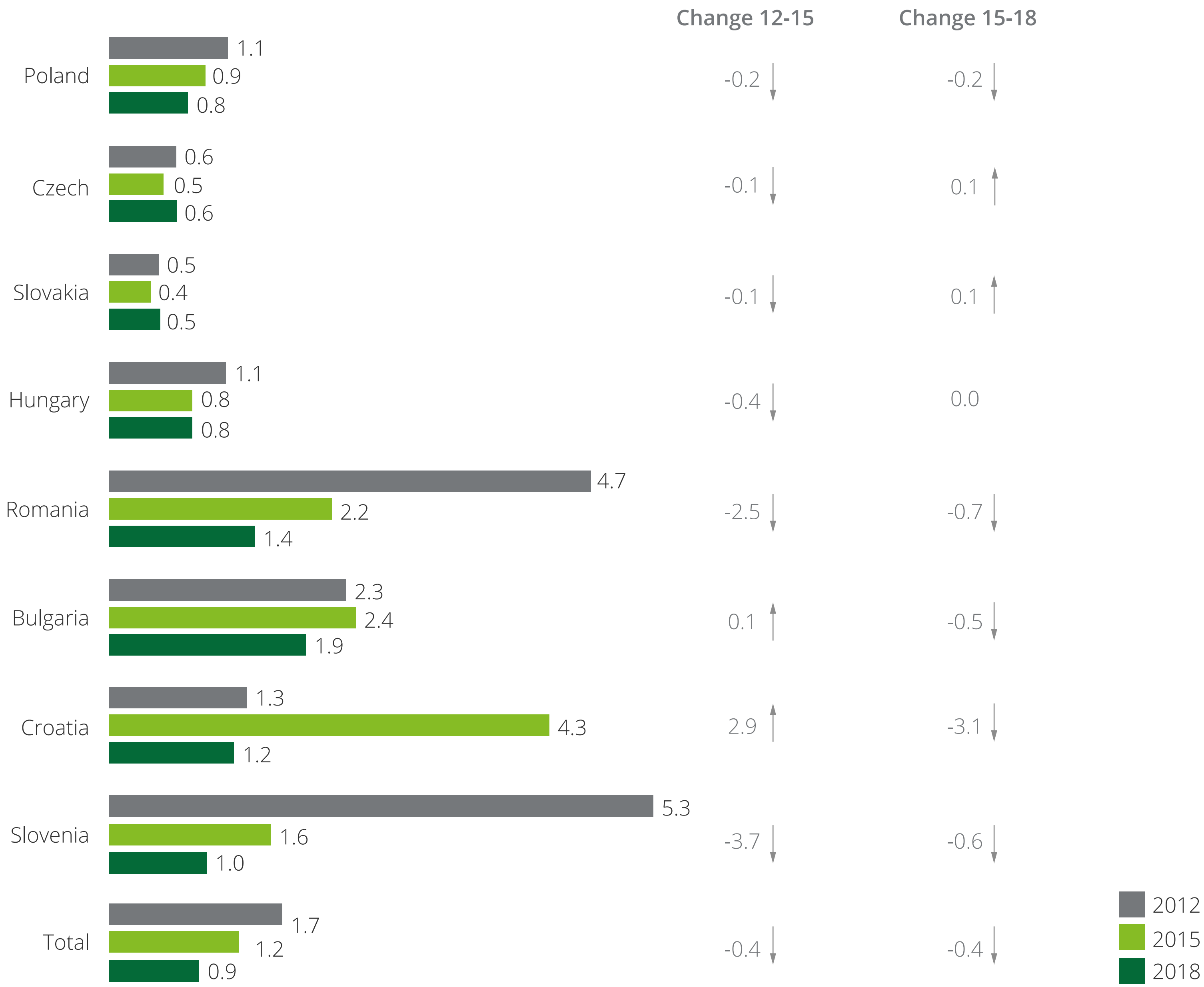
## Risk costs in CE are declining, on the back of improving asset quality, and southern countries are the main beneficiaries

With asset quality in the region improving, risk costs are also moving lower and countries in the South will be the main beneficiaries. Risk costs in the region fell from a recent peak of 2.0% (of avg. gross loans) in 2013 to 1.2% in 2015 and are expected to drop to 0.9%[5] in 2018. This decline is mainly driven by countries in the South, where risk costs have fallen from 4.1% in 2013 to 2.2% in 2015 and are expected to continue to drop to 1.2% in 2018. Risk costs among countries in the North are much lower and improving more moderately from 0.9% in 2013 to 0.8% in 2015 and to an expected 0.7% in 2018. Risk costs can be volatile and, based on 1H16 results, both Hungary and Slovenia appear likely to have abnormally low risk costs this year (resulting from a release of provisions created in prior years). Thus, for CE overall, the drop in risk costs we expect by 2018 may materialize as early as this 2016, levelling out in 2017-18. On a country level, Croatia is expected to see the steepest drop in risk costs (-3.1 p.p.) from 4.3% in 2015 to 1.2% in 2018, as it was burdened in 2015 by one-off costs of CHF mortgage conversion. Most other countries in the South are expected to also see substantial declines over this period, -0.7 p.p. to 1.4% in Romania, -0.6 p.p. to 1.0% in Slovenia, and -0.5 p.p. to 1.9% in Bulgaria. Only Hungary, among southern countries, is expected to see no improvement in 2015-18 as its risk costs last year of 0.8%[6] were already relatively low, due to a release of provisions created in prior periods. In contrast, among northern countries, only Poland is expected to see an improvement in risk costs in 2015-18 by -0.2 p.p. to 0.75%. The Czech Republic and Slovakia have both benefited from a remarkably benign environment in 2015 and, after bottoming out, their risk costs are each expected to rise +0.1 p.p. to 0.6% and 0.5% respectively.

5 Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.

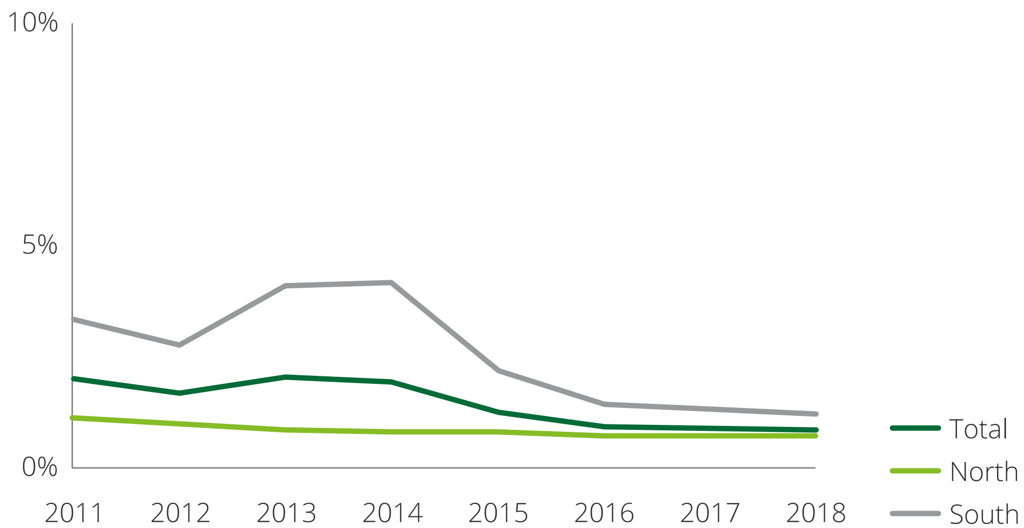
6 Excluding a reversal of provisions booked as extraordinary losses.

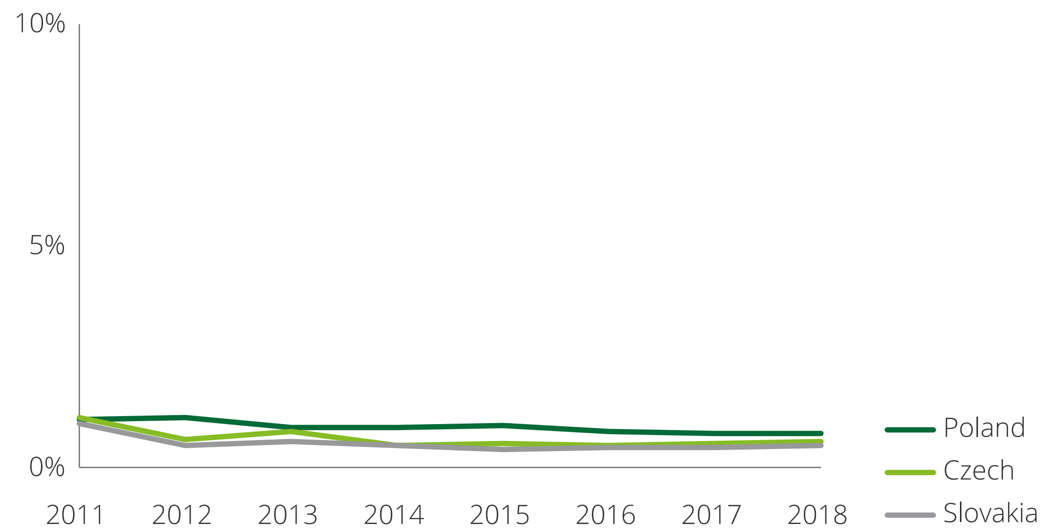
**Cost of risk should decline across CE in 2016-18. Exceptions are SK and CZ which bottomed out in 2015**

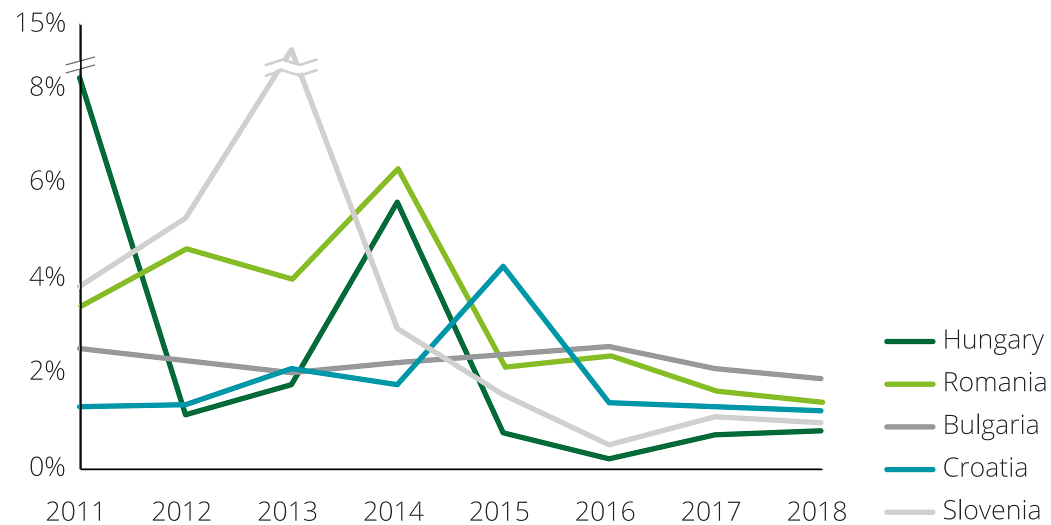



*Source: Central Banks, Deloitte estimates*

**Risk costs in CE are declining, as asset quality improves, and southern countries are the main beneficiaries**




*Source: Central Banks, Deloitte estimates*

## Loan growth relatively fast (vis-a-vis Europe) and improving

The recovery of loan growth in CE in recent years has outpaced the Euro area and the region's relatively healthy economic growth should support a further acceleration in 2016-18. Non-financial sector loan growth in CE has picked up from 0.8% y/y in 2013 to 3.4% y/y in 2015 (3 p.p. above Euro area) and is expected to rise further to 5.0% y/y in 2018. The recovery has been led so far by retail loan growth (4.9% y/y in 2015 up from 2.4% y/y in 2013) but corporate loans returned to positive growth last year (2.4% y/y in 2015 up from -2.4% in 2013). While retail loan growth is expected to ebb and remain between 4-5% in 2016-18, corporate loan growth is expected to continue to accelerate to more than 5% in 2018, supported by a pick-up in investment. Housing loan growth (5.7% y/y in 2015 up from 3.8% y/y in 2013) has led the retail segment in recent years but the pace of growth is expected to moderate to 4-5% in 2016-18. This is expected to result in part from tighter regulation in some countries, imposing stricter lending standards (e.g. higher down payment requirements). In contrast, consumer loan growth (3.7% y/y in 2015 up from 0.2% y/y in 2013), underpinned by robust household spending, is expected to further accelerate to 5-6% in 2017-18.

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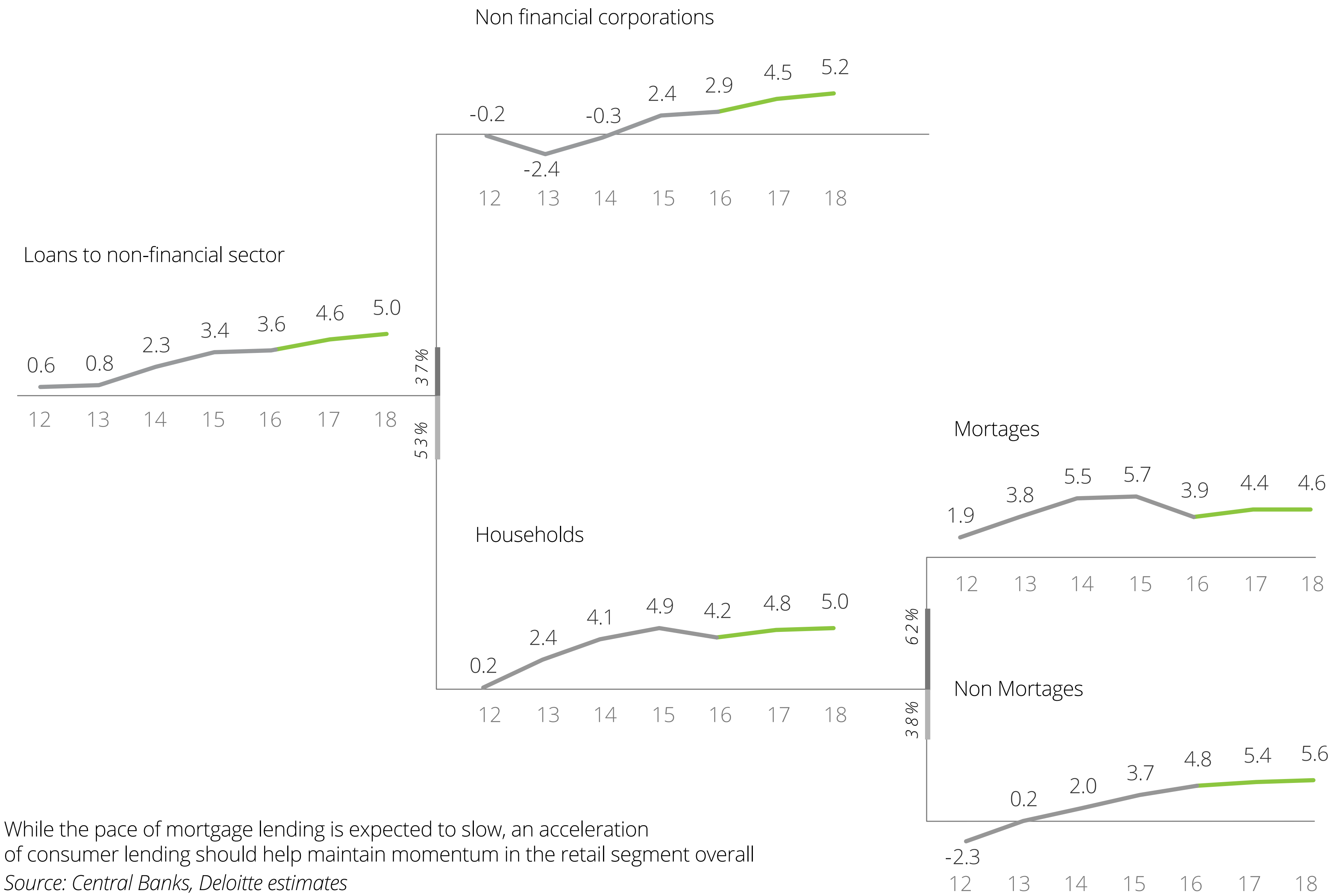
**Loans have been led by retail but corporate lending is expected to accelerate in 2016-18**

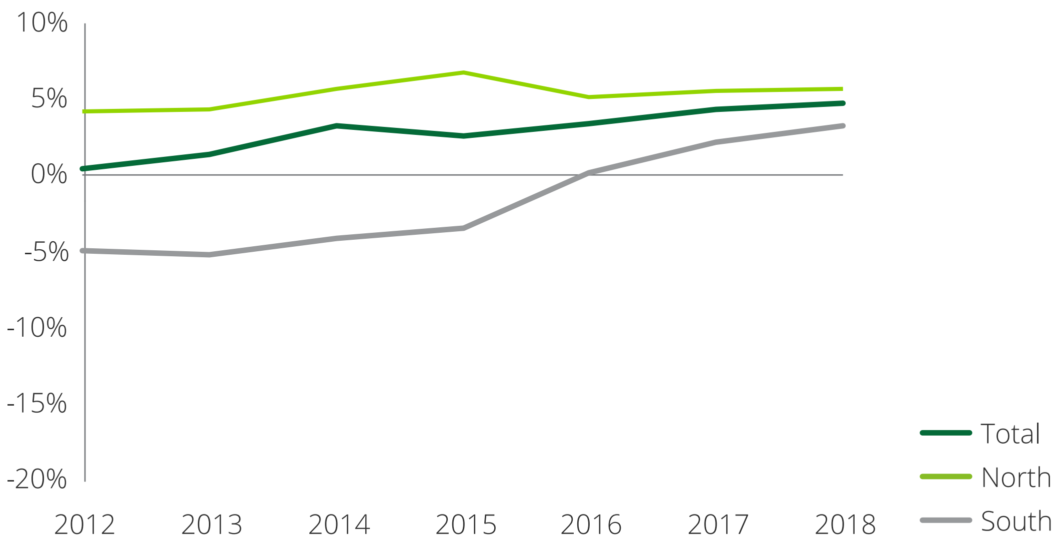


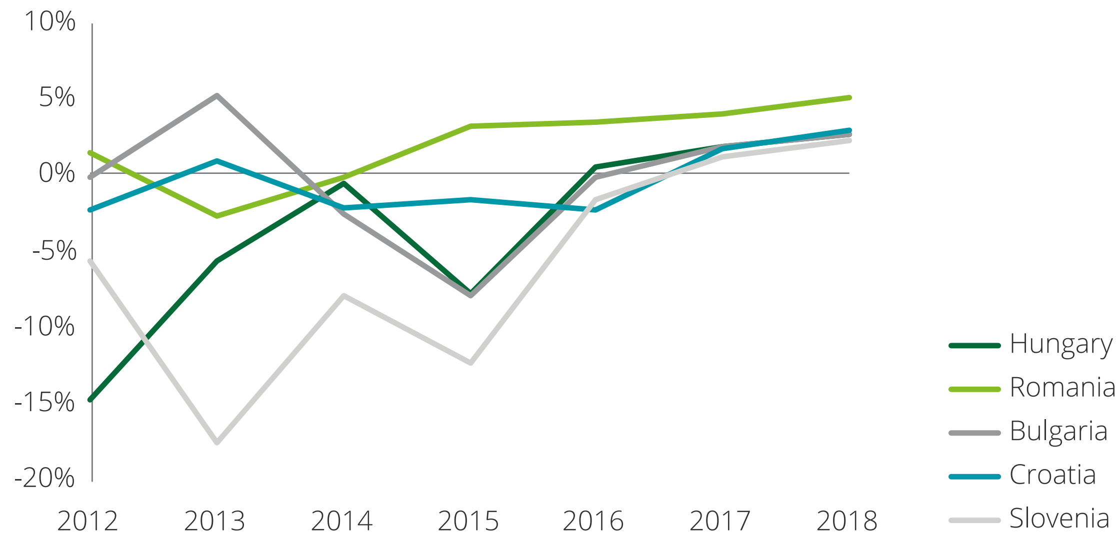

While the pace of mortgage lending is expected to slow, an acceleration of consumer lending should help maintain momentum in the retail segment overall
*Source: Central Banks, Deloitte estimates*

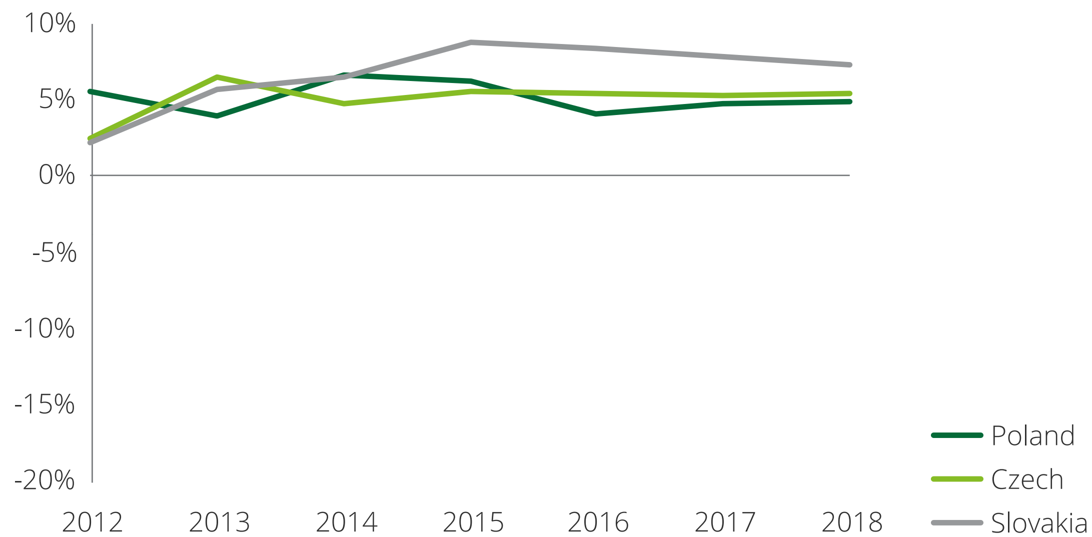
# Large disparities remain in loan growth but should narrow

Large disparities in loan growth remain between the leading countries in the north and those still deleveraging in the south but the gap should narrow markedly in 2016-18. While loan growth in northern countries is expected to moderate from 6.8% y/y in 2015 to 5-6% y/y in 2016-18, southern countries are expected to recover from a drop of -3.5% y/y in 2015 to positive growth this year and accelerate to 3.3% y/y in 2018. The need for further deleveraging in the south has greatly diminished in recent years, with a decline in non-financial loans/deposits from ~120% in 2012 to ~90% in 2015. Asset quality in the banking sector is also improving and the reluctance to borrow in these countries should diminish over time if their economies remain healthy, as we expect they will.
The leaders of CE loan growth are Slovakia and Poland but these countries are expected to lose some of their momentum. Loan growth in Poland is expected to slow from 6.9% y/y in 2015 to 5-6% in 2018, while loan growth in Slovakia is expected to slow from 8.7% y/y in 2015 to 7-8% in 2018. While some moderation is natural vis-a-vis last year's strong performance (also positively influenced in Poland by PLN depreciation), tighter regulation and Poland's new bank levy are contributing factors. Czech loan growth was a more moderate 5.5% y/y in 2015 and is expected to be stable at 5-6% through 2018. In the South where recovery has lagged, loan growth is still negative in most countries but it should be positive for all by 2017-18. Only Romania had positive loan growth in 2015 at 2.5% y/y and is expected to accelerate to 4.6% in 2018 thanks to its strong economic growth (fastest in CE in 2016-18). This is despite a new law on debt discharge in Romania this year that will weigh on its mortgage loan growth in 2016-18. Loan growth in Hungary is expected to turn positive this year and in Bulgaria, Slovenia, Croatia next year, gradually improving to a level of 2.5-3.0% in 2018.

**Large disparities in loan growth between countries remain but should narrow in 2016-18**



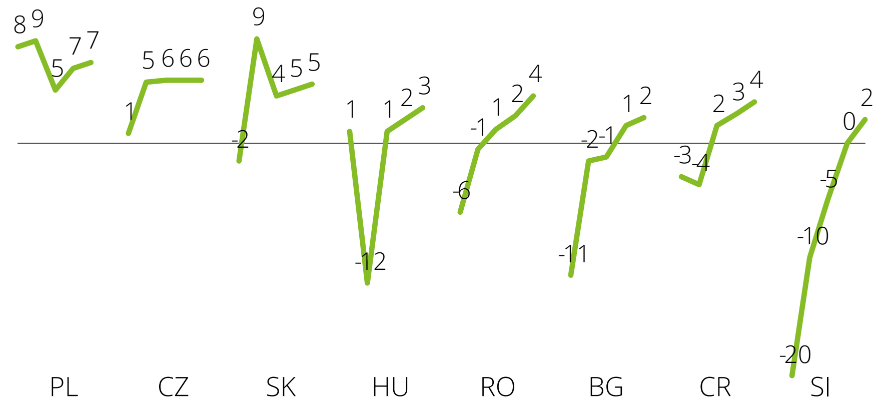




*Source: Central Banks, Deloitte estimates*

**Disparities between countries in loan growth are expected to narrow for both the corporate and retail segments**

Corporate loan growth (%) 2014-2018




Non-financial loan growth (%) 2014-2018


Retail loan growth (%) 2014-2018


*Source: Central Banks, Deloitte estimates*

## Mortgages have led retail growth in leading countries but should slow in 2016-18, while consumer loans accelerate

Mortgage growth (%) 2014-2018


Non-mortgage growth (%) 2014-2018


Tighter regulations will contribute to slowing mortgage loan growth in PL, SK, and RO

*Source: Central Banks, Deloitte estimates*

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## Tightening regulation is a factor that will weigh on loan growth in leading CE markets

Tightening regulation is a factor that will weigh on loan growth in the leading CE markets. Most CE countries have introduced some macro-prudential regulation on lending since the financial crisis, most commonly implementing limits on loan-to-value (LTV), debt service-to-income, or loan maturity. Poland, Slovakia, and the Czech Republic have all introduced new LTV regulations in 2014-15 and the requirements in each case continue to be gradually tightened (i.e. LTV limits are decreasing over time for residential mortgages). Since higher down payment requirements reduces the level of qualifying customers, loan growth in these countries will be lower going forward than it otherwise could have been. Another factor that is expected to weigh on loan growth in Poland is the country's new bank levy (asset tax), as this increases for banks the marginal cost of loans. The impact of this tax is higher proportionately for products with narrow spreads such as residential mortgages vis-a-vis those with higher spreads such as consumer loans. Romania has introduced a new law on debt discharge that permits mortgage borrowers[7] to settle their loan commitments by turning over the title of the mortgaged property to banks. This has naturally driven Romanian banks to increase down payment requirements for new housing loans, which will drive a slowdown in the segment in 2016 and 2017.

7 Mortgages up to EUR 250k, excluding First Home program

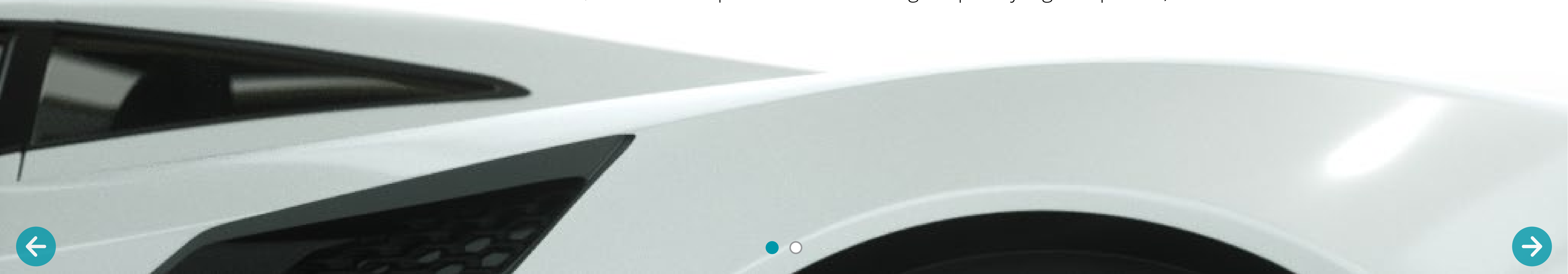
**Tightening regulation will negatively impact loan growth particularly for housing loans in Romania, Slovakia and Poland**

| | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|---|
| Loan-to-value (LTV) | **Romania** 31.10.2011 | | | **Poland** 01.01.2014<br>**Slovakia** 01.11.2014 | **Hungary** 01.01.2015<br>**Czech Republic** 01.06.2015 | **Slovenia** 30.08.2016 |
| Debt-service-to income (DSTI) | **Romania** 31.10.2011 | | | | **Hungary** 01.01.2015 | **Slovenia** 30.08.2016 |
| Loan maturity | **Romania** 31.10.2011 | | | **Poland** 01.01.2014 | **Slovakia** 01.03.2015 | |
| Other | | | | **Croatia** 01.01.2014 *Risk weights* | **Slovakia** 01.03.2015 *Loan amortisation* | **Romania** 28.04.2016 *Datio in solutum* |

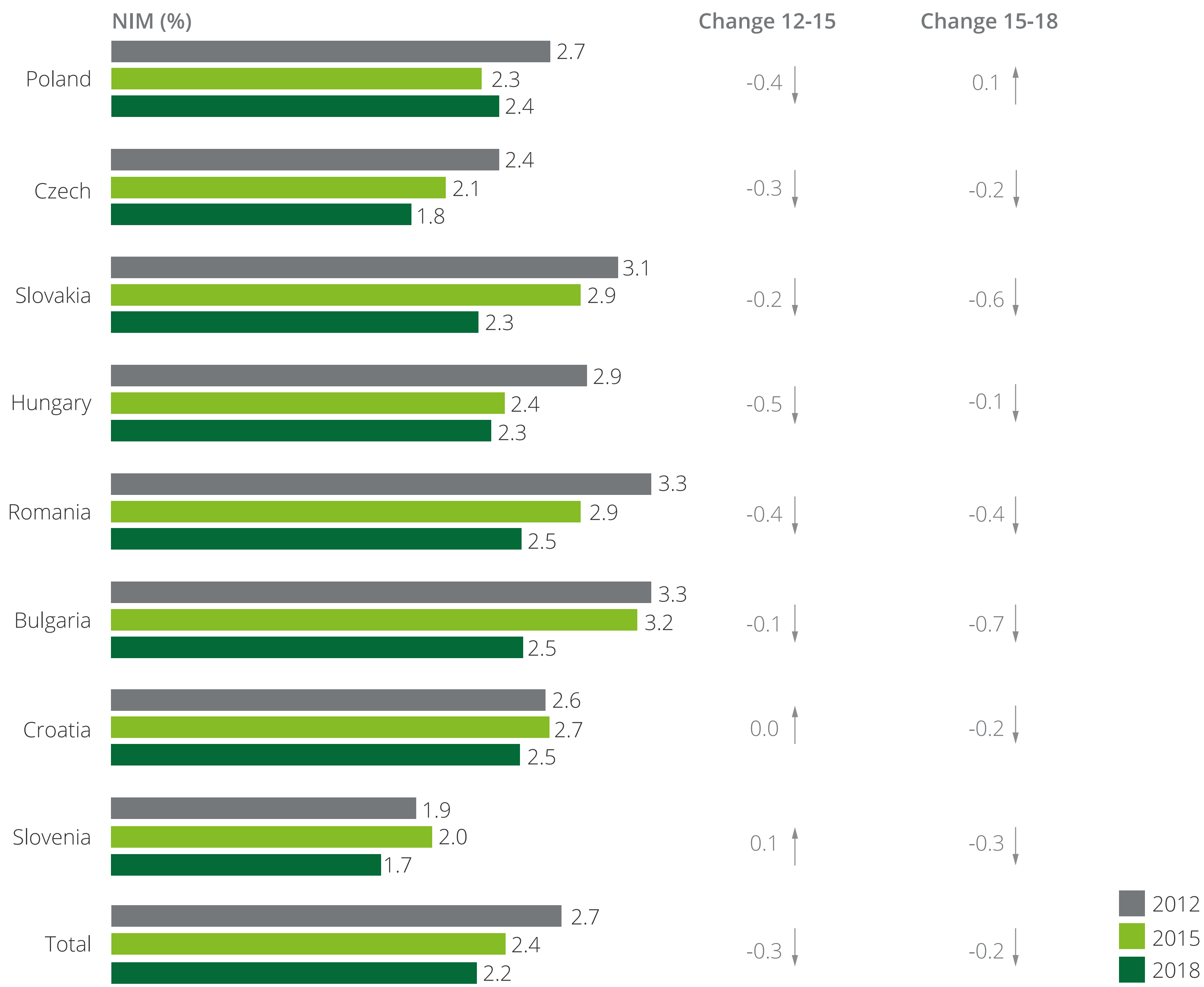
*Source: ECB, Central Banks*

## Net interest margin pressure is visible across region but Poland may buck the trend in 2016-18

Net interest margin pressure is visible across region, due to the low interest rate environment, but Poland may buck the trend in 2016-18. After falling from 2.7% in 2012 to 2.4% in 2015, the net interest margin of CE banks is expected to drop to 2.2% in 2018, driven by intensifying competition for loans and a rollover of bonds (and hedge instruments) onto lower rates. With many banks having excess deposits (visible in the decline of the sector loans to deposits ratio to ~95%) and government bond rates less attractive, competition for loans will continue to escalate. In 2012-15, there was a drop in the margin of all countries except in Croatia and Slovenia, where the improvement in funding costs was enough to offset the impact of falling asset yields. Going forward, there will be less room for banks to compensate through lower deposit rates (and a shift in structure to lower-cost current accounts), hence in 2015-18 the scope of margin decline will broaden to include Croatia and Slovenia as well. Poland suffered a relatively steep net interest margin decline of -0.3 p.p. in 2012-15 but it is expected to be an exception to the sector trend in 2016-18, following the introduction of Poland's bank levy (asset tax). Banks are expected to compensate for this tax, which increases the marginal cost of loans, through less competition (and consequently higher spreads) for new volumes.



**Ongoing margin decline across CE but Poland to buck trend after introduction of bank levy**




*Source: Central Banks, Deloitte estimates*

## Cost/income of CE banks deteriorated sharply in 2015 but should partially recover by 2018, despite headwinds from margin pressure and bank levies

The cost/income ratio of CE banks deteriorated in 2015 and the sector faces headwinds from margin pressure and bank levies in 2016-18 but cost containment efforts should provide gradual improvement. While the cost/income ratio of CE banks jumped by more than 4 p.p. from 52.4% in 2014 to 56.6% in 2015, the sector is expected to make a partial recovery to 54.6% by 2018.

The deterioration of the cost/income ratio in 2015 was as much due to margin pressure and a consequent decline in net interest income, as it was to rising operating costs. Net interest income in CE declined by EUR 1.1bn (-4.4% y/y) and net fee income by EUR 0.1bn (-1.3% y/y) in 2015, while operating costs increased by EUR 1.0bn (5.5% y/y)[8]. While higher regulatory burdens (e.g. deposit insurance fees) contributed to cost growth in the region, more than half of the increase can be attributed to one-off payments by Polish banks, including a EUR 480m one-off guarantee fund payment after the bankruptcy of SK bank and EUR 140m to endow a new mortgage borrower support fund.

The improvement of the cost/income ratio through 2018 will be limited by continued margin pressure across most of CE, resulting in net interest income declines for many countries. While net interest income in CE is expected to rise at a 2015-18 CAGR of 1.5% overall, a decline of -1.1% is expected outside of Poland. While Polish banks should benefit from relatively strong revenue growth, the new bank levy (asset tax) is expected to cost them EUR ~1.1bn in 2018. Hence, though operating costs in CE are expected to rise at a 2015-18 CAGR of 0.5%, a decline of -0.4% is expected outside of Poland. Polish banks are expected to see costs rise at a 2015-18 CAGR of 1.8% but excluding one-offs and the bank levy, cost growth should be flat.

8 Changes in revenue and costs, assuming constant FX rates

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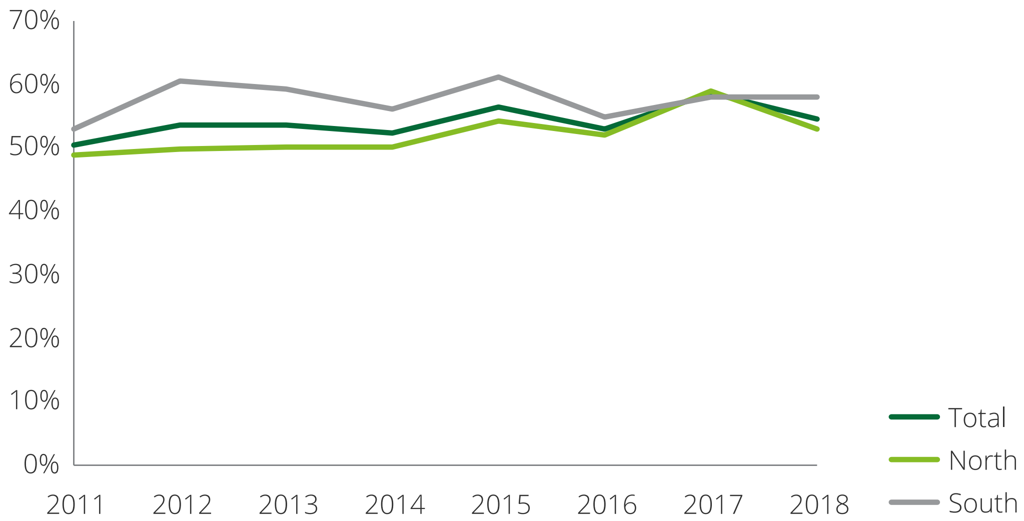
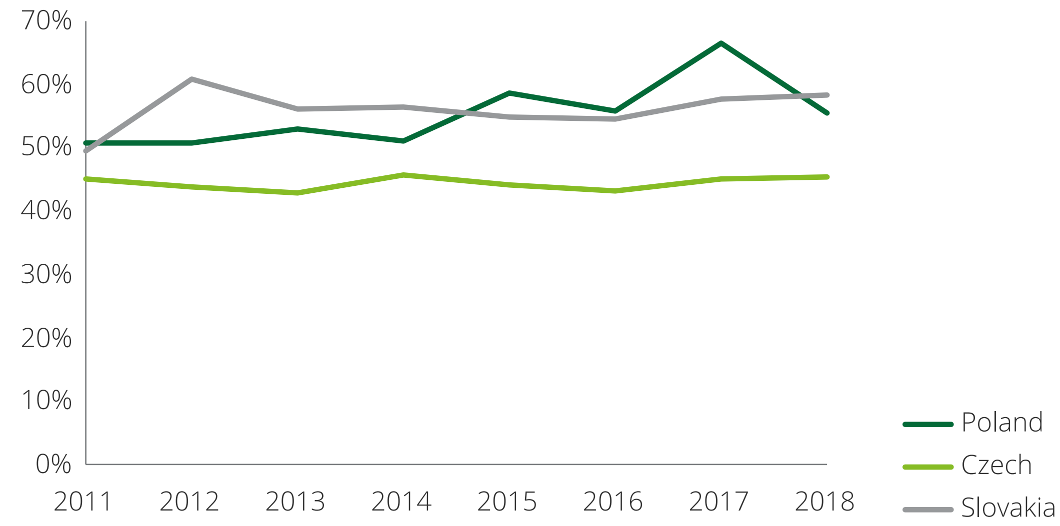
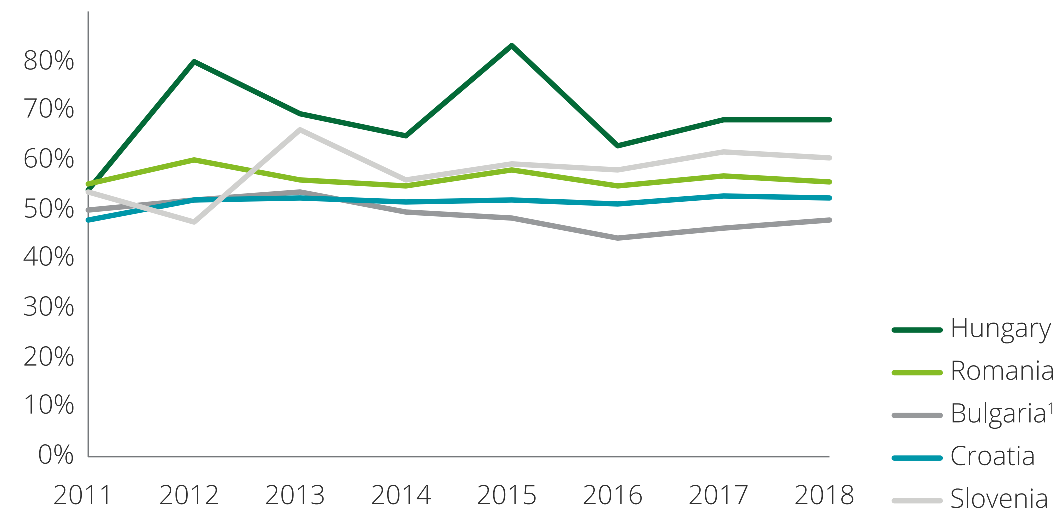
**Cost/income of CE banks deteriorated in 2015 driven by Poland and Hungary but should partially recover by 2018**



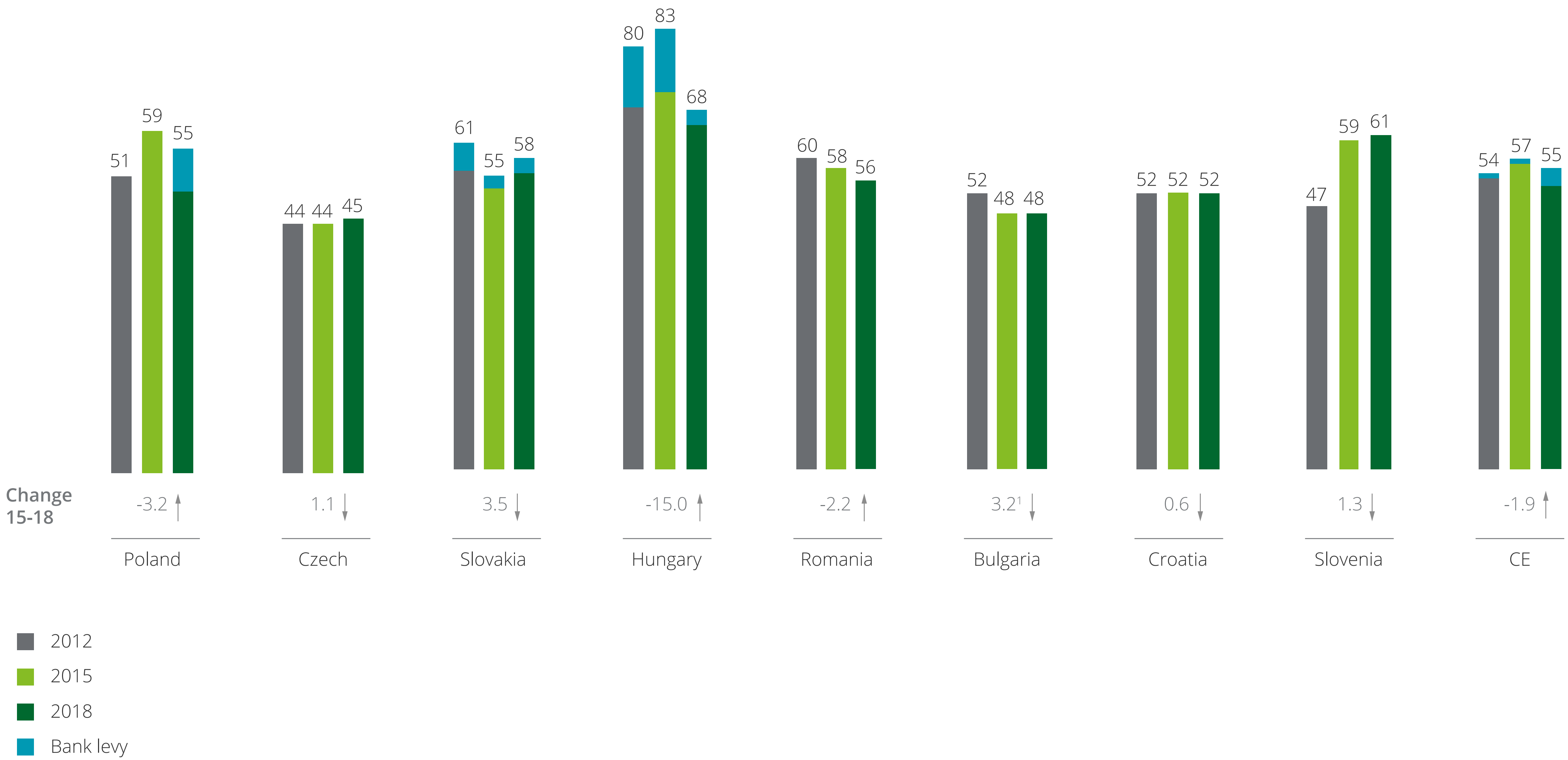




[1] Bulgaria's cost/income flat is expected to be flat on a reported basis but this reflects a change in accounting from 2016, with deposit insurance no longer booked in operating costs and instead booked in net other income. Excluding this change, cost/income increases by 3.2 p.p. in 2015-18

*Source: Central Banks, Deloitte estimates*

**CE banks will struggle to lower C/I against headwinds from higher regulatory burdens and margin pressure**




[1] Cost/income flat is expected to be flat on a reported basis but this reflects a change in accounting from 2016, with deposit insurance no longer booked in operating costs and instead booked in net other income

*Source: Central Banks, Deloitte estimates*

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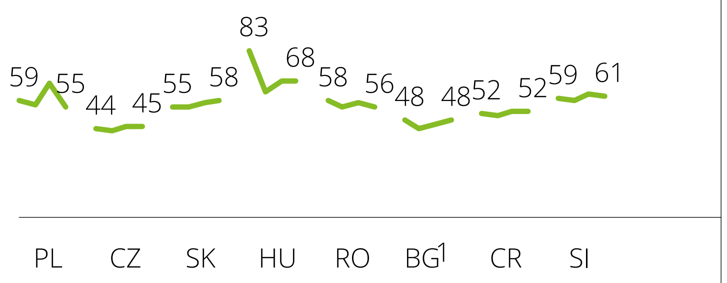
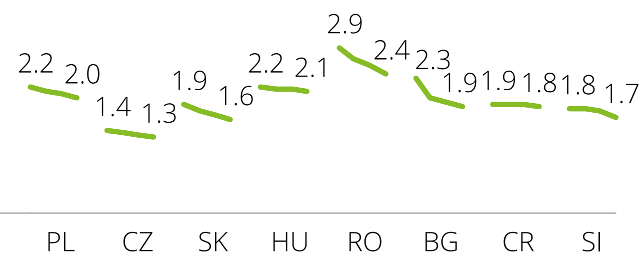
## C/I declines have various grounds across CE

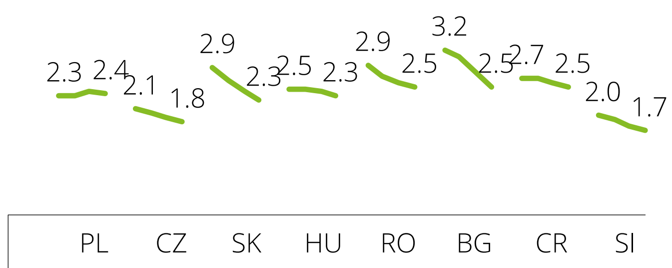
Cost/Income (%) 2015-2018



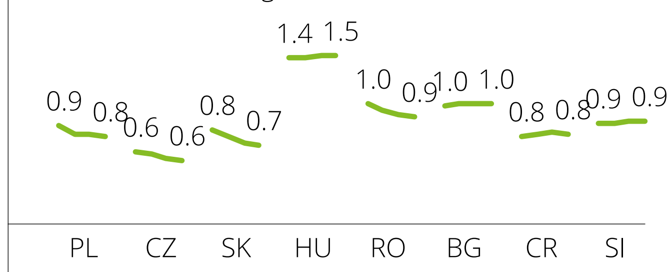

Cost/Avg. assets (%) 2015-2018



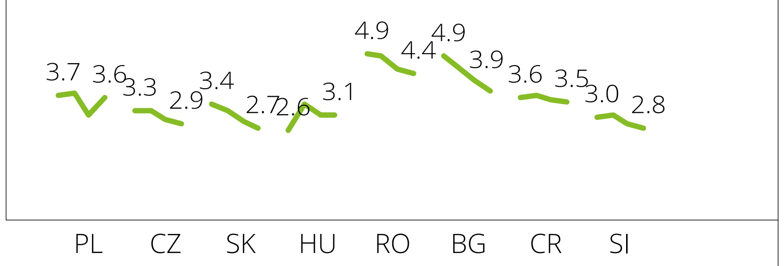

Net interest income /Avg. assets (%) 2015-2018



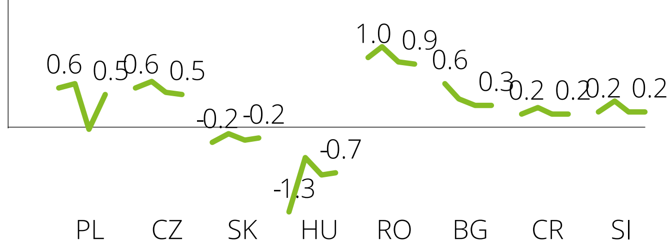

Net fee income/Avg. assets (%) 2015-2018




Revenue/Avg. assets (%) 2015-2018




Other income/Avg. assets (%) 2015-2018




[1] Cost/income flat is expected to be flat on a reported basis but this reflects a change in accounting from 2016, with deposit insurance no longer booked in operating costs and instead booked in net other income. Excluding this change, cost/income increases by 3.2 p.p. in 2015-18

*Source: Bankscope, Bulgarian National Bank*

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## Despite overall improvement in CE in 2015-18, cost/income will rise in many countries

While the sector overall should manage improvement, cost/income ratios are expected to rise in a majority of CE countries in 2015-18. This includes the Czech Republic (+1.1 p.p. to 45%), Slovakia (+3.5 p.p. to 58%), Slovenia (+1.3 p.p. to 61%), Croatia (+0.6 p.p. to 52%) and, on an underlying basis, Bulgaria (+3.2 p.p. to 48%[9]). Bulgaria, Slovakia, and Slovenia are among the CE countries facing the steepest margin declines, while Slovakia and the Czech Republic are expected to see relatively strong upward cost pressure. Cost/income ratio declines are expected in Hungary (-15.0 p.p. to 68%), Poland (-3.2 p.p. to 55%) and Romania (-2.2 p.p. to 56%). Hungarian banks will benefit from a reduction of the country's bank levy and are expected to suffer relatively little margin pressure. While Poland will face a new bank levy, the cost of this is expected to be gradually passed through to customers via a higher margin. Romanian banks are expected to manage a relatively deep cost reduction (2015-18 CAGR of -1.8%).

9 Cost/income is expected to be flat on a reported basis but this reflects a change in accounting from 2016, with deposit insurance no longer booked in operating costs and instead booked in net other income.

## Banks are cutting branches and employment in CE, following the broader European trend

In an effort to improve cost efficiency and reflecting a shift in customer behavior towards increasing use of digital channels, CE banks have been cutting branches and employment in recent years, following the broader European trend. From 2013 to 2015, CE banks have cut the number of branches by -5.7%, which is in line with the Eurozone reduction of -5.5%. The biggest branch network reductions in CE over this period were in Hungary (-11%), Romania (-10%), and Slovenia (-6%), countries which performed weakest in profitability in 2013-14. Only Slovakian banks (+2.8%) increased the number of branches between 2013 and 2015, which may be attributed to its relatively fast loan growth. From 2013 to 2015, CE banks have also cut the number of employees by -2.3%, in line with the Eurozone reduction of -3.3%. In employment, the biggest reductions in CE were in Slovenia (-7%) and Bulgaria (-6%). Hungary saw relatively little impact on employment (-1.3%) from its branch reduction. There were staff increases in both Slovakia (+1.9%) and the Czech Republic (+2.3%), both faster growing markets. The trend to reduce branch networks is expected to continue, as the underlying drivers will only become increasingly evident (need to improve efficiency, shift in customer behavior towards using digital distribution channels).

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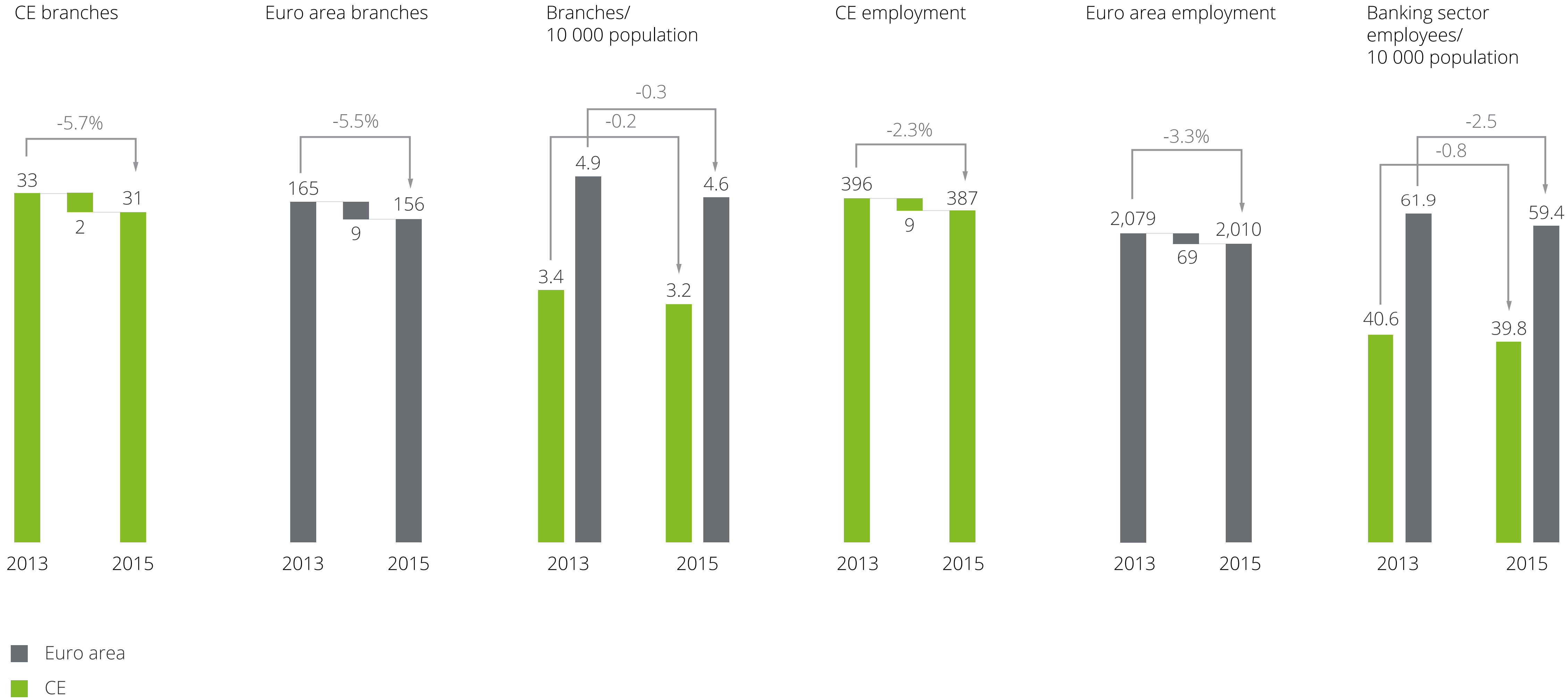
**Banks in CE have cut branches and employment in recent years following the broader european trend**




*Source: ECB, Central Banks*


**Largest branch reductions have come in Hungary and Romania, while the only increase has been in Slovakia**

| | Branches change % 2013-2015 | Employees change % 2013-2015 | Absol. change 2013-2015 branches ('00) | Absol. change 2013-2015 employees (K) |
|---|---|---|---|---|
| Bulgaria | -2.1 | -6.4 | -0.8 | -2.1 |
| Croatia | -3.0 | -3.6 | -0.4 | -0.8 |
| Czech Republic | -2.9 | 2.3 | -0.6 | +0.9 |
| Hungary | -11.1 | -1.3 | -3.5 | -0.5 |
| Poland | -5.2 | -2.0 | -8.0 | -3.4 |
| Romania | -9.9 | -4.6 | -5.5 | -2.7 |
| Slovakia | 2.8 | 1.9 | +0.4 | +0.4 |
| Slovenia | -6.5 | -6.9 | -0.4 | -0.8 |

*Source: ECB, Central Banks*

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## Sector profit distribution is uneven and skewed in favor of banks with larger market share

Revisiting an examination of the importance of scale, the distribution of banking sector net profit in CE is uneven and skewed towards banks with higher shares in their local markets. Only banks in the top quartile achieve an acceptable ROE on average, which leaves most small banks in a challenging position. Among 121 banks covered by Bankscope in CE (excluding Croatia and banks with ROE < -50% or > 50%), banks in the top quartile (market share > 6.8%) in 2015 had an average ROE of 10.0% and more than 70% exceed the regional average ROE of 6.6%. In contrast, banks in the bottom quartile (market share < 0.7%) are at breakeven, with more than half loss-making and more than 80% with an ROE below the regional average. Even in the second quartile (market share of 0.7% to 2.5%), the average ROE was just 1.8% and more than 70% had an ROE below the regional average. This underlines the need for smaller banks to get bigger or to consider an exit, which has been and will be an important driver for consolidation.

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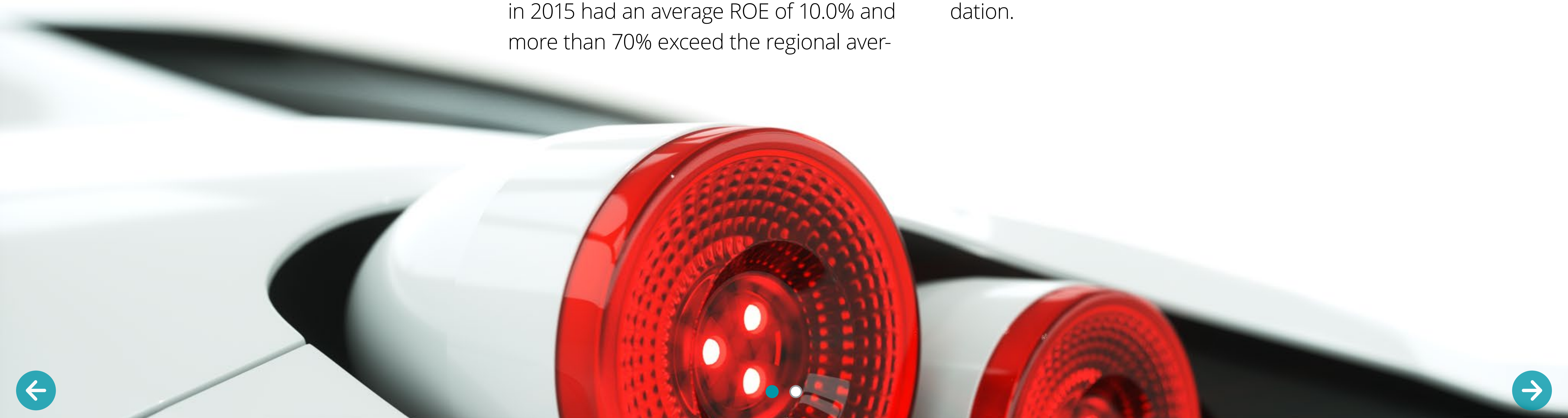
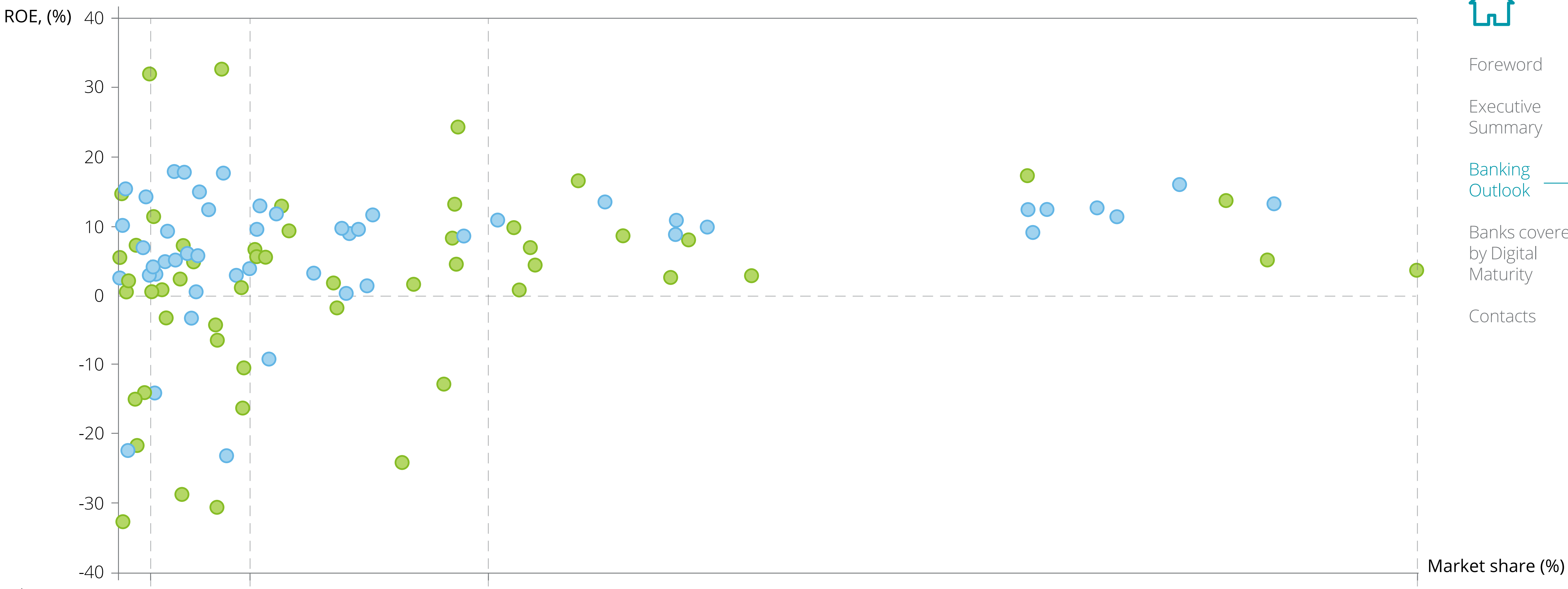


**While top quartile banks achieve an average ROE of 10% a majority of bottom quartile banks were loss making in 2015**




| | | | | |
|---|---|---|---|---|
| Market share | 0.7 | 2.5 | 6.8 | 23 |
| Avg. ROE % | -0.1 | 1.8 | 5.0 | 10.0 |
| % of loss making | 52 | 40 | 33 | 13 |
| # of banks | 31 | 30 | 30 | 30 |
| % of below average | 81 | 73 | 47 | 27 |
| Quartile | 1 | 2 | 3 | 4 |

7.6 is ROE average for CE exc Croatia
6.6 CE average inc Croatia

North banks
South banks

*Source: Bankscope, Banks' Annual Report*

## M&A has been picking up in CE, with increasing activity in Southern countries and by PE funds

M&A in CE banks has picked up visibly in recent years, with increasing activity in Southern countries and by PE funds. The number of transactions per annum involving a target with at least EUR 0.7bn of assets has grown steadily from 1-2 in 2011-12 to 5-7 in 2014-15. The most active market over the past 6 years has been Poland, accounting for 9 out of 25 transactions. While most of these were in 2011-13, Poland has heated up again with BPH changing hands already this year and possible sales of Raiffeisen Polbank and Bank Pekao ahead. Notable particularly for the size of their assets, Raiffeisen Polbank (EUR 13.4bn) and Bank Pekao (EUR 40.4bn) are larger than any bank that has changed hands in the last 6 years. Growing activity on markets in the South has been a key driver of the pick-up in recent years, particularly in Hungary, Slovenia and Romania, which accounted for 11 of 17 transactions in 2014-16.

After many years of climbing NPLs, stabilizing asset quality and a return to profitability is helping drive a pick-up in transactions on these markets. There has been no clear trend in valuation, which has varied widely in recent years depending on the quality and profitability of the target between a trailing P/BV of 0.3x and 2.3x. However, among buyers of CE banks, there has been increasing activity by non-bank players such as private equity funds or insurers (i.e. PZU), which were not active in 2011-13 but accounted for 8 of 17 transactions in 2014-16. This portends further growth of M&A activity going forward as these many of these PE players will seek to build the value of their holdings through consolidation (and restructuring) before eventually exiting in the coming years.

## M&A transactions have picked up in 2014-15and momentum has carried into 2016

| Year of an-nouncement | Country | Target | Buyer | Seller | Target Assets (m EUR) | Deal Value (m EUR) | Book value multiple |
|---|---|---|---|---|---|---|---|
| 2011 | Austria | Volksbank International AG | Sberbank of Russia | Volksbanken AG, BPCE S.A., DZ Bank AG | 9400 | 505 | 1.1 |
| | Poland | Bank Zachodni WBK SA | Babco Santander, S.A. | Allied Irish Banks Plc | 13372 | 4290 | 2.5 |
| 2012 | Poland | Bank BGŻ (40%) | Rabobank NV | Government of Poland | 7494 | 301 | 1.2 |
| | | Kredyt Bank S.A. | Bank Zachodni WBK SA | KBC Groep NV | 9422 | 1061 | 1.5 |
| 2013 | Bulgaria | MKB Unionbank AD | First Investment Bank | MKB Bank Zrt. | 875 | N/A | N/A |
| | Poland | Bank BGŻ BNP Paribas SA | BNP Paribas SA | Rabobank NV | 8612 | 1081 | 1.3 |
| | | Nordea Bank Polska SA | PKO BP SA | Nordea AB | 8180 | 629 | 1.1 |
| | | Santander Consumer Bank S.A. (60%) | Bank Zachodni WBK SA | Santander Consumer Finance, S.A. | 2860 | 514 | 1.5 |
| 2014 | Austria | Hypo Group Alpe Adria AG | Advent International Corp; EBRD | Heta Asset Resolution AG | 8032 | 200 | 0.2 |
| | Czech Republic | LBBW Bank CZ a.s. | Expobank LLC | Landesbank Baden-Wurttemberg | 1147 | 80 | 0.7 |
| | Hungary | MKB Bank Zrt. (99%) | Government of Hungary | Bayerische Landesbank | 6606 | 55 | 0.1* |
| | Poland | Meritum Bank ICB S.A. (97.9%) | Alior Bank S.A. | EBRD; Innova Capital Sp zoo; WCP Cooperatief UA | 711 | 84 | 1.4 |
| | Romania | Volksbank Romania S.A. | Banca Transilvania SA | Immigon Portfolioabbau AG; Westdeutsche Genossenschafts-Zentralbank; DZ Bank AG; BPCE Group | 2765 | 81 | 0.2 |
| 2015 | Hungary | Budapest Bank Zrt. | Corvinus Nemzetkozi Befektetesi Zrt. | GE Equity (General Electric) | 2838 | 615 | 1.7 |
| | Poland | Alior Bank S.A. (25.3%) | Powszechny Zakład Ubezpieczeń SA | Carlo Tassara SpA | 9382 | 396 | 2.3 |
| | | FM Bank PBP SA | AnaCap Financial Partners LLP | Abris Capital Partners | 753 | N/A | N/A |
| | Slovakia | Sberbank Slovensko, a.s. (99.5%) | Penta Investments Limited | Sberbank Europe AG | 2023 | N/A | N/A |
| | Slovenia | Celje Banka | Abanka | | 1713 | N/A | N/A |
| | | Nova Kreditna Banka Maribor d.d. | Apollo Global Management, LLC; EBRD | Government of the Republic of Slovenia | 4369 | 250 | 0.4 |
| | | Raiffeisen Banka d.d. | Biser Bidco | Raiffeisen Bank International AG | 999 | N/A | N/A |
| 2016 | Hungary | AXA Bank Hungary | OTP Bank Plc | AXA Bank Europe S.A. | 1201 | N/A | N/A |
| | | Erste Bank Hungary Zrt (30%) | Corvinus Nemzetkozi Befektetesi Zrt.; EBRD | Erste Group Bank AG | 6090 | 248 | 1.1 |
| | | MKB Bank Zrt. | Pannonia Pension Fund; METIS Private Capital Fund; Blue Robin | Government of Hungary | 6184 | 118 | 0.3 |
| | Poland | Bank BPH SA (66%) | Alior Bank S.A. | GE Capital Corporation | 3049 | 358 | 0.9 |
| | Romania | Banca Comerciala Carpatica S.A. (54.8%) | Nextebank S.A. | Ilie Carabuela, non-dosclosed shareholders | 747 | 27 | 1.0 |

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## Regional bank footprints are shifting gradually via M&A and this trend will continue

Regional bank footprints in CE are shifting gradually via M&A and this trend will continue, with transactions driven either by the needs of the parent (for capital, re-defining core businesses) or the needs of subsidiaries to obtain scale or exit. In 2014-16, there have only been a handful of transactions involving regional players. The most active has been Raiffeisen Bank International, selling its sub-scale operations in Slovenia (market share of 1.8%) last year and planning to exit its Polish operations (market share of 3.5%) this year. Sberbank has sold its small subsidiary in Slovakia (market share of 2.7%) and Erste has sold a 30% stake in its Hungarian operations (market share of 5.9%) to the State and EBRD. OTP Bank has also been active as an acquirer, buying Axa Bank Hungary this year and Millennium Bank Romania (market share of 0.7%) last year. There is a clear tendency of these transactions to involve the smaller sub-scale businesses of regional banks and for good reason. In 2015, only 3 of 14 regional bank subsidiaries with less than 5% market share had an ROE above the CE average or a cost/income ratio below the CE average. We expect this area to remain the focus of future M&A.

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## Regional players' countries of operation in CE (2015)

| Group bank | Bank Name | Maket Share 2015 | ROAE 2015 | Cost to income 2015 |
|---|---|---|---|---|
| EFG | Eurobank Bulgaria AD-Postbank | 6.6 | 9.7 | 46.3 |
| | Bancpost SA | 3.0 | N/A | N/A |
| | Ceska Sporitelna a.s. | 17.5 | 12.6 | 47.2 |
| | Erste Bank Hungary ZRT | 5.9 | -13.0 | 74.2 |
| | Banca Comerciala Romana SA-Romanian Commercial Bank SA | 16.3 | 17.1 | 59.5 |
| | Slovenska sporitel'na as-Slovak Savings Bank | 20.7 | 13.0 | 49.7 |
| | ERSTE&STEIERMÄRKISCHE BANK d.d. | 14.7 | -10.2 | 57.7 |
| Intesa | CIB Bank Ltd-CIB Bank Zrt | 5.1 | -24.2 | 90.0 |
| | Banca Comerciala Intesa Sanpaolo Romania SA | 1.1 | 2.2 | 72.6 |
| | Banka Koper d.d. | 6.1 | 4.1 | 62.7 |
| | Vseobecna Uverova Banka a.s. | 17.9 | 11.2 | 47.4 |
| | PRIVREDNA BANKA ZAGREB d.d. | 17.2 | 2.7 | 51.5 |
| KBC | Ceskoslovenska Obchodni Banka A.S.- CSOB | 19.0 | 15.9 | 47.2 |
| | CIBANK JSC | 3.1 | 9.0 | 65.8 |
| | K&H Bank Zrt | 7.9 | 18.9 | 53.2 |
| | Ceskoslovenska obchodna banka CSOB | 10.0 | 10.8 | 59.5 |
| NBG | United Bulgarian Bank - UBB | 7.5 | 4.3 | 45.5 |
| | Banca Romaneasca S.A. | 1.8 | -4.6 | 91.1 |
| OTP | DSK Bank Plc | 12.7 | 20.4 | 37.4 |
| | OTP Bank Plc | 20.6 | 5.1 | 55.1 |
| | OTP Bank Romania SA | 2.2 | -16.2 | 69.1 |
| | OTP Banka Slovensko. as | 2.1 | 2.7 | 68.5 |
| | OTP BANKA HRVATSKA d.d. | 3.9 | -4.6 | 66.1 |
| Piraeus | Piraeus Bank Bulgaria AD | 3.3 | -35.8 | 85.0 |
| | Piraeus Bank Romania | 1.8 | 32.4 | N/A |

● - increase in market share >1p.p.); inrease in ROAE and decrease in C/I <-3 p.p.

● - decrease in market share <1p.p.); decrease in ROAE and increase in C/I >3 p.p.

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## Further consolidation is ahead. Many regional bank subsidiaries are sub-scale with below average profitability

| Group bank | Bank Name | Maket Share 2015 | ROAE 2015 | Cost to income 2015 |
|---|---|---|---|---|
| RBI | Raiffeisenbank akciova spolecnost | 1.9 | 11.5 🟢 | 53.4 🟢 |
| | Raiffeisenbank (Bulgaria) EAD | 4.57 | 6.8 🟢 | 57.6 |
| | Raiffeisen Bank Zrt | 7.4 | 8.0 🟢 | 102.7 ⚫ |
| | Raiffeisen Bank Polska SA | 6.0 | 3.0 | 77.9 ⚫ |
| | Raiffeisen Bank SA | 3.5 | 13.0 ⚫ | 60.2 |
| | Raiffeisen Banka dd | 8.2 🟢 | -30.9 | 79.0 ⚫ |
| | Tatra Banka a.s. | 1.8 ⚫ | 12.1 | 56.7 🟢 |
| | RAIFFEISENBANK AUSTRIA d.d. | 16.7 🟢 | -3.2 ⚫ | 60.7 ⚫ |
| Sberbank | Sberbank CZ as | 7.8 | 0.3 ⚫ | 81.8 ⚫ |
| | Sberbank Magyarorszagi ZRT | 1.4 | -28.8 | 105.6 🟢 |
| | Sberbank Banka dd | 1.2 | -2.2 ⚫ | 53.3 🟢 |
| | Sberbank Slovensko. as | 5.1 | -9.4 ⚫ | 75.0 |
| | SBERBANK d.d. | 2.7 | -15.0 ⚫ | 74.5 |
| SG | Komercni Banka | 2.4 | 12.2 | 51.9 🟢 |
| | Societe Generale Expressbank | 16.3 | 12.9 🟢 | 44.1 🟢 |
| | Eurobank | 6.0 | 10.6 ⚫ | 65.9 ⚫ |
| | BRD-Groupe Societe Generale SA | 0.1 | 7.8 🟢 | 53.4 ⚫ |
| | SKB Banka DD | 13.1 | 9.8 🟢 | 53.9 🟢 |
| | SOCIÉTÉ GÉNÉRALE-SPLITSKA BANKA d.d. | 6.8 | 3.4 | 53.2 🟢 |
| Unicredit | Unicredit Bank Czech Republic and Slovakia AS | 6.7 | 8.7 | 49.2 |
| | UniCredit Bulbank AD | 10.0 | 13.5 🟢 | 39.6 |
| | UniCredit Bank Hungary Zrt | 19.8 | 16.4 🟢 | 51.1 🟢 |
| | Bank Polska Kasa Opieki SA-Bank Pekao SA | 8.2 | 9.7 | 53.6 ⚫ |
| | UniCredit Bank SA | 10.5 | 8.4 🟢 | 51.0 🟢 |
| | UniCredit Banka Slovenija d.d. | 9.0 | 3.4 🟢 | 55.0 🟢 |
| | ZAGREBAČKA BANKA d.d. | 6.8 | -0.8 ⚫ | 51.50 |

🟢 - increase in market share >1p.p.); inrease in ROAE and decrease in C/I <-3 p.p.

⚫ - decrease in market share <1p.p.); decrease in ROAE and increase in C/I >3 p.p.

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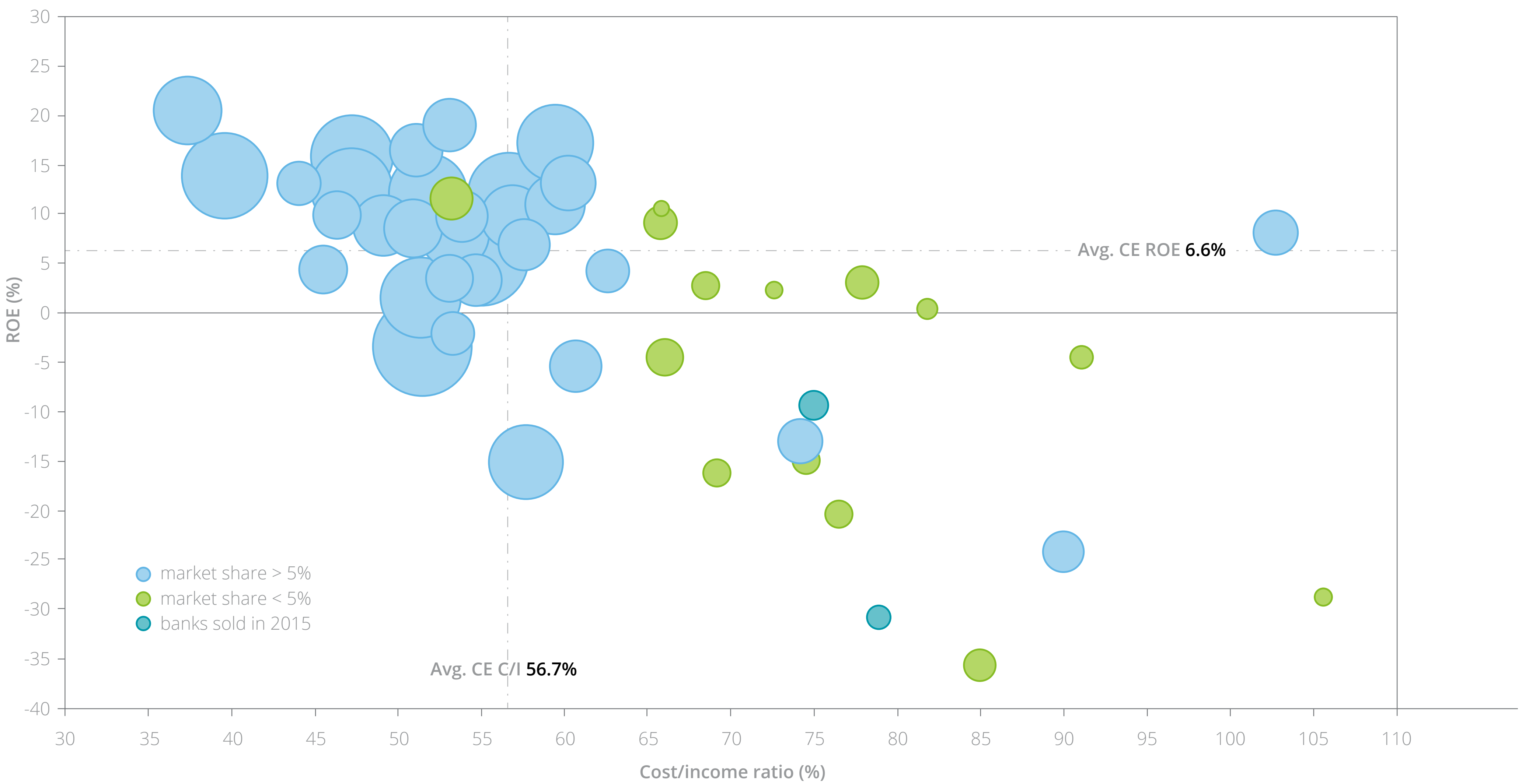
**Regional bank operations that are sub-scale with below average profitability could benefit from consolidation**




*Source: Bankscope, Deloitte estimates*

## Strategic directions: In every CE country, investment in digitalization is a strategic priority for banks

Examining the strategic priorities of banks in CE over the next 3 years, there is a common theme. As low interest rates and competition drive margin compression and as regulatory burdens rise, operating efficiency is in focus. Digitalization will be an important avenue for banks to update service models and reduce cost to serve, while maintaining service levels and customer experience. As there will be less need for physical contact, banks will be able to continue to cut branches and employment. Digital banking itself will be an area of competition, with customers increasingly banking online and using mobile devices. Banks that move faster will have an advantage and, while some CE banks are ahead of the curve in online and mobile functionality, others are lagging behind due to legacy issues. In addition to growth by acquiring new clients, banks will increasingly aim to activate their existing clients (to improve cross-selling). Making better use of data analytics and improving customer intelligence should enable banks to cross-sell more effectively with less effort, by better identifying and segmenting customers according to their needs and what they are willing to pay for. By improving customer experience, it can also support customer retention, which can become more important as competition intensifies.

## Strategic directions: In every CE country, investment in digitalization becomes a strategic priority for banks

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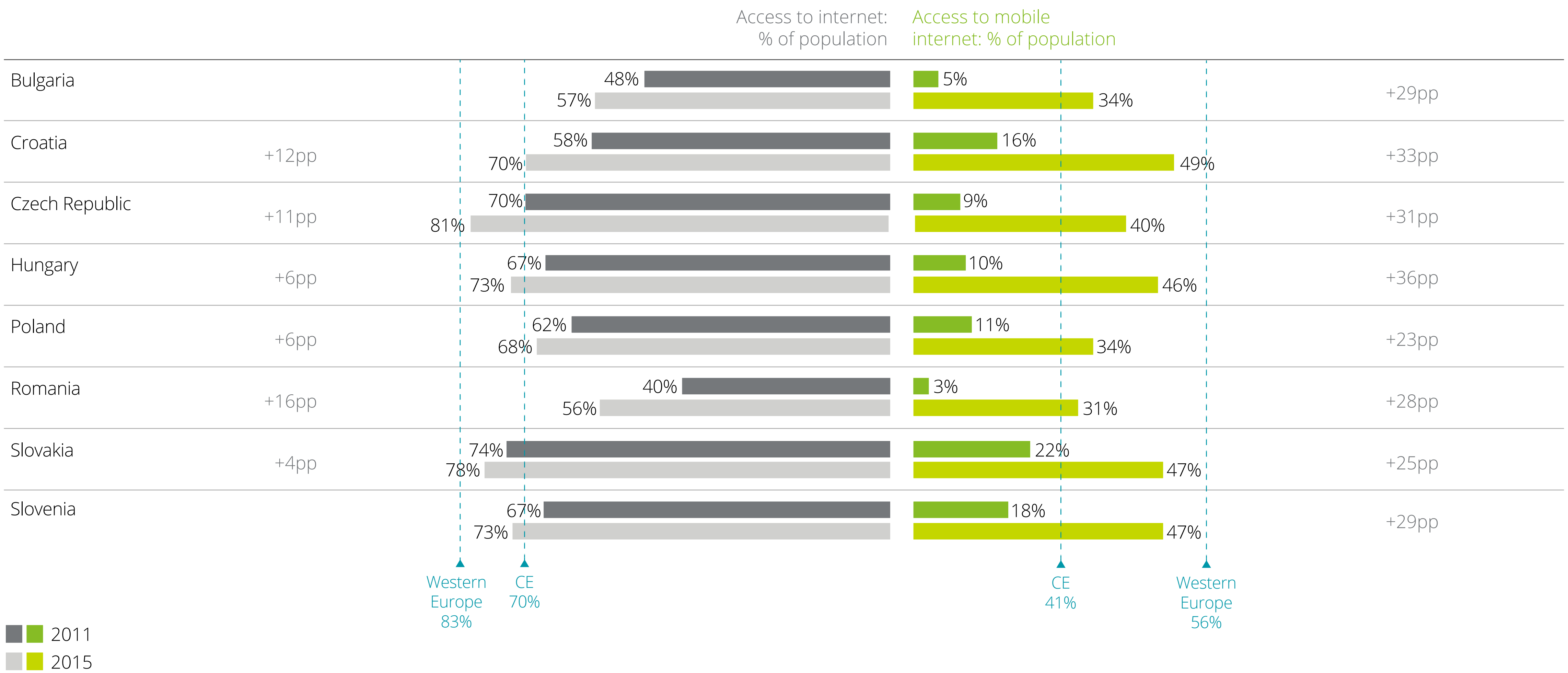
## Need for a digitalization of banking services is driven by the recent technological disruptions and broader access to internet

Need for a digitalization of banking services is driven by the recent technological disruptions which increased an access to broadband and mobile internet. 70% of individuals in CE countries have used an internet at least once in 3 months comparing to 61% in 2011. Expansion of mobile internet is even faster: 41% in 2015 vs. 12% in 2011. Benchmarking these results with other European countries we see even more room for growth as in many countries access to internet is nearly reaching entire population (e.g. Norway 97%, Denmark 96%), whereas mobile internet connectivity has reached levels above 90% (UK 92%, Netherlands 91%).

This view is also confirmed by more detailed analysis of age structure: 94% of individuals in CE from 16 to 29 years old used internet in last 3 months, whereas 76% used internet on a mobile phone.[10]

Given the rapid expansion of internet services in recent years banks have put digital agenda high on their priorities list. According to Deloitte research conducted with leading CE banks, 90% of them believe that digital has an impact on the industry. Moreover, 95% of banks claim to have a clear vision and strategy for digital transformation.

10 Source: Eurostat




*Source: Eurostat*

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## To examine the maturity of digital banking services we have analyzed over 350 functionalities in 76 banks across 8 CEE countries

During our assessment of banking digital channels we have examined over 350 functionalities in 76 banks across 8 CEE countries. We have analyzed each bank from the point of view of 3 main channels: a public website, an internet banking platform and a native mobile banking app. Due to the fact that many of the 350 functionalities exist both in internet and mobile channel, in fact we examined more than 650 aspects of banking channels.

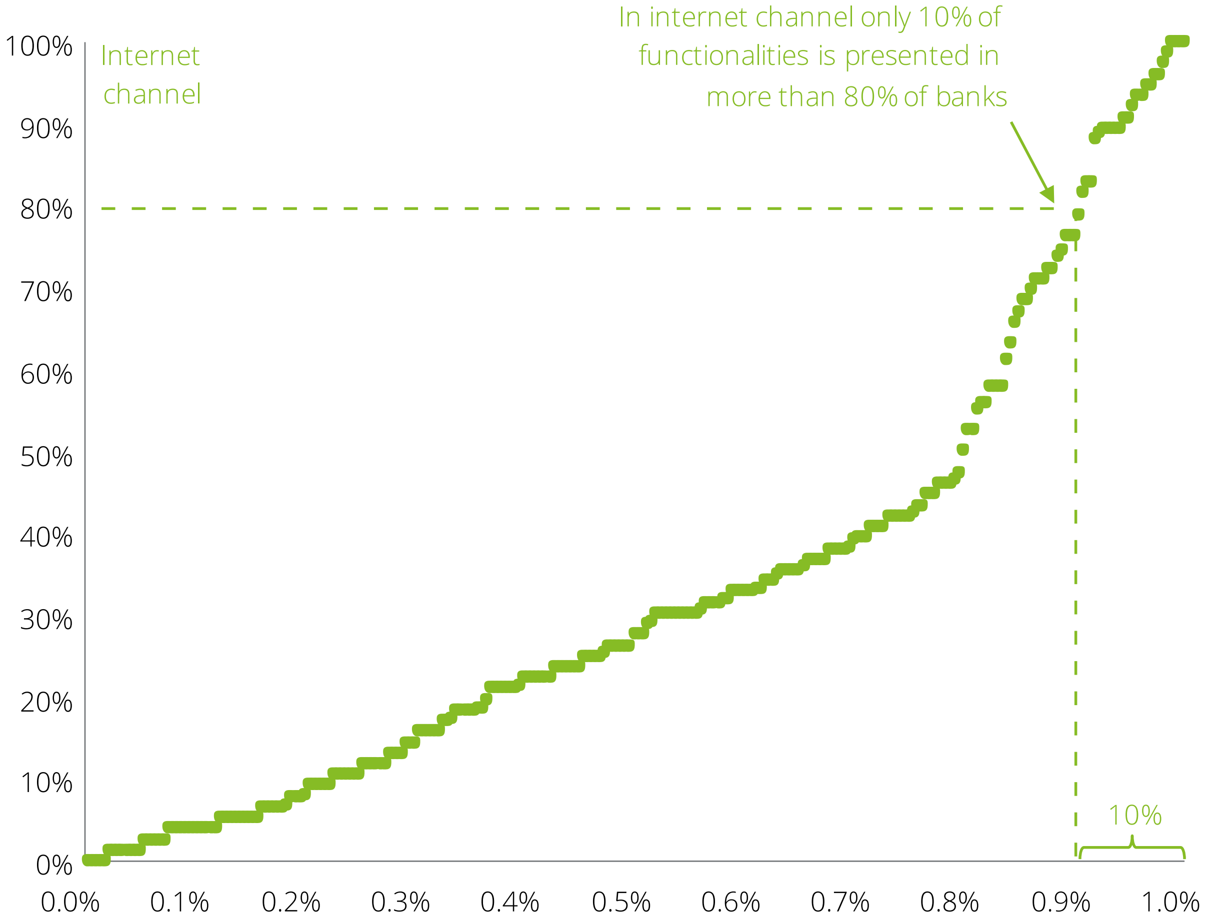
To make sure that we are fully covering customers' digital experience, our local researchers went through entire Customer Journey framework. Each of nearly 50 testers had opened current account in analyzed bank and checked functionalities supporting key 6 steps: information gathering, account opening, customer onboarding, day-to-day banking, expanding relationship and finally closing the current account. Following this approach we have analyzed 76 banks in CE, although to make results more comparable between markets, during the assessment of digitalization on country level we took into consideration only the 5 biggest banks in terms of assets for each country.
Given the considerable variety of introduced digital features between banks, we decided to benchmark all countries and banks to functionalities offered by aggregation of features available in five leading banks in terms of available digital features. Thanks to this approach we are making sure that we are taking into consideration only functionalities which can be described as best practices, not features which can be introduced someday, but are still a matter of the future (e.g. an end-to-end automation of sell process for mortgages).

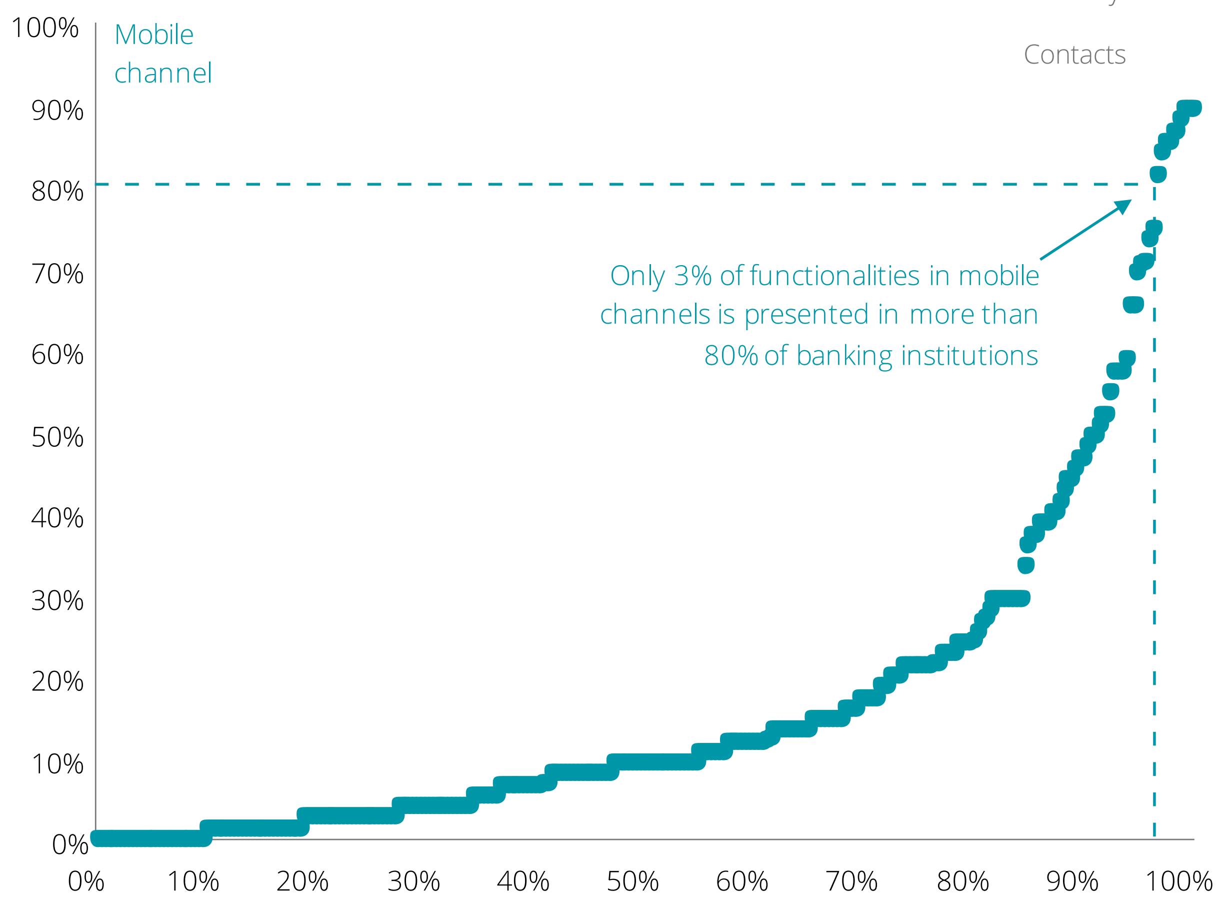
## As banks are experimenting with online and mobile functionalities, set of core features in CE is limited

Digital agenda has been in the spotlight of banking institutions for more than a decade, but given the pace of technology innovations banks are still experimenting with functionalities to meet changing client needs and to differentiate from competition. It is represented by the presence of the digital "Pareto principle": out of 361 assessed functionalities in 76 CE banks in internet channel, only 10% of them were present in more than 80% of banks. These features are mainly focused around basic operations like transfers or providing information about main banking products. On the other side, nearly 120 functionalities (33%) were unique for less than 15 banks (20%). Such tendency is even more visible for mobile banking apps, where 114 functionalities (32%) were available only in less than 7 banks (10%).

Many of identified unique functionalities are digital innovations firstly introduced by pioneers and then adapted by other players – for example Personal Finance Managers functionalities (PFMs), which are currently embedded into internet banking platforms in one third of analyzed banks. Surprisingly, some uncommon functionalities are often provided by banks which are considered as laggards in digital race. For example, one bank is offering Facebook transfers, whereas its customers cannot conduct most of the basic operations linked to debit and credit card management as these functionalities are not available online.

**% of analysed banks with implemented functionality**

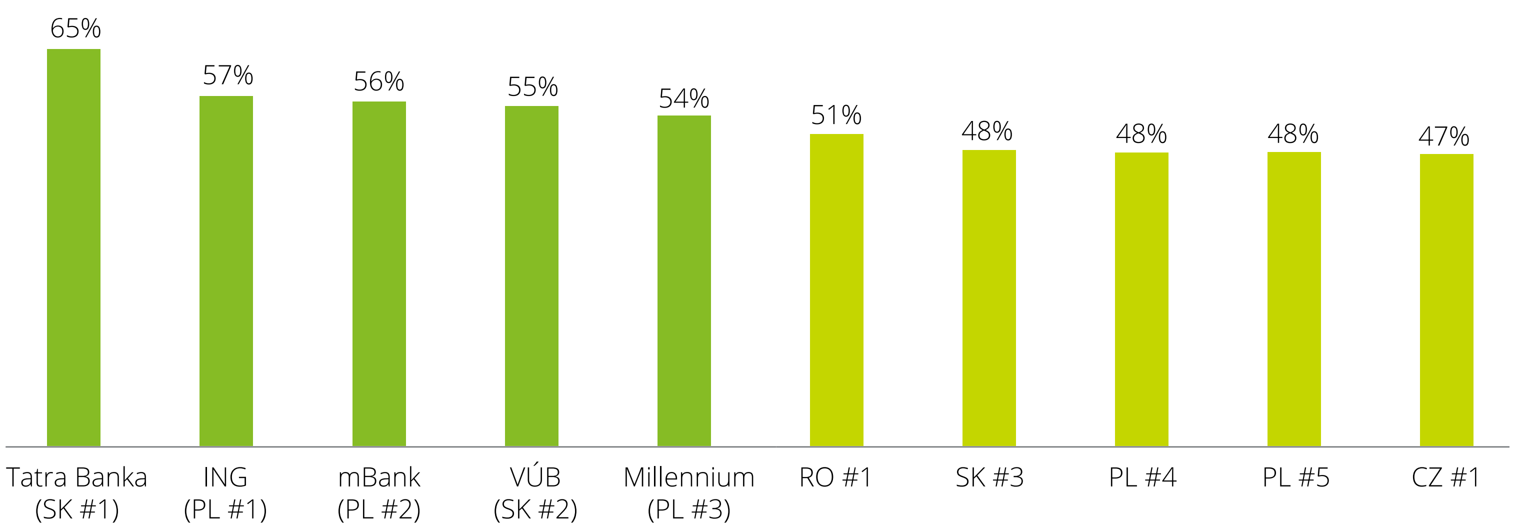


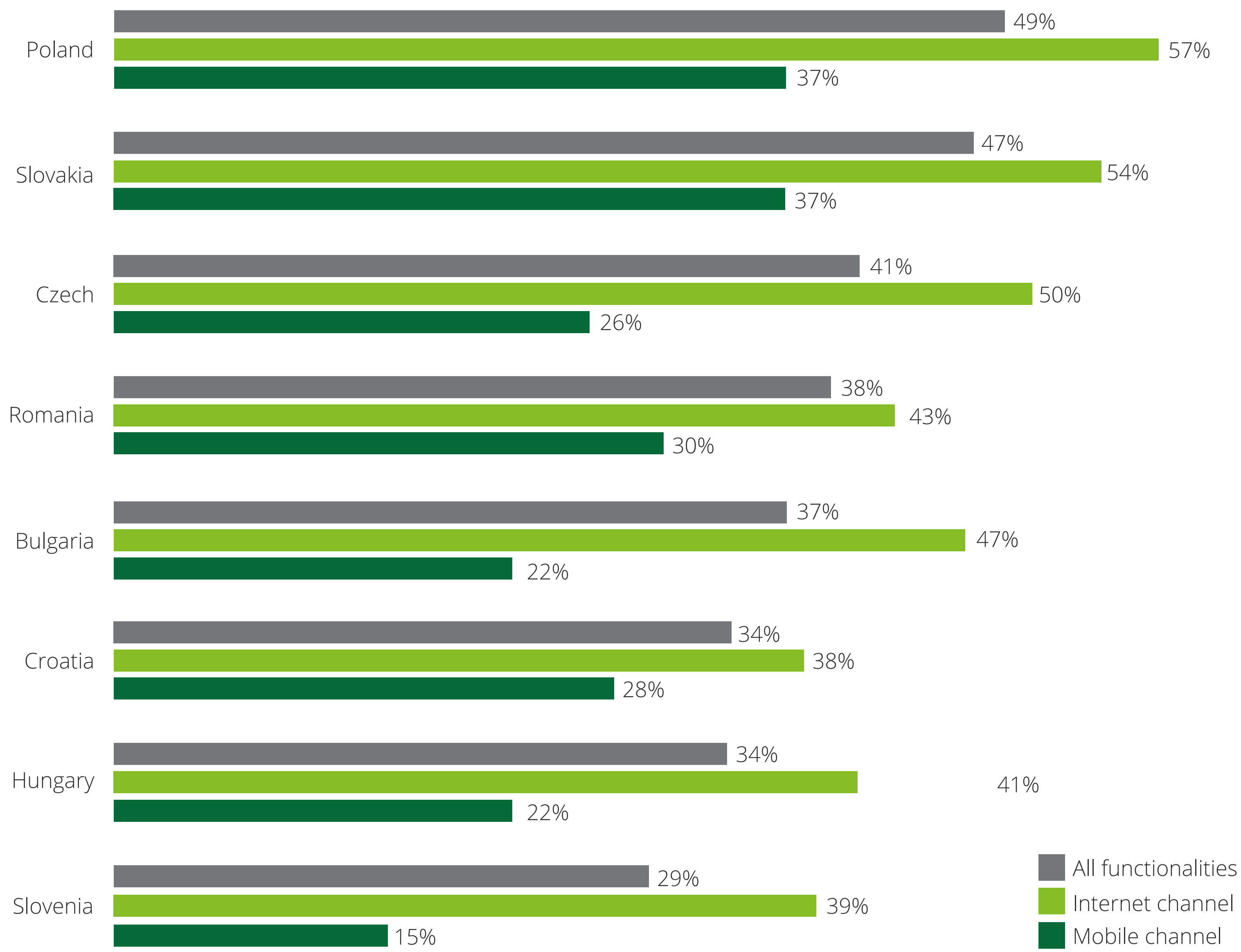
# Digital banking maturity is highly differentiated among CE countries with clearly visible pioneers and laggards

Digital banking maturity is highly differentiated among CE countries with clearly visible pioneers and laggards with similar insights both on country and particular banks level. Poland (49%) and Slovakia (47%) are leading CE in digital capabilities in terms of level of accordance with best practices: in the top 5 banks, first and third place are taken by Slovakian Tatra Bank (65%) and VUB (55%), whereas remaining positions belong to Polish ING (57%), mBank (56%) and Millennium (54%). The Czech Republic (41%), Romania (38%) and Bulgaria (37%) are positioned in the middle of the ranking followed by Hungary (34%) and Croatia (34%). Final place belongs to Slovenia (29%), where one of the top 5 banks doesn't yet have a native mobile banking application – the only case among analyzed leading 76 CE banks.

100% = all functionalities introduced in top 5 banks in terms of digital in CE = best practices



**% of functionalities in line with best practises[1]**




**Notes:** [1]Scores for countries are based on results for TOP 5 biggest banks in given country in terms of assets.

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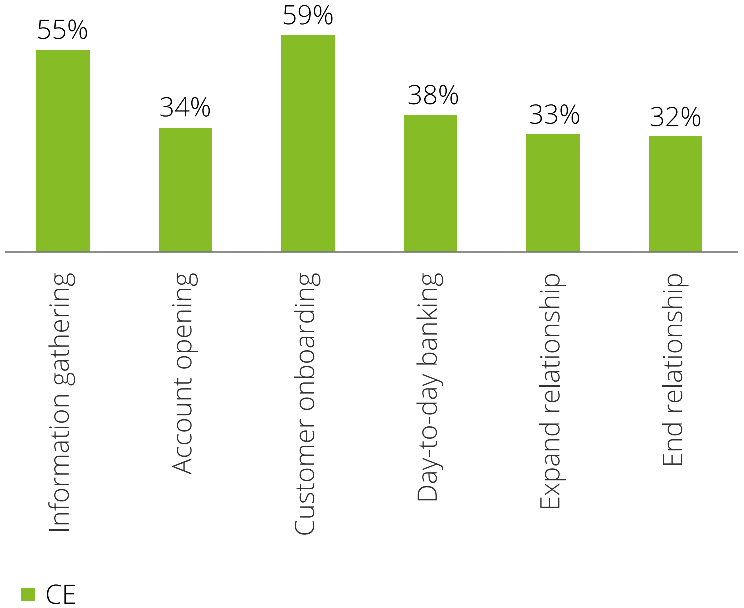
# Functionalities in digital channels primarily support customer acquisition

To analyze client perspective on digital banking channels, we grouped functionalities into six steps of digital Customer Journey: information gathering (on average CE banks achieved 67% of best practices from the 5 most digitalized banks in this category in internet channel), account opening (42%), customer onboarding (55%), day-to-day banking (46%), expanding relationship (41%) and ending relationship (36%). Analysis of mobile only functionalities revealed similar maturity of particular categories, but on lower levels (23%, 12%, 66%, 28%, 16%, 26% accordingly). Achieved high results in information gathering and customer onboarding show that in their digital efforts banks are focusing mainly on functionalities supporting customer acquisition.

Information gathering process is critical for customers during making their purchasing decisions, whereas customer onboarding builds engagement on two levels: onboarding in overall services of given bank (both offline and online) and specific digital onboarding. On the other hand, relatively low average score for account opening may be quite surprising, but more detailed analysis reveals that this category has the highest differences between countries, ranging from 20% in Croatia to 58% in Poland. Low level of digitalization of closing account process shows that bank are focusing on using traditional channels to leverage retention opportunities during mainly face-to-face interactions with bank representative.

On average CE banks are following 38% of best practices in day-to-day banking, but more detailed analysis reveals that banks do not have problems with functionalities related to transfers and payments (57% in internet channel in CE). More challenging is a lack of features concerning payment cards management (from 7% in Croatia to 52% in Slovakia), which is pushing customers to branches or call-center to conduct even the simplest operations like changing the PIN or card daily payment limits.

**% of functionalities in line with best practises**

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## Banks are making first steps in full digitalization of sales processes, which will have a significant impact both on revenue and cost side

In “expanding relationship” step in Customer Journey framework we have analyzed functionalities supporting cross-sell processes of banking products (features related to current accounts, debit and credit cards were analyzed in day-to-day banking section). Although end-to-end automation of sales through digital channels supports not only revenue side, but also has a considerable impact on cost reduction, banks are just starting their efforts in this area. Rationale behind this is straightforward – banks firstly focused on digitalization of transactional banking to shift basic operations from branches to online channels and as many of them are already mature in this area, institutions started to invest more into digitalizing sales. This observation is well illustrated by the fact that Poland leaped away in this category from other countries. For example, every player from top 5 biggest Polish banks enables end-to-end opening of credit cards in internet channel, whereas this process is generally not feasible at all in the majority of analyzed countries. Moreover, this trend is further expanding to mobile channel in which 2 banks in Poland are already offering fully digitalized cash loans.

Even though digitalizing complex products requiring professional advisory services in branches (e.g. mortgages) is not very likely in short term, we believe there is still room for improvement. Availability of features explaining to customer the offer in online channels may decide whether the client will show at branch of his main bank or whether he will decide to check also other options. Currently only 15% of banks in CE provide interactive calculators for mortgages and 12% still don’t provide clear information about mortgage application process.

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**% of Top 5 Banks in given country offering digital sales[1]**

| | Internet channel | | | Mobile channel | | |
|---|---|---|---|---|---|---|
| | Overdraft | Cash loan | Credit card | Overdraft | Cash loan | Credit card |
| Poland | 40% | 100% | 100% | 40% | 20% | 20% |
| Slovakia | 60% | 60% | | | 20% | |
| Czech Republic | 40% | 60% | 40% | 40% | 40% | |
| Romania | 40% | 60% | 20% | 20% | 40% | 20% |
| Bulgaria | 40% | 40% | 20% | | 20% | |
| Croatia | 60% | 20% | | 60% | 20% | |
| Hungary | 20% | | 40% | | | |
| Slovenia | 60% | 40% | 20% | | | |

**Notes:** [1]Including sales through digital channels which require signature on documents delivered by courier.

## Looking into the future: in less advanced countries mobile can leapfrog internet

Different pace of technology disruptions in access to broadband internet vs. mobile internet was reflected in banks priorities and in consequence internet banking platforms offer currently wider set of functionalities (average of 34%, including all functionalities which exist in both channels) than mobile banking (18%). In the next years we are expecting further convergence of mobile and internet banking in accordance with omnichannel approach. Finally, mobile will be able to surpass the possibilities of internet channel thanks to easier access to contextual information in line with “mobile first” concept.

We see two possible paths how banks can converge mobile with internet channel. Firstly, banks can focus on development of functionalities in internet channel and then converge mobile applications to internet features standards. This approach seems reasonable for categories with high discrepancy between internet and mobile channel (e.g. features from category day-to-day banking in Bulgaria: 47% vs 23%). Convergence will especially need to happen in more digitalized countries as our research reveals that more advanced markets have bigger discrepancies between internet and mobile banking functionalities (avg. difference in PL and SI: 23 and 21 p.p.; in Slovenia and Croatia: 11 p.p. and 8 p.p.).

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The second option is a parallel development of functionalities in internet and mobile banking which should especially be appealing for mentioned less digitalized markets. In Poland and Slovakia many internet capabilities were developed in pre-smartphone age, whereas countries like Slovenia have right now possibilities to create apps on much more technically advanced handsets, hence “superiority” of internet channel over mobile is not so straightforward.

Moreover, Slovenia has also higher mobile internet access (47% vs. 34% in Poland)[11] which even expands the potential number of customers with access to this channel. These factors enable leap-frogging directly to mobile banking in a similar way in which CE countries mitigated the need for broader introduction of checks due to an implementation of payment cards.

11 Source: Eurostat

## Overpriced digital channels are challenging growth in less digitalized countries and create disruption opportunities

Demand for banking digital channels can be curbed not only by low number of useful functionalities, but also by additional fees charged for an access to these services. The least digitalized banking sectors in CE are the only markets without any offer of free access to internet and mobile banking. It is creating a vicious cycle in which banks are not incentivized to develop digital channels due to limited growth potential, whereas clients are avoiding these services due to low value added comparing to expected fees. On the other hand, digital pioneers are taking exactly opposite approach: Tatra Banka, the leader of this edition of digital benchmarking, offers 50% discount for monthly fees if client used at least two innovations in given month (in combination with other conditions client can receive access completely for free).

Second challenge is a successful onboarding of customers starting their journey with digital channels. Also in this matter banks considered as digital laggards offer limited guidance for new users in comparison to pioneers. Limited digital functionalities, additional fees for online channels and unsuccessful onboarding process are creating a situation in which banks challenging such status quo may cause significant market disruptions.

*If you want to know detailed data for digital banking benchmarking, contact us.*

# Key Insights

**Economic growth has gained pace, reaching 3.0%** in 2015, and rising private consumption is underpinning continued momentum, supported by an improving labor market and rising wages.

**Loan growth is expected to turn positive in 2017.** Loans are expected to fall again in 2016, affected by deleveraging and NPL sales, but new business is picking up as the economic recovery becomes more firmly entrenched and falling loan rates make credit more affordable.

**The NPL ratio is set to rise in 2016 after AQR,** on a reclassification of 'performing' corporate loans, but should renew its decline next year.

**ROE (8.0% in 2015) is above average for CE** but is expected to fall back to 6-7% in 2018, as falling loan rates will drive net interest margin compression over the next few years.



# Economy

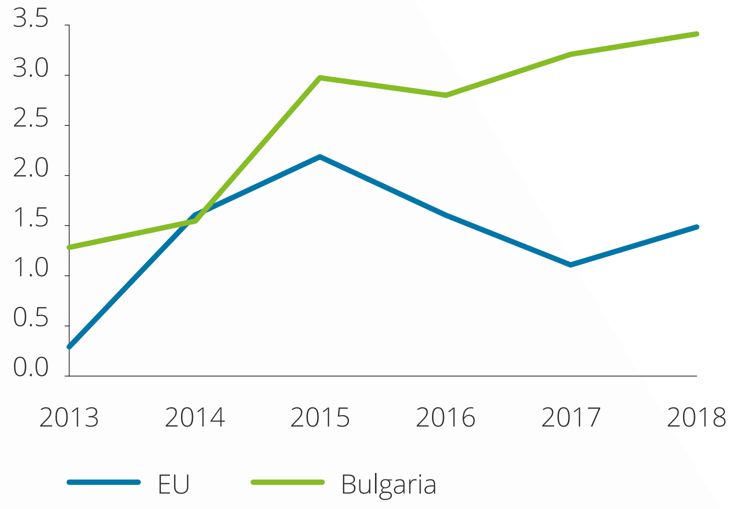
## Economic growth has gained pace

Economic growth in Bulgaria has gained pace, reaching 3.0% in 2015, and rising private consumption should underpin continued momentum in 2016-18. This is supported by an improving labor market, with falling unemployment and strong growth of real wages (+8% y/y in 2015). Consumer confidence has been rising and is near to a post-crisis high. Net exports were the most important contributor to GDP growth last year and should remain a positive driver in 2016 and 2017 but growing import demand is expected to see the size of contribution decline. The contribution to GDP from investment last year is also expected to pull back in 2016, due to lower absorption of EU funds, before gradually picking up again in 2017-18. Business confidence should improve as the economic recovery becomes more firmly entrenched and falling loan rates will make credit more affordable. Business confidence should improve as the economic recovery becomes more firmly entrenched and falling loan rates will make credit more affordable.

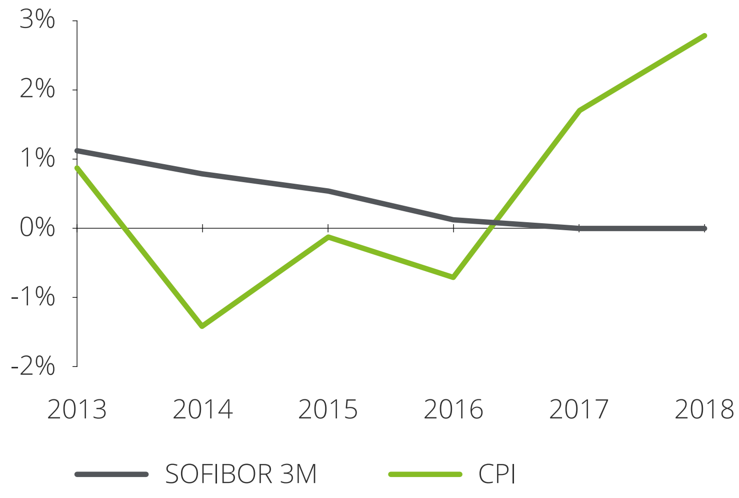


## Real GDP growth

*(yoy%)*

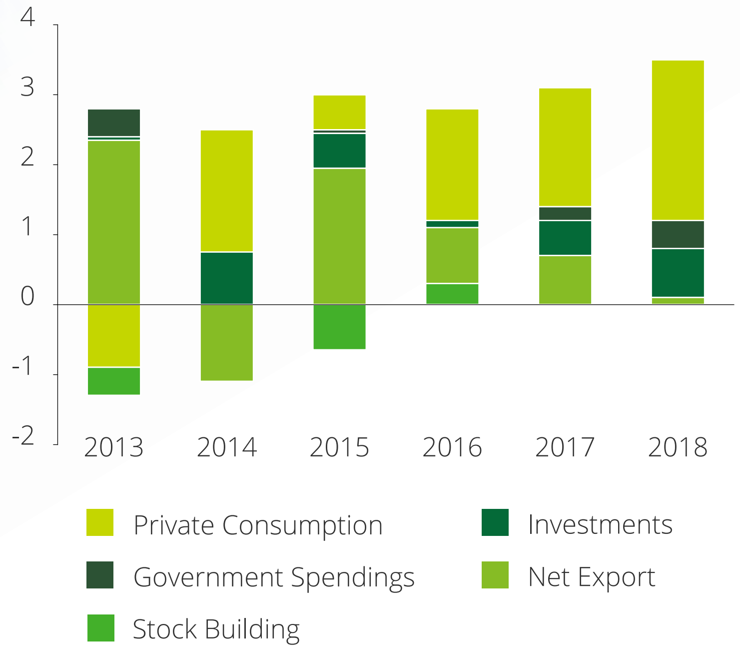



## Interbank interest rate and CPI

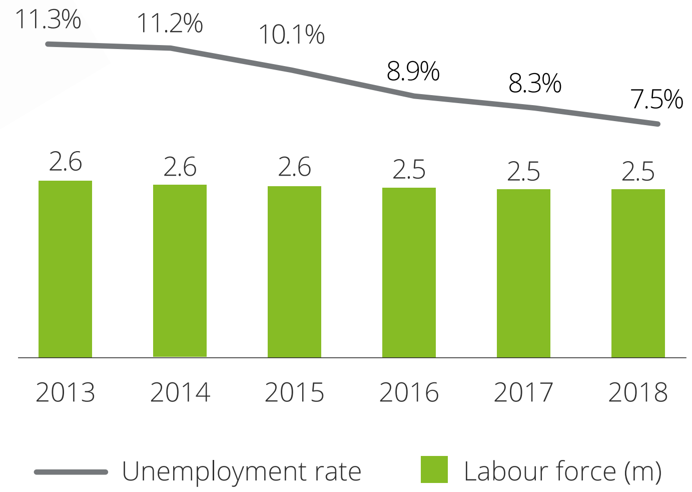



## Real GDP drivers

*(change as a percentage of real GDP)*




## Labour market




*Source: Economist Intelligence Unit*
*Source for interest rate and CPI chart: Economist Intelligence Unit, Bloomberg, Deloitte estimates*

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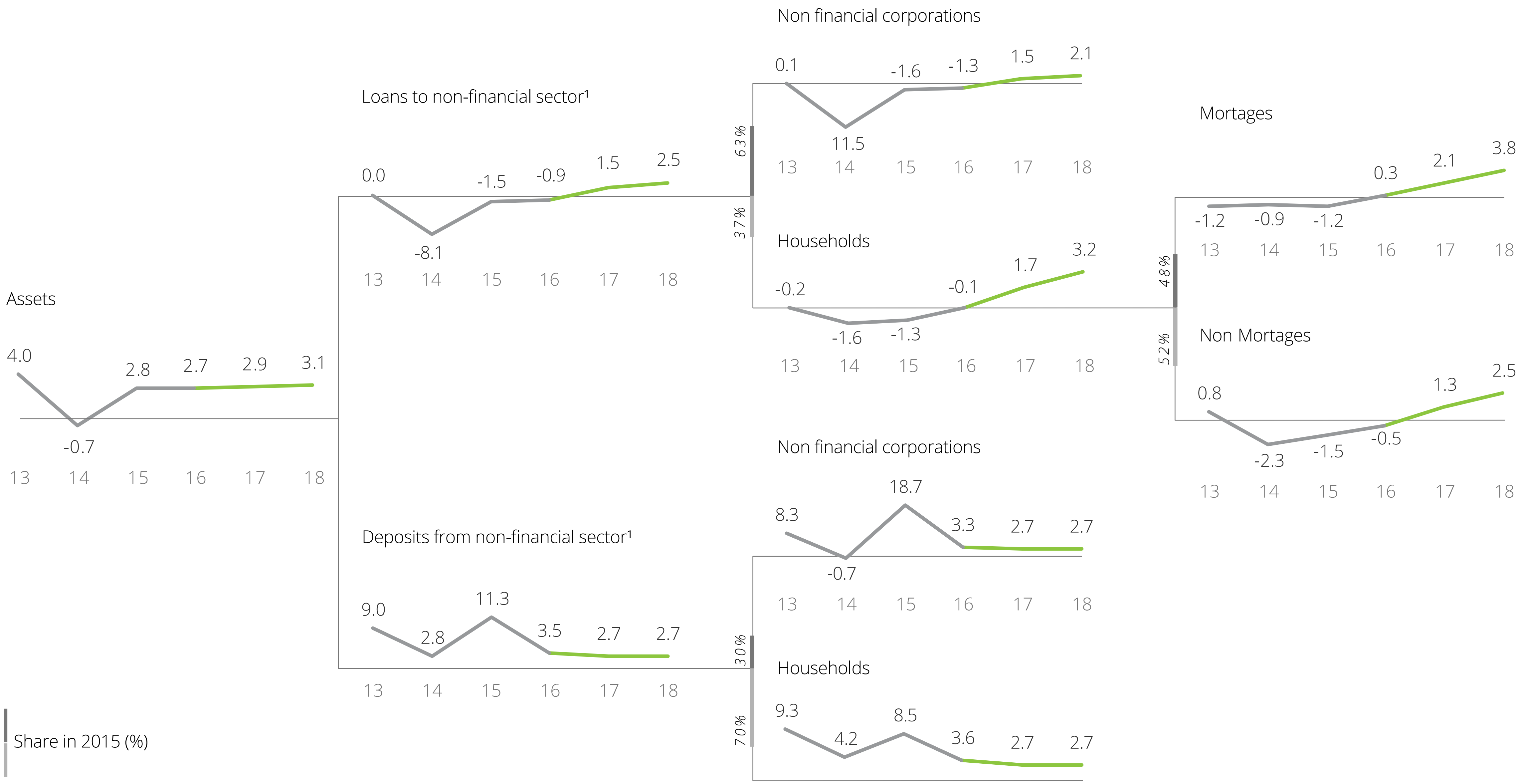
# Balance Sheet

## Loan growth is expected to turn positive in 2017

After declining in 2014-15,loans are expected to fall again in 2016 before returning to positive growth at a level of 2-3% in 2017-18. While deleveraging and NPL sales have continued to drive a decline of stock volumes, new business has been picking up in 2016 in both retail and corporate segments. Retail loans (-1.3% y/y) are expected to be led by mortgages and should remain flat in 2016 before rising by 2-3% in 2017-18. Demand for housing loans will be underpinned by an improving labor market and better affordability (rising wages, falling loan rates), while house prices are growing (+4.0% y/y in 2015). Consumer loan demand is also picking up, though non-bank lenders (+17% y/y in 2015, 14% share of total market) are capturing a growing share of this segment from banks. Corporate loans (-1.6% y/y in 2015) continue to be affected by deleveraging in some segments (e.g. real estate, construction) and are expected to decline by -1% in 2016 before rising 1-2% in 2017-18. Deposit growth (2010-15 CAGR of 9%) is expected to slow on the back of falling interest rates to 4% in 2016 and 3% in 2017-18. However, there are no funding constraints to lending. The sector's non-financial gross loans/deposits fell to 80% in 2015, while the AQR-adjusted CET1 capital ratio was 18.9% at year-end 2015.



## Banking sector balance sheet drivers
(yoy growth %)




¹ Excludes government

*Source: Bulgarian National Bank, Deloitte Estimates*

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# Asset Quality

## Downward trend in NPL ratio interrupted by AQR in 2016 but set to resume

Asset quality in Bulgaria has been improving, with the sector NPL ratio down last year from 17.2% to 15.7%, but the recently completed asset quality review (AQR) is expected to drive an increase in 2016 before the downward trend resumes. This will be due to a reclassification of 'performing' corporate loans that were identified by the AQR as non-performing. Consequently, after declining from 20% to 17.5% last year, the reported corporate NPL ratio is expected to rise back to 20% in 2016. Thereafter, the declining trend should resume, with the support of asset disposals and strong economic growth.

The AQR will not lead to any significant adjustments in the retail segment. After falling from 13.2% to 13.0%, the decline of the retail NPL ratio is expected to accelerate to drop below 10% in 2018. The improving labor market will support the financial standing of households, while falling interest rates should ease the burden of repayment.

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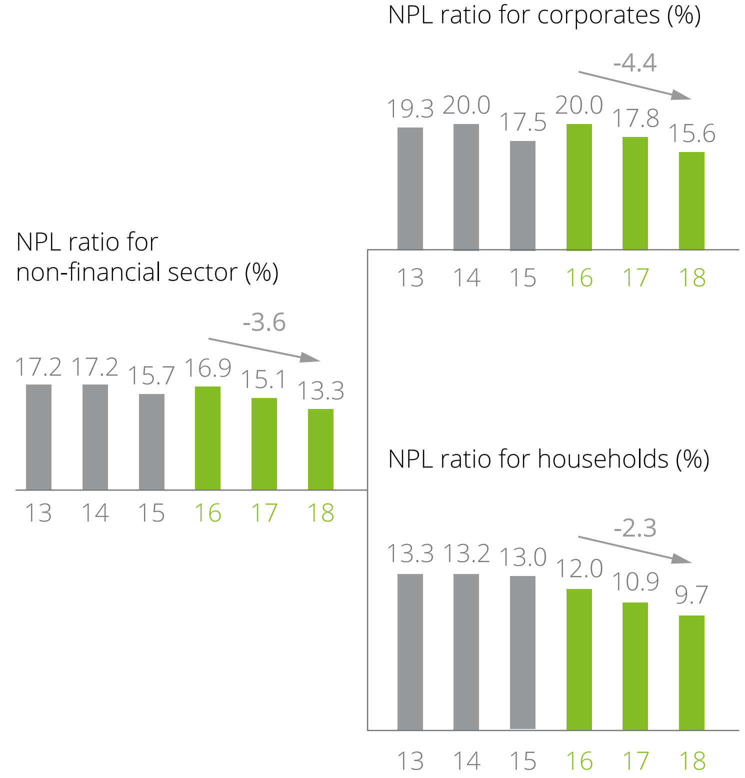
## Asset quality of the banking sector



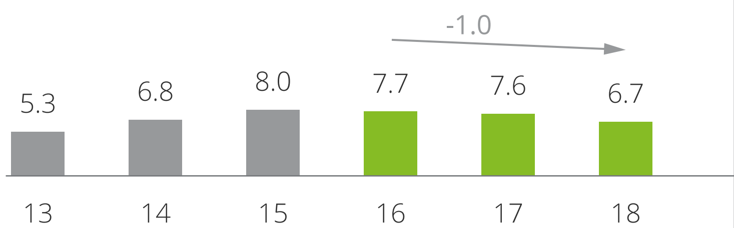
# Profitability


After improving in recent years, ROE (8.0% in 2015) is expected to come under pressure in 2016-18. The banking sector is facing higher provision requirements in 2016 in the wake of the AQR, while net interest margin compression is expected to increasingly weigh on revenues in 2017-18. Bulgaria's AQR identified a need for value adjustments of EUR 340m, mostly for corporate loans. Hence, risk costs are expected to rise from 238bp to 255bp (of average gross loans) in 2016, before an improving trend in loan quality can be reflected in a decline to 190bps by 2018. Deposit re-pricing helped improve the net interest margin by 13bp to 3.2% last year and has continued to cushion the downward pressure in 2016. However, with deposit rates already at very low levels, falling loan rates are expected to drive a sharp drop in the net interest margin to 2.5% by 2018. This is expected to drive a decline of total revenues in 2017-18. Although net fee income has been growing fast (+7% y/y in 2015) the pace of growth should slow down due to competition and regulation (eg. standardized pricing of basic bank accounts). Operating costs are expected to be flat[1] in 2016, but banks should respond with cuts as there will be upward pressure on the cost/income ratio in 2017-18.

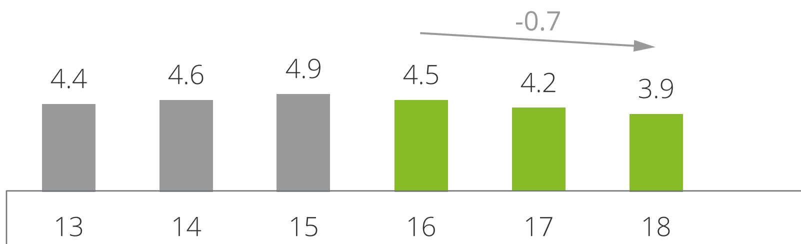
1 Flat on an underlying basis. Due to an accounting change in 2016, whereby deposit insurance fees were shifted to other operating expenses (part of net banking revenue), reported operating costs will decline.

## Banking sector profitability[3]

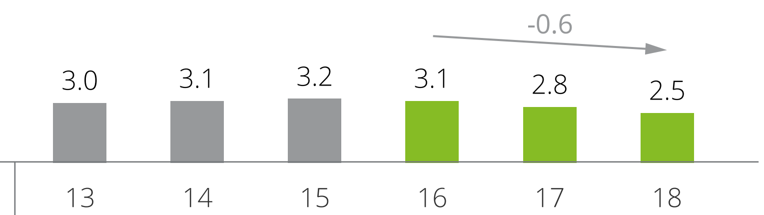
Return on equity (%)



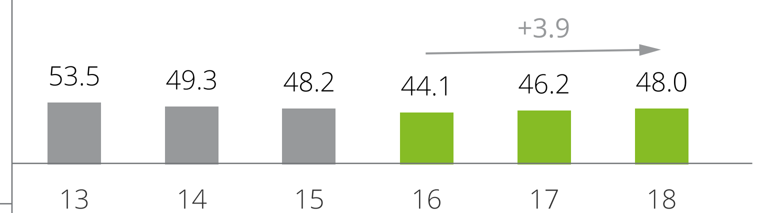

Net revenue/ Avg. assets (%)



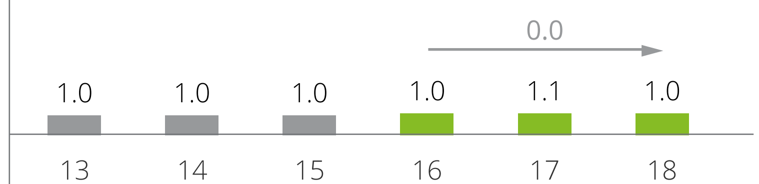

Net interest income/ Avg. assets (%)



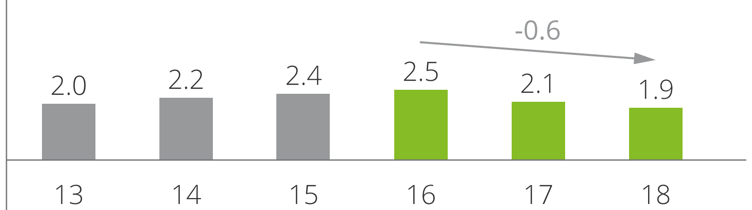

Cost/ Income (%)[2]



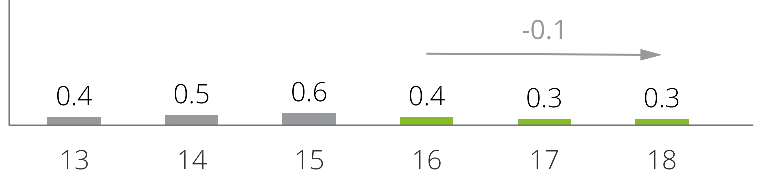

Net fees and commission income/ Avg assets (%)



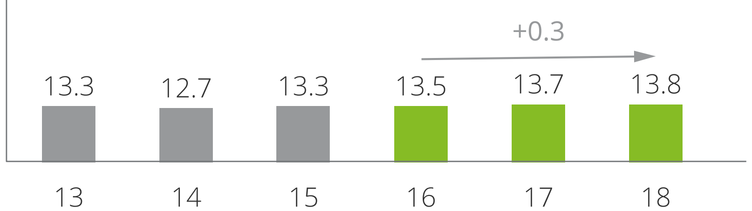

Cost of risk/ Avg. gross loans (%)[1]




Other income/ Avg. assets (%)




Equity/ Total assets (%)




[1] Average non-financial loans. excluding government
[2] Cost/income decline in 2016, impacted by a change in accounting (-3.3 p.p.), with deposit insurance no longer booked in operating costs and instead booked in net other income.
[3] Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.

*Source: Bulgarian National Bank, Deloitte Estimates*

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# Top 10 Banks

## Leading banks, UniCredit Bulbank (#1) and DSK (#2), have gained market share

In the top tier of the sector, UniCredit Bulbank (#1) and DSK (#2), have gained market share over the past year in both lending and deposits, widening the gap to the local player FIB (#3) and UBB (#4). DSK (ROE of 20.4%) and UniCredit Bulbank (13.6%) are also leading the sector in terms of profitability, reflecting their scale advantage, low cost/income ratios, and below-average risk costs. Retail-oriented DSK also benefits from a higher yield loan book and consequently wider net interest margin. The below-average ROEs of FIB (2.4%) and UBB (4.3%) in the past year, mainly reflect their higher than average risk costs.

Among mid-sized players, SG Expressbank (#7) and local player Central Cooperative Bank (#8) gained the most market share in loans and deposits last year. The ROE of SG Expressbank (12.9%) is also one of the best in the sector, thanks to its consistently below average risk costs. Local banks and Greek-owned banks have faced higher funding costs in recent years although the gap has narrowed for most of these players in the past year as rates have declined.



## Main balance sheet items *(LEV bn)*

| | Loans MS 2015 change | Loans Deposits (BGN bn) (BGN bn) / Assets (BGN bn) | Deposits MS 2015 change | Assets MS 2015 change |
|---|---|---|---|---|
| **UniCredit** | 17.8% ↑ +0.4pp | 17.4 | 19.5% ↑ +2.5pp | 19.8% ↑ +2.4pp |
| **DSK Bank** | 13.6% ↑ +0.3pp | 11.1 | 13.5% ↑ +0.9pp | 12.7% ↑ +1.0pp |
| **First Investment Bank** | 10.9% ↓ -1.0pp | 8.7 | 10.8% ↓ -0.9pp | 9.9% ↓ -0.2pp |
| **UBB** | 9.0% ↓ -0.1pp | 6.5 | 7.3% ↓ -0.7pp | 7.5% ↓ -0.2pp |
| **Raiffeisenbank** | 7.1% ↓ -0.3pp | 6.5 | 6.9% ↑ +0.2pp | 7.4% ↑ +0.4pp |
| **Eurobank** | 8.4% ↑ +0.3pp | 5.8 | 6.7% ↓ -1.3pp | 6.6% ↓ -0.6pp |
| **Societe Generale** | 6.5% ↑ +0.4pp | 5.3 | 6.3% ↑ +0.6pp | 6.0% ↑ +0.7pp |
| **Central Cooperative Bank** | 4.0% ↑ +0.7pp | 4.6 | 6.0% ↑ +0.2pp | 5.3% ↑ +0.4pp |
| **Piraeus Bank** | 3.9% ↓ -0.9pp | 2.8 | 3.0% ↓ -0.6pp | 3.3% ↓ -0.6pp |
| **CIBANK** | 2.9% ↑ +0.2pp | 2.7 | 2.0% ↑ +0.1pp | 3.1% ↑ +0.2pp |
| **Total Market (BGN bn)** | **54.121**[1] | | **69.276**[2] | **87.524** |

[1] Loans include government and non-credit institutions but market share is based only on retail and corporate loans.
[2] Deposits and market share are based on retail, corporate, government and non-credit institutions deposits
*Source: Bankscope, Central Bank, Deloitte estimates*

Retail
Corporate and others
Total volume/ breakdown not available
Assets (BGN bn)

## Top 10 bank profitability drivers 2013-15

1 UniCredit
2 DSK Bank
3 First Investment Bank
4 UBB
5 Raiffeisenbank
6 Eurobank
7 Societe Generale
8 Central Cooperative Bank
9 Piraeus Bank
10 CIBANK


*Source: Bankscope, Bulgarian National Bank*

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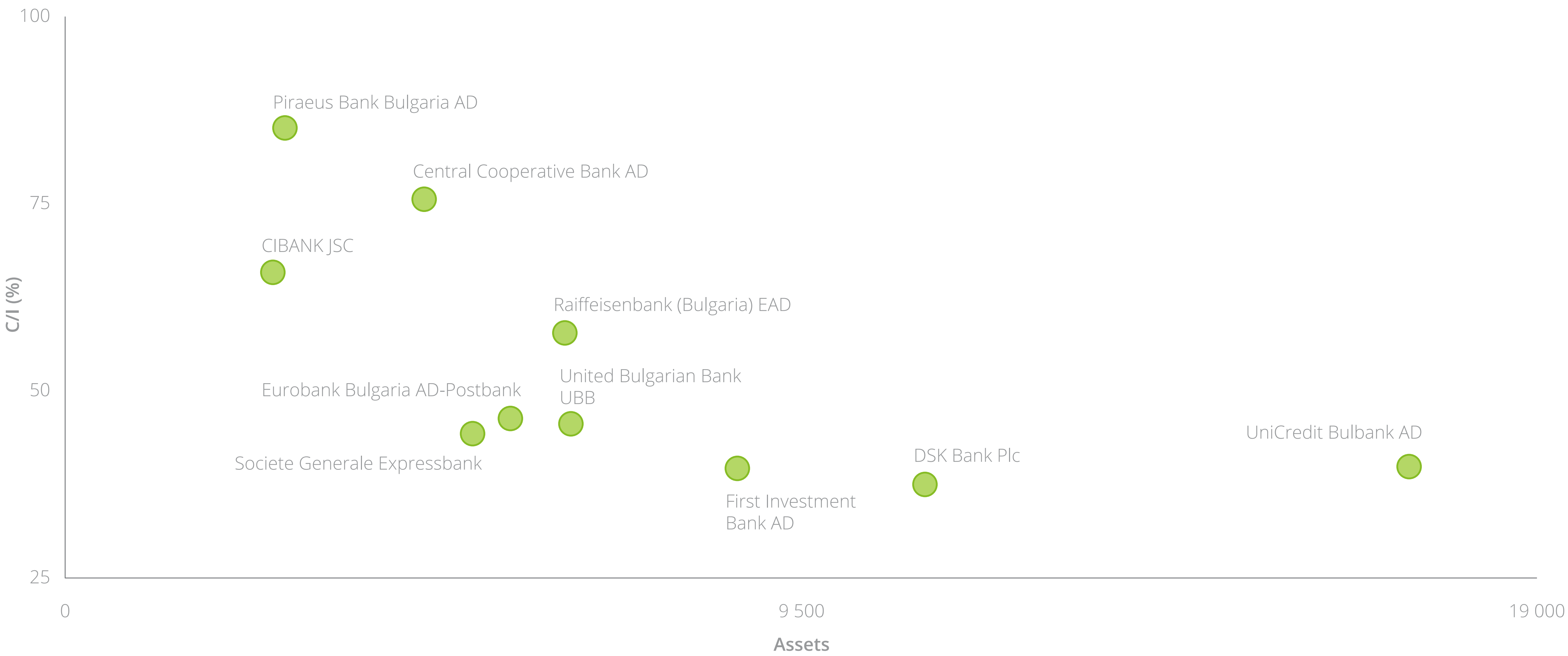
## C/I ratio versus assets, 2015




*Source: Bankscope*

# Strategy

## Operating efficiency will be in focus as low interest rates drive margin pressure

Operating efficiency is expected to be in focus over the next few years, with low interest rates and competition expected to drive margin compression and lower banking sector profitability. Smaller banks will face increasing pressure to participate in sector consolidation in order to thereby achieve better scale and synergies. Large banks and foreign players with lower funding costs will have an advantage but all will aim to minimize operating costs. Digitalization will be an important avenue for banks to update service models and improve efficiency, while maintaining service levels and customer experience.

This should coincide with simplification of products and improved digital functionality (e.g. opening accounts, getting loans on-line). Making better use of data analytics and improving customer intelligence should enable banks to cross-sell more effectively with less effort. It can also support customer retention, which may become more important if competition for loan refinancing picks up on the back of falling interest rates. Given the still high NPL ratio in the sector, effective balance sheet cleaning, including portfolio sales, restructuring, and work-outs will remain a priority for many banks.

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# Digital Maturity

Bulgaria is ranked 5th among CE countries in digital maturity (based on the overall score of its 5 biggest banks) behind Poland, Slovakia, Czech Republic and Romania. The internet capabilities of Romania and Bulgaria are at a similar level of development but the mobile channel is less developed in Bulgaria. Analysis of the Customer Journey reveals that the digital functionalities responsible for customer acquisition are the most digitally mature (similar to most CE countries) and there is a strong focus on customer onboarding, which is even better than in more developed markets. From a products perspective, the most digitalized are term deposits and saving accounts, which is unique for Bulgaria, as other markets banks focus more on loan services.

*If you want to know detailed data for digital banking benchmarking, contact us.*

# Contact

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# Key Insights

**Croatia's economy is growing,** after pulling out of 6-year recession in 2015. While growth is still the slowest in CE, there has been a strong pick up in private consumption and investment.

**Loans will decline again in 2016,** led by a sharp drop in mortgages due to CHF loan conversion, but should return to growth in 2017, as the economic recovery becomes more entrenched.

**Asset quality is now on the mend.** The NPL ratio dropped from 17.4% in 2014 to 17.0% in 2015, and the decline will accelerate, as bank NPL sales rise and the economic recovery continues.

**Profitability will recover in 2016,** after a massive loss in 2015 (ROE of -8%) on the back of CHF loan conversion. Risk costs should continue to fall in 2017-18 but margin pressure is also ahead.



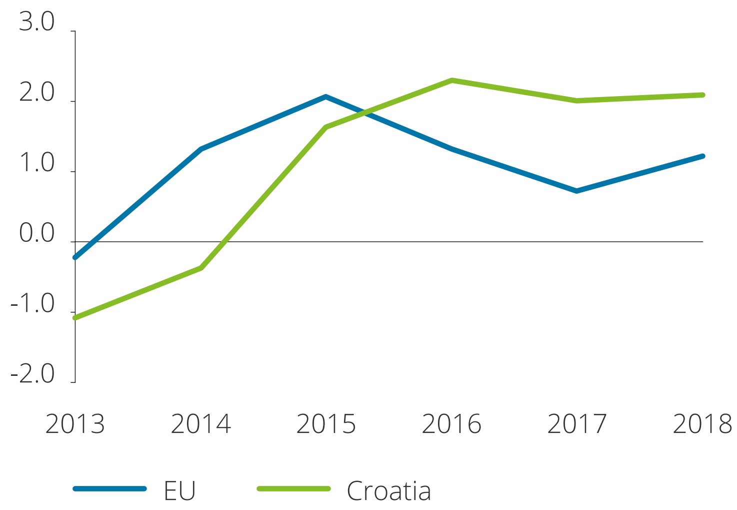
# Economy

## After a long recession, the Croatian economy is growing again

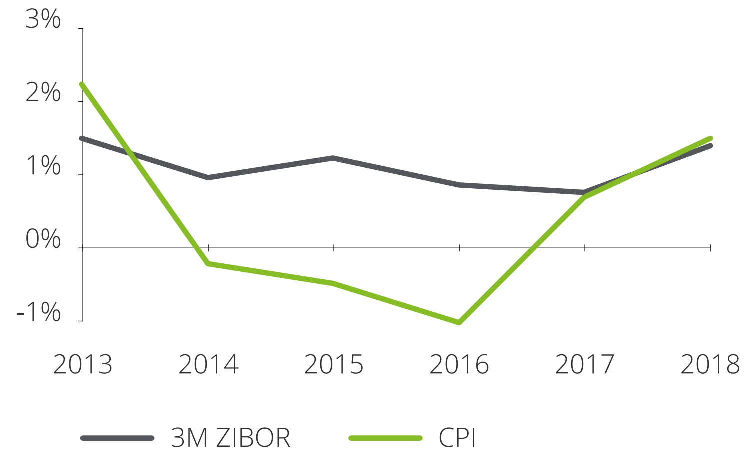
The Croatian economy is growing again, after pulling out of 6-year recession in 2015, but at the slowest pace in the CE region. After GDP growth of 1.6% in 2015, further moderate growth is expected at 1.9-2.0% in 2016-18. The largest contributor to economic growth has been a pick-up in private consumption and this trend should continue on the back of and rising employment and wages. Unemployment in Croatia is the highest in CE but it has declined from 17.3% in 2014 to 16.3% in 2015 and is expected to fall towards 13-14% in 2018. This has helped improve consumer confidence back to levels not seen since 2007. Investment has also been picking up in 2016, mainly driven by the private sector, while public investment should benefit from improved EU funds absorption going forward. Growth of net exports should continue to be supported by the gradual economic recovery in Europe lifting external demand.



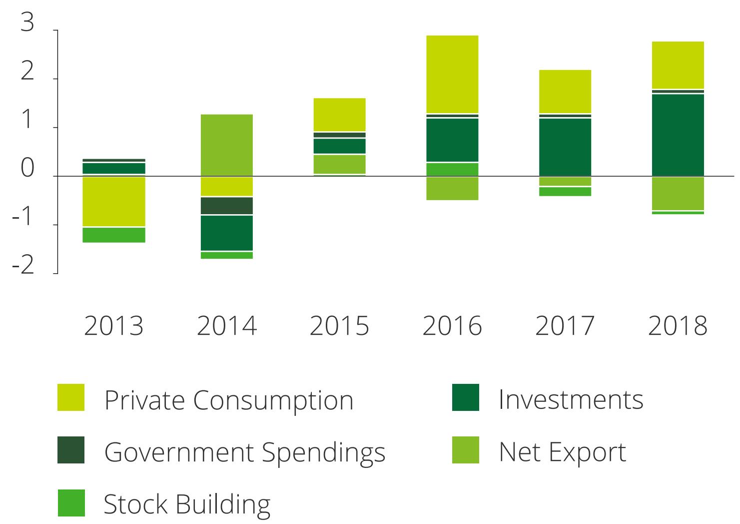
## Real GDP growth
(yoy%)



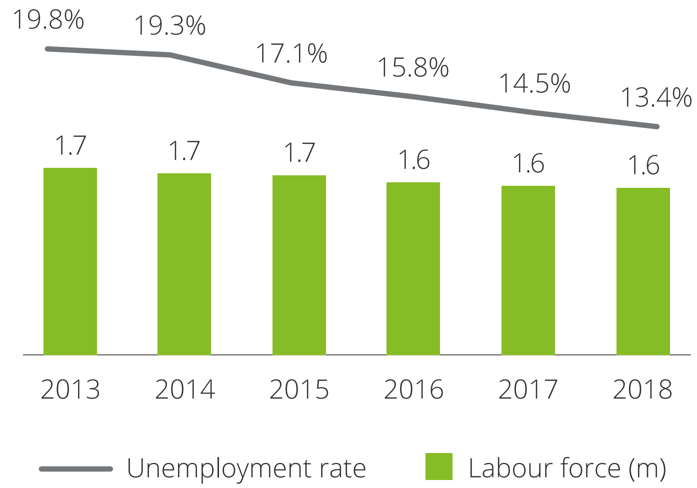

## Interbank interest rate and CPI




## Real GDP drivers
(change as a percentage of real GDP)




## Labour market




*Source: Economist Intelligence Unit*
*Source for interest rate and CPI chart: Economist Intelligence Unit, Bloomberg, Deloitte estimates*

# Balance Sheet

## Loans are set to fall again in 2016 but growth should turn positive in 2017

After declining for the last 4 years and by -1.9% y/y in 2015, loans will fall again in 2016 before gradually returning to positive growth in 2017-18. The drop in 2016 will mainly be driven by a double-digit reduction (c. -14% y/y) in housing loans, driven by the conversion of CHF mortgages. Thereafter, the improving labor market and affordability of property should support a slight rise of up to 1-2% y/y in housing loans in 2017-18. Accelerating consumer spending is expected to bring a faster recovery of consumer loans, growing already by 1-2% y/y in 2016-17 and rising to 3-4% y/y in 2018. Corporate loan growth has been negative in recent years, reflecting deleveraging but also NPL sales and the availability of cheaper EUR borrowing abroad for some companies. However, with Croatia's economic recovery becoming more entrenched, growing investment should drive corporate loans return to positive growth of 1-2% y/y in 2016 and an acceleration to 3-4% y/y by 2018. The constraints to lending are now mainly on the demand side. The banking sector is well capitalized (tier 1 CAR of 19.1%). Deposit growth (2012-15 CAGR of 4%) is expected to slow due to lower deposit interest rates but the loans-to-deposits ratio has fallen from 119% in 2012 to 103% in 2015 and should drop below 100% in 2016.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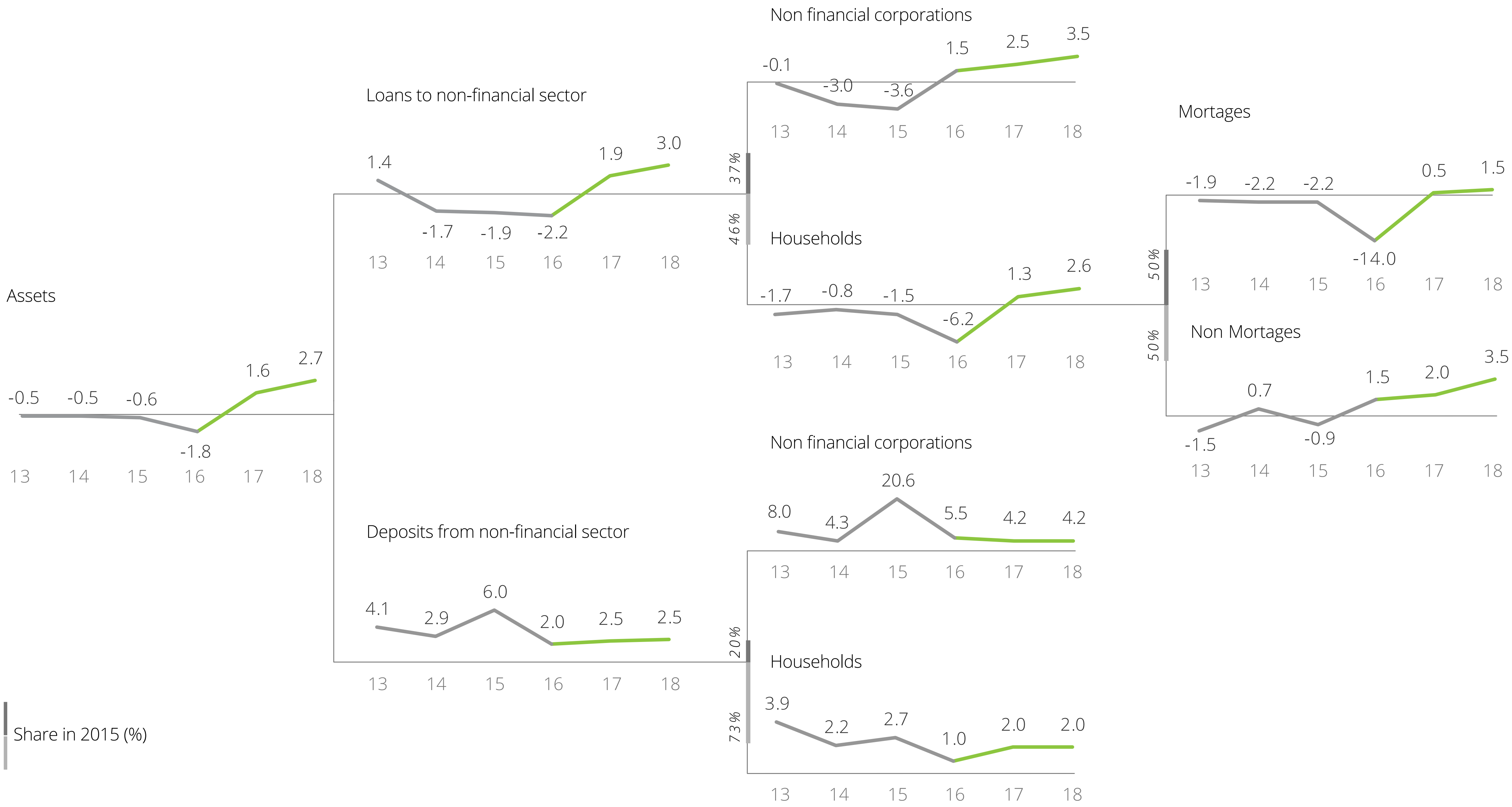
## Banking sector balance sheet drivers (yoy growth %)




*Source: Croatian National Bank, Deloitte Estimates*

# Asset Quality

## NPL ratio is one of the highest in CE but asset quality is now on the mend

The NPL ratio of Croatia is one of the highest in CE but the trend of improvement that began in 2015 should continue in 2016-18. The overall NPL ratio declined from 17.4% in 2014 to 17.0% in 2015, driven by a drop in the corporate NPL ratio from 30.8% to 30.1%. Balance sheet cleaning is expected to pick up, as banks are planning to sell more NPLs. Combined with the impact of the more favorable economic environment, this should help drive a decline of corporate NPLs to 27% in 2016 and to 21% by 2018. The retail NPL ratio remained on a rising trend during 2015, increasing from 12.0% to 12.2%, but has since moved lower. With the financial standing of households supported by CHF mortgage conversion, the improving labor market, and falling loan rates, a gradual improvement in the retail NPL ratio is expected to 11.5% in 2016 and to below 10% in 2018.

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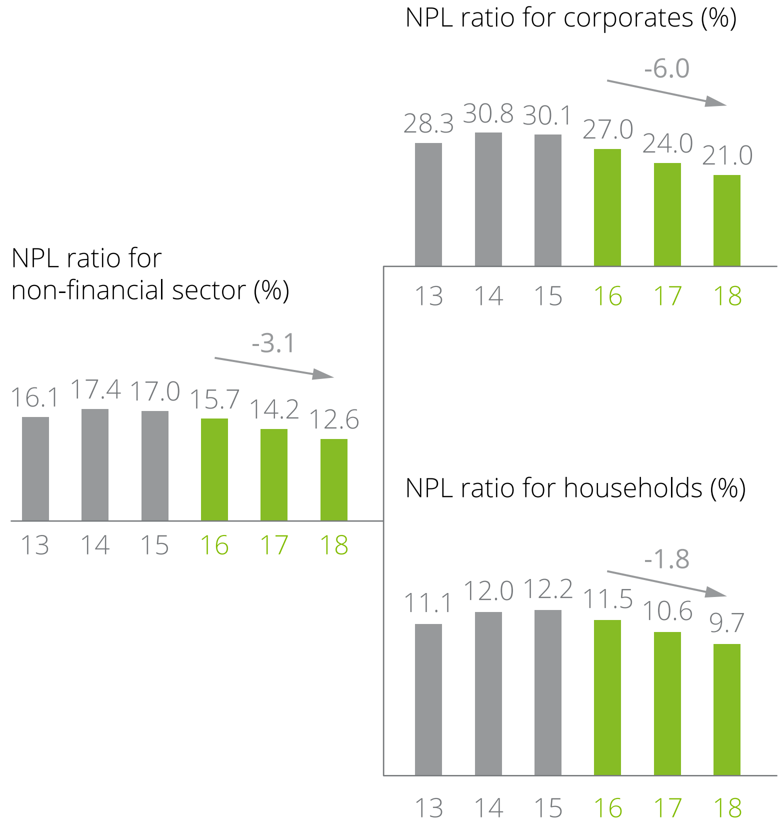
## Asset quality of the banking sector

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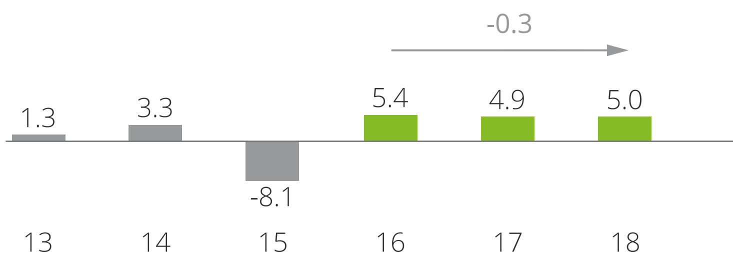
# Profitability

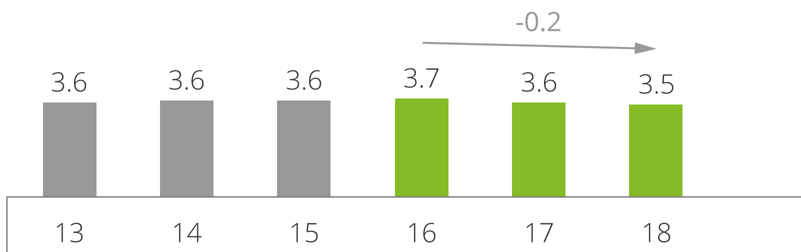
After suffering a large net loss in 2015, due to the costs of CHF loan conversion (EUR 0.9bn), the Croatian banking sector should return to profitability in 2016. The ROE dropped from 3.3% in 2014 to -8% in 2015 but is expected to rise back above 5% in 2016 and remain at ~5% in 2017-18. A reduction of risk costs is the main driver of the recovery but an offset is expected from net interest margin pressure in 2017-18. While the increase in risk costs from 1.8% (of average gross loans) in 2014 to 4.4% in 2015 can be entirely attributed to the cost of CHF loan conversion, there was a net release of provisions in 1Q16. Hence, even on an adjusted basis, the outlook is for sharply lower risk costs in 2016. Against a backdrop of the ongoing economic recovery, risk costs are expected to drop to 1.4% in 2016 and to 1.2% by 2018. As the structure of funding in the sector has improved (less borrowing from financial institutions, shift in customer deposits to current accounts), the net interest margin of Croatian banks increased by 13bp in 2014-15 to 2.7%. However, a turning point has been reached and the margin is expected to fall back to 2.5% by 2018, as loan rates will decline faster than deposit rates in the next few years. Banks have cut branches and employment by 3-4% between 2013 and 2015 and a continuation of this trend should keep cost growth contained. However, due to the margin squeeze on revenue, banks will not significantly improve the cost/income ratio.

## Banking sector profitability[1]

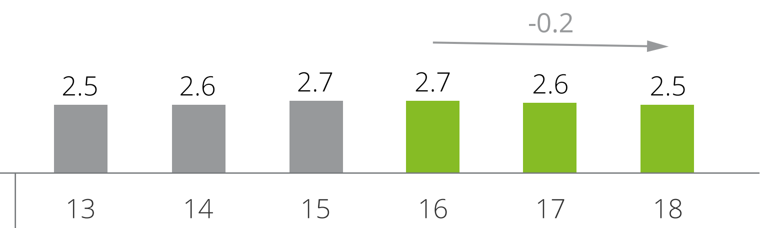
Return on equity (%)



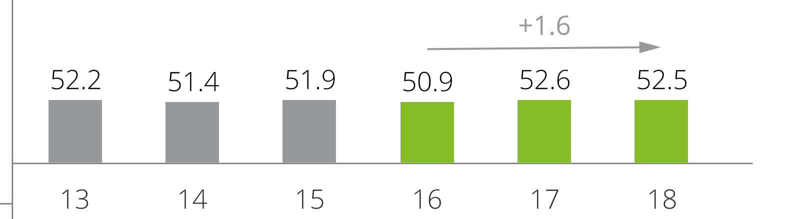

Net revenue/ Avg. assets (%)



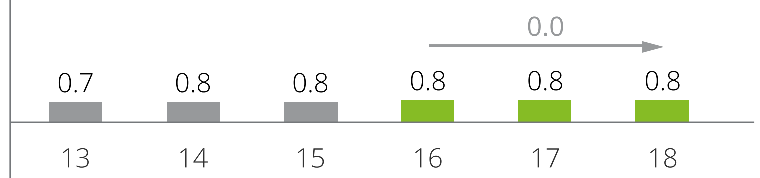

Net interest income/ Avg. assets (%)



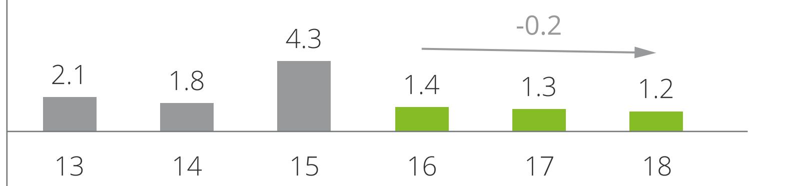

Cost/ Income (%)



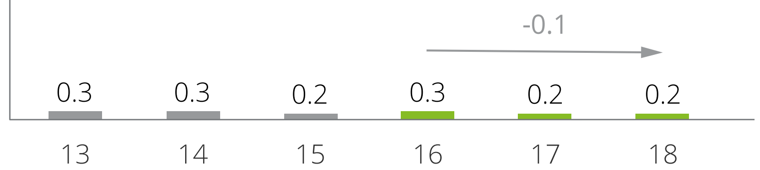

Net fees and commission income/ Avg assets (%)



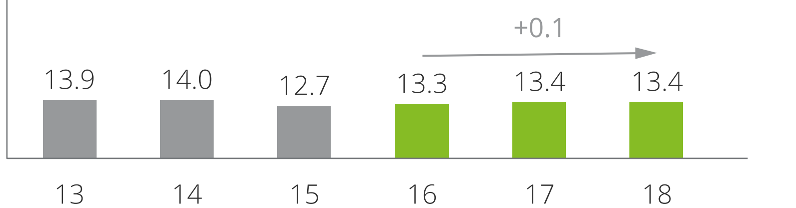

Cost of risk/ Avg. gross loans (%)




Other income/ Avg. assets (%)




Equity/ Total assets (%)




[1] Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.
*Source: Croatian National Bank, Deloitte Estimates*

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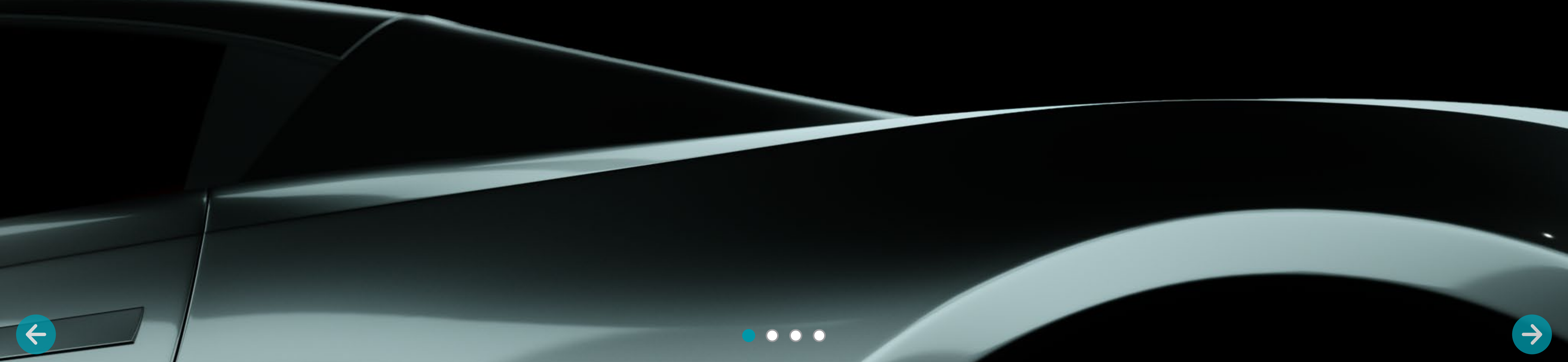
# Top 10 Banks

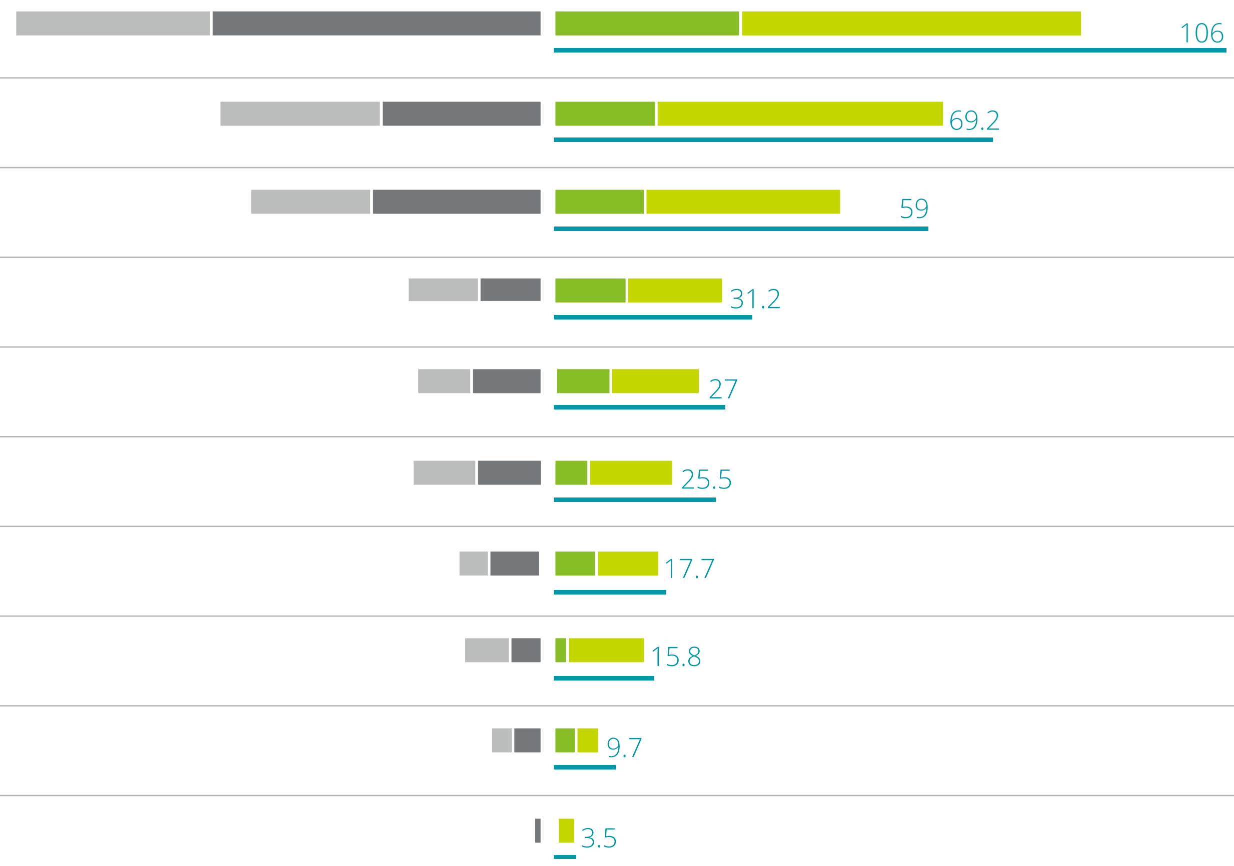
## Top tier banks, Zagrebacka (#1) and Privredna (#2), outperform the sector ROE

While the losses imposed by CHF loan conversion weighed heavily on results in 2015, the top tier outperformed the sector ROE, with #2 Privredna remaining profitable (2.8%) and #1 Zagrebacka suffering only a minor loss (-0.8%). This resilience of these banks reflects their advantage of scale (low cost/income ratios) as well as their relatively low cost of risk (excluding the effects of CHF loan conversion). Although loans have been stagnant, both banks also gained market share in lending. Among the remaining top 10 players, the most resilient ROEs last year were at #6 Societe-Generale Splitska (3.4%) and #7 Hrvatska Postanska (9.5%), players that were relatively less exposed to CHF loans. Hrvatska Postanska also gained market share in lending over the past year, particularly in the housing loan segment. The banks that were growing fastest in 2013-14, #8 OTP and #9 Sberbank, were less aggressive in 2015. However, the banks that gave up the most market share in 2013-14, #4 Raiffeisenbank and #6 Hypo Alpe-Adria Bank, were also those shrinking their loan books most in 2015.





## Main balance sheet items, HRK bn



| | Loans MS 2015 change | Loans (HRK bn) / Deposits (HRK bn) – Assets (HRK bn) | Deposits MS 2015 change | Assets MS 2015 change |
|---|---|---|---|---|
| **ZABA** | 28.6 % +0.7pp | 106 | 27.1% +2.1pp | 26.4% +1.0pp |
| **PBZ** | 17.6 % +0.1pp | 69.2 | 20.0% -0.2pp | 17.2% +0.2pp |
| **Erste & Steiermärkische** | 15.9 % -0.1pp | 59 | 14.7% +0.1pp | 14.7% -0.2pp |
| **Raiffeisenbank** | 7.4% -0.4pp | 31.2 | 8.7% -0.4pp | 7.8% 0.0pp |
| **Societe Generale – Splitska** | 6.8% 0.0pp | 27 | 7.5% -0.6pp | 6.7% -0.4pp |
| **Hypo Alpe-Adria** | 7.0% -0.4pp | 25.5 | 6.0% -0.4pp | 6.4% -0.6pp |
| **HPB** | 4.5% +0.1pp | 17.7 | 5.4% -0.2pp | 4.4% +0.1pp |
| **OTP** | 4.4% +0.1pp | 15.8 | 4.7% -0.4pp | 3.9% 0.0pp |
| **Sberbank** | 2.8% -0.1pp | 9.7 | 2.4% +0.1pp | 2.4% -0.1pp |
| **Kreditna** | 0.7% -0.1pp | 3.5 | 1.0% -0.3pp | 0.9% -0.2pp |
| **Total Market (HRK tn)** | 271.595[1] | | 264.182[2] | 401.297 |

**Note:** Market share calculation based on unconsolidated annual reports
[1] Loans to non-financial sector 2. Deposits from non-financial sector
*Source: Croatian National Bank, Bankscope, Central Bank, Deloitte estimates*

Retail
Corporate and others
Total volume/ breakdown not available
Assets (HRK bn)

## Top 10 bank profitability drivers 2013-15[1]

1 ZABA
2 PBZ
3 Erste & Steiermärkische
4 Raiffeisenbank
5 Societe Generale – Splitska
6 Hypo Alpe-Adria
7 HPB
8 OTP
9 Sberbank
10 Kreditna

| Indicator | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| ROE (%) | -0.8 | 2.7 | -10.2 | -3.2 | 3.4 | -69.1 | 9.5 | -4.6 | -15.0 | 3.1 |
| Net Revenues / Average Assets (%) | 4.1 | 5.1 | 4.5 | 5.5 | 4.3 | 1.6 | 4.4 | 4.6 | 3.2 | 2.3 |
| Cost to Income (%) | 51.5 | 51.5 | 57.7 | 60.7 | 53.2 | 152.1 | 62.2 | 66.1 | 74.5 | 79.4 |
| Cost of risk (%) | 2.9 | 2.6 | 4.3 | 4.0 | 1.9 | 11.1 | 1.3 | 6.1 | 4.2 | 0.5 |
| Equity / Assets (%) | 13.3 | 16.9 | 10.4 | 12.5 | 13.1 | 10.1 | 9.9 | 10.7 | 12.6 | 8.1 |
| Net interest revenue (%) | 2.7 | 3.2 | 3.1 | 2.9 | 2.9 | 1.6 | 2.9 | 3.1 | 2.6 | 1.5 |
| Net fees and commision revenue (%) | 1.0 | 1.6 | 0.9 | 1.3 | 0.9 | 0.1 | 1.1 | 0.8 | 0.5 | 0.5 |
| Other revenues (%) | 0.4 | 0.3 | 0.5 | 1.3 | 0.5 | -0.1 | 0.4 | 0.6 | 0.2 | 0.3 |

- Trend in 2013 - 2015

13.0% - 2015

[1] Bankscope ratios for 2015 were modified to place CHF loan conversion costs in cost of risk and to exclude them from costs

*Source: Bankscope, Deloitte analysis*

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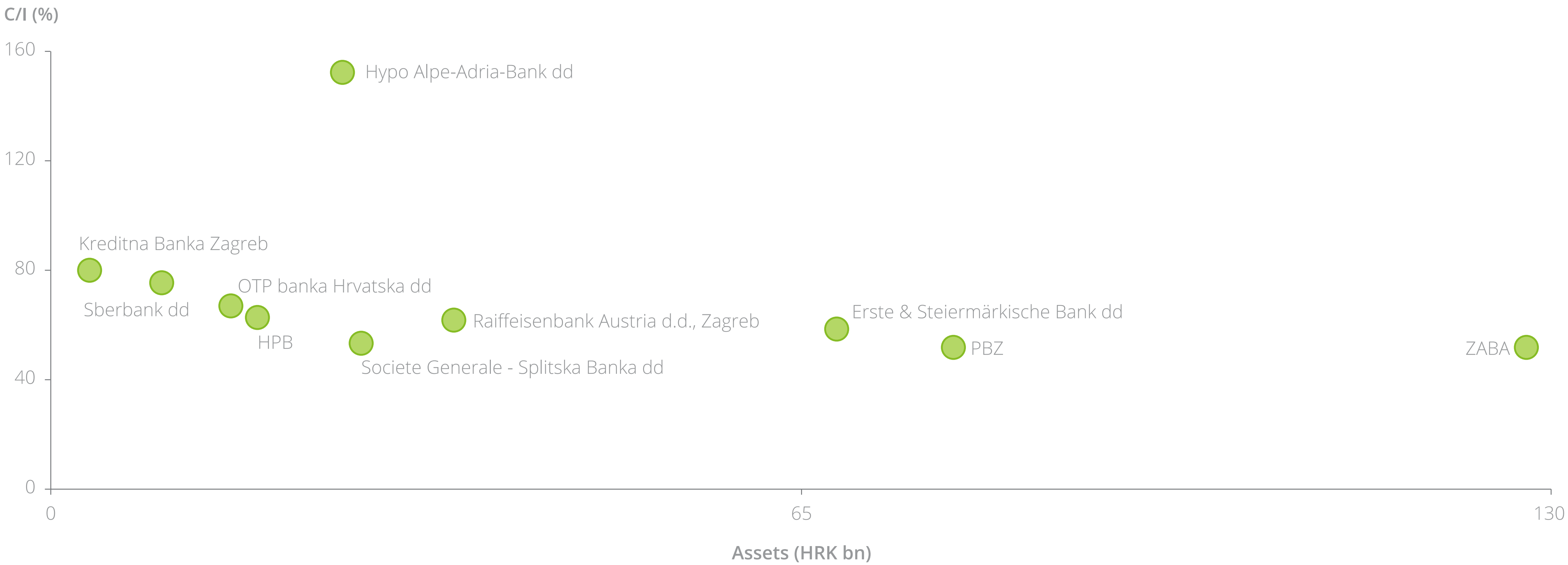
## C/I ratio versus assets[1], 2015




[1] Based on consolidated financial statements

*Source: Bankscope*

# Strategy

## As competition intensifies, improving operating efficiency will be a priority

Against the backdrop of an ongoing economic recovery and with asset quality now on the mend, competition in the banking sector will be intensifying, particularly in lending and for high quality corporate and retail clients. One aspect of this will be price competition and the resulting margin pressure will increase the need for many banks to improve operating efficiency. Small and mid-sized players that lag in efficiency will be encouraged to consider consolidation. Banks will also be competing on quality of service and efficiency of processes (e.g. time to yes for loan applicants). With increasing usage of on-line and mobile banking, the functionality of digital channels is of growing importance to meet customer expectations and banks in a leadership position will have an advantage. Digitalization of internal processes will also enable banks to shift resources towards sales and to reduce the cost to serve. Another ongoing priority for banks is the reduction of credit risk costs and the cleaning of balance sheets. Third-party debt sales are an aspect of this and will be expanding.



# Digital Maturity

Croatia is ranked 6th among CE countries in digital maturity (based on the overall score of its 5 biggest banks) behind Poland, Slovakia, Czech Republic, Romania and Bulgaria. The best Croatian bank ranks 18th, while its biggest laggard ranks last. From a Customer Journey perspective, the digital functionalities responsible for information gathering are the most digitally mature, an area in which Croatia is also a leader in CE. However, other categories fall behind the CE average, especially account opening. Croatian banks are also exceptionally well developed in functionalities supporting account closure, which is a direction not followed by more advanced markets.

*If you want to know detailed data for digital banking benchmarking, contact us.*

# Contact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# Key Insights

**GDP growth jumped to 4.5% in 2015** on a surge in investment and will slow in 2016 before it picks up again. Consumer spending is growing steadily thanks to a strong labor market.

**Lending accelerated in 2015 (+5.5% y/y),** driven by mortgages (+8.8% y/y). Momentum should continue in 2016-18, with low rates encouraging consumer spending and corporate investment.

**Lowest NPL ratio (4.4% in 2015) in CE** is set to further decline, thanks to a strong economy and labor market. However, risk costs (50bp of gross loans) are at bottom and likely to rise.

**ROE (12.9% in 2015) is the best in CE** but profitability should erode in 2017-18 due to continued net interest margin pressure on the back of low interest rates and growing risk costs.

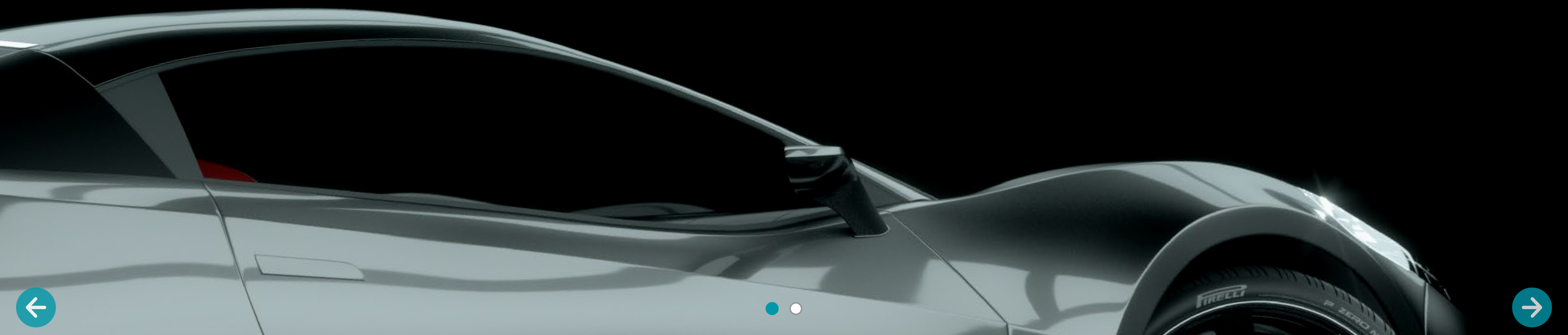


# Economy

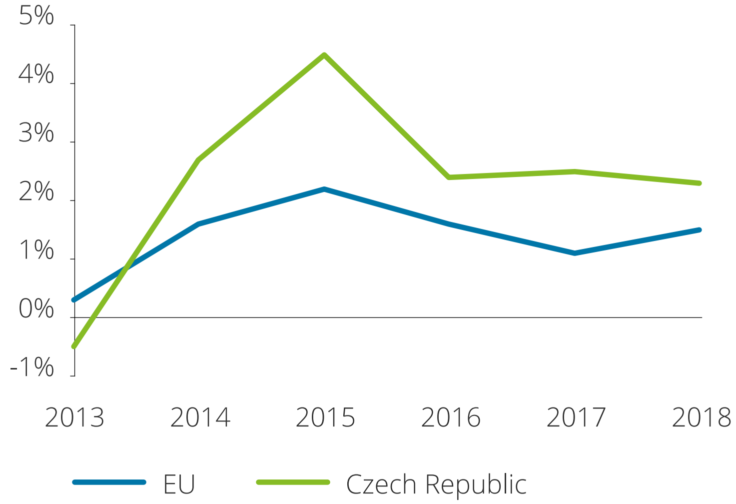
## Economic growth will slow in 2016 before it picking up again in 2017

Following the jump in GDP growth to 4.5% in 2015, Czech economic growth will slow in 2016 before it picks up again next year. This up and down reflects mainly a surge and decline in the level of public investment co-financed by EU funds. Investment should return to growth in 2017. Public and private consumption continue to rise steadily and are the main driver of the economy. Consumer spending is supported by an improving labor market (growing employment, rising wages) and low interest rates that encourage credit growth. Czech unemployment is the lowest in CE and, after falling steadily from 7.0% in 2013 to 5.1% in 2015, should continue to decline. Net exports will contribute to economic growth in 2016 but this contribution is expected to diminish in 2017. Rising investment next year is expected to lift imports, while moderate currency strengthening next year could weigh on exports. The CNB's commitment to maintain a rate CZK 27 to the euro is currently expected to end as of mid-2017.

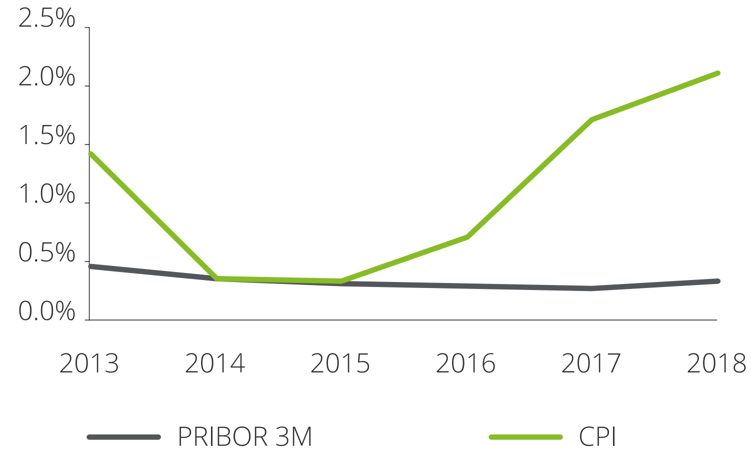




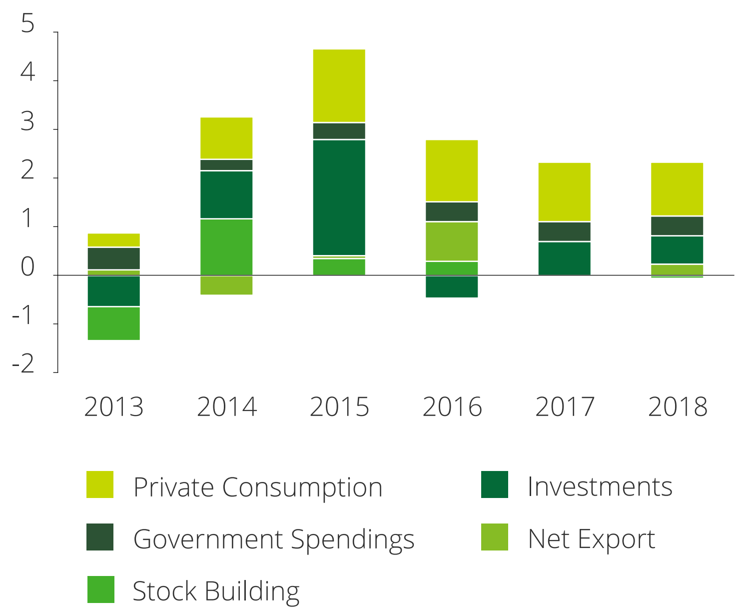
## Real GDP growth
*(yoy%)*



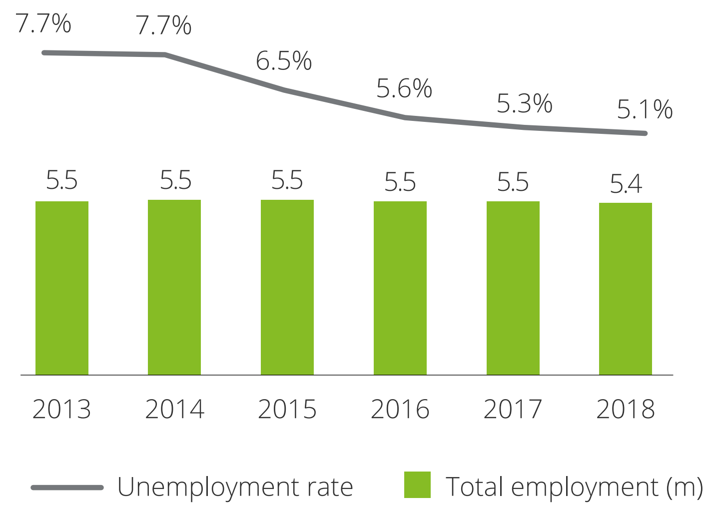

## Interbank interest rate and CPI




## Real GDP drivers
*(change as a percentage of real GDP)*




## Labour market



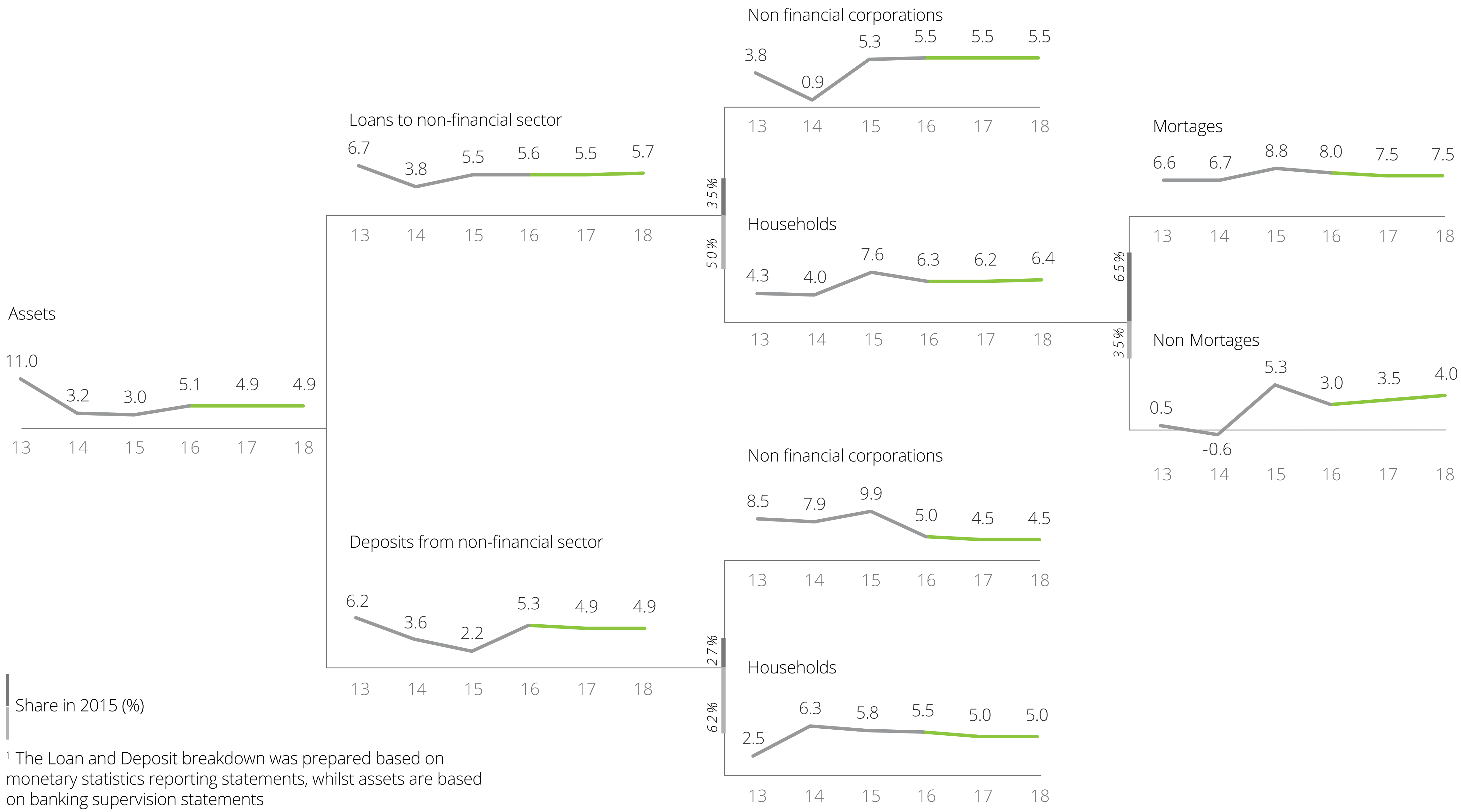

*Source: Economist Intelligence Unit*
*Source for interest rate and CPI chart: Economist Intelligence Unit, Bloomberg, Deloitte estimates*

# Balance Sheet

## Loan growth accelerated in 2015, driven by housing loans

Loan growth accelerated in 2015, led by housing loans (+8.8% y/y). Demand for housing loans is supported by low interest rates helping affordability, while rising property prices (+4.5% y/y for apartments in 2015) are contributing to higher ticket sizes. Mortgage loan growth is expected to remain at 8% y/y in 2016 but should moderate slightly in 2017-18, as the central bank tightens its recommendation limiting LTV mortgages. Consumer loan growth lags that of housing loans but should pick up gradually on the back of rising consumer spending, helped by lower rates brought about by competition. Corporate lending picked up in 2015 to 5.3% y/y and should continue to grow at a similar pace of 5-6% in 2016-18, as low interest rates will continue to encourage investment. The banking sector has ample capital (tier 1 CAR of 17.9% in 2015) and funding. Retail deposits grew by 5.8% y/y in 2015 and should continue to grow at 5-6% in 2016-18, supported by rising household income and employment. Low interest rates encourage a shift to alternative investments but households will likely retain a preference for low-risk assets. Corporate deposit growth has been rapid (9.9% y/y in 2015) but should slow to 4-5% in 2016-18, as companies invest a greater part of their cash reserves. Hence, a rising trend is expected in the loans/deposits ratio, which is one of the lowest in CE (78% in 2015).

## Banking sector balance sheet drivers (yoy growth %)




[1] The Loan and Deposit breakdown was prepared based on monetary statistics reporting statements, whilst assets are based on banking supervision statements

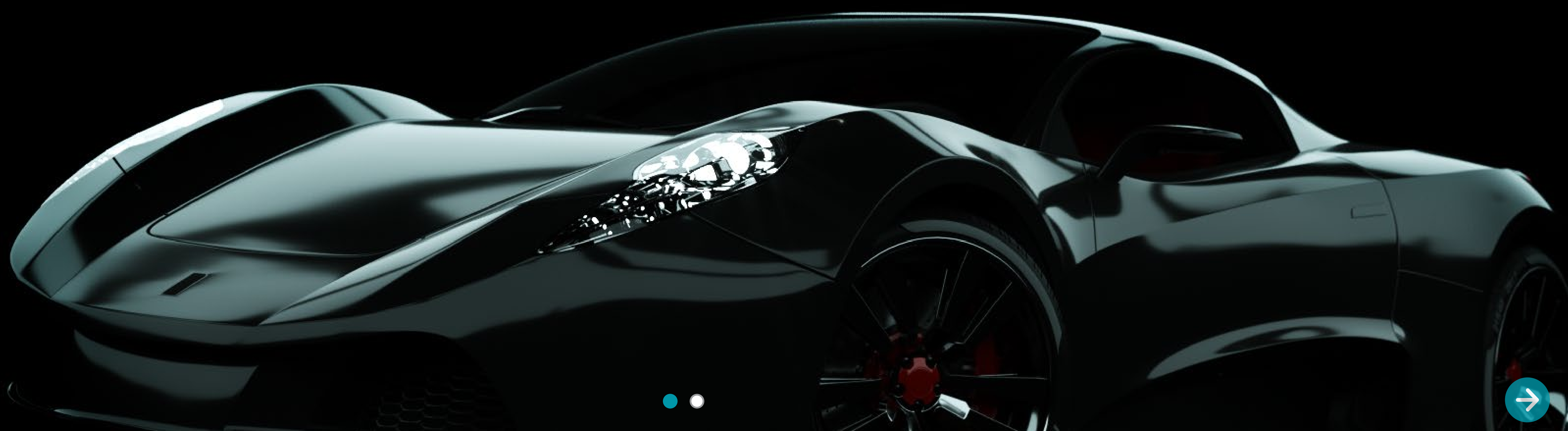
*Source: Czech National Bank, Deloitte Estimates*

# Asset Quality

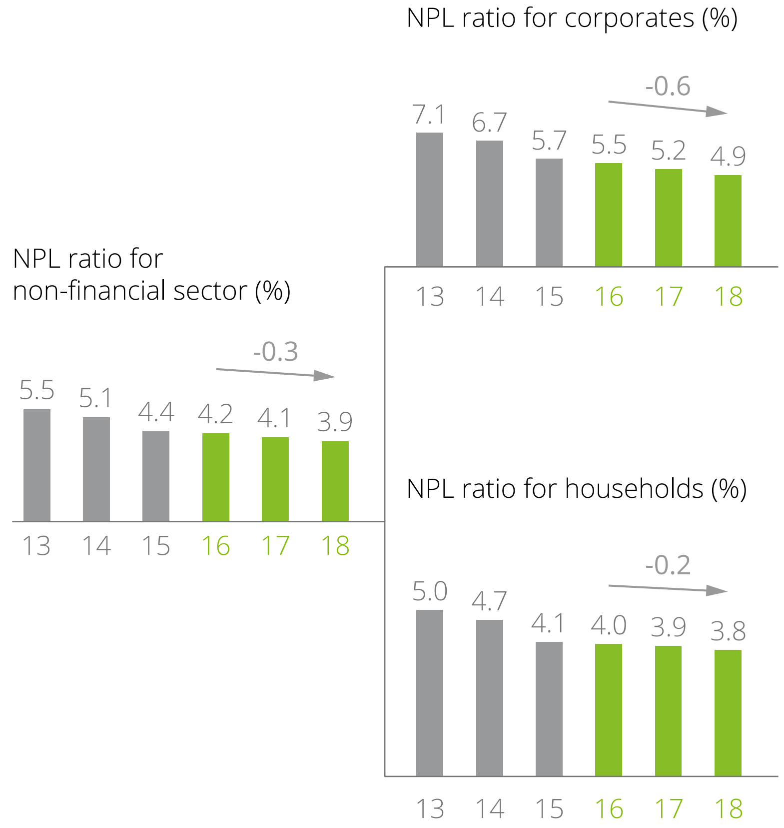
## Lowest NPL ratio in CE is expected to continue to decline

Asset quality is the best in CE and the Czech Republic's very low NPL ratio is expected to continue to decline. The drop in the overall NPL ratio from 5.1% to 4.4% in 2015 reflects positive developments in both the retail segment, down from 4.7% to 4.1% and in the corporate segment, down from 6.7% to 5.7%. The growing economy has been supportive for the financial standing of most companies (higher aggregate profit, few loss making companies) while households benefit from the improving labor market and low interest rates ease the burden of repayment. Consequently, default rates have declined over the past year and the outlook is for them to remain low. Also supported by steadily growing gross loan volumes (base effect), the NPL ratio is expected to continue decline over the next few years to below 4% in the retail segment and below 5% in the corporate segment.





## Asset quality of the banking sector



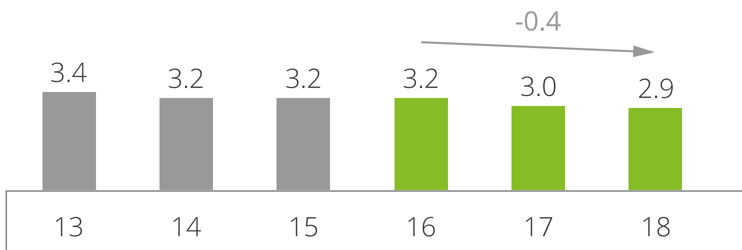
# Profitability

The Czech banking sector has the highest ROE in CE at 12.9% in 2015, but the outlook is for a gradual decline in 2017-18. There should be a slight increase in ROE in 2016, due to one-off gains on the Visa transaction[1], but profit ability should erode thereafter, with risk costs having bottomed out and low interest rates driving continued net interest margin pressure. Czech banks have faced margin pressure for the last several years and this trend will continue on the back of competition for loans and as bonds roll over onto lower rates. Thus, despite stronger loan growth, net interest income is not expected to rise. Net fee income has been declining in recent years and should fall again in 2016, with a cut in interchange rates, an ongoing trend to lower-fee or free current accounts, and new consumer loans being issued without servicing fees. As these headwinds diminish and volumes continue to rise, net fee income should slowly begin to rise by 2018. The cost/income ratio of banks is expected to gradually rise. Banks are progressively cutting branches but operating costs are expected to grow due to wage pressure and rising investment in digital channels. Risk costs were steady at 50bp of average gross loans in 2014-15 and the strong economy and improving labor market will continue to be supportive. However, this low level of risk costs is not expected to be sustainable so a moderate increase is anticipated by 2018.

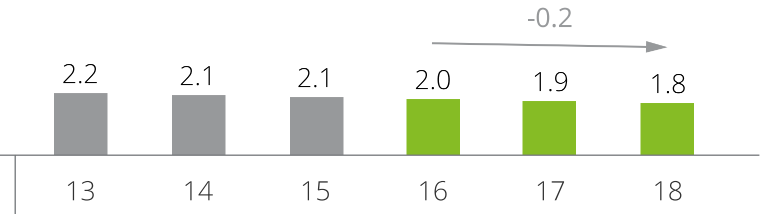
1 The acquisition by Visa Inc. of Visa Europe Ltd. (owned by its principal members) has generated significant capital gains for banks across Europe and CE in 2Q16.

## Banking sector profitability

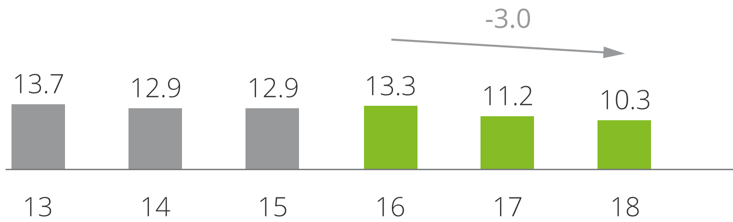
Net revenue/ Avg. assets (%)



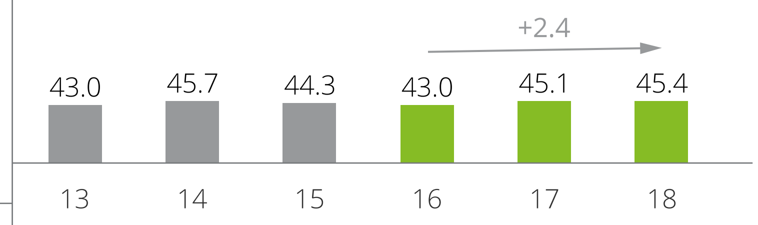

Net interest income/ Avg. assets (%)



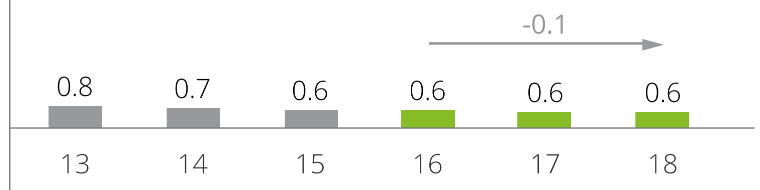

Return on equity (%)



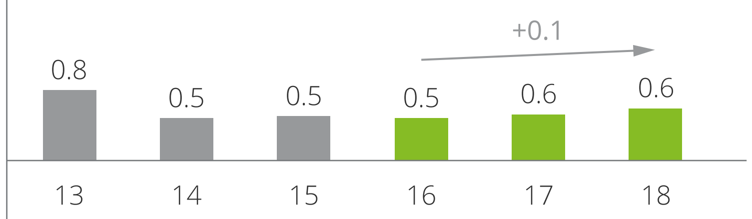

Cost/ Income (%)[2]



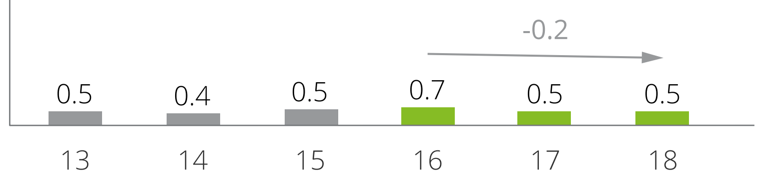

Net fees and commission income/ Avg assets (%)



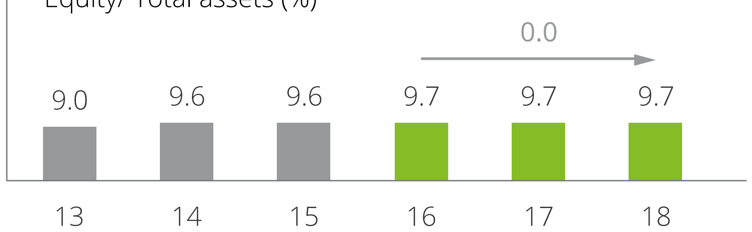

Cost of risk/ Avg. gross loans (%)[1]




Other income/ Avg. assets (%)




Equity/ Total assets (%)




[1] Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.
*Source: Czech National Bank, Deloitte Estimates*

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# Top 10 Banks

## ROE of the top 3 is better than for mid-tier players

The ROE of the Czech banking sector's top 3 banks (13.4%) is better than that of the next 5 mid-sized banks (11.0%) but the gap between these groups has closed in recent years. In 2013, the ROE of the top tier was nearly 2x that of the mid-tier banks. The main factor behind this trend has been the decline of risk costs in the sector, down from 44bp to 32bp for the top tier but down from 145bp to 61bp for mid-sized banks. Under such favorable conditions, and with the sector's ample customer deposits, competition for loans is intensifying.

The top 3 overall gained market share in lending over the past year, with CSOB (#2) and Komercni Banka (#3) outpacing Ceska Sporitelna (#1), while Raiffeisenbank (#5) and J&T Banka (#7) achieved the highest growth in the top 10 overall. Both of the smaller top 10 banks have been rapidly growing their number of customers, Sberbank (+44% y/y) and AirBank (+33% y/y). However, their profitability is relatively low and customer growth has not translated into market gains in lending over the past year.

## Main balance sheet items, CZK bn

| | Loans MS 2015 change | Loans (CZK bn) / Deposits (CZK bn) / Assets (CZK bn) | Deposits MS 2015 change | Assets MS 2015 change |
|---|---|---|---|---|
| **ČSOB²** | 20.5% -0.1pp | 1 040 | 20.0% -0.7pp | 19.0% +1.0pp |
| **Česká spořitelna** | 19.7% +0.1pp | 956 | 20.2% +0.7pp | 17.5% +0.5pp |
| **Komerční banka** | 19.7% +0.2pp | 891 | 18.7% -1.0pp | 16.3% -1.7pp |
| **UniCredit Bank¹** | 8.5% -0.3pp | 547 | 8.1% +0.7pp | 10.0% +0.9pp |
| **Raiffeisenbank** | 6.9% +0.2pp | 250 | 5.3% +0.4pp | 4.6% +0.2pp |
| **Moneta Money Bank** | 4.3% -0.2pp | | 3.1% +0.3pp | 2.6% -0.1pp |
| **J&T Banka** | 2.6% +0.1pp | 155 | 3.5% +0.4pp | 2.8% +0.3pp |
| **PPF Banka** | 1.0% 0.0pp | 104 | 1.7% -0.6pp | 1.9% -0.2pp |
| **Sberbank¹** | 1.9% -0.2pp | 76 | 1.6% +0.3pp | 1.4% +0.1pp |
| **Air Bank¹** | 1.0% 0.0pp | 77 | 2.0% +0.4pp | 1.4% +0.2pp |
| **Total Market (CZK bn)** | 2,782.377 | | 3,509.678 | 5,468.596 |

¹ Unconsolidated Statements
² Volumes and market share adjusted upwards to reflect 55% ownership of CMSS, which in 2015 had assets of CZK 153bn, deposits of CZK 142bn, and loans of CZK 127bn
*Source: Bankscope, Annual Reports, Central Bank, Deloitte estimates*

Retail
Corporate and others
Total volume/ breakdown not available
Assets (CZK bn)

## Top 10 bank profitability drivers 2013-15

1 Česká spořitelna
2 ČSOB
3 Komerční banka
4 UniCredit Bank
5 Raiffeisenbank
6 Moneta Money Bank
7 J&T Banka
8 PPF Banka
9 Sberbank
10 Air Bank

Net interest revenue (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 2.8 | 2.4 | 2.2 | 1.8 | 2.7 | 6.6 | 2.2 | 2.5 | 2.0 | 3.2 |

Net Revenues / Average Assets (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 4.2 | 3.6 | 3.3 | 2.8 | 4.1 | 8.5 | 3.0 | 3.0 | 2.7 | 3.5 |

Net fees and commision revenue (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 1.1 | 0.7 | 0.8 | 0.7 | 0.8 | 1.6 | 0.4 | 0.2 | 0.6 | 0.5 |

Cost to Income (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 47.2 | 47.2 | 51.8 | 49.2 | 53.4 | 45.7 | 50.1 | 26.2 | 81.8 | 54.6 |

Other revenues (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 0.3 | 0.5 | 0.3 | 0.4 | 0.7 | 0.3 | 0.5 | 0.3 | 0.1 | -0.2 |

ROE (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 12.6 | 15.9 | 12.2 | 8.7 | 11.5 | 12.8 | 11.6 | 17.4 | 0.3 | 5.5 |

Cost of risk (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 0.5 | 0.2 | 0.3 | 0.3 | 0.5 | 0.7 | 1.0 | 3.5 | 0.6 | 3.6 |

Equity / Assets (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 12.4 | 9.5 | 11.9 | 10.8 | 10.2 | 19.9 | 9.8 | 7.1 | 10.6 | 6.6 |

- Trend in 2013 - 2015
13.0% - 2015

*Source: Bankscope*

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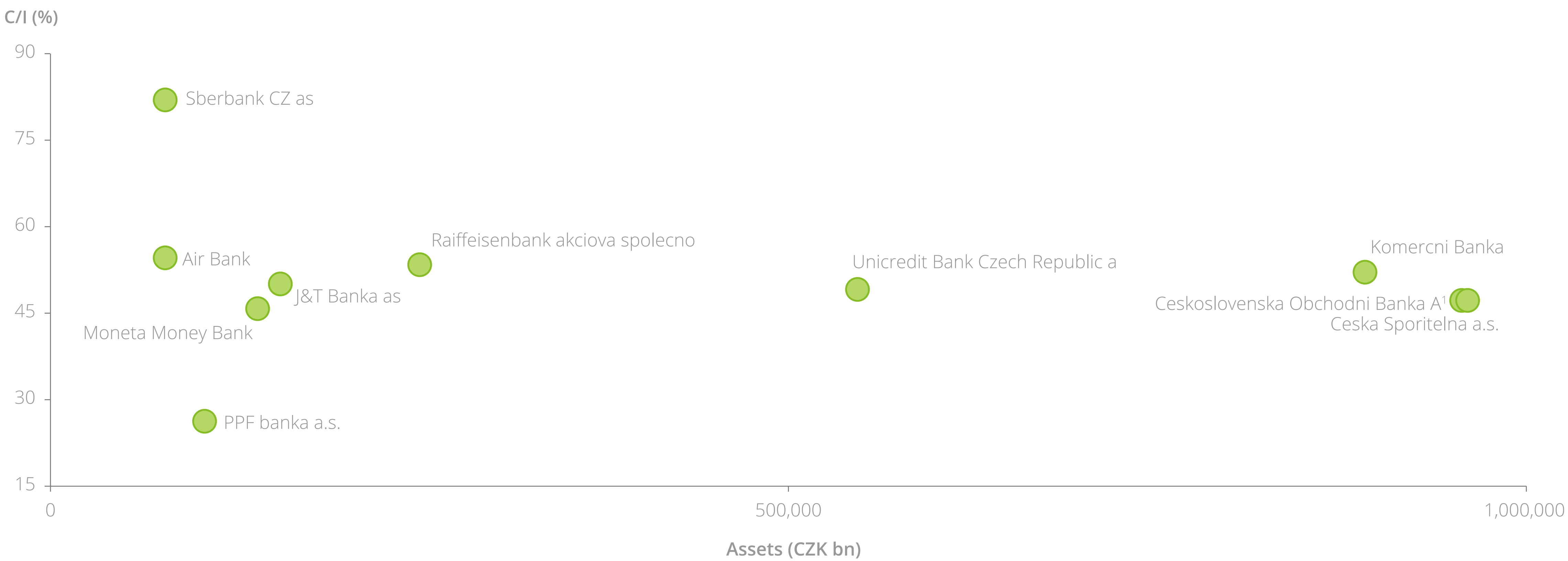
## C/I ratio versus assets[1], 2015




[1] Not including assets of 55% owned CMSS, which is accounted for as a joint venture

*Source: Bankscope*

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# Strategy

## Investment in digitalization is important to meet the demands of customers

Although the Czech banking sector is highly profitable and volume growth is robust, continued margin pressure due to the low interest rate environment will keep cost cutting on the agenda of many banks. At the same time, investment in digitalization to improve the functionality of on-line and mobile platforms is becoming increasingly important to meet the demands of customers. This will allow large banks to further trim their branch networks and reduce their cost to serve but the newer banks (e.g. Air Bank, Zuno) in the sector are finding it necessary to grow their branch numbers. The aim in each case will be to build a more effective omni-channel platform. Service levels and advisory should be adjusted to meet the needs and expectations of each customer segment. Due to margin erosion, smaller banks are likely to face increasing pressure to participate in consolidation or become more focused by exiting non-core business lines (e.g. sale of Citibank's retail business to RBI, potential sale of Zuno by RBI).

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# Digital Maturity

The Czech Republic ranks third in terms of digital banking maturity in CE (based on the overall score of its 5 biggest banks), positioned right behind Poland and Slovakia. In terms of individual players, however, the best Czech bank is ranked 10th, with a considerable gap to digital leaders. Such results are mainly caused by poor digitalization of the mobile channel (5th place in CE) as internet banking functionalities are not far behind leading solutions. From a Customer Journey perspective, the digital functionalities responsible for customer acquisition are the most digitally mature (similar to most CE countries). What is unique for the Czech Republic is the fact that banks are offering advanced cross-selling functionalities ("expand relationship" step), whereas transactional banking features are only in line with CE average. Cash loans is the most digitalized product in the Czech Republic, although digitalization of mortgages is also much higher than in the other analyzed countries.

*If you want to know detailed data for digital banking benchmarking, contact us.*

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# Key Insights

**Loans are approaching a turning point after years of decline.** Portfolio cleaning and repayments will offset new business in 2016 but transactions are picking up and loan growth should return to positive growth in 2017.

**Asset quality is improving with support of portfolio sales.** In 2015, the NPL ratio dropped from 13.8% to 9.6% in the corporate segment, driven largely by a NPL sale from MKB to the Resolution Asset Manager, and from 19.0% to 17.6% in the retail segment.

**Hungary is reducing its bank levy in 2016-18.** The scheduled reduction of the bank levy from HUF 133bn in 2015 to HUF 60bn in 2016 and HUF 40bn in 2017 will have a positive impact on the sector ROE of 2-3 pp.

**ROE is expected to rebound (to 12%) in 2016,** on a reduction of the bank levy and very low risk costs, before falling back to 5-6% in 2017-18 as risk costs normalize. A need for efficiency gains will remain, with cost/income (>65%) and low interest rates bringing margin pressure.

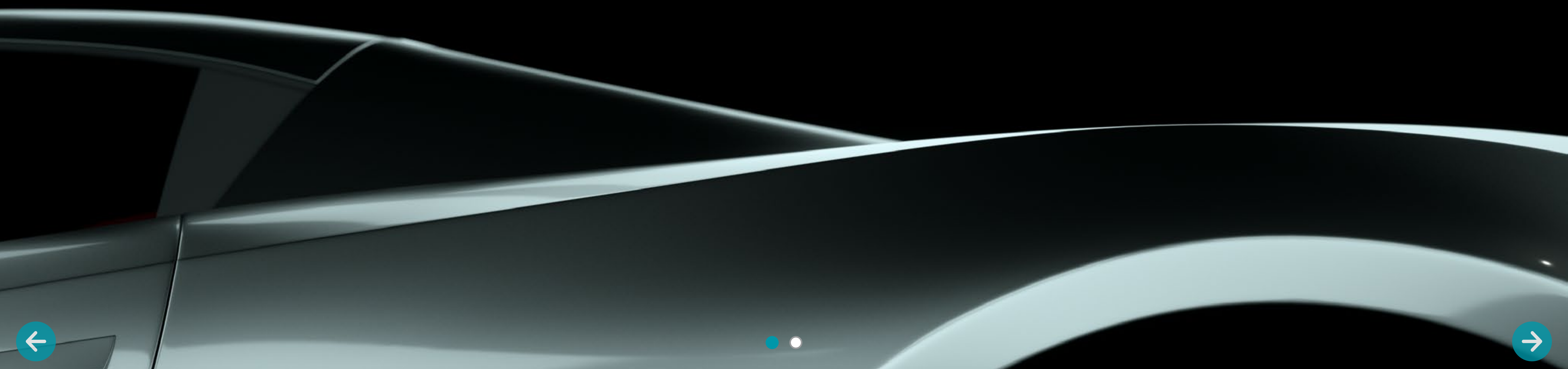


# Economy

## Economic growth remains robust on the back of rising private consumption

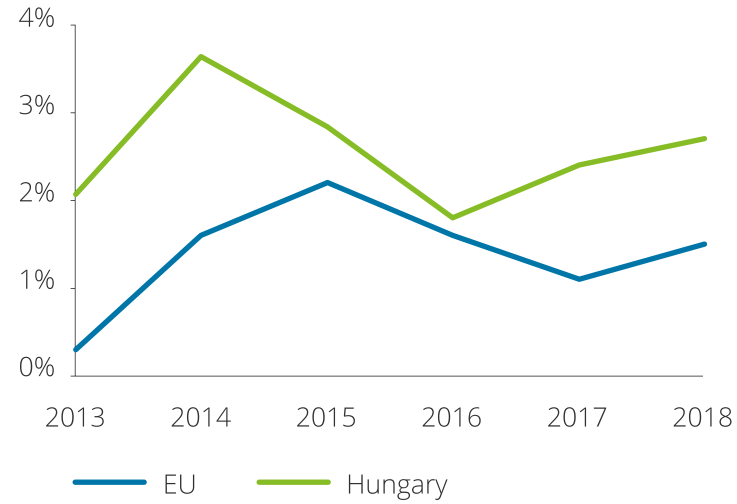
Although Hungary's economic growth remains robust on the back of rising private consumption, it has lost momentum in 2015 and 2016 due to a slowdown in investment. While growth is expected to remain below the CE average at 2.3-2.7% in 2017-18, the pace of growth should improve as investment recovers. A pick up in investment growth over the next year should be supported by both improved EU funds absorption and private sector investment. The economic recovery in Hungary has been creditless so far but lending is at turning point. The clean-up of the banking sector balance sheet has progressed, while borrowing is encouraged by interest rates at record lows and government programs. Household spending is expected to remain strong. Household balance sheets have benefited from FX debt relief, while consumption is supported by an improving labor market (falling unemployment), growing disposable income growing wages, low inflation, and low interest rates.



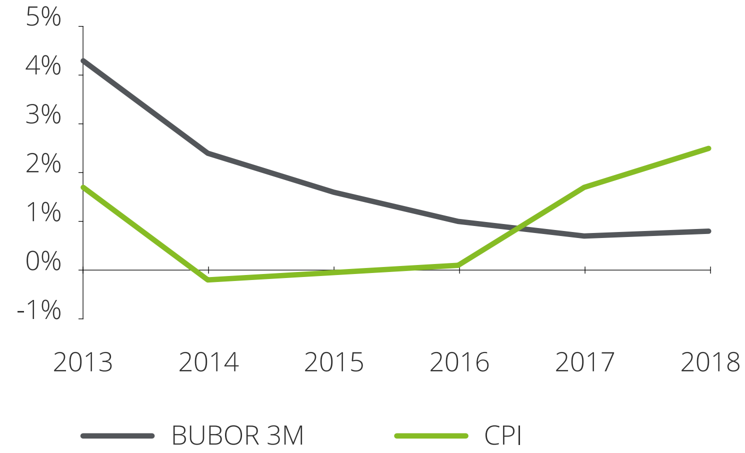


## Real GDP growth

*(yoy%)*

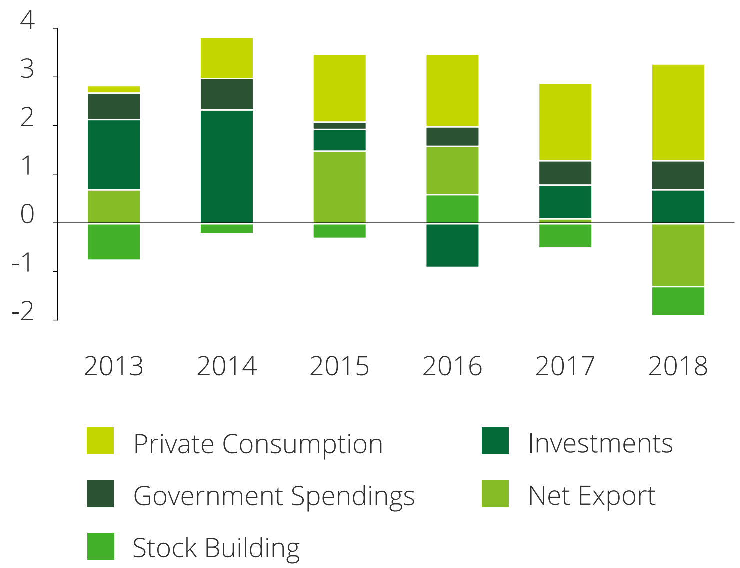



## Interbank interest rate and CPI

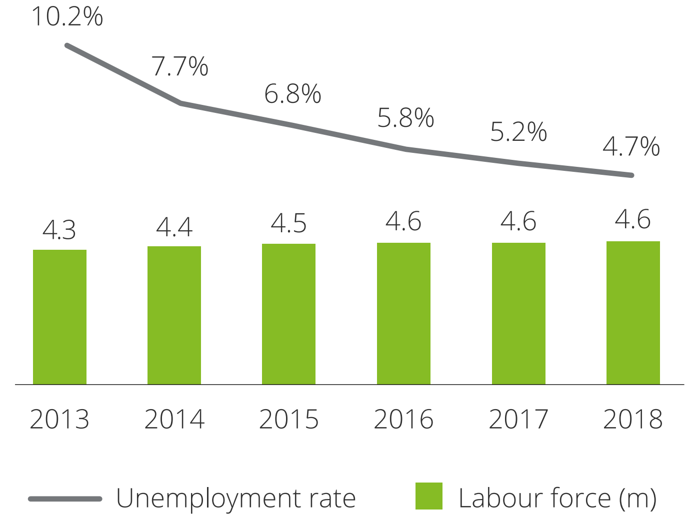



## Real GDP drivers

*(change as a percentage of real GDP)*




## Labour market




*Source: Economist Intelligence Unit*
*Source for interest rate and CPI chart: Economist Intelligence Unit, Bloomberg, Deloitte estimates*

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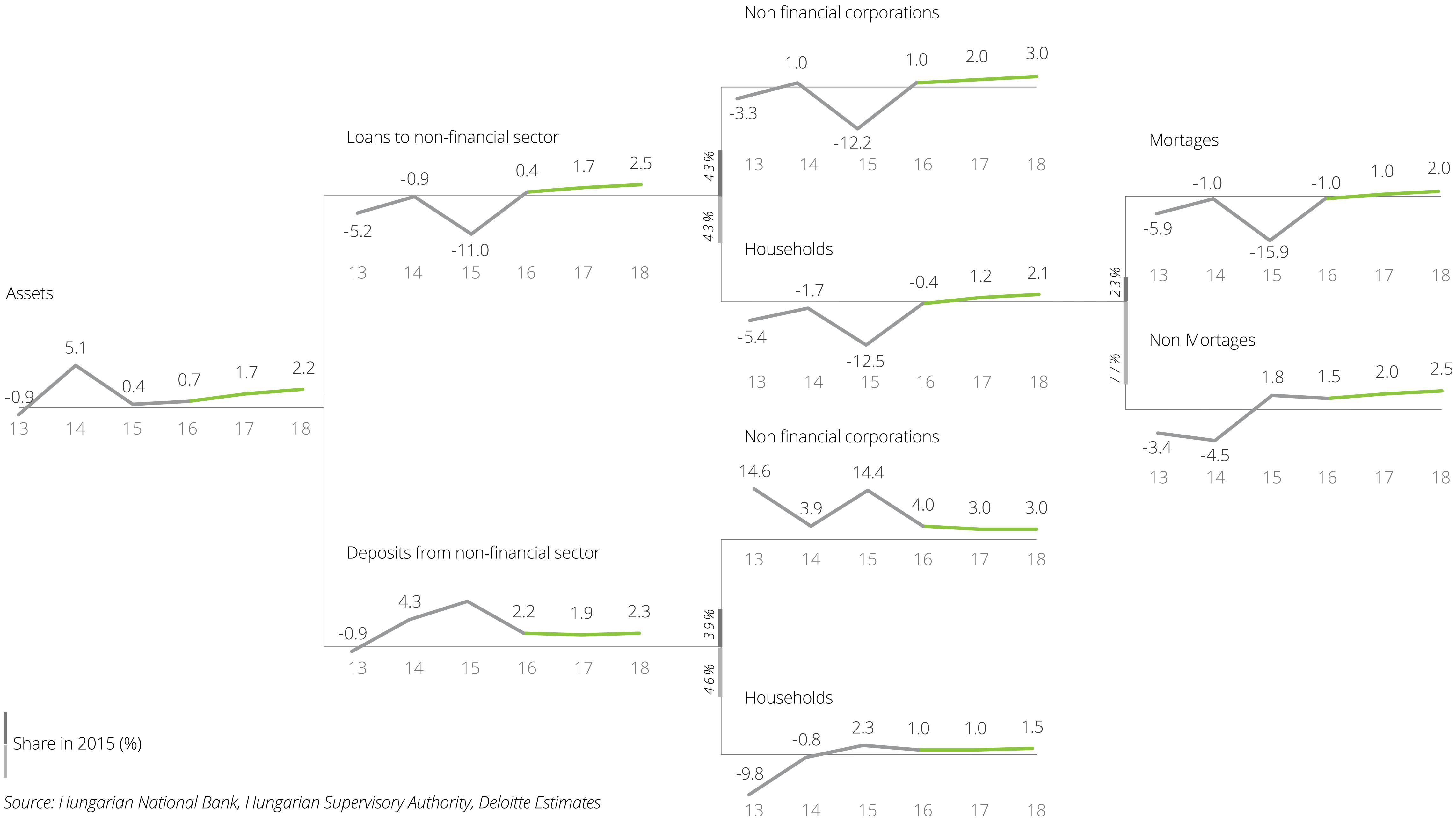
# Balance Sheet

## Loans are approaching a turning point after years of decline

After declining sharply in recent years, loans in Hungary are approaching a turning point. Loans should remain flat in 2016 and grow moderately in 2017-18. The sharp decline in mortgages by 16% y/y in 2015 was mainly due to FX debt relief but repayment of principal has also more than offset new mortgage issuance over the past year. Mortgages are expected to decline by 1% y/y in 2016 before rising new business volumes, aided by a VAT decrease on new homes and extended family housing allowances, turn the tide in 2017. After returning to positive growth of 1.8% y/y in 2015, consumer loans should continue to rise at a moderate pace, propelled by growing household spending. The steep fall in corporate loans by 12% y/y in 2015 was affected by portfolio cleaning and this will continue to weigh on stock volumes. However, with help from the MNB's market-based lending scheme, corporate loans should rise in 2016 and gain pace in 2017-18. The pace of deposit growth is expected to slow, from 7.4% y/y in 2015, to a level of 1-2% per annum in 2016-18. Corporate deposits can be volatile due to large transactions but a greater part of their cash should be invested while households will continue to prefer alternative investments (e.g. mutual funds, retail government bonds) in a low interest rate environment. Banks are nonetheless well funded with loans/deposits of 90% and a strong tier 1 CAR of 16.6% in 2015.

## Banking sector balance sheet drivers
(yoy growth %)




*Source: Hungarian National Bank, Hungarian Supervisory Authority, Deloitte Estimates*

# Asset Quality

## Asset quality is improving with the support of portfolio sales

The clean-up of the banking sector balance sheet is an ongoing process that has accelerated over the past year. While the favorable economic environment and improving labor market is limiting defaults, portfolio cleaning is a major factor. Following the downtrend of recent years, the corporate NPL ratio dropped from 13.8% in 2014 to 9.6% in 2015, helped by portfolio sales and particularly by a large transfer of NPLs from MKB to the National Resolution Asset Manager. There will be further support in 2016 from a new central bank vehicle (MARK) that will buy NPLs from banks at market prices. The corporate NPL ratio is expected to drop to 7% in 2016 and then fall further towards 6% in 2018. Less progress has been made on retail NPLs but they are also trending lower. Helped by FX debt settlements and portfolio sales, the retail NPL ratio finally fell from 19.0% in 2014 to 17.6% in 2015. A large majority of NPLs are mortgages and the market should benefit from the end of the eviction moratorium, permitting creditors to execute collateral. Retail NPLs are expected to fall to 16.5% in 2016 and to 14% by 2018.

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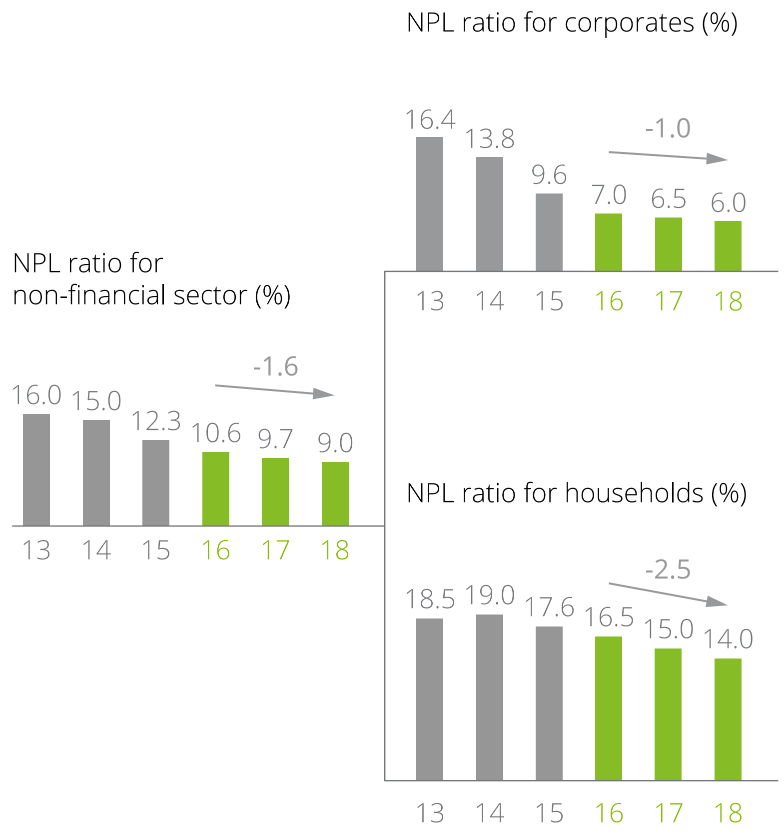
## Asset quality of the banking sector

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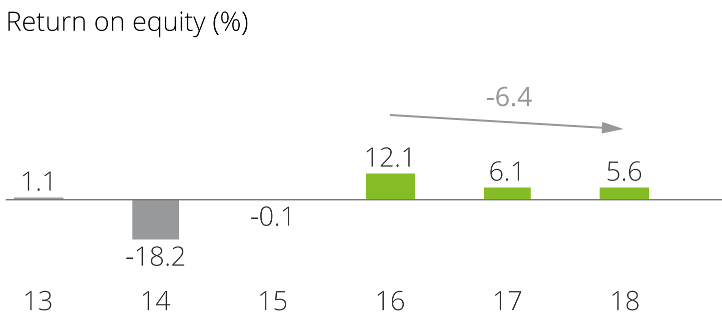
# Profitability


The Hungarian banking sector is set for an earnings recovery in 2016, helped by a sharp reduction in risk costs and a reduction of the bank levy. After a huge loss in 2014 due to costs of FX mortgage relief and returning to break even in 2015, the ROE of Hungarian banks is expected to rise to 12% in 2016 before falling back to a level of 5-6% in 2017-18. A reduction of the bank levy from HUF 133bn in 2015 to HUF 60bn in 2016 and HUF 40bn in 2017 will lift the sector ROE by 2-3 pp. As asset quality in Hungary improves and as loan portfolios are cleaned, there have been provision releases that have lowered risk costs[1] in 2015 and this has continued in 2016. Risk costs are expected to drop to 20bp of average gross loans in 2016 before climbing back to 70-80bp in 2017-18. Net fee income is expected to grow at a steady pace (2-3%) but net interest income will be relatively weak, as low interest rates and increasing competition for loans drives margin erosion. Hence, banks will continue to cut branches and staff to contain cost growth (< 1%), while facing wage pressure and higher rents and investments in digitalization. Cost/income should decline over 2016-18 (helped by the reduction of the bank levy[2]) but will remain very high (>65%).

1 Risk costs on an underlying basis declined from an estimated 155bp in 2014 to 70bp in 2015. The headline cost of risk of 560bp in 2014 followed by a -346bp in 2015 reflected an accounting change, where provisions created for FX debt relief in 2014 were rebooked in 2015 as extraordinary losses.

2 Hungary's bank levy, which is included in net other operating income, is expected to fall from HUF 133bn in 2015 to HUF 40bn in 2017. It's negative impact on cost/income should thereby fall from 12 p.p. to 3 p.p..

## Banking sector profitability[3]





[1] Cost of risk for 2015 excludes the reversal of provisions booked as extraordinary losses
[2] Hungarian bank levy adds 3.0-12.0 p.p to cost/income
[3] Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.

*Source: Hungarian National Bank, Hungarian Supervisory*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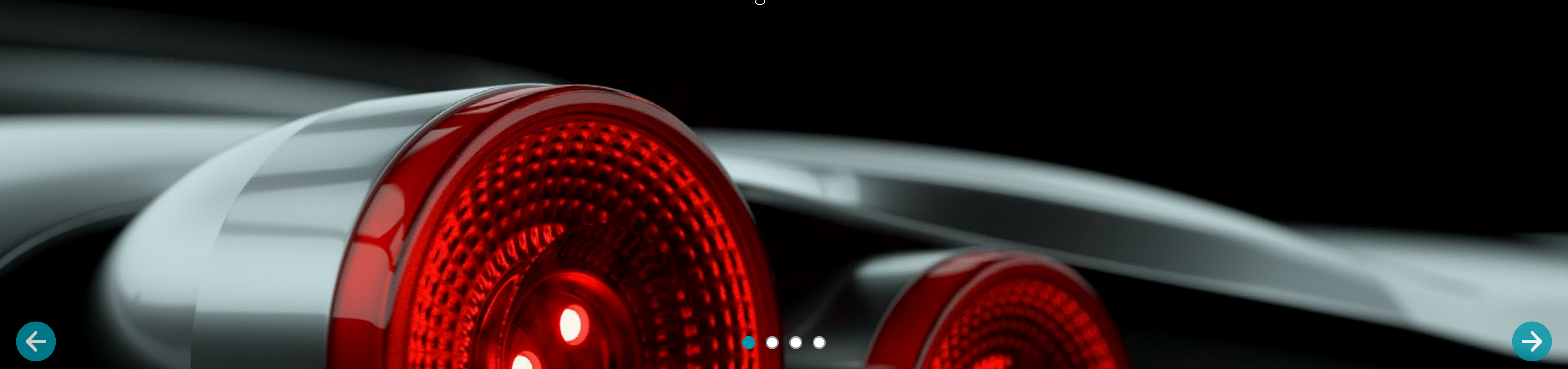
# Top 10 Banks

## Despite the steep decline in the sector, UniCredit (#2) grew its loan book in 2015

Against the backdrop of a steep decline of loans in the banking sector, only corporate-oriented UniCredit (#2) managed to grow its loan book in 2015, while K&H (#3) and Budapest Bank (#8) also gained market share. Retail oriented OTP Bank (#1) lost share in lending but still outperformed much of the sector thanks to its leadership in new mortgage origination and increasing share in the corporate segment. These four banks also lead the sector in ROE and, in general, have been less distracted by the process of balance sheet restructuring.

The banks that lost market share in lending last year performed better in deposits and thereby most (Raiffeisen, MKB, Erste, CIB, Sberbank) have now succeeded in bringing loans/deposits ratios below 100%. This better positions these banks to start growing again. These banks have also typically been loss-making in recent years and, with the exception of Raiffeisen (which booked a profit in 2015), still face the challenge of returning to profitability in 2016.





## Main balance sheet items, HUF tn

| | Loans MS 2015 change | Loans (HUF tn) Deposits (HUF tn) | Deposits MS 2015 change | Assets MS 2015 change |
|---|---|---|---|---|
| **OTP Bank[1]** | 17.5% -0.4pp | 6.8 | 29.4% -1.5pp | 20.6% -1.2pp |
| **K&H Bank** | 8.7% +0.2pp | 2.6 | 10.8% +0.5pp | 7.9% +0.4pp |
| **UniCredit** | 8.2% +1.1pp | 2.7 | 9.9% +1.4pp | 8.2% +1.4pp |
| **Raiffeisen Bank** | 7.9% -1.7pp | 2.0 | 8.5% -0.8pp | 6.0% -0.4pp |
| **MKB Bank** | 7.0% -2.3pp | 2.0 | 9.0% -0.1pp | 5.9% 0.0pp |
| **Erste Bank** | 8.2% -0.8pp | 1.9 | 8.3% -0.5pp | 5.9% 0.1pp |
| **CIB Bank** | 8.0% -0.7pp | 1.7 | 7.7% -0.1pp | 5.1% -0.2pp |
| **Budapest Bank** | 4.7% 0.1pp | 1.0 | 4.3% +0.2pp | 2.9% +0.2pp |
| **FHB Mortgage Bank** | 2.8% -0.2pp | 0.7 | 2.2% +0.1pp | 2.3% -0.1pp |
| **Sberbank Magyarorszagi** | 1.4% -0.4pp | 0.4 | 1.5% -0.3pp | 1.2% -0.2pp |
| **Total Market[2] (HUF tn)** | 13.719 | | 15.274 | 32.886 |

[1] Based on OTP Core
[2] Non-financial sector loans and deposits
*Source: Bankscope, Annual Reports, Central Bank, Deloitte estimates*

Retail
Corporate and others
Total volume/ breakdown not available
Assets (HUF tn)

## Top 10 bank profitability drivers 2013-15

1 OTP Bank
2 K&H Bank
3 UniCredit
4 Raiffeisen Bank
5 MKB Bank
6 Erste Bank
7 CIB Bank
8 Budapest Bank
9 FHB Mortgage Bank
10 Sberbank Magyarorszagi

Net interest revenue (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 5.1 | 2.9 | 2.6 | 1.9 | 2.2 | 3.3 | 1.7 | 4.6 | 1.9 | 2.0 |

Net Revenues / Average Assets (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 7.8 | 6.5 | 5.0 | 4.2 | 4.9 | 6.0 | 3.5 | 15.6 | 1.6 | 6.1 |

Net fees and commision revenue (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 2.0 | 2.1 | 1.6 | 1.6 | 1.4 | 2.2 | 1.6 | 2.6 | 0.9 | 0.8 |

Cost to Income (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 55.1 | 53.2 | 51.1 | 102.7 | 87.9 | 74.2 | 90.0 | 87.3 | 157.5 | 105.6 |

Other revenues (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 0.7 | 1.4 | 0.8 | 0.7 | 1.4 | 0.5 | 0.1 | 8.4 | -1.3 | 3.3 |

ROE (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 5.1 | 18.9 | 16.4 | 8.0 | -51.5 | -13.0 | -24.2 | 12.7 | -10.7 | -28.8 |

Cost of risk (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 4.8 | 0.9 | 0.9 | -0.5 | 3.3 | 3.5 | 3.0 | -0.3 | 0.2 | 1.2 |

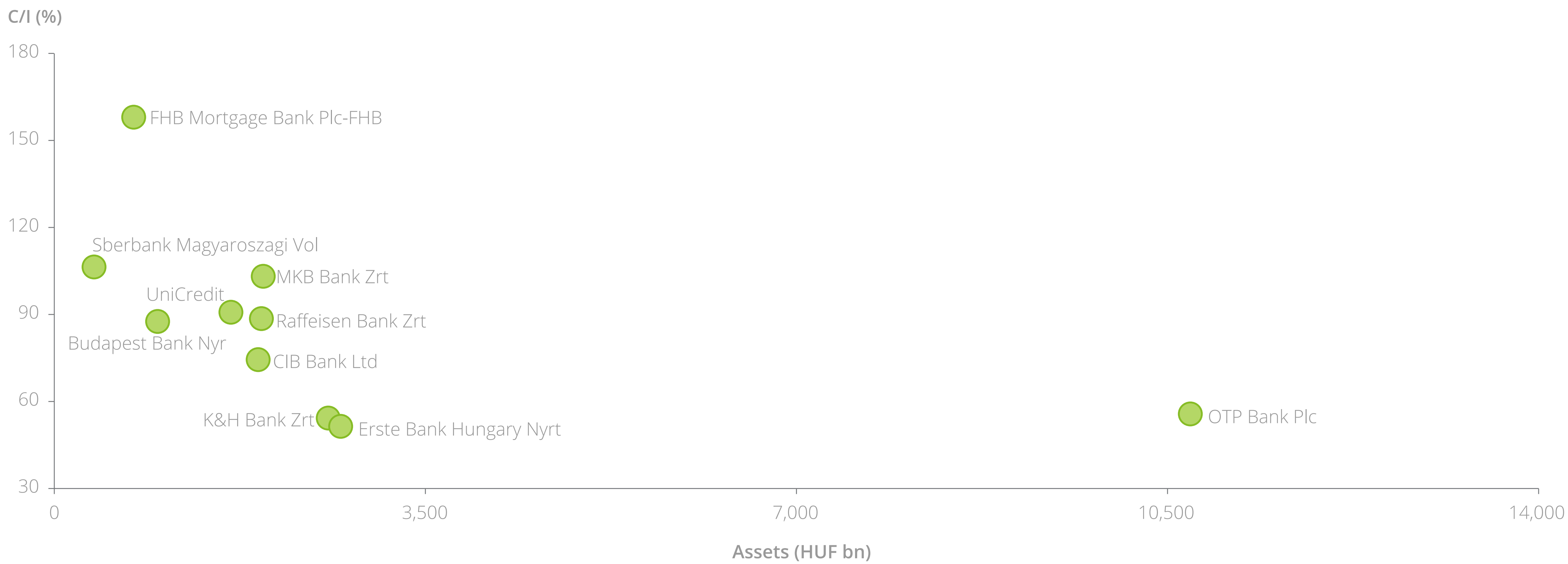
Equity / Assets (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 11.5 | 8.6 | 9.2 | 8.0 | 5.5 | 8.3 | 8.8 | 12.2 | 10.3 | 8.5 |

- Trend in 2013 - 2015
13.0% - 2015

*Source: Bankscope*

## C/I ratio versus assets, 2015




Based on OTP Consolidated

*Source: Bankscope*

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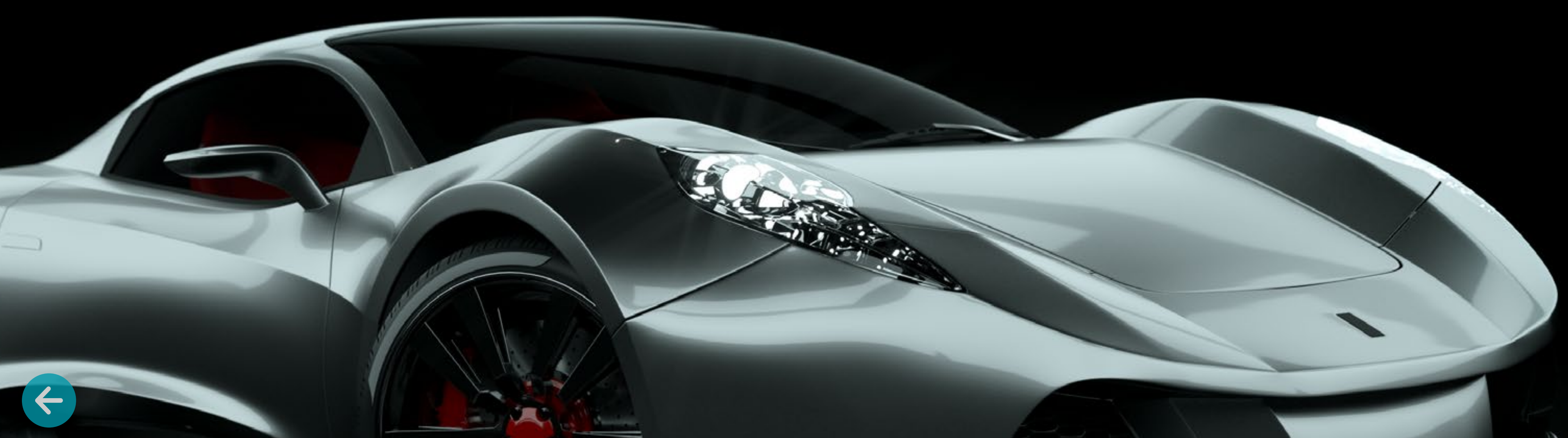
# Strategy

## A drive for efficiency will lead to further consolidation

Industry consolidation will continue over the next few years, as banks face ongoing pressure to raise efficiency. Budapest Bank is scheduled to be sold by the state and one or more foreign banks could exit or partially exit (disposal of business line) Hungary. Banks are redefining operations that are a part of their core business, capable of generating acceptable returns, and will continue to sell non-core and non-performing assets and portfolios. Hungarian banks have already greatly reduced branches (-15% y/y in 2015) and further cuts are ahead, as banks will increasingly invest in digital sales channels. Digital banking itself will be an area of competition, with some banks ahead of the curve in on-line and mobile functionality and others lagging behind due to legacy issues. However, the main focus of competition in the next few years should be on lending, intensifying as volumes increase. Banks will compete on price to acquire customers but will need to simultaneously emphasize improving customer experience to improve retention.





Hungary

# Digital Maturity

Hungary ranks 7th out of the 8 CE countries we analyzed in terms of digital maturity (based on the overall score of its 5 biggest banks) and is followed only by Slovenia. Markets often have a better position in one of the channels but Hungary ranks similarly in both internet and mobile functionalities. The best Hungarian bank is ranked 21st out of the 76 banks we analyzed. As in many other countries, the Customer Journey perspective reveals that the digital functionalities responsible for information gathering and customer onboarding are the most digitalized. However, Hungary is below the CE average in both of these areas. Mutual funds and term deposits are the most digitalized products but Hungary ranks below the CE average in 10 out of 13 product areas.

*If you want to know detailed data for digital banking benchmarking, contact us.*

# Contact

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# Key Insights

**Loan growth will lose momentum in 2016.**
After relatively strong loan growth of 6-7% in 2014-15, moderation is expected to 4-5% in 2016, due to postponed investment in the corporate sector and tighter credit standards in the retail segment.

**NPL ratio is falling as portfolio sales have grown to new highs**
(PLN 16bn in 2015). The NPL ratio of Polish banks has been steadily declining in the last 3 years to reach 7.6% in 2015 and this trend should continue.

**Consolidation continues.**
The merger of the two banks propelled Bank BGZ BNP Paribas to #8 in 2015, while Alior Bank's acquisition of the core of Bank BPH will bring it into the top 10 in 2016 and RBI has announced plans to sell Raiffeisen Polbank.

**FX debt conversion is a key risk.**
The regulator's plan to encourage voluntary conversion of FX mortgages by increasing the risk-weight may not be effective. This could lead to a new law forcing conversion at below-market rates in 2017-18.

**ROE will remain under pressure from bank levy and regulatory costs**
Banks face a recurring bank levy (a tax 0.366% monthly on assets > PLN 4bn) and the one-off cost of FX spread refunds (to mortgage borrowers), expected to have a combined impact of ~60% of pre-tax profit in 2017.

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# Economy

Poland's economic growth in recent years has consistently outpaced the CE average.

Poland's economic growth in recent years has consistently outpaced the CE average and this trend should continue in 2016-18. Domestic demand has been and will remain the key driver. Private consumption has been accelerating and the outlook is for robust growth, buoyed by an improving labor market (falling unemployment, rising wages), government transfers (500+ child benefits), and record low interest rates. Consumer confidence has been rising and is nearing pre-crisis 2007-8 levels.

Investment in Poland should continue to grow relatively fast (in a CE comparison). The pace of investment has slowed over the past year, in part due to a transition period for EU funding. Business confidence is also down from 2014-15 levels, with companies facing uncertainty about external environment and tax/legal environment. However, investment is expected to pick up as capacity utilization is relatively high and companies can benefit from low interest rates.

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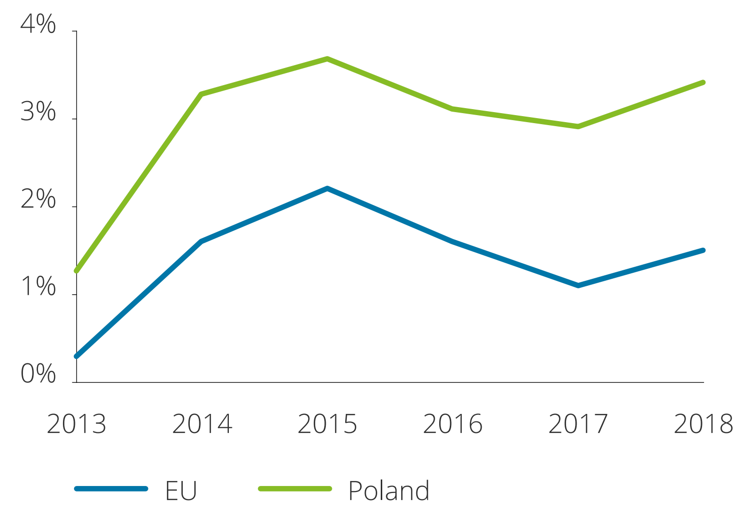
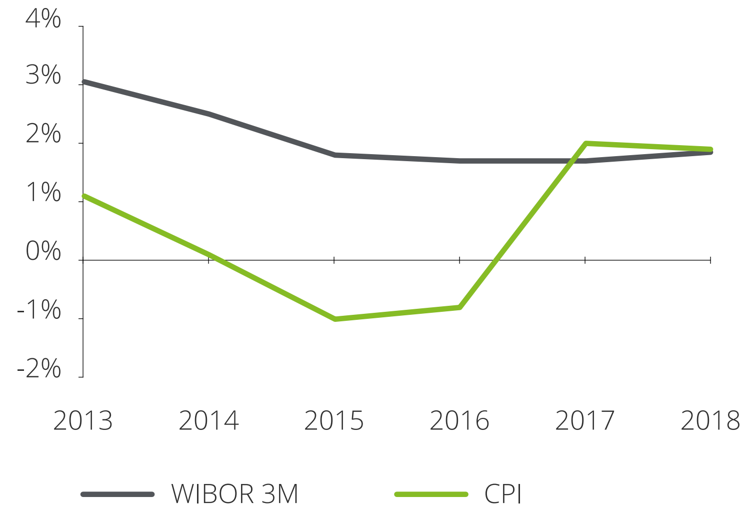
## Real GDP growth

*(yoy%)*

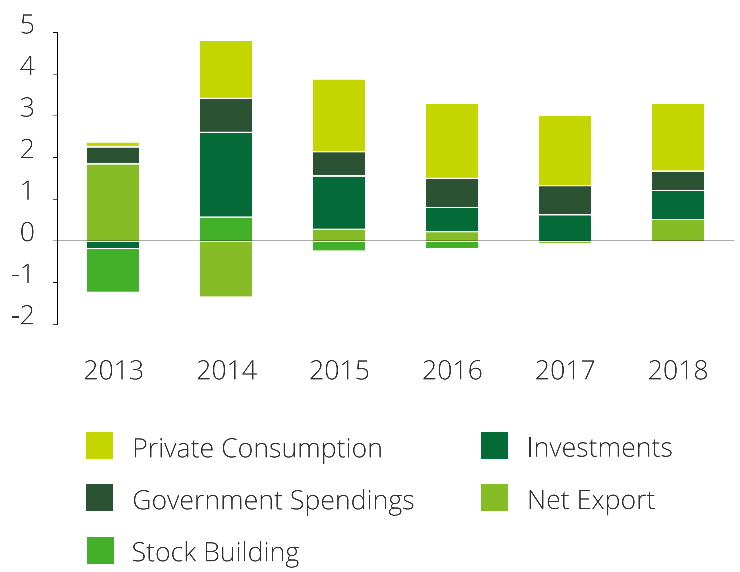



## Interbank interest rate and CPI

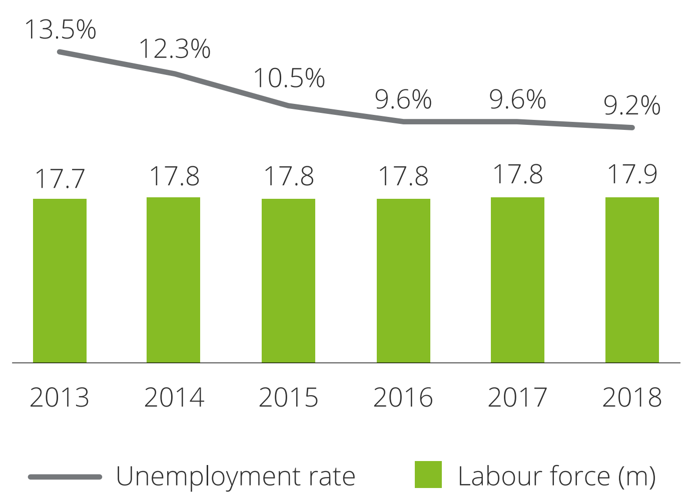



## Real GDP drivers

*(change as a percentage of real GDP)*




## Labour market




*Source: Economist Intelligence Unit*
*Source for interest rate and CPI chart: Economist Intelligence Unit, Bloomberg, Deloitte estimates*

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# Balance Sheet



## Following relatively strong loan growth of 6-7% in 2014-15, Poland is facing a slowdown in 2016.

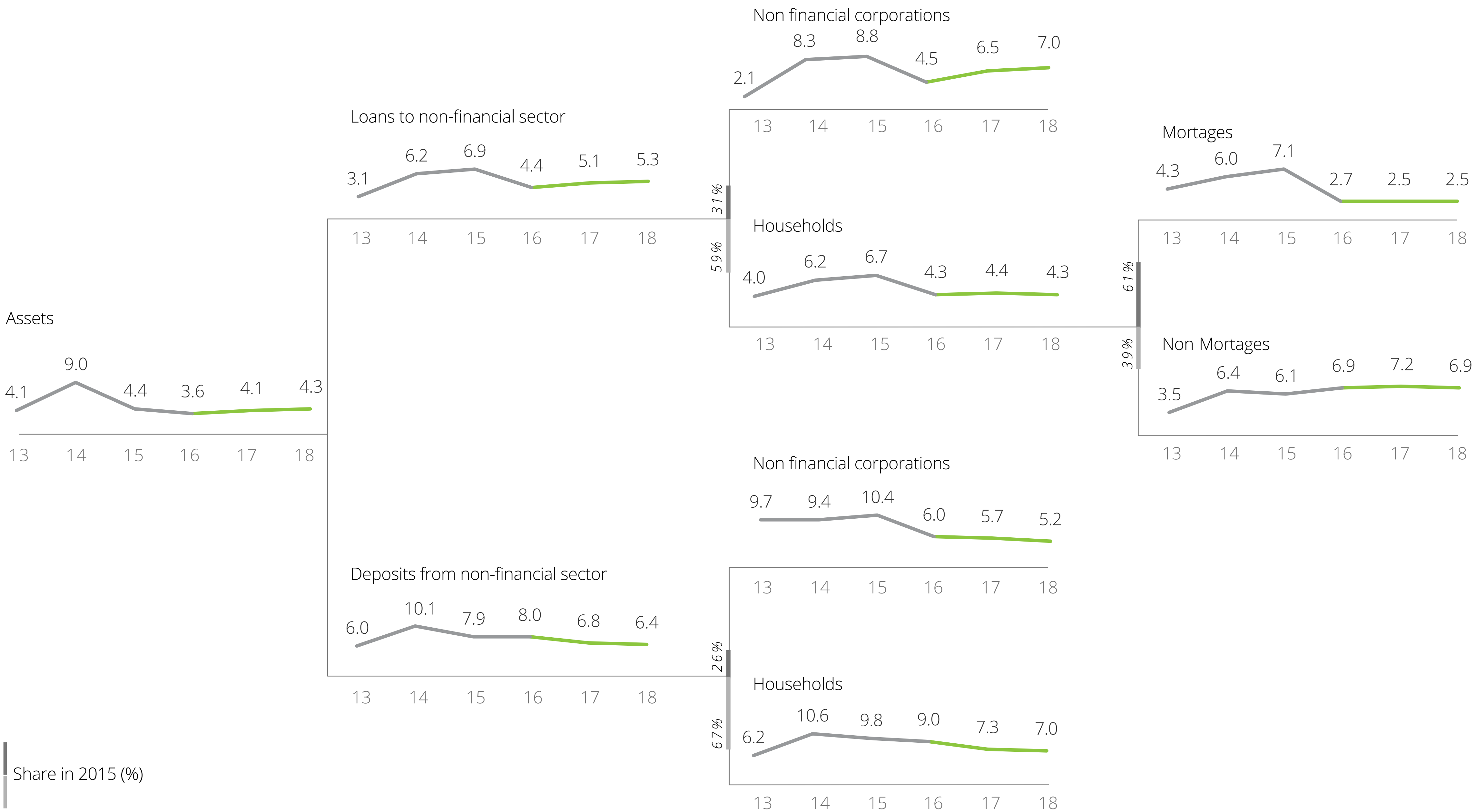
Following relatively strong loan growth of 6-7% in 2014-15, Poland is facing a slowdown in 2016. Corporate loan growth is expected to ease from 9% last year to 4-5% in 2016. While low interest rates support investment, some decisions may be postponed due to uncertainty and the bank levy (asset tax) is expected to lead to more large companies borrowing abroad. Mortgage loan growth was 7% in 2015, lifted by PLN depreciation, and is expected to slow to 2-3% in 2016, as the amortization of principal of FX mortgages, which are not growing, offsets much of the growth of PLN mortgages.

While credit demand from households will be encouraged by low interest rates, the improving labor market, and government transfers (500+ child benefits), supply of PLN mortgages will be curbed by the tightening of the maximum LTV by the regulator and other credit worthiness checks by banks. Tightening by banks vis-a-vis mortgages is to be expected, as the profitability of this low margin product is particularly affected by the new asset tax. In contrast, banks are targeting increased sales of high-margin consumer loans, which are expected to accelerate to a growth rate of ~7% in 2016.

Deposit growth has been very robust and is expected to remain at 8% in 2016, before slowing moderately as households shift to alternative investments and corporates utilize cash reserves. Nonetheless, the level of loans/deposits is trending gradually downwards towards 100%.

The sector is well capitalized, with a tier 1 ratio of 15.2% at year-end 2015 but faces the prospect of the regulator ratcheting up risk weights on FX mortgages in the coming year, to encourage banks to cut deals with borrowers to convert the mortgages to local currency at below market interest rates. This may limit growth at some of the banks more exposed to FX-mortgages.

## Banking sector balance sheet drivers (yoy growth %)




*Source: NBP, PFSA, Deloitte Estimates*

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# Asset Quality

The NPL ratio of Polish banks has been steadily declining in the last 3 years to reach 7.6% in 2015 and this trend should continue.

The NPL ratio of Polish banks has been steadily declining in the last 3 years to reach 7.6% in 2015 and this trend should continue. Low interest rates, the strong economy, and the improving labor market should all contribute to low default rates, while banks' sale of NPLs is reaching new highs (PLN 16bn in 2015). A large majority (>75%) of NPLs sold in Poland are consumer loans but there has been a steady flow of corporate NPLs and the market has begun to open mortgage NPLs as well in 2014-15. The decline of corporate NPL ratio accelerated last year, dropping from 11.3% in 2014 to 10.3% in 2015 and it could drop to as low as 8% by 2018, helped by the improving financial standing of companies. The retail NPL ratio decline has been more gradual, from 6.5% in 2014 to 6.2% in 2015, as a function of the mortgage NPL ratio, falling from 3.1% to 2.8%, and the consumer NPL ratio, falling from 12.5% to 12.4%. A continued gradual decline of the retail NPL ratio is anticipated towards 5.5% by 2018.

## Asset quality of the banking sector


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# Profitability

The ROE of the Polish banking sector fell sharply from 10.0% in 2014 to 6.8% in 2015 and, while one-off gains will provide some respite in 2016, it is expected to fall to back to 3-4% in 2017 before it can improve back to 8% in 2018 on a more sustainable basis. The sharp decline in 2015 was driven in large part by one-off costs, including PLN 2bn of additional deposit guarantee payments after the bankruptcy of SK Bank and PLN 600m of payments towards the setup of a borrower support fund. However, banks also faced margin pressure due to falling interest rates and lower fee income after the reduction of interchange rates. In 2016, banks will book one-off gains from the Visa transaction (c. PLN 2bn) but they will also suffer a recurring bank levy (a tax 0.366% monthly on assets > PLN 4bn) that will cost the sector over PLN 3bn in its first year. Next year, banks are expected to face a further one-off cost of FX spread refunds (to mortgage borrowers) of PLN 9.3bn[1]. While an earnings rebound in 2018 would be expected in the absence of one-off costs, there is a high level of uncertainty over the costs that will voluntarily (under regulatory pressure) be borne by banks in relation to FX mortgage conversion.

On an underlying basis, excluding one-offs effects and the bank levy, a rising trend in operating profitability of banks is expected in 2015-18. An easing of competitive pressure should permit a moderate improvement in the net interest margin over the period. A slight decline in net fee income is expected in 2016, affected by slower sales of investment and insurance, but there should be an increase in 2017-18. Supported by a further reduction of branches and staff, banks should manage to keep operating costs flat in 2016-18. While risk costs have been stable in recent years (~90bp of average gross loans in 2013-15), Poland's healthy economy and labor market should support a moderate decline in 2016-18.

1 While the President has estimated the cost of the FX spread refund at up to PLN 4bn, estimates from the NBP and KNF indicate the cost could reach PLN 8.0-9.3bn if the terms are not changed.

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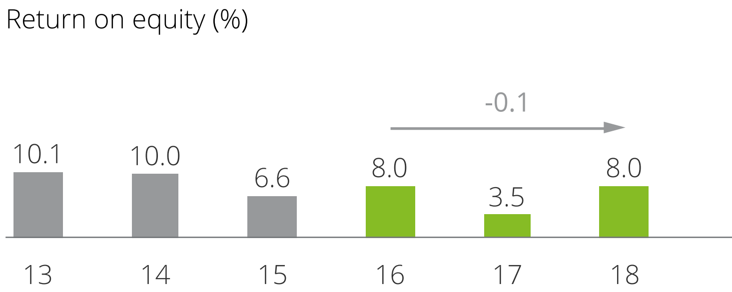
# Banking sector profitability[3]

## Banking sector profitability





[1] Poland's bank levy introduced in March 2016 adds 5.7 p.p to cost/income in 2016 and 7.5 p.p in 2017. The expected cost of a refund of the FX spread on FX mortgages (included in net other operating income) is expected to add an additional 3.4 p.p. in 2017.
[2] Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.

*Source: NBP, PFSA, Deloitte Estimates*

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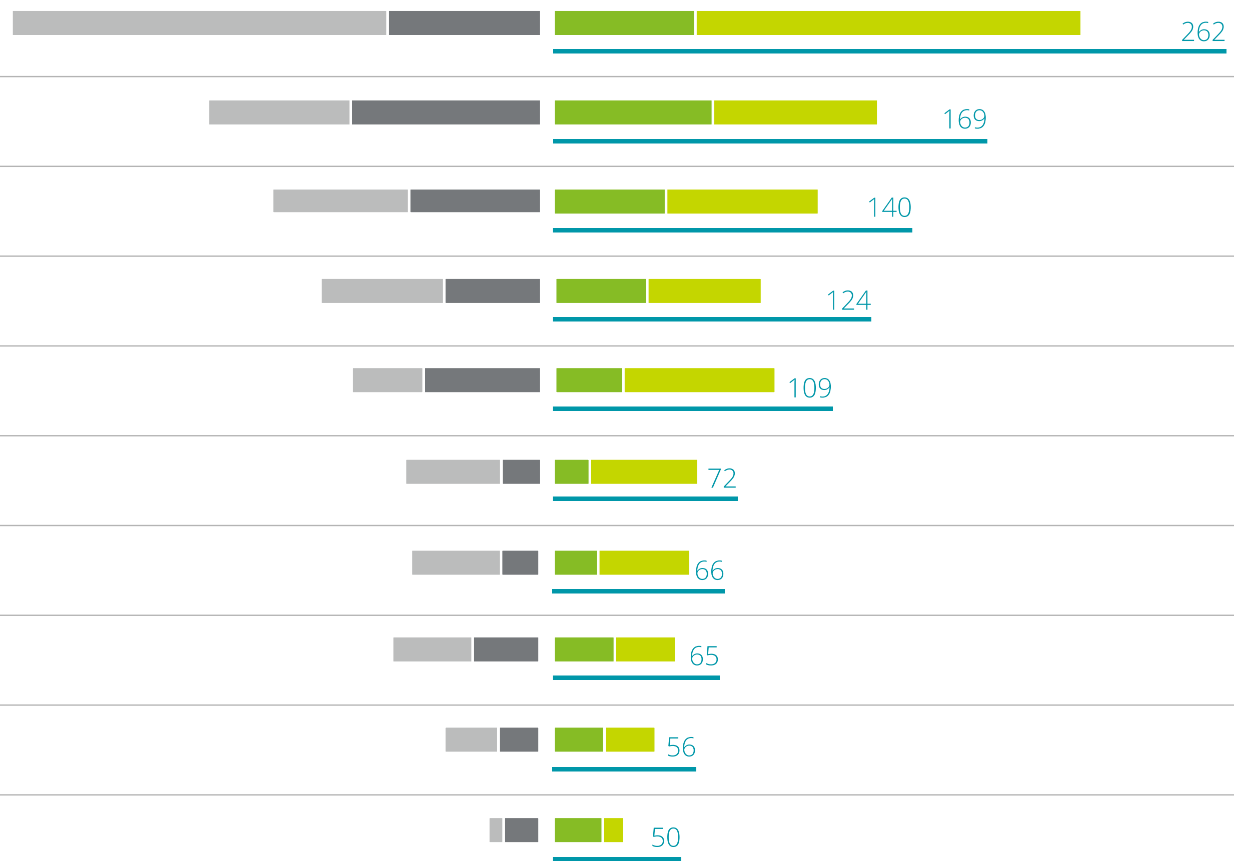
# Top 10 Banks

At the top of the sector, the loan market share of PKO BP has been relatively stable.

At the top of the sector, the loan market share of PKO BP has been relatively stable with a gain in the corporate segment offsetting slower growth in retail. The banks that gained the most overall market share in lending last year, ING BSK (#5) and BZ WBK (#2), outpaced the sector in both corporate and retail segments. Many of the banks that have lost market share in lending (mBank #4, GNB #6 and Bank Millennium #7, Raiffeisen Polbank #9) have a relatively high share of FX mortgages. These banks were more successful gathering deposits, leaving only Raiffeisen Polbank (109%) with a loans/deposits ratio above 100%. Current accounts remain a focal point for competition and Bank Millennium and Raiffeisen Polbank were among the winners in this segment, along with ING Bank and Alior Bank. Consolidation continues to play a role in shaping the top 10 banks. The merger of the two banks has propelled Bank BGZ BNP Paribas to #8 in 2015, while Alior Bank, with the acquisition of the core of Bank BPH expected to be completed in 4Q16, should break into the top 10 in 2016. RBI has announced plans to sell Raiffeisen Polbank. The introduction of the bank levy (asset tax) will promote further consolidation in the Polish banking sector as economies of scale help the top 5 banks achieve an above average ROA (1.0-1.9% versus a sector average of 0.7%).

## Main balance sheet items, PLN bn

| | Loans MS 2015 change | Loans (PLN bn) / Deposits (PLN bn) – Assets (PLN bn) | Deposits MS 2015 change | Assets MS 2015 change |
|---|---|---|---|---|
| **PKO Bank Polski[1]** | 18.6% -0.1pp | 262 | 20.4% +0.1pp | 16.4% +0.5pp |
| **Bank Pekao** | 11.8% -0.1pp | 169 | 12.6% -0.6pp | 10.5% -0.4pp |
| **BZ WBK** | 9.5% +0.3p | 140 | 10.3% -0.1pp | 8.7% 0.0pp |
| **mBank** | 7.7% -0.1pp | 124 | 8.2% +0.3pp | 7.7% 0.0pp |
| **ING BS** | 6.6% +0.7pp | 109 | 8.7% +0.6pp | 6.8% +0.3pp |
| **Getin Noble Bank[1]** | 4.8% -0.2pp | 72 | 5.7% -0.2pp | 4.5% +0.1pp |
| **Bank Millenium** | 4.5% -0.1pp | 66 | 5.3% +0.1pp | 4.1% +0.2pp |
| **Bank BGZ BNP Paribas** | 5.2% +2.1pp | 65 | 4.7% +1.1pp | 4.1% +1.4pp |
| **Raiffeisen Polbank[1]** | 3.4% -0.3pp | 56 | 3.9% +0.2pp | 3.5% 0.0pp |
| **Bank Handlowy** | 1.9% +0.1pp | 50 | 2.8% -0.1pp | 3.1% -0.2pp |
| **Total Market (PLN bn)** | 1,057.186 | | 987.186 | 1,599.986 |



Retail
Corporate and others
Total volume/ breakdown not available
Assets (PLN bn)

[1] Based on unconsolidated statements

*Source: Bankscope, Annual Reports, Central Bank, Deloitte estimates*

## Top 10 bank profitability drivers 2013-15

1 PKO Bank Polski
2 Bank Pekao
3 BZ WBK
4 mBank
5 ING BŚ
6 Getin Noble Bank
7 Bank Millenium
8 Bank BGŻ BNP Paribas
9 Raiffeisen Polbank
10 Bank Handlowy

Net interest revenue (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 2.7 | 2.5 | 3.2 | 2.1 | 2.4 | 1.7 | 2.2 | 2.7 | 1.8 | 2.0 |

Net Revenues / Average Assets (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 4.1 | 4.3 | 5.1 | 3.2 | 3.6 | 2.2 | 3.5 | 4.0 | 2.9 | 4.1 |

Net fees and commision revenue (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 1.1 | 1.2 | 1.4 | 0.7 | 1.0 | 0.5 | 0.9 | 0.8 | 1.0 | 1.3 |

Cost to Income (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 57.0 | 53.6 | 50.8 | 50.3 | 57.1 | 60.3 | 58.5 | 83.6 | 77.9 | 62.3 |

Other revenues (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 0.3 | 0.6 | 0.5 | 0.3 | 0.2 | 0.0 | 0.4 | 0.5 | 0.1 | 0.9 |

ROE (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 9.0 | 9.7 | 13.1 | 11.2 | 10.7 | 1.1 | 9.0 | 0.3 | 3.0 | 8.8 |

Cost of risk (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 0.7 | 0.4 | 0.8 | 0.6 | 0.3 | 0.8 | 0.5 | 0.7 | 0.4 | -0.1 |

Equity / Assets (%)

| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| 11.3 | 13.9 | 14.7 | 9.9 | 9.8 | 7.3 | 9.7 | 9.6 | 10.3 | 13.8 |

- Trend in 2013 - 2015
13.0% - 2015

*Source: Bankscope*

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## C/I ratio versus assets[1], 2015


[1] Based on consolidated financial statements

*Source: Bankscope*

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# Strategy

While the advantage conveyed by economies of scale will continue to encourage consolidation.

With profitability under pressure from increased regulation (limiting fees, increased deposit insurance), the bank levy, lower interest rates, and growing competition from fintech companies, it is essential that Polish banks improve efficiency. While the advantage conveyed by economies of scale will continue to encourage consolidation, competition will also intensify as mid-tier banks target stronger market positions. Growth strategies are being orientated around the concept of being a main bank for customers rather than a product champion. In addition to growth by acquiring new clients, banks will increasingly aim to activate their existing clients (to improve cross-selling). Successful banks will use data analytics to better know their customers and add value via advisory, while taking advantage of direct channels to improve customer experience. Customers are increasingly banking on-line and using mobile devices, while the gradual adjustment of service models towards digital channels is reflected in a declining number of bank branches (-5% between 2013 and 2015). Banks will need to continue to use digitalization to improve processes, reduce cost to serve, and increase efficiency.

Poland

# Digital Maturity

Poland is the digital leader among CE countries, both from the perspective of the overall position of the 5 biggest banks in terms of assets (first place), as well as on the level of particular banking institutions (3 out of the top 5 digital leaders in CE are from Poland). Not surprisingly, the features of the internet channel are the most developed in this country, although the advantage over Slovakia in the mobile channel is minimal. From a Customer Journey perspective, the digital functionalities responsible for customer acquisition and transactional banking are the most digitally mature (similar to most other CE countries). However, Poland performs better than other countries in the area of potential cross-sell possibilities, measured in the step "expanding relationship". This is especially reflected in products like cash loans and overdrafts, which are the most digitalized products, with some players already offering end-to-end automation, even in the mobile channel.

*If you want to know detailed data for digital banking benchmarking, contact us.*

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# Key Insights

**The fastest growing economy in CE in 2016-18** is expected to be driven by private consumption, fueled by higher disposable income (higher wages, lower VAT), with steady investment.

**Loan growth turned positive in 2015 and should accelerate in 2016-18,** despite a slowdown in housing loans, as accelerated economic growth and lower NPL sales drive a recovery of corporate and consumer lending.

**The NPL ratio declined sharply from 20.7% in 2015 to 11.3% in 1H16** but further improvement is expected to be more gradual. NPL recognition may increase, as the sector prepares for AQR in 2017.

**A new CHF loan conversion law[5] could generate losses for banks** estimated by the central bank at RON 2.4bn, including RON 1.7bn in excess of current provisioning.

**ROE soared from -12.9% in 2014 to 11.8% in 2015 but is set to fall.** ROE is expected to be cut to 7% in 2016 by CHF loan conversion losses and limited to 8-9% in 2017-18 by margin pressure.

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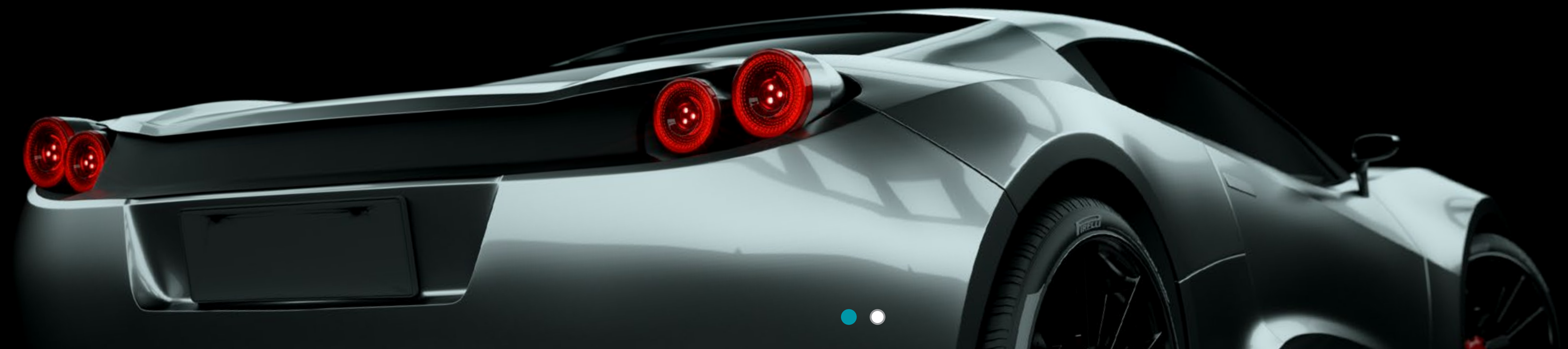
# Economy

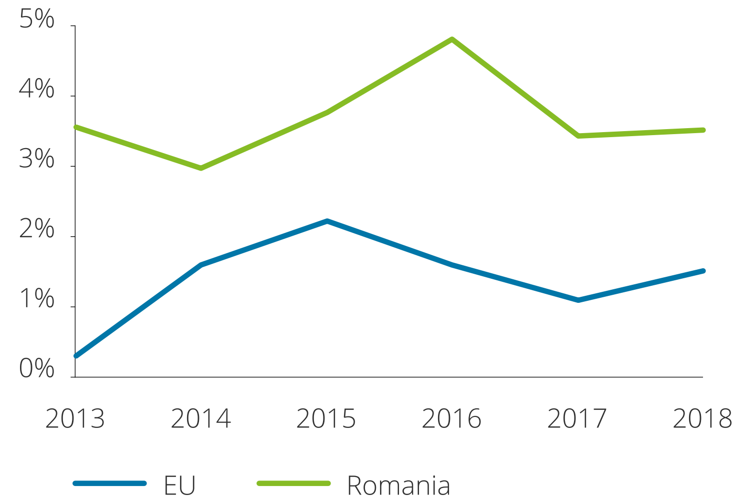
## The fastest growing economy in CE in 2016-18

Romania is expected to have the fastest growing economy in the CE region in 2016-18. Following an acceleration to 3.8% in 2015, Romania's GDP growth is expected to rise again to a minimum of 4.5% in 2016 before moderating to 3.3% in 2017-18. The key driver of this expansion has been an acceleration of private consumption growth in recent years to the highest level in CE. This has been fueled by rising household disposable income, on the back of fast real wage growth, a higher minimum wage, and VAT cuts, while consumer confidence has returned to near 2007-8 pre-crisis levels. This has come despite a relatively stagnant labor market. Unemployment in Romania was flat in 2015, in contrast to the improvement seen across other CE countries, and the outlook for decline in 2016-18 is relatively modest. Investment picked up in 2015 and should make a stable contribution to GDP in the next few years, helped by improving EU funds absorption under the new programming period. Net exports are expected to continue their negative contribution to GDP growth in 2016-18, mainly reflecting the impact of strong domestic demand on imports.

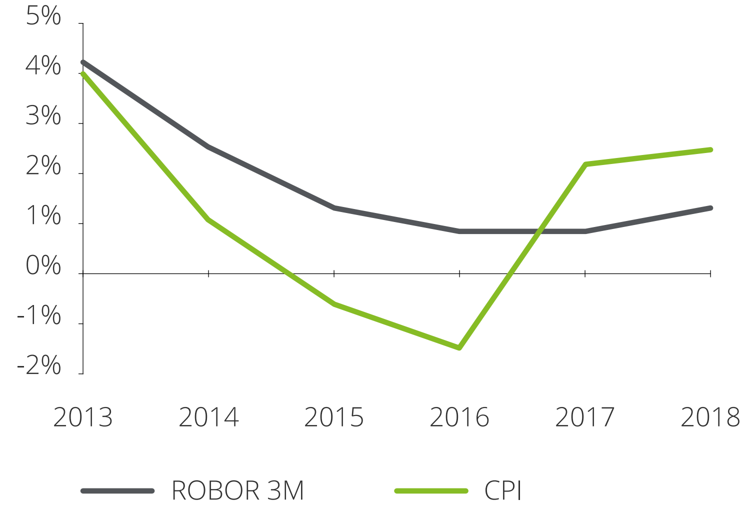




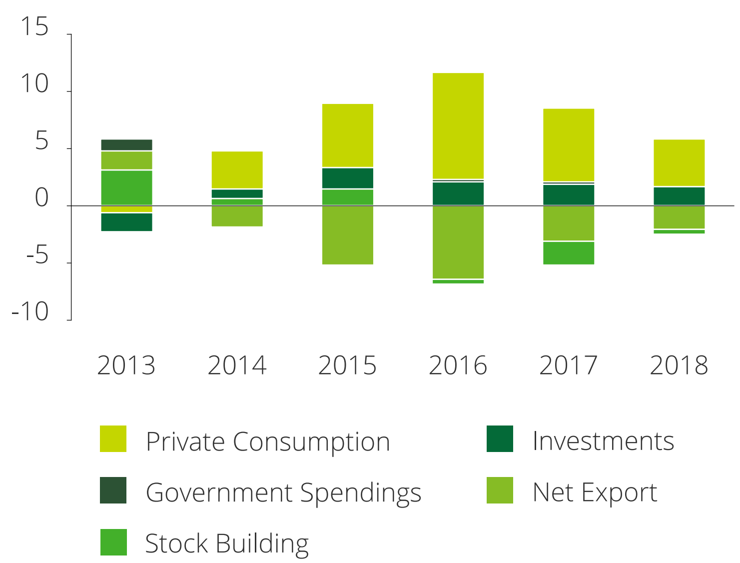
## Real GDP growth
*(yoy%)*



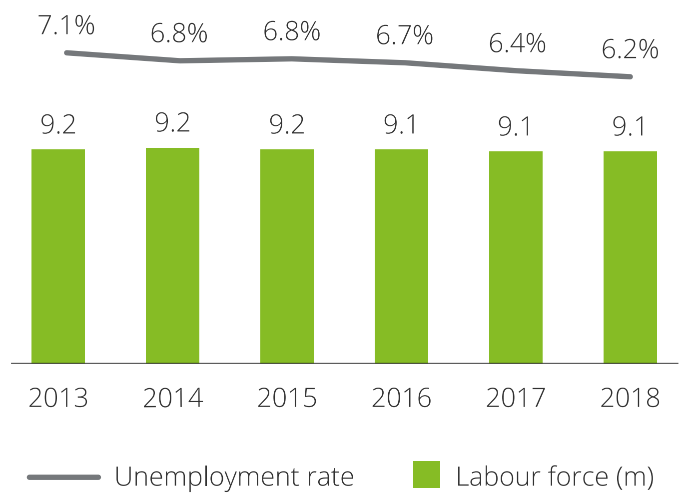

## Interbank interest rate and CPI




## Real GDP drivers
*(change as a percentage of real GDP)*




## Labour market




*Source: Economist Intelligence Unit*
*Source for interest rate and CPI chart: Economist Intelligence Unit, Bloomberg, Deloitte estimates*

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# Balance Sheet

## Loan growth turned positive in 2015 and should accelerate

Loan growth turned positive in 2015 and should accelerate in 2016-18, as robust economic growth drives a recovery of corporate and consumer lending. The recovery last year was led by housing loans (+16.5% y/y in 2015), supported by government guarantee program First Home. However, housing loans now face a slowdown (2015-18E CAGR of 6%), as Romania's new law on debt discharge[1] (walk away) has driven banks to increase down payment requirements, while the First Home program may also be redesigned on less favorable terms. Consumer loan growth, impacted by NPL sales, was negative last year (-2.6% y/y in 2015) but should turn positive in 2016 and accelerate to 4-5% in 2017-18, supported by rising household spending. Balance sheet cleaning is particularly weighing on corporate loans (-0.6% y/y in 2015) but a return to positive growth in 2016 and improvement to 2-4% in 2017-18 is expected as low interest rates encourage investment. The banking sector is well capitalized (tier 1 CAR of 16.7% in 2015) and its funding structure has improved. On the back of strong non-financial deposit growth (2012-15 CAGR of 9%), the sector's domestic gross loans/deposits ratio fell to 92% in 2015. Deposit growth is expected to moderate (2015-18E CAGR of 6%), on low interest rates and as companies increase utilization of cash reserves for investment, but loans/deposits should remain on a downward trend through 2018.

1 The law on debt discharge (from April 2016) permits mortgage borrowers (up to EUR 250k, excluding First Home program) to settle their loan commitments by turning over the title of the mortgaged property to banks.

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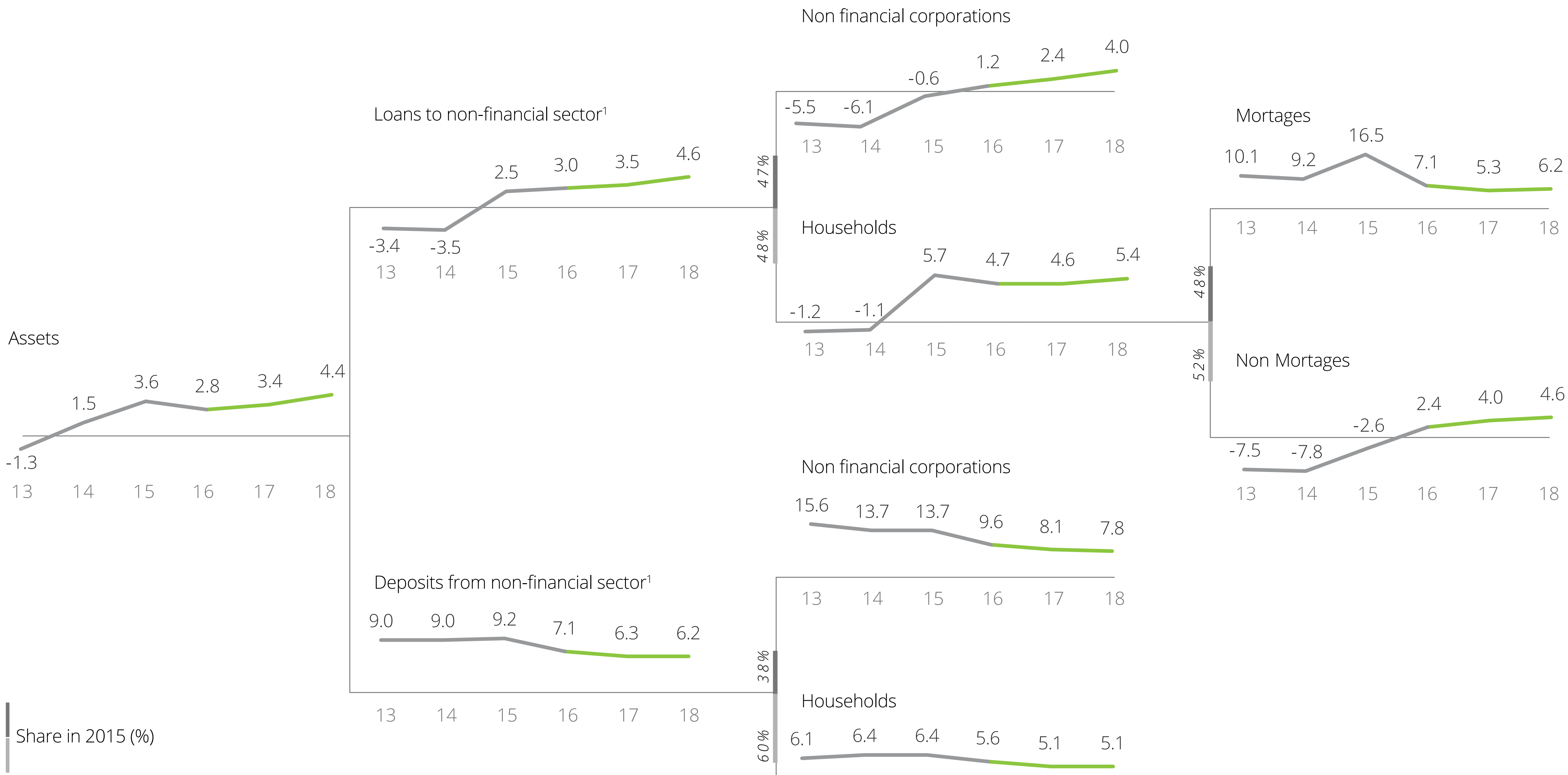
## Banking sector balance sheet drivers[2]

*(yoy growth %)*




[1] Categories including domestic loans/deposits only
[2] Assets of the banking sector was prepared based on ECB statistics about banking sector. Loans and Deposits breakdown was from monetary stastistics reporting statements.

*Source: The National Bank of Romania, Deloitte Estimates*

# Asset Quality

## NPL ratio has fallen sharply but further improvement will be more gradual

After a sharp decline in the total NPL ratio[2] of the banking sector over the past year, further improvement is expected to be gradual. The total NPL ratio declined from 20.7% in 2014 to 13.5% in 2015 and further to 11.3% in 1H16. While the decline last year was supported by substantial balance sheet cleaning (a net reduction of RON 1bn in retail and corporate NPLs), it was also influenced by a one-off base effect (~3 p.p.)[3], which may partially unwind. While balance sheet cleaning will continue, an offset is expected over the coming year from increased NPL recognition, as the banking sector expects an asset quality review (AQR) in 2017. Hence, the total NPL ratio will likely remain near 11% in 2016-17 and fall to 10% only in 2018.

The retail NPL ratio dropped from 13.4% in 2014 to 10% in 2015 and is expected to fall within a range of 8-9% in 2016-18. After a decline from 32% in 2014 to 27% in 2015, the corporate NPL ratio is expected to fall to 22% in 2016 but thereafter drop below 20% only in 2018. Sector NPL provision coverage (EBA definition) increased from 56% in 2014 to 58% in 2015 and is likely to continue to trend upwards in front of the AQR next year.

2 Based on EBA methodology (from September 2014), NPLs include exposures overdue >90 days as well as debtors unlikely to pay or unable to meet obligations without realization of collateral. Denominator includes loans to general government, credit institutions and central banks.

3 In 2015, gross loans included in the definition increased 20-25% y/y, due to the addition of RON ~50bn of performing loans to central banks and other credit institutions.

## Asset quality of the banking sector


[1] NPL definition changed between 2013 and 2014 so that data from these years are not comparable

*Source: The National Bank of Romania, Deloitte Estimates*

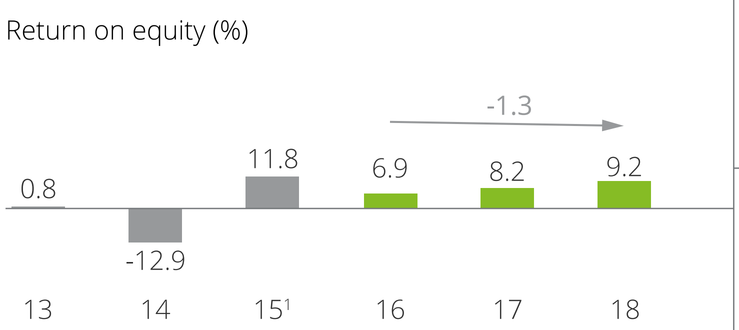
# Profitability

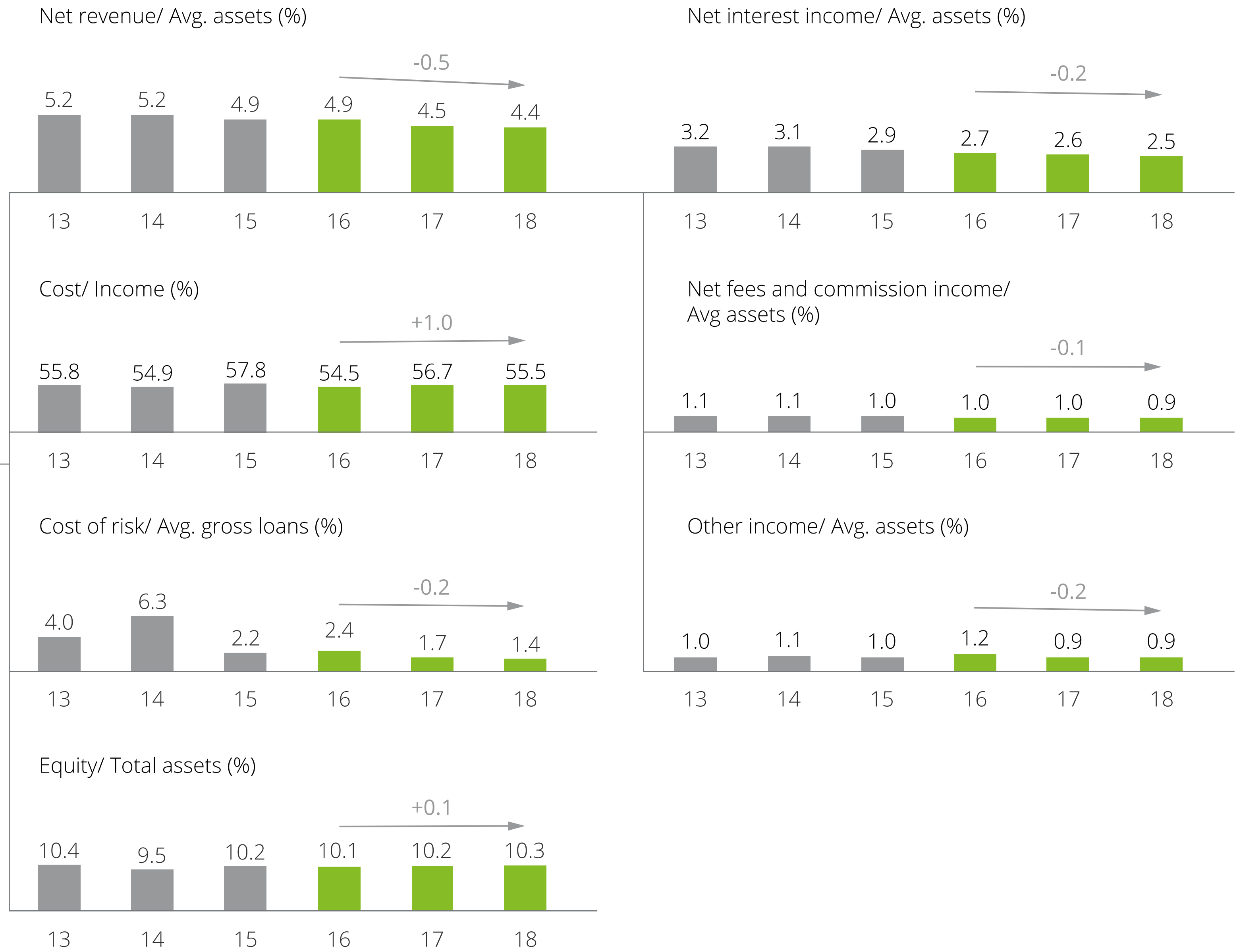
After soaring from -12.9% in 2014 to 11.8% in 2015, the ROE of the Romanian banking sector is expected to fall. ROE is expected to be cut to 7% in 2016 by one-off CHF loan conversion losses and limited to 8-9% in 2017-18 by margin pressure. While the main driver of the earnings recovery last year was a sharp reduction of risk costs from 6.3% (of average gross loans) in 2014 to 2.2% in 2015, the ROE was also boosted (~4 p.p.) by a one-off revaluation gain on Banca Transilvania's bargain purchase of Volksbank Romania. While the ROE of the banking sector remained above 12% in 1H16, this was helped by gains booked on the Visa transaction[4]. In 2H16, the banking sector faces a large loss from a law on CHF loan conversion[5] that may reduce the sector's full-year profit by a third and lower ROE to 7% in 2016. Risk costs should be a supporting factor for earnings, with an expected decline to 1.7% in 2017 and then, following AQR, to 1.4% in 2018. However, banks have been facing pressure on their net interest margin (-23bp y/y to 2.9% in 2015) that, in a low interest rate environment with intensifying competition for loans, is expected to decline to 2.5% in 2018. Net fee income (-3% y/y in 2015) will also decline again in 2016 on competition and a cut in interchange rates before a gradual return to positive growth in 2017-18. While cost/income increased last year to nearly 58%, a reduction of costs on lower branches and employment, aided by sector consolidation, is expected to drive a slow decline to a level of 55-56% in 2018.

4 The acquisition by Visa Inc. of Visa Europe Ltd. (owned by its principal members) has generated significant capital gains for banks across Europe and CE in 2Q16.

5 Romania's parliament has passed a bill that would allow conversion of CHF loans into local currency at historical below-market rates. To become a law, it must be approved by Romania's president.

## Banking sector profitability[2]




[1] Based on net profit of RON 4.4 bn including a one-off revaluation gain at Banca Transilvania of RON 1.65 bn, equating to ROE impact of 4.4 p.p.
[2] Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.

*Source: ECB, Deloitte Estimates*

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# Top 10 Banks



## The biggest market share gainer in the sector has been Banca Transilvania (#3)

Romania's largest banks, BCR (#1) and BRD-GSG (#2) both continued to lose market share in loans in 2015 to mid-tier players. At the same time, however, their profitability greatly improved on the back of improving loan quality and falling risk costs. The biggest market share gainer in the sector last year was local player Banca Transilvania (#3, BT), which acquired Volksbank (previously #8) and improved organically. BT was also a leader in terms of ROE (49%, excluding one-off bargaining gain 18%), thanks to its above average net interest margin and fee income generation.

The other top 10 market share gainers in both loans and deposits over the past year were ING (#7) and Raiffeisen (#4) UniCredit (#5), and Garanti (#10). ING and Raiffeisen are also distinguished by their high double-digit ROEs, achieved on the back of strong operating profitability and low risk costs. CEC (#6) gained market share in loans but it lost in deposits, its relatively weak loan quality and high risk costs limited it to a breakeven result. Alpha (#8), which lost share in loans and deposits, was the only loss-making bank in the top 10 last year.

## Main balance sheet items, LEI bn

| | Loans MS 2015 change | Loans (LEI bn) / Deposits (LEI bn) / Assets (LEI bn) | Deposits MS 2015 change | Assets MS 2015 change |
|---|---|---|---|---|
| **BCR** | 17.2% -1.3pp | 62 | 17.5% -0.4pp | 16.3% -0.4pp |
| **BRD** | 14.1% -0.6pp | 50 | 16.9% +0.8pp | 13.1% +0.6pp |
| **Transilvania Bank** | 12.6% +3.3p | 48 | 15.7% +2.3pp | 12.4% +2.7pp |
| **UniCredit Tiriac** | 10.7% +0.2pp | 35 | 7.0% +0.3pp | 9.0% +0.3pp |
| **Raiffeisen** | 8.6% +0.8pp | 32 | 9.7% +0.3pp | 8.2% +0.4pp |
| **CEC Bank** | 6.8% +0.6pp | 28 | 9.6% -0.8pp | 7.2% -0.4pp |
| **ING Bank[1]** | 6.5% +1.3pp | 23 | 7.6% +1.3pp | 6.1% +1.2pp |
| **Alpha Bank** | 4.7% -0.2pp | 15 | 2.6% -0.8pp | 3.9% -0.7pp |
| **Bancpost** | NA | 11 | NA | 3.0% -0.1pp |
| **Garanti Bank** | 3.0% +0.3pp | 10 | 2.3% +0.5pp | 2.5% +0.3pp |
| **Total Market (LEI bn)** | 222.953[2] | | 243.713[3] | 382.484 |

[1] Bankscope, Bancherul
[2] Excluding external assets
[3] Excluding external liabilities
*Source: Bankscope, Bancherul, Central Bank, Deloitte estimates*

Retail
Corporate and others
Total volume/ breakdown not available
Assets (LEI bn)

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## Top 10 bank profitability drivers 2013-15

1 BCR
2 BRD
3 Transilvania Bank
4 UniCredit Tiriac
5 CEC Bank
6 Raiffeisen
7 ING Bank
8 Alpha Bank
9 Bancpost
10 Garanti Bank

| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| ROE (%) | 17.1 | 7.8 | 48.8 | 8.4 | 0.5 | 13.0 | 24.0 | -1.9 | n.a. | 5.5 |
| Net Revenues / Average Assets (%) | 5.0 | 5.4 | 6.8 | 4.5 | 4.0 | 6.7 | n.a. | 2.9 | n.a. | 4.5 |
| Net interest revenue (%) | 3.2 | 3.1 | 4.7 | 2.6 | 3.0 | 3.5 | n.a. | 2.6 | n.a. | 3.3 |
| Net fees and commision revenue (%) | 1.2 | 1.6 | 1.2 | 0.9 | 0.7 | 2.1 | n.a. | 0.4 | n.a. | 0.4 |
| Other revenues (%) | 0.6 | 0.7 | 1.0 | 1.0 | 0.4 | 1.1 | n.a. | -0.1 | n.a. | 0.8 |
| Cost to Income (%) | 59.5 | 53.4 | 45.9 | 51.0 | 57.7 | 60.2 | 56.0 | 81.9 | n.a. | 61.5 |
| Cost of risk (%) | -0.2 | 2.0 | 3.5 | 1.8 | 3.2 | 1.6 | n.a. | 1.1 | n.a. | 1.5 |
| Equity / Assets (%) | 9.4 | 12.5 | 13.1 | 9.7 | 7.8 | 10.2 | n.a. | 9.6 | n.a. | 11.0 |

- Trend in 2013 - 2015
13.0% - 2015

[1] Boosted by one-off bargaining gain of RON 1.65bn on acquisition of Volksbank Romania, excluding which ROE would have been 16%
[2] Based on company press statement

*Source: Bankscope*

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## C/I ratio versus assets, 2015


*Source: Bankscope*

# Strategy

## Drive for efficiency encourages consolidation as well as digitalization

As low interest rates and growing liquidity will drive intensifying competition for loans, particularly for better quality customers, banks will need to optimize processes to improve time to yes and time to cash – especially in corporate clients area. At the same time, efficient underwriting processes will needed to improve loan quality. While banks will increasingly invest in digitalization, as they adapt to changing customer behavior (increasing usage of remote channels), those that move faster will have an advantage. To improve customer retention/acquisition, banks will need to deliver a better customer experience, while data analytics will be used to better identify and segment customers according to their needs and what they are willing to pay for. As there will be less need for physical contact, banks will be able to continue to cut branches and employment and improve operating efficiency. With margin pressure and growing competition, consolidation in the sector is expected to continue, as the active smaller players will be encouraged to increase scale or exit via M&A. One or more Greek-owned banks may also be sold, as their parents re-focus operations on core markets.

# Digital Maturity

Romania ranks 4th in digital banking maturity in CE (based on the overall score of its 5 biggest banks) behind Poland, Slovakia and the Czech Republic. Although the best Romanian bank ranks as high as 6th, the remaining players impact the country's overall score. The country ranking is negatively affected mainly by poor digitalization in the internet channel, as mobile banking functionalities are not far behind leading solutions.

Analysis of the Customer Journey reveals that features responsible for information gathering and customer onboarding are the most digitally mature, while there is a significant gap in the account opening process in comparison to leading markets. Term deposits and cash loans are the most digitalized products but there is also a visible focus on car loans, which are more digitalized in Romania than in any other CE country.

*If you want to know detailed data for digital banking benchmarking, contact us.*

# Contact

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# Key Insights

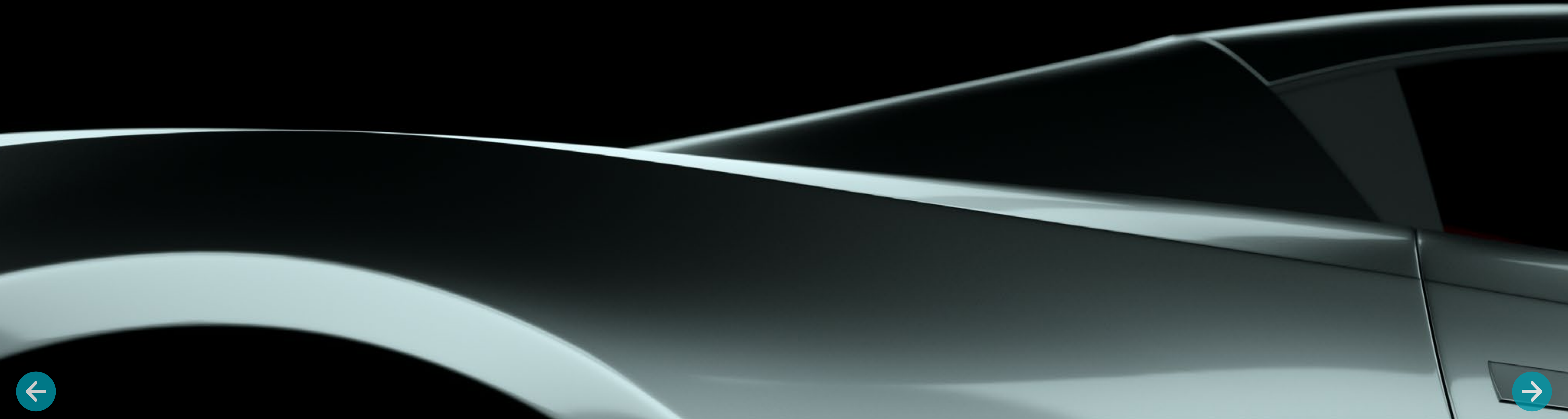
**A strong economy outpacing CE region,** Slovakia's consumer spending is accelerating on the back of a steadily improving labor market, while business confidence is near a five-year high.

**Loan growth is the highest in CE but should slow.** Regulation is on the rise to safeguard quality in the booming housing loan segment, while corporate loans should also grow more moderately.

**NPL ratio is very low and on an improving trend,** supported by record low interest rates and healthy economic growth. However, risk costs are the lowest in CE and may rise.

**Profitability is relatively strong,** with ROE rising to 8.4% in 2015, but net interest margin pressure is expected to drive a decline over the next few years despite strong volume growth.





# Economy

## Economic growth has accelerated in recent years

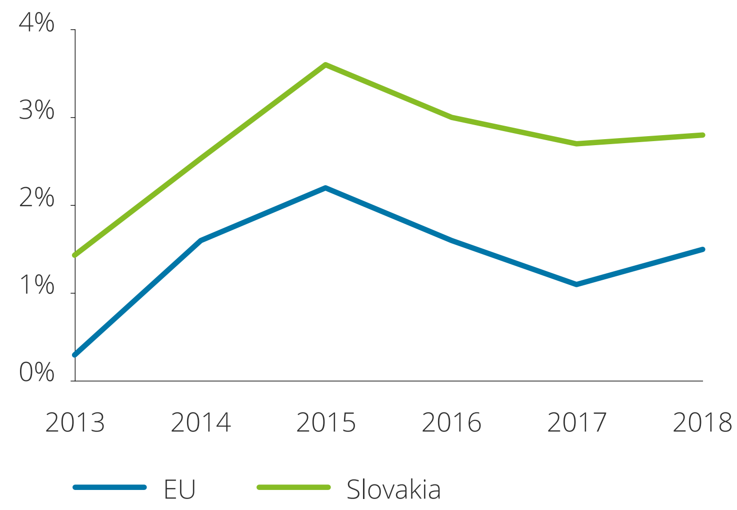
Slovakia's economy has accelerated in recent years, with GDP up 3.5% in 2015, and growth should remain above the CE average in 2016-18. After a surge in investment in 2015, backed by increased EU funds absorption before the close of the 2007-13 financing program, a slowdown is anticipated in 2016. However, business confidence is near a five-year high and private investment is encouraged by easier credit terms, relatively high capacity utilization, and the ongoing Eurozone recovery.

Nonetheless, the key driver of economic growth in 2016 will be consumer spending, accelerating on the back of a steadily improving labor market and low interest rates that encourage borrowing and discourage saving. Slovakia's relatively high unemployment rate (second only to Croatia in CE) has been dropping and should fall below 10% by next year, while employment and wages have been rising, supporting household confidence.

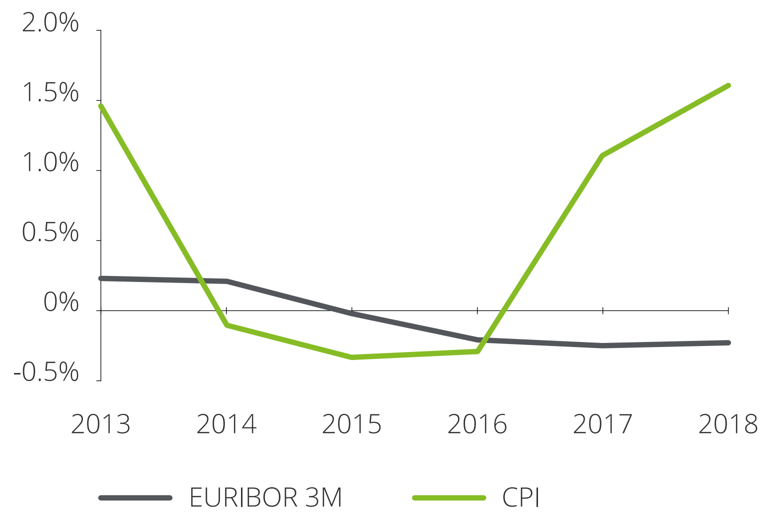


## Real GDP growth

*(yoy%)*

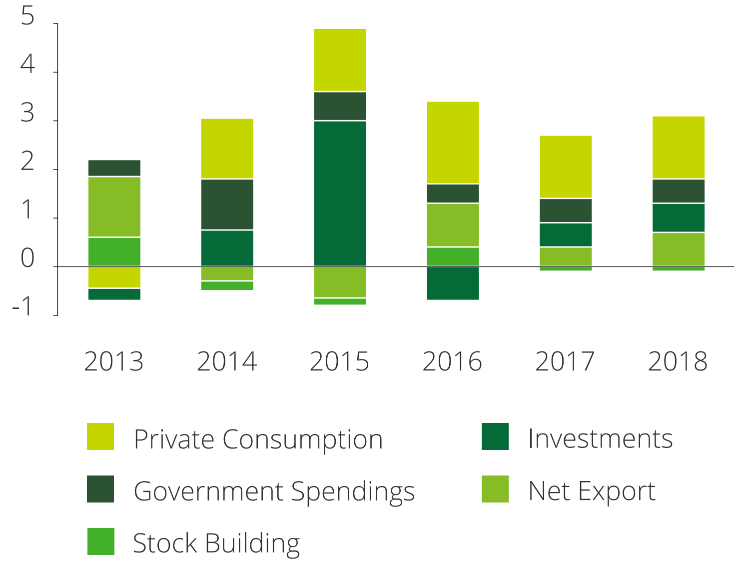



## Interbank interest rate and CPI

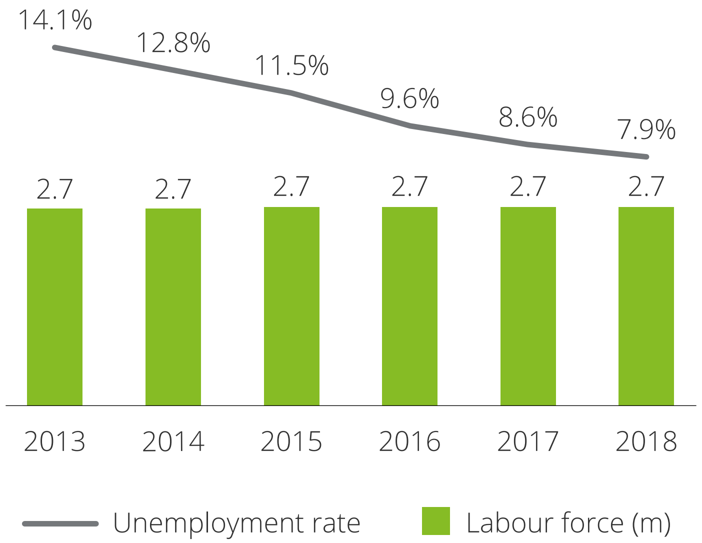



## Real GDP drivers

*(change as a percentage of real GDP)*




## Labour market




*Source: Economist Intelligence Unit*
*Source for interest rate and CPI chart: Economist Intelligence Unit, Bloomberg, Deloitte estimates*

# Balance Sheet

## Loan growth is the highest in CE but should slow

Slovakia has the highest loan growth in CE but should slow moderately. Housing loans have been booming, at a 5Y CAGR of 12.9% and grew 14.8% y/y in 2015, supported by falling interest rates and affordable property prices that have started to rise. Other retail loans were up only 5% y/y in 2015 and should pick-up, as strong confidence drives growth of consumer spending. However, regulation is also on the rise (e.g. limitations on levels of high LTV mortgages, maturity of consumer loans) to safeguard credit quality and this is expected to reduce overall retail loan growth.

Corporate loan growth jumped to 9.0% y/y in 2015 versus a 5Y CAGR of 1.5%, helped by easier credit terms, and is also expected to return to a more moderate pace. The capital and funding of the sector is strong, with the tier 1 capital ratio increasing from 16.0% to 16.5% in 2015, while loans/deposits declined last year to 95%. Deposits have been very robust, rising 10.2% y/y in 2015, but should lose momentum in the next few years, as low interest rates drive a shift in demand towards alternative investments.

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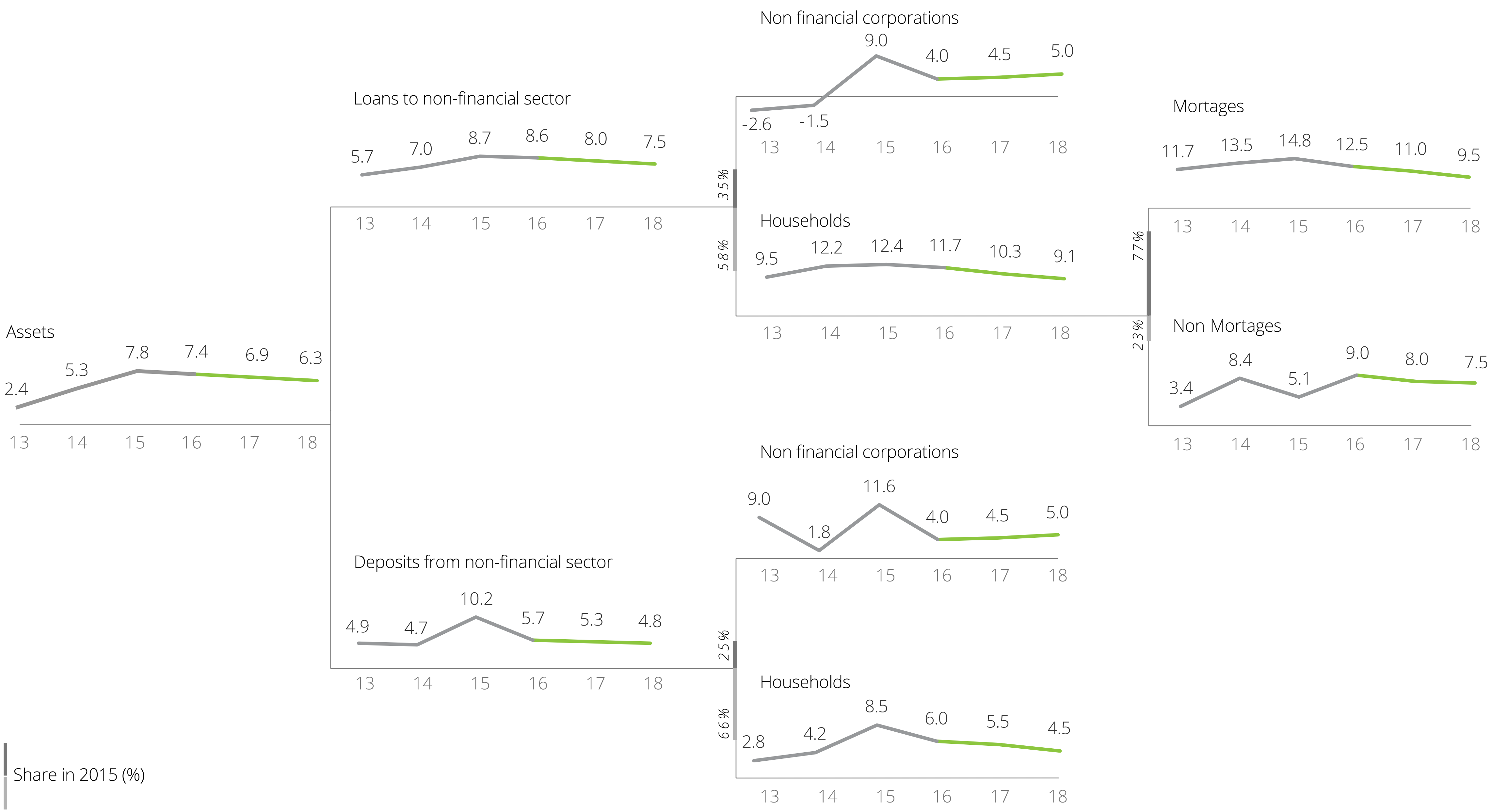
## Banking sector balance sheet drivers (yoy growth %)




*Source: The National Bank of Slovakia, Deloitte Estimates*

# Asset Quality

## NPL ratio is very low and on an improving trend

Asset quality in Slovakia is very strong and should remain on an improving trend, supported by record low interest rates and healthy economic growth. In CE, only Czech Republic has a lower NPL ratio. The total NPL ratio in Slovakia fell from 5.6% to 5.0% in 2015, with improvement in both the corporate segment, from 8.6% to 7.3% and in the retail segment from 4.3% to 3.9%. While the decline of the NPL ratio has been supported by a base effect (i.e. strong growth of gross loans in the retail and corporate segments), new defaults are at low levels. The outlook is for a further decline of the NPL ratio, as households will benefit from a further drop in unemployment, while rising real wages and low interest make payments more affordable. The corporate sector is potentially more volatile, as the direction may be determined by larger exposures, but should also continue to benefit from a strong economy.

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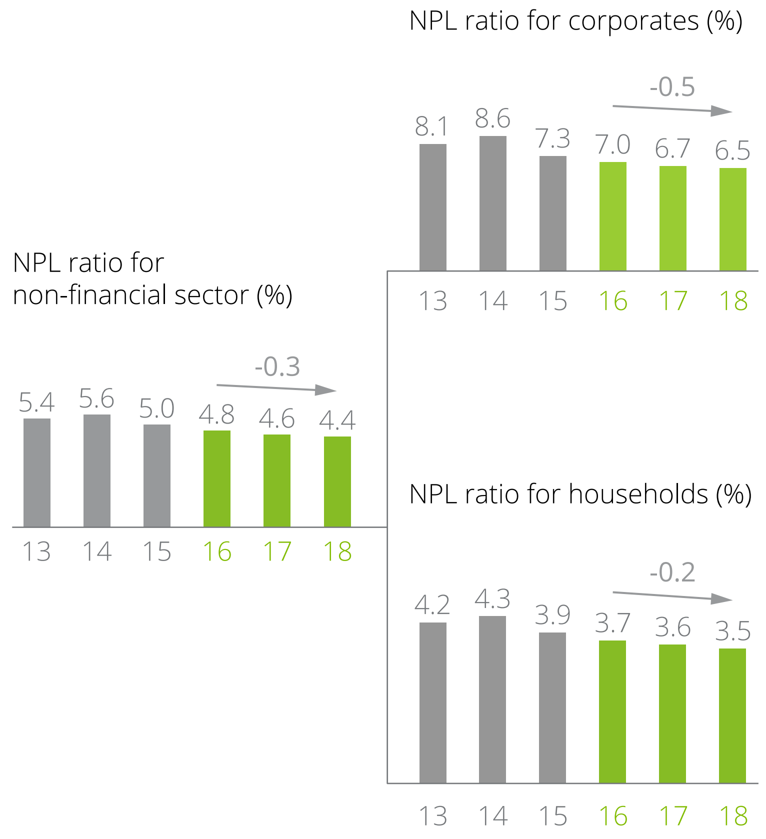
## Asset quality of the banking sector




*Source: The National Bank of Slovakia, Deloitte Estimates*

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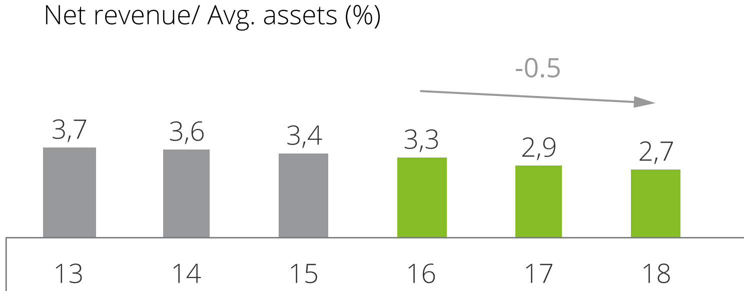
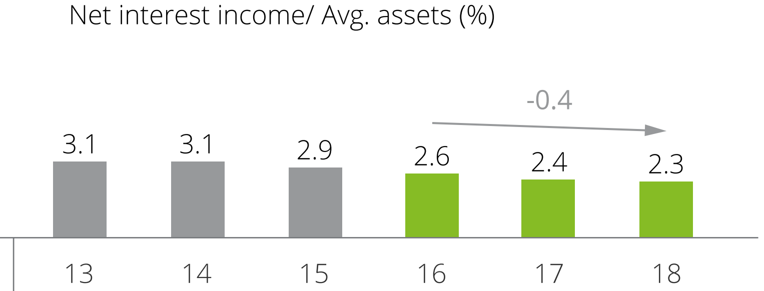
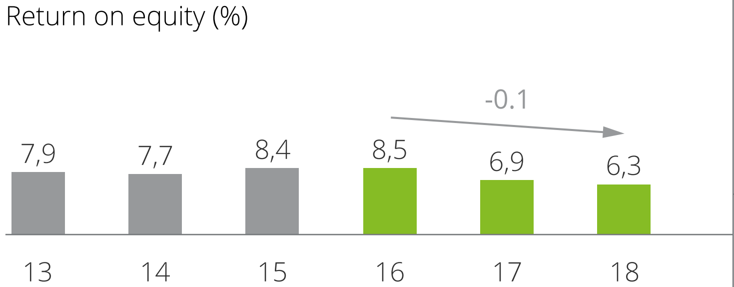
# Profitability

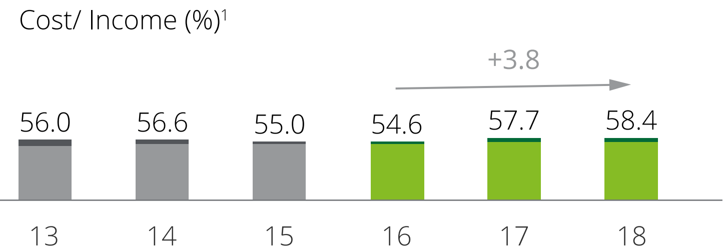
The ROE of Slovakian banks is relatively strong, rising from 7.7% in 2014 to 8.4% in 2015, but net interest margin pressure is expected to drive a decline over the next few years. With interest rates at record lows and little room to further re-price deposits, falling lending rates spurred by refinancing activity will significantly reduce margins and drive a decline of net interest income. Rising volumes and sales of investments and insurance will support net fee income but growth will be limited by lower interchange fees, competition, and a shift to lower cost channels. Last year's earnings benefited significantly from a drop in Slovakia's bank levy from 0.4% to 0.2% of liabilities (after accumulating > EUR 500m) but recent government proposals indicate there will probably not be a further reduction to 0.1% (as originally planned) when the fund reaches EUR 750m in 2017. Cost/income fell to 55% in 2015 but a rising trend is expected over the next few years. Banks will be under pressure to cut operating costs but some growth should be anticipated, due to wage pressure in the economy and the need for up-front investment in digitalization. Banks also benefited from a decline in risk costs from 50bp in 2014 to just 40bp in 2015, the lowest level in CE. Such low risk costs are unsustainably low and an increase should be expected in the next few years, albeit limited due to the healthy economic outlook.

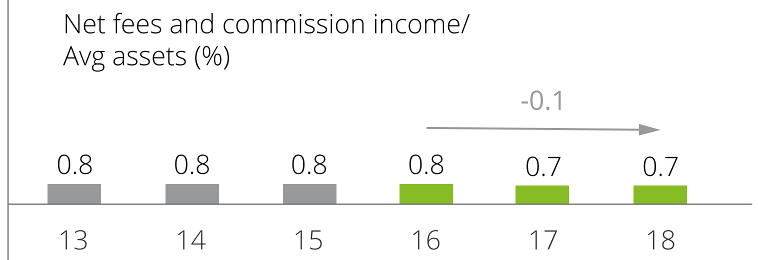
## Banking sector profitability[2]

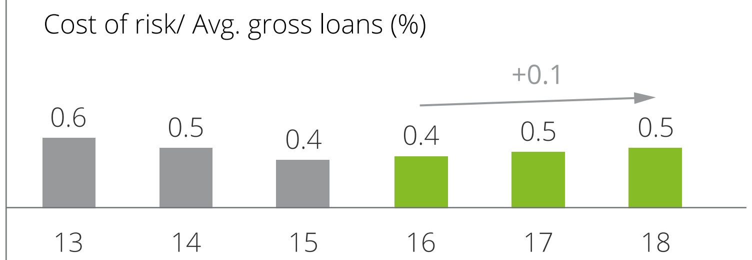


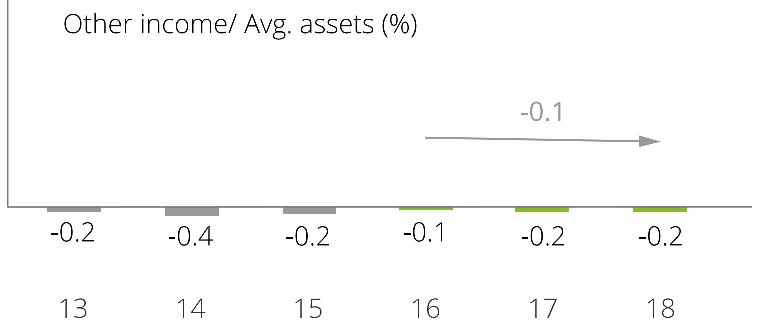



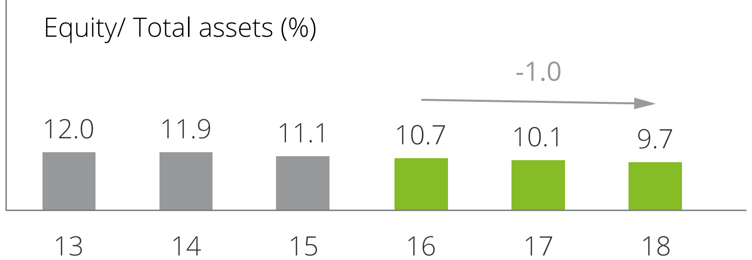




[1] Slovakia's bank levy adds 2.5-4.0 p.p to cost/income
[2] Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.

*Source: The National Bank of Slovakia, Deloitte Estimates*

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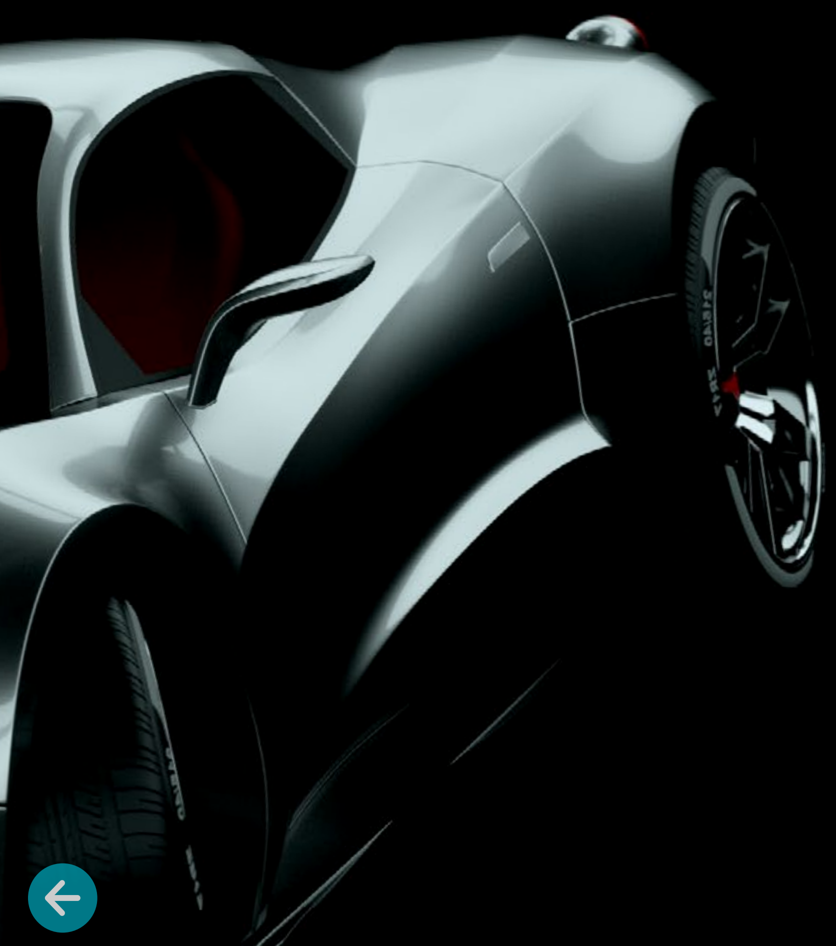
# Top 10 Banks

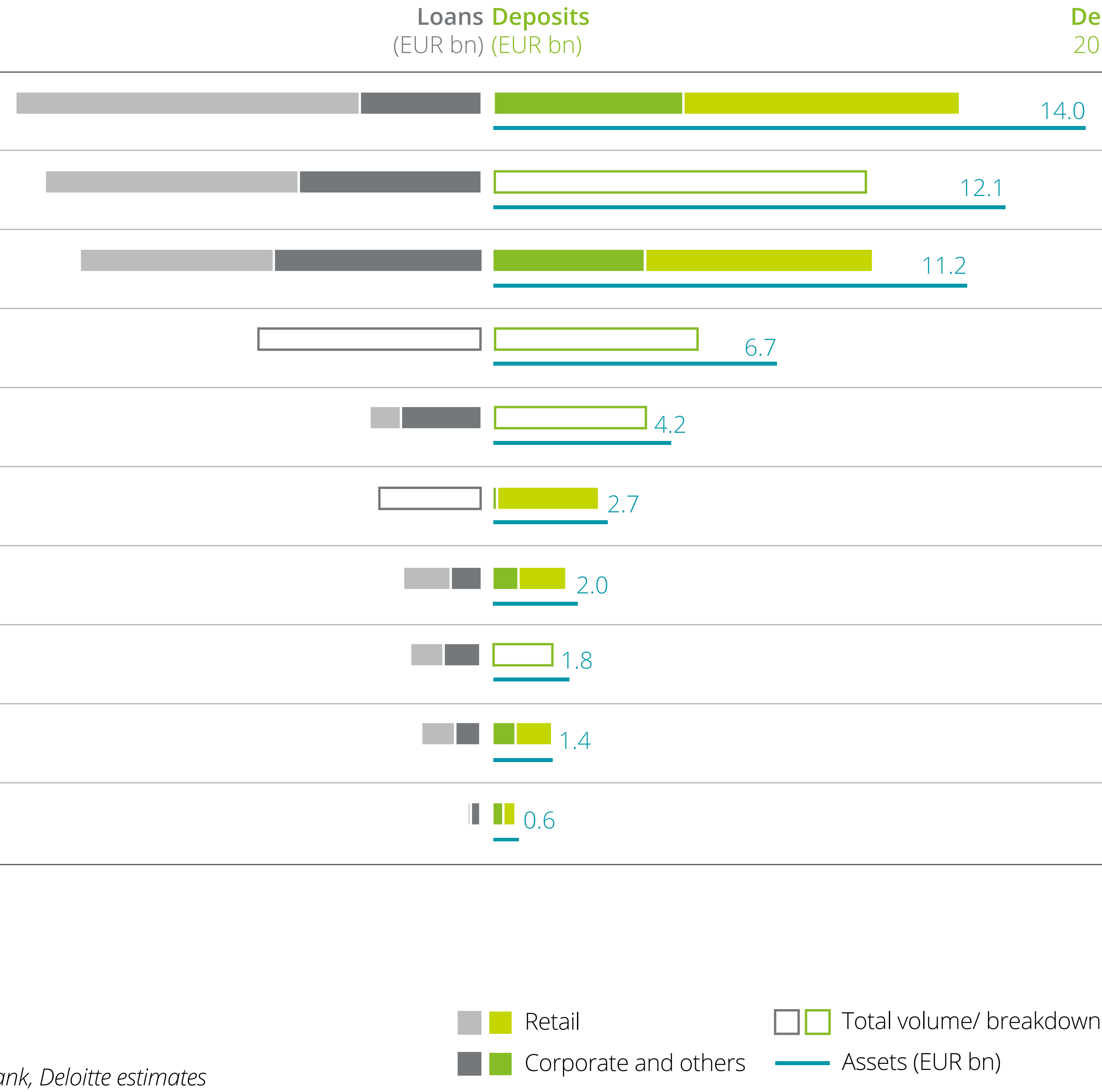
## Slovakia's leading banks have been gained market share at the expense of smaller players

The largest player Slovenska sporitelna was also the biggest market share gainer in 2015 thanks to its leading position on the booming housing loan market. However, all of Slovakia's top 4 banks (including VUB, Tatra banka, and CSOB) have gained market share over the past year, at the expense of smaller banks (most notably #5 Postova banka and #8 Sberbank, which saw declines in their corporate loans). As the refinancing market has picked up in 2016, the biggest winner among the top 4 banks has been VUB, gaining 0.6 p.p. of loan market share in 1H16. Slovenska sporitelna and the other top 4 banks are also leading the sector in terms of ROE. While the low interest rate environment is reducing bank margins, the top 4 banks are achieving above-average net revenues thanks to their low funding costs. This a particular advantage given the ongoing sectoral shift towards housing loans where there is intensifying price competition. The smaller banks with relatively high margins, Postova banka and OTP Banka, have retail loan books that are composed mainly of consumer loans and face higher risk costs that reduces their profitability. Lacking scale, many smaller banks in the sector will struggle to maintain adequate profitability as margins continue to fall, encouraging consolidation. This has already started with Sberbank's recent sale of its Slovakian subsidiary to Penta Investments, majority owner of #7 Prima banka and #10 Privatbanka.



## Main balance sheet items, EUR bn

| | Loans MS 2015 change | Deposits MS 2015 change | Assets MS 2015 change |
|---|---|---|---|
| **Slovenska sporitelna** | 20.7% +1.2pp | 21.2% +0.1pp | 20.7% 0.0pp |
| **VUB banka** | 19.4% +0.2pp | 16.9% -0.1pp | 17.9% 0.0pp |
| **Tatra Banka** | 17.9% +0.7pp | 17.3% +1.4pp | 16.7% +1.2pp |
| **CSOB** | 9.8% +0.8pp | 9.5% +0.2pp | 10.0% +0.4pp |
| **Postova banka** | 5.0% -0.8pp | 7.0% -0.8pp | 6.2% -0.5pp |
| **Prva stavebna sporitelna** | 4.4% -0.2pp | 4.8% -0.3pp | 4.0% -0.2pp |
| **Prima banka** | 3.5% +0.2pp | 3.3% +0.2pp | 3.0% 0.0pp |
| **Sberbank** | 3.1% -0.8pp | 2.8% -0.1pp | 2.7% -0.5pp |
| **OTP** | 2.6% -0.1pp | 2.4% -0.2pp | 2.1% -0.2pp |
| **Privatbanka** | 0.6% 0.0pp | 1.0% +0.2pp | 0.9% -0.1pp |
| **Total Market (EUR bn)** | 45.548 | **50.457** | **67.353** |




*Source: Bankscope, Annual Reports, Central Bank, Deloitte estimates*

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## Top 10 bank profitability drivers 2013-15

1 Slovenská sporiteľňa
2 VÚB banka
3 Tatra Banka
4 ČSOB
5 Poštová banka
6 Prvá stavebná sporiteľňa
7 Prima banka
8 Sberbank
9 OTP
10 Privatbanka

| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| ROE (%) | 13.0 | 11.2 | 12.1 | 10.8 | 8.3 | 9.5 | 3.9 | -9.4 | 2.7 | 9.2 |
| Net Revenues / Average Assets (%) | 4.5 | 4.6 | 4.3 | 4.0 | 5.6 | 2.9 | 3.4 | 2.9 | 3.8 | 3.6 |
| Cost to Income (%) | 49.7 | 47.4 | 56.6 | 59.5 | 41.0 | 48.7 | 61.7 | 75.0 | 68.5 | 52.4 |
| Cost of risk (%) | 0.6 | 0.3 | 0.4 | 0.3 | 2.9 | 0.4 | 0.7 | 1.4 | 1.2 | 1.2 |
| Equity / Assets (%) | 11.0 | 11.9 | 8.2 | 9.1 | 14.5 | 8.8 | 6.6 | 10.5 | 7.9 | 9.9 |
| Net interest revenue (%) | 3.5 | 3.4 | 2.8 | 2.9 | 4.5 | 2.4 | 2.6 | 2.0 | 3.2 | 2.3 |
| Net fees and commision revenue (%) | 0.9 | 1.0 | 1.3 | 0.8 | 0.7 | 0.7 | 0.8 | 0.4 | 0.7 | 1.2 |
| Other revenues (%) | 0.1 | 0.2 | 0.3 | 0.4 | 0.4 | -0.2 | 0.0 | 0.5 | -0.1 | 0.2 |

- Trend in 2013 - 2015

13.0% - 2015

*Source: Bankscope*

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## C/I ratio versus assets, 2015


*Source: Bankscope*

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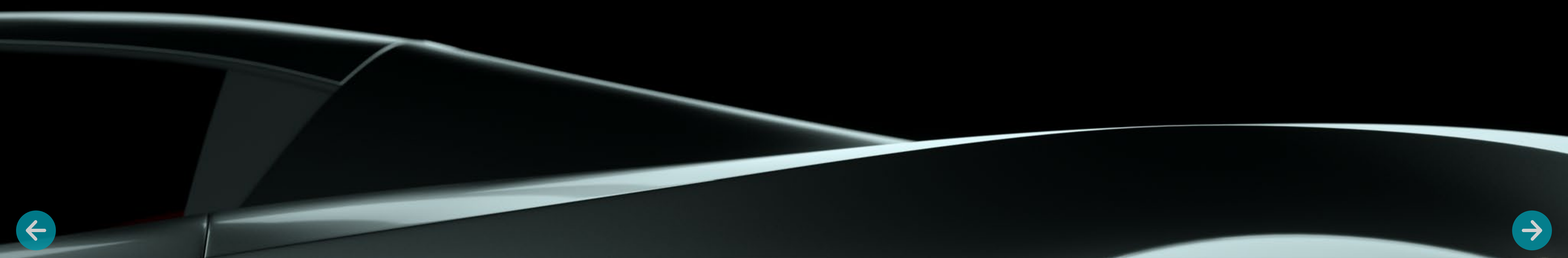
# Strategy

## With business volumes booming, banks aim to maximize their sales while improving efficiency

While the business volumes of Slovak banks are booming, low interest rates and intensifying competition are driving margin compression and will erode banking sector profitability, making it important for banks to maximize their sales while improving efficiency. Competition is fiercest in mortgages and mortgage refinancing, a big ticket product that can trigger churn of retail banking customers, while a majority of sales (>50%) come through intermediaries. Price is a key factor but banks will be better positioned to win market share if they are able to make easier and faster loan application and approval processes for customers and their external partners. Given the potential for churn to rise, retention strategies will be important for larger banks and those with a higher proportion of active customers will have an advantage, as these are less likely to switch. Digitalization will continue to be important to meet customer expectations for increased functionality, particularly with mobile devices. At the same time, banks will need to leverage digital investments to update service models, in order to reduce their cost to serve and improve operating efficiency.





# Digital Maturity

Digital maturity in Slovakia is one of the highest among CE countries, both from the perspective of the overall position of the 5 biggest banks (second place after Poland), as well as on the level of particular banking institutions, as the most digitalized bank in CE is from Slovakia (Tatra Banka). Internet and mobile channel functionalities are only marginally less developed than in Poland – the second place ranking reflects the disparity (largest in CE) between individual banks in Slovakia, from the above-mentioned first place to 60th position across 76 analyzed banks. From a Customer Journey perspective, Slovak banks achieved the highest maturity in the steps focused on customer acquisition (similar to most CE countries). What is unique for Slovakia is that its banks' day-to-day banking functionalities are outstanding with the highest score in CE. On the other hand, the results for cross-selling capabilities ("expand relationship" step) are only average, with cash loans and saving accounts the most digitalized products.

*If you want to know detailed data for digital banking benchmarking, contact us.*

# Contact

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# Key Insights

**The pace of economic growth is set to moderate in 2016-18,** with a pullback in government investment but there is ongoing support from private consumption thanks to an improving labor market.

**Loans are expected to remain in decline (-1% y/y) in 2016** but the pace of the contraction has eased and a return to positive growth (+2-3% y/y) is expected in 2017-18, led by housing loans.

**Asset quality is steadily improving.** The NPL ratio of the non-financial sector is down again in 2016, from 10.8% in 2015 to 8.6% in 1H16, supported by another asset transfer (2.0 p.p.) to the BAMC.

**Profitability should improve sharply in 2016,** after one-off gains on the Visa transaction and a net provision release in 1H16, but net interest margin compression poses an ongoing challenge.



# Economy

## The pace of economic growth is set to moderate in 2016-18

Following a second year of strong GDP growth in 2015 (+2.9% y/y), the pace of Slovenia's economic recovery is expected to moderate to a level of 1.8-2.0% in 2016-18, below average for CE. A key driver of the downshift in growth is the pattern of government investment, falling back in 2016 from a peak period in 2014-15. This reflects a slow start in disbursement of EU funds in the new programming period, after very high levels at the close of the previous period. Investment is expected to pick-up in 2017-18, also with the help growth in the private sector spending (spurred by high capacity utilization and record low interest rates). After accelerating last year, private consumption should maintain momentum in 2016-18, supported by an improving labor market. Unemployment is steadily declining while wage growth has been picking up. While Slovenia has a relatively large trade surplus that has contributed to its economic recovery, the contribution to GDP growth is expected to moderate in 2016-18, as domestic demand drives growth of imports.

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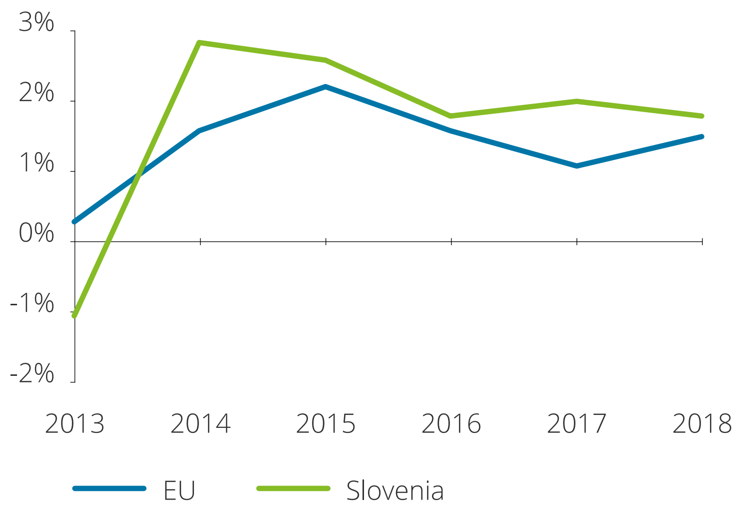
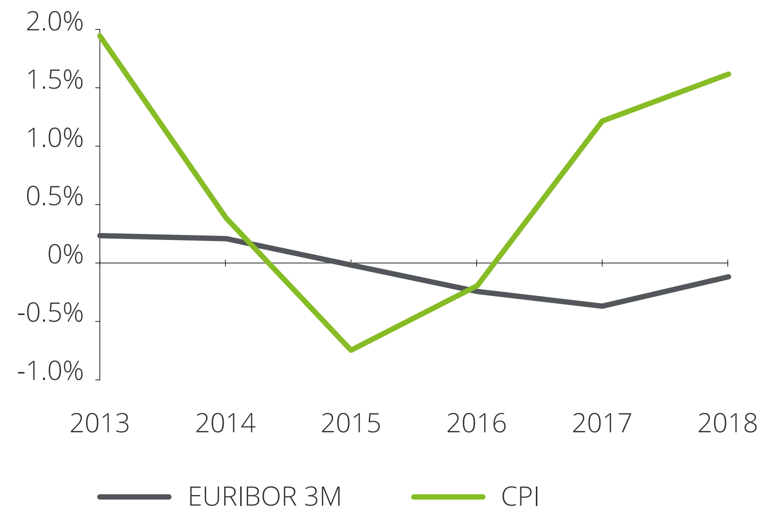
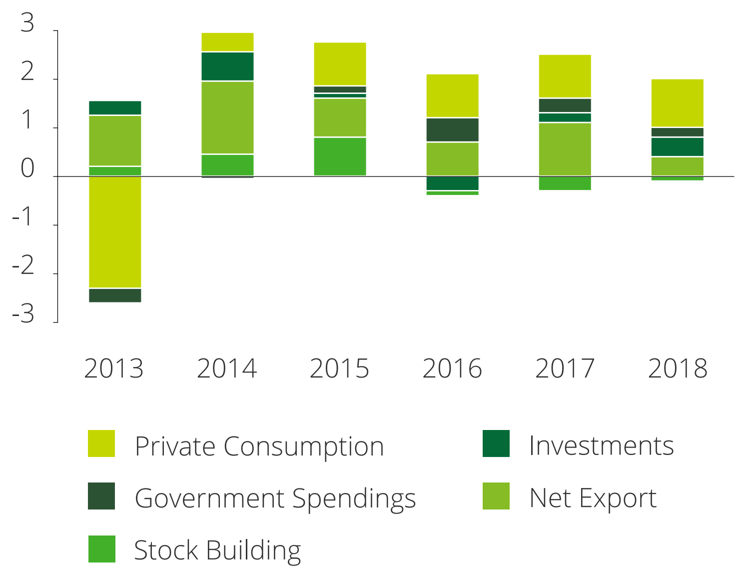
## Real GDP growth
*(yoy%)*



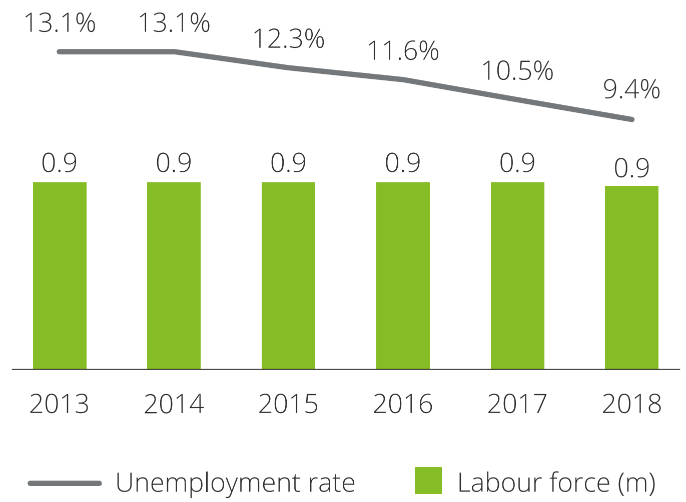

## Interbank interest rate and CPI




## Real GDP drivers
*(change as a percentage of real GDP)*




## Labour market




*Source: Economist Intelligence Unit*
*Source for interest rate and CPI chart: Economist Intelligence Unit, Bloomberg, Deloitte estimates*

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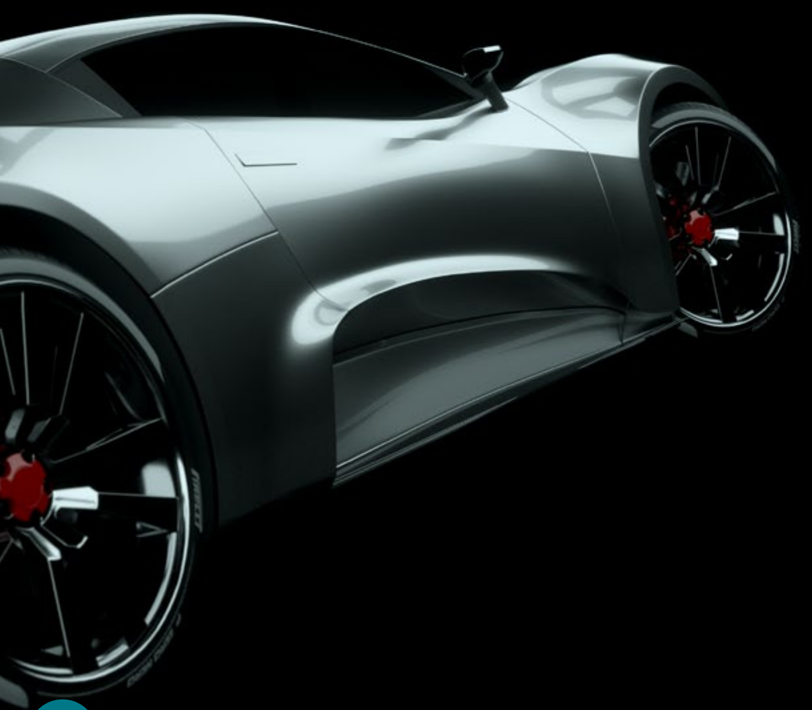
# Balance Sheet

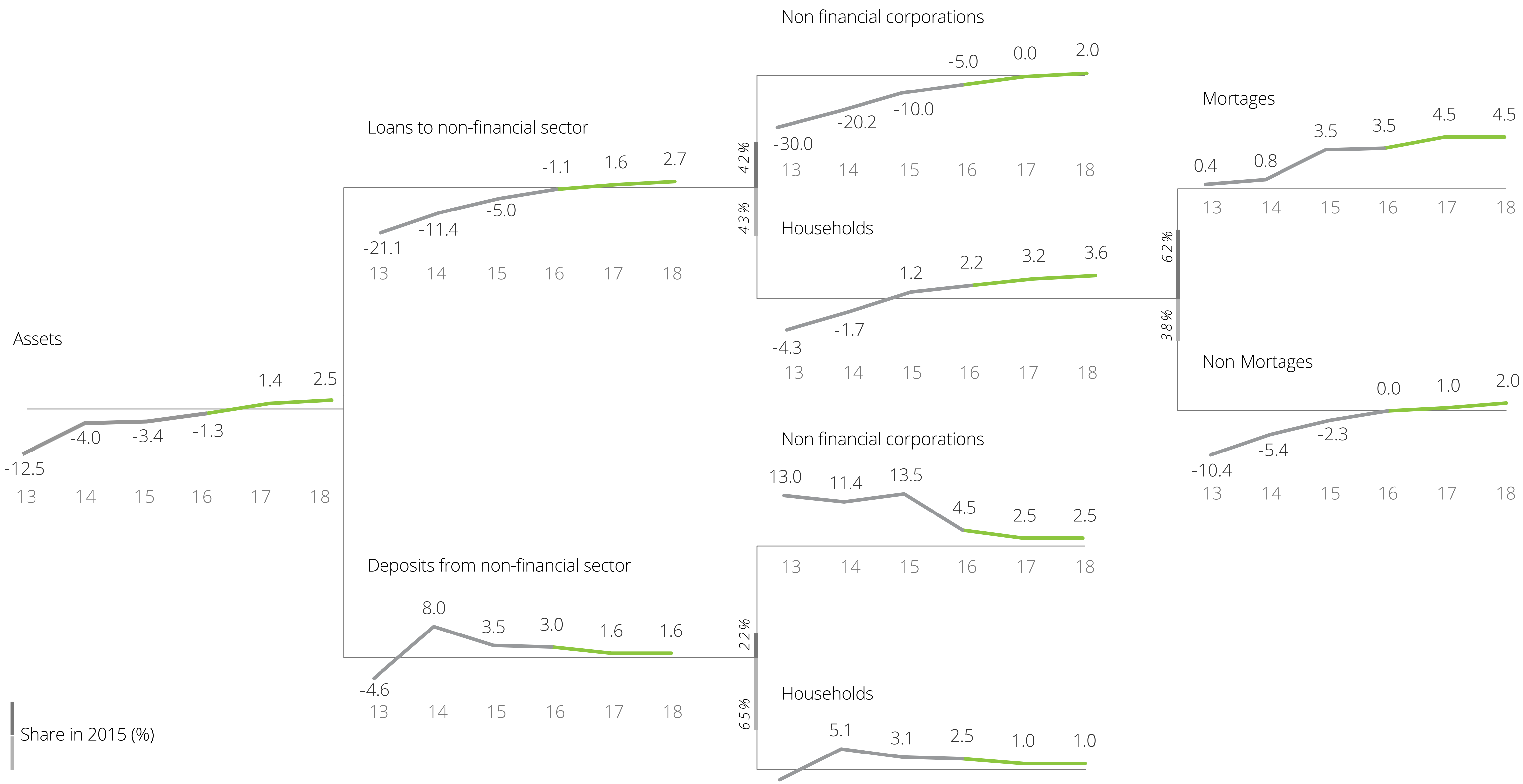
## Loans are expected to continue to decline in 2016 but return to positive growth in 2017-18

Loans are expected to continue to decline in 2016 but the pace of the contraction has eased and a return to positive growth is expected in 2017-18. Corporate loans (-10% y/y in 2015) have been the main driver of the decline and will fall again in 2016, due to ongoing deleveraging, write-offs, and NPL sales. However, as investment spending picks up, corporate loans are expected to stabilize in 2017 and rise in 2018. Corporate borrowing will be encouraged by low interest rates, while the spread between lending rates in Slovenia and the Euro area has continued to narrow in 2016. Retail loan growth turned positive in 2015, driven by mortgages (+3.5% in 2015). Mortgages should grow at a similar pace in 2016 and accelerate moderately in 2017-18, supported by improvement on the real estate market. Property prices have stabilized over the past year, while the number of transactions has picked up. The decline of consumer loans has slowed down (-2.3% y/y in 2015) and a stabilization in 2016 is expected to be followed by growth of 1-2% in 2017-18, as continued improvement in the labor market supports consumer spending. While corporate and retail deposit growth is expected to slow down in 2016-18 on the back of low interest rates, the funding position has greatly improved in recent years, with loans/deposits having fallen to 81% in 2015. The capitalization of banks has also improved, with CET1 ratio reaching 20% in 2015.



## Banking sector balance sheet drivers

*(yoy growth %)*




[1] Loans are presented in net values

*Source: Bank of Slovenia, Deloitte Estimates*

# Asset Quality

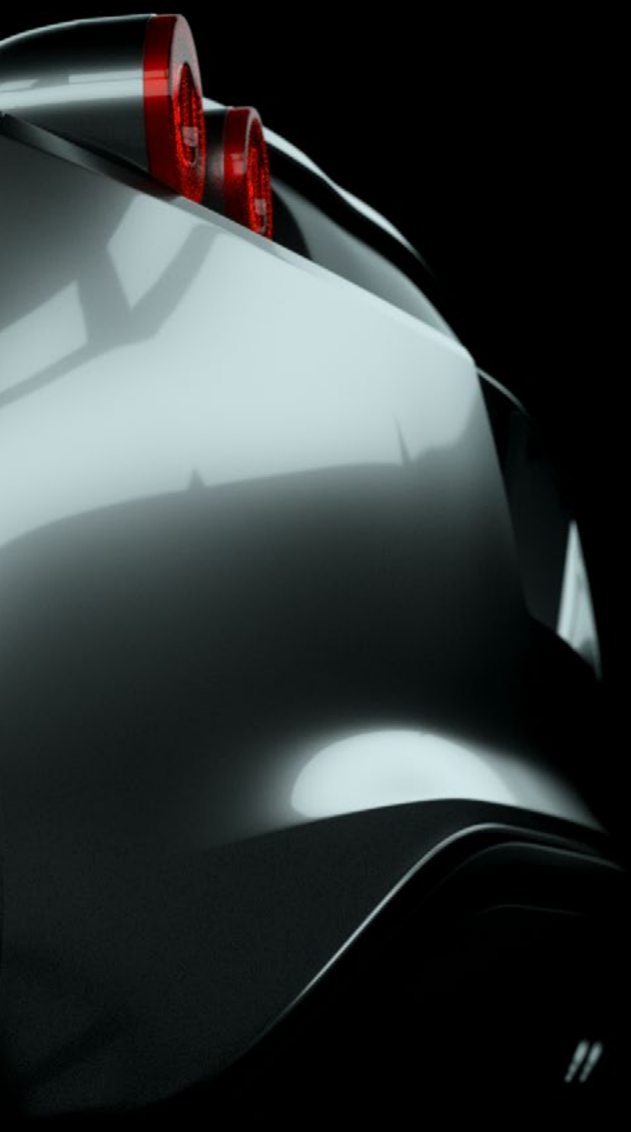
## Asset quality is steadily improving

Asset quality in the banking sector has steadily improved in recent years and this trend should continue. The NPL ratio of the non-financial sector, after a decline from 13.0% in 2014 to 10.8% in 2015 and 8.6% in 1H16, and is expected to fall below 7% in 2018. A key factor behind the NPL drop in 1H16 was the asset transfer of c. EUR 0.7bn (2.0 p.p.) to the BAMC related to the wind-down of Factor banka and Probanka. The financial standing of Slovenian households is relatively healthy. The retail NPL ratio has improved from 5.3% in 2014 to 4.7% in 2015 and to 4.2% in 1H16. While there is limited room for a further decline, an improving labor market should help keep the NPL ratio near 4% through 2018. The steady decline in the corporate NPL ratio 17.7% in 2014 to 15.3% in 2015 and to 12.0% in 1H16 is set to continue to a level of 9-10% in 2018. While continued economic growth and low interest rates will contribute to fewer defaults, there is an ongoing trend of balance sheet cleaning (write-downs, loan sales). This will be supported by the sector's relatively strong provision coverage of NPLs (up 4 p.p. to 65% in 2015).



## Asset quality of the banking sector

# Profitability



After returning to a positive ROE of 2.7% in 2015, Slovenian banks are expected to see a sharp improvement to 7% in 2016 before falling back to an ROE of 3-4% in 2017-18. While the ROE of the banking sector soared to 12% in 1H16, this was boosted by one-off gains on the Visa transaction and a net provision release. Net provisioning is expected to remain very low at 0.5% (of average gross loans) for full-year 2016 but should normalize next year. Reflecting an ongoing improvement in asset quality, net provisioning is expected to trend lower versus the 2015 level (1.5%) to 1.1% in 2017 and 0.9-1.0% in 2018. While the net interest margin of Slovenian banks is the lowest in the region, it faces ongoing pressure from low interest rates, the rollover of bond portfolios and intensifying competition for loans. After declining by 15bp to 2.0% in 2015, a further steady decline of the net interest margin is forecast towards 1.6% in 2018. Net fee income has been declining (-3% y/y in 2015 and -6% y/y in 1H16) but should return to growth in 2017-18, as banks will aim to offset a falling top line. Cost cutting is expected at 2-3% per annum in 2016-18, driven by reductions in branches and employment, but margin pressure is nonetheless expected to drive a rise in cost/income (59% in 2015) to 61% in 2018.

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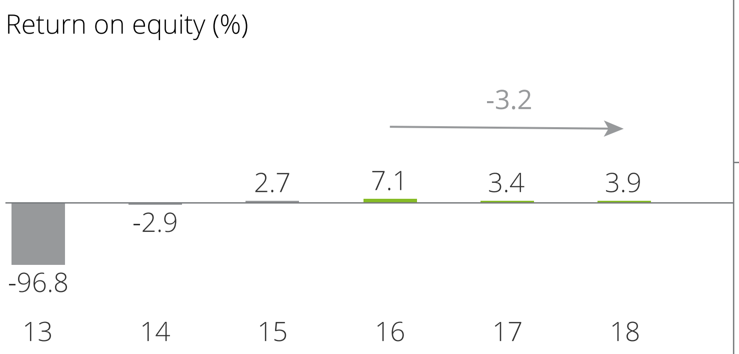
## Banking sector profitability[1]





[1] Expectations for asset quality and risk costs do not take into account the impact of IFRS 9 implementation.

*Source: Bank of Slovenia, Deloitte Estimates*

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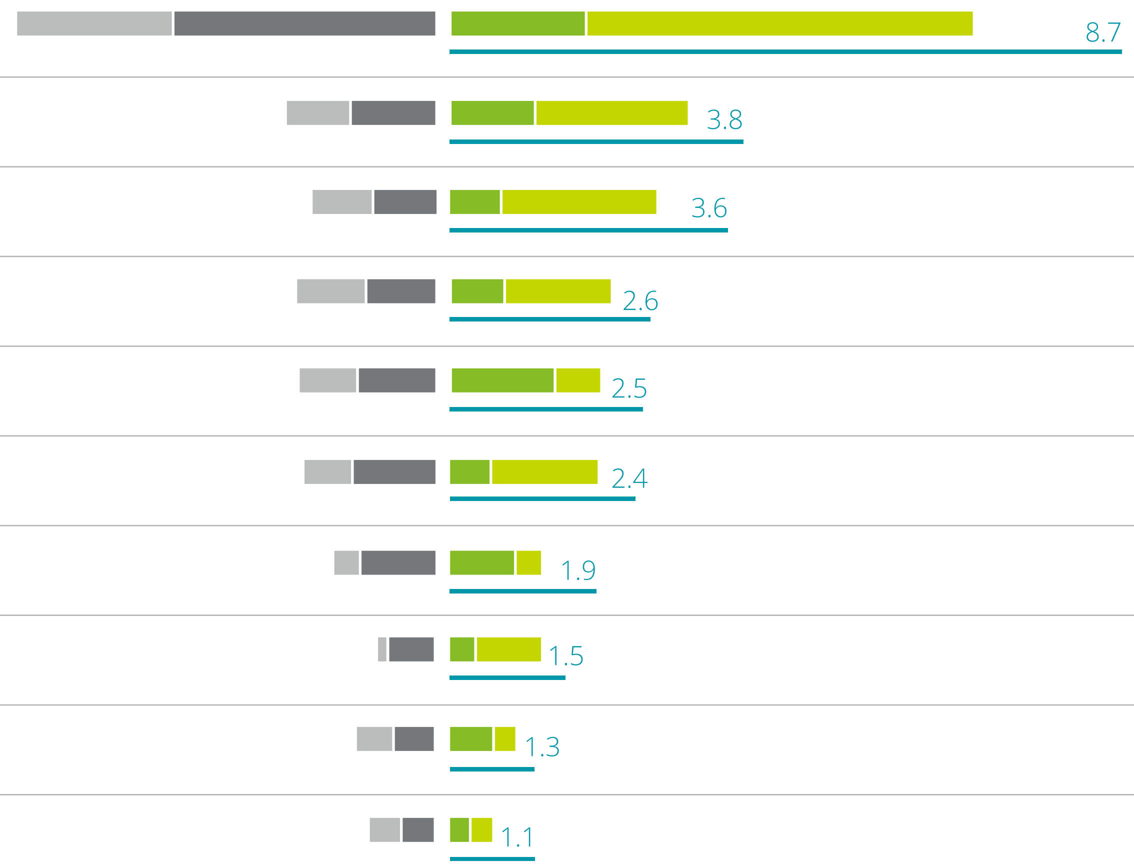
# Top 10 Banks

The most efficient banks in the sector are mid-sized foreign-owned players

The sector leader NLB (#1) suffered erosion of its market share last year in both loans and deposits, mainly to mid-sized foreign owned players, including SKB (#4), UniCredit (#5), and Sberbank (#7). However, the biggest market share gainer (+4 p.p. to 9.2% in loans) was Abanka (#2), thanks to its merger with Banka Celje (previously #7). NLB's profitability improved last year to an above-average level (6.8%), thanks to its relatively strong net interest margin and a decline in its risk costs, but its cost/income ratio (62.5%) remains above the sector average. The most efficient banks in the sector are the same mid-sized foreign-owned players that have been gaining market share Sberbank (53% cost/income), SKB (54%), and UniCredit (55%), as well as Abanka (55%). The least profitable player in the sector was Hypo Alpe Adria Bank (ROE -56%), renamed Addiko Bank, which is being restructured under new ownership (after being acquired by Advent last year).



## Main balance sheet items, EUR bn



| | Loans MS 2015 change | | Loans (EUR bn) / Deposits (EUR bn): Assets (EUR bn) | Deposits MS 2015 change | | Assets MS 2015 change | |
|---|---|---|---|---|---|---|---|
| **NLB** | 25.6% | -0.8pp | 8.7 | 26.2% | -0.9pp | 23.3% | +0.3pp |
| **Abanka** | 9.2% | +4.1pp | 3.8 | 11.8% | +3.9pp | 10.2% | +3.5pp |
| **NKBM** | 7.6% | +0.2p | 3.6 | 10.4% | -0.2pp | 9.5% | +0.2pp |
| **SKB** | 8.6% | +0.4pp | 2.6 | 8.1% | +0.4pp | 6.8% | +0.3pp |
| **UniCredit** | 8.3% | +0.2pp | 2.5 | 7.6% | +1.7pp | 6.8% | +0.1pp |
| **Koper** | 8.0% | -0.1pp | 2.4 | 7.4% | -0.3pp | 6.1% | +0.2pp |
| **Sberbank** | 6.3% | +0.3pp | 1.9 | 4.6% | +0.3pp | 5.1% | +0.5pp |
| **Gorenjska** | 3.6% | -0.2pp | 1.5 | 4.6% | +0.1pp | 3.9% | +0.2pp |
| **HypoAlpe-Adria** | 4.9% | -0.2pp | 1.3 | 3.3% | -0.3pp | 3.6% | +0.1pp |
| **Sparkasse** | 4.1% | 0.0pp | 1.1 | 2.3% | +0.3pp | 2.9% | +0.2pp |
| **Total Market (EUR bn)** | 20.358[1] | | | **24.081** | | **37.414** | |

Retail

Corporate and others

Total volume/ breakdown not available

Assets (EUR bn)

**Note:** Based on unconsolidated annual reports.
Loans market share calculated based on net values.
[1] Non-financial loans incl. non-bank financial institutions
*Source: Bankscope, Annual Reports, Central Bank, Deloitte estimates*

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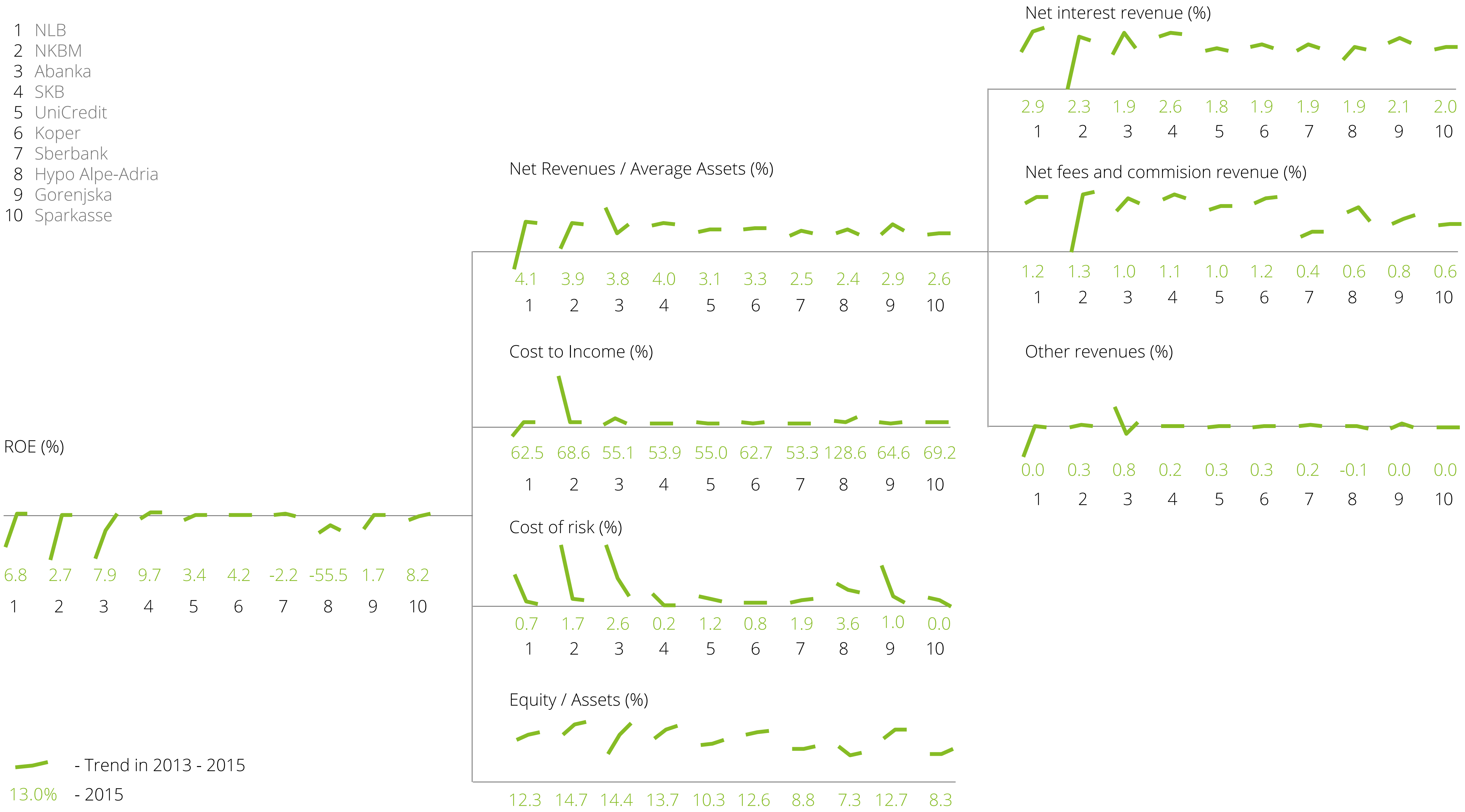
## Top 10 bank profitability drivers 2013-15




*Source: Bankscope*

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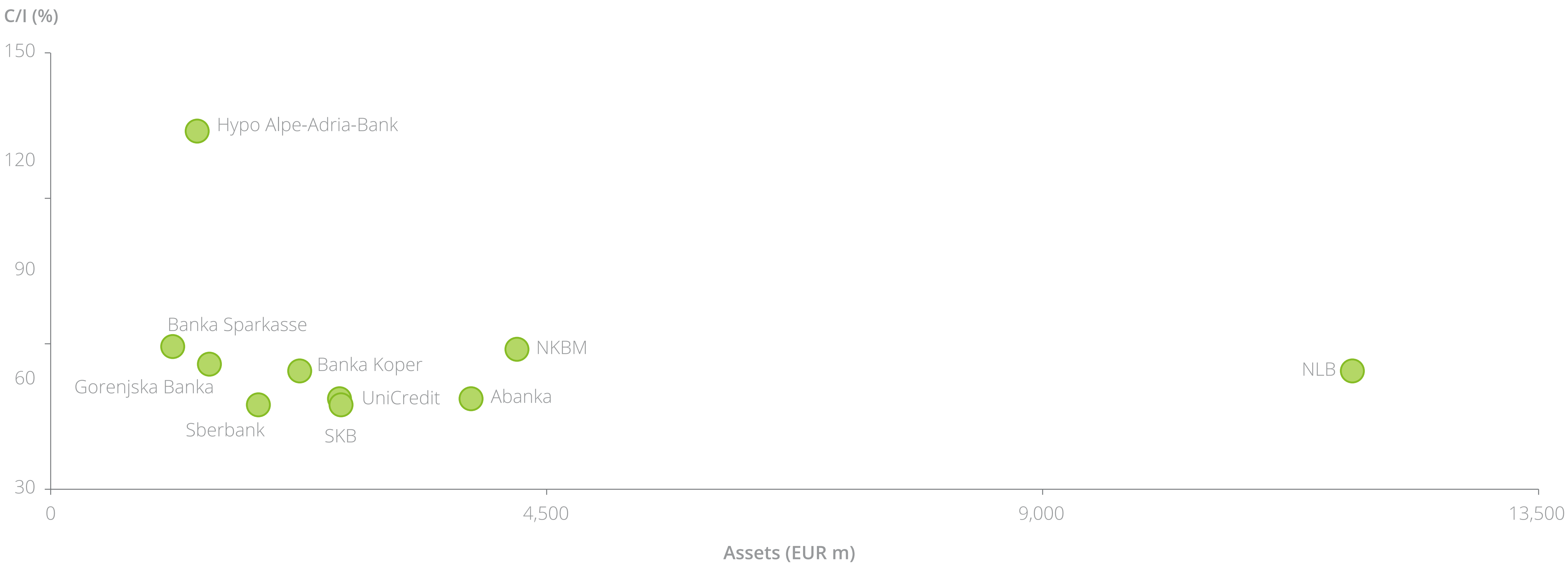
## C/I ratio versus assets, 2015




*Source: Bankscope*

# Strategy

## Need to improve operating efficiency is driving sector consolidation

Against a backdrop of ongoing margin compression, improving operating efficiency is a strategic priority, which is driving sector consolidation. After its merger with Banka Celje last year, Abanka will carry out a large scale restructuring. The new owner of NKBM (#3), Apollo Global Management, plans to merge it with Postna banka Slovenije and the KBS banka (formerly Raiffeisen Banka). Addiko Bank (former Hypo Alpe Adria Bank) owner Advent may also choose to grow via acquisitions, while the owners of Gorenjska banka (#8) have agreed to sell a controlling stake and Sberbank (#7) may be considering an exit. Investment in digitalization is another key to improving efficiency. Growth of digital channels will help facilitate further downsizing of branch networks and employment levels. At the same time, banks that are able to offer a better customer experience, with easier faster processes, will have an advantage in customer acquisition and growing sales volumes.

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# Digital Maturity

Slovenia is ranked last among CE countries in digital maturity (based on the overall score of its 5 biggest banks). Its banks are facing challenges, especially in the mobile channel, as many applications offer only very basic functionalities. One of its banks still doesn't have a native mobile application. As in many other countries, the Customer Journey perspective reveals that the digital functionalities responsible for information gathering and customer onboarding are the most advanced. However, the results in these areas are still below the CE average. Moreover, 3 out of 6 areas are least developed in Slovenia among the analyzed countries. Overdrafts and term deposits are the most digitalized products but similarly to the Customer Journey steps, they are also below CE standards.

*If you want to know detailed data for digital banking benchmarking, contact us.*

# Contact


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# We have analysed 76 banks in 8 CEE countries

## The Czech Republic

- Air Bank
- Ceska sporitelna
- Ceskoslovenska obchodni banka
- Equa bank
- ERA Banka
- Fio banka
- ING bank
- Komercni banka
- mBank
- Moneta Money Bank
- Raiffeisenbank
- Sberbank
- UniCredit Bank
- ZUNO bank

## Slovenia

- Abanka
- Banka Koper
- Gorenjska Banka
- Hypo Alpe Adria
- Nova kreditna banka Maribor
- Nova Ljubljanska Banka
- Sberbank
- SKB banka
- Unicredit

## Croatia

- Addiko bank
- Erste&Steiermarkische Bank
- Hrvatska Postanska Banka
- Privredna Banka Zagreb
- Raiffeisenbank
- Sberbank
- Splitska banka
- Zagrebacka banka


## Poland

- Alior Bank
- Bank BGZ BNP Paribas
- Bank Ochrony Srodowiska
- Bank BPH
- Bank Zachodni WBK
- Credit Agricole
- Citi Handlowy
- Deutsche Bank
- Getin Bank
- ING Group
- mBank
- Bank Millennium
- Bank Pekao
- Powszechna Kasa Oszczednosci Bank Polski
- Raiffeisen Polbank

## Bulgaria

- Allianz Bank Bulgaria
- Bulgarian American Credit Bank
- Eurobank
- Central Corporate Bank
- CIBANK
- DSK Bank
- First Investment
- Bank
- Municipal Bank
- Piraeus Bank
- Raiffeisenbank
- Societe Generale Expressbank
- United Bulgarian Bank
- Unicredit Bulbank

## Slovakia

- Ceskoslovenska Obchodna Banka
- OTP Banka Slovensko
- Postova banka
- Slovenska sporitelna
- Tatra Banka
- UniCredit Bank
- Vseobecna uverova banka

## Hungary

- Erste Bank
- Kereskedelmi es Hitelbank
- OTP Bank
- Raiffeisen Bank
- Unicredit

## Romania

- BCR
- BRD - Groupe Societe Generale
- Banca Transilvania
- ING Bank
- Raiffeisen Bank Romania

*If you want to know the place of your bank in the digital arms race, contact us.*

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# Methodology

The material presented in the report, analyzing economic and banking sector trends, is based on central bank and market data, as well as information from leading data providers such as EIU, and Bankscope. In the process of assessing the market outlook, we conducted a series of interviews with subject matter experts in each of the 8 CE markets covered in the report.

Digital Maturity Survey: Study performed on 76 banks from 8 CE markets, testing experience on public website, internet banking platform and mobile banking app with 3 proprietary Deloitte frameworks (perspectives of customer, bank, and segment).

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