Regulatory Reporting for Banks - 4th Annual Forum

Advocating Smart Compliance by Aligning Regulatory Reporting Requirements with Internal Risk Management Steering Expectations and Indicators

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ERSTE Group

⇨ Abstract

Smart Compliance is illustrated by a **clever implementation of Regulatory Requirements** in such a way as **to benefit Internal Risk Management Steering as well**.

While primarily **targeting the fulfilment of those requirements** to a large degree, **banks can leverage the corresponding tools and key indicators by integrating them in the existing Internal Risk Management Steering framework**.

Keeping in mind the increased focus and complexity of the regulatory governance exercised over the banking industry, the best approach to fulfil business targets within the limits enforced by Risk Appetite Statement, while still preserving the risk profile defined in the Risk Strategy, is to convey the aforementioned in an all-encompassing seasonal document.

⇨ Abstract

The subsequent presentation will consist of a rundown of the most **comprehensive internal risk steering report**, designed to satisfy the expectations of the stakeholders, from the Management Board to the Regulators.

⇨ Converging **multiple dimensions towards a holistic view** without adding unnecessary complexity:

- ✓ **Risk Cockpit**, as overview of the **bank's performance at a glance**
- ✓ **EBA risk dashboard** used for **benchmarking Erste's performance** vs. EU banking industry

⇨ Fulfilling the need to **synthesize information from different Risk areas** without getting bogged down in details:

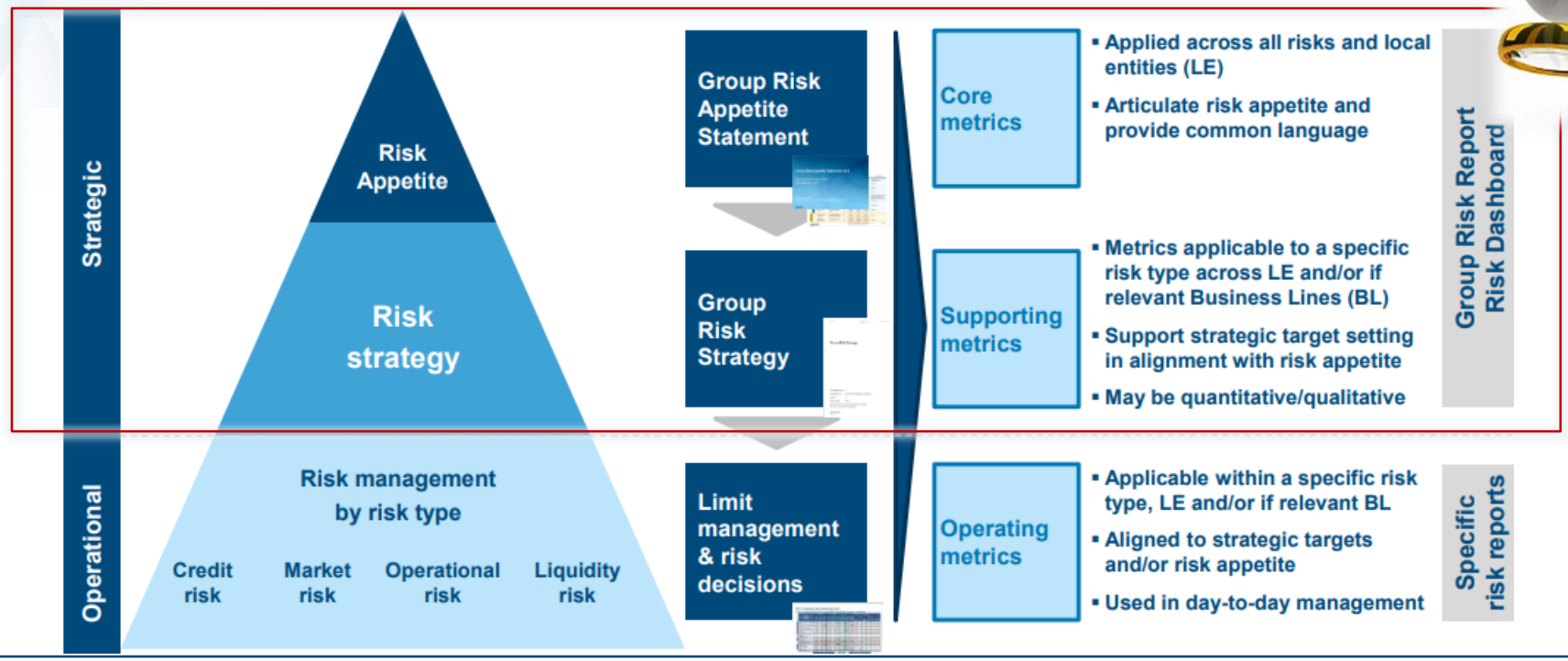
- ✓ Sections dedicated to Capital Adequacy, Credit Risk, Non-financial Risk, Market & Liquidity Risk, as well as to the monitoring of recovery thresholds
- ✓ Overview on how various regulatory requirements are implemented in terms of KRIs
- ✓ "Hot topics" highlighted in a dedicated "In Focus" section, emphasizing the most impactful events towards the Bank's profile

⇨ Serving as an **overarching framework** for **monitoring developments and outlook**, supporting targeted audience with a basis for educated decisions, extending up to **trigger/limit breaches** and subsequent mitigating actions.

Advocating Smart Compliance by Aligning Regulatory Reporting Requirements with Internal Risk Management Steering Expectations and Indicators (1/2)

⇨ Risk Monitoring Framework

- ✓ All the risks a bank is exposed to, along with the relevant exposures should be monitored on a continuous basis and managed on certain levels, such as: portfolio, organisational and risk type level
- ✓ Consequently, Erste Group's Risk Monitoring Framework consisting of both **strategic** and **operational** risk oversight as depicted in the picture below



Advocating Smart Compliance by Aligning Regulatory Reporting Requirements with Internal Risk Management Steering Expectations and Indicators (2/2)

⇨ Risk Monitoring Framework

In this presentation, the emphasis will be placed on **strategic oversight**, respectively:

- ✓ The **Risk Appetite Statement** (RAS) sets the **boundary for the maximum risk the bank is willing to accept** in order to pursue its **business objectives.** This includes a **set of core steering metrics** with **trigger levels** providing strategic guidelines for risk management and planning
- ✓ The **Risk Strategy** sets **strategic risk targets** based on the **target risk profile** and **RAS**, and provides a balanced **risk-return view** considering the strategic focus and business plans
- ✓ Both are **regularly monitored and reported** in the **Group Risk Report**, including a **traffic light** overview together with respective measures to address deviations from strategic plans or objectives identified. The Group Risk Report is presented and discussed in the Management Board, the Risk Committee of the Supervisory Board, as well as the Supervisory Board

Converging multiple dimensions towards a holistic view without adding unnecessary complexity (1/3)

⇨ **Risk Cockpit**, as overview of the **bank's performance at a glance** as follows:

Key Risk Indicators ~ KRIs:

⇨ **Capital Adequacy**
- ✓ Capital ratios - fully loaded: CET 1, Tier 1 and Solvency Ratios
- ✓ Economic Capital Adequacy
- ✓ Total RWA Pillar I

⇨ **Leverage** - Leverage Ratio

⇨ **Risk Return** - Risk Earnings Ratio

⇨ **Credit Risk**
- ✓ CR RWA Pillar 1 and Pillar 2
- ✓ Loans to Customers (GCA)
- ✓ Cost of Risk Ratio
- ✓ NPL Ratio and NPL Coverage Ratio
- ✓ Texas Ratio
- ✓ New Retail FX Lending

⇨ **Non-Financial Risk**
- ✓ OR RWA Pillar 1 and Pillar 2
- ✓ OR Losses (P&L based) + Litigations
- ✓ OR Loss Events

⇨ **Market Risk**
- ✓ MR RWA Pillar 1 and Pillar 2
- ✓ Δ EVE as % of Tier 1

⇨ **Liquidity Risk**
- ✓ SPA
- ✓ LCR; NSFR
- ✓ Structural Liquidity (mismatch >1Y, >2Ys, >3Ys)
- ✓ Intra-group Contagion Risk (>7Ds, >1Y)
- ✓ Asset Encumbrance Ratio

Converging multiple dimensions towards a holistic view without adding unnecessary complexity (2/3)

1 Management Summary and Risk Cockpit | 2 Capital Adequacy and RER | 3 Credit Risk | 4 Non-Financial Risk | 5 Market Risk | 6 Liquidity Risk | 7 Focus Topic | 8 Annexes and Glossary

Group Risk Report Q1 2019

Risk Cockpit

Quarterly development | Budget / Forecast | RAS / Risk Strategy | Recovery Plan | Status ~ RAG ~ traffic light

Key Risk Indicators		Unit	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	FC1-19	2019 Group RAS/ Group Risk Strategy	Group Recovery Plan	Overall Status
Capital Adequacy	CET 1 Ratio fully loaded	%	12.5%	12.5%	12.4%	13.5%	13.2%	14.3%	>12,7%	<12,2% (I) <8,8% (T)	G
	Tier1 ratio fully loaded	%	13,3%[5]	13.4%	13.3%	14.3%	14.4%	15.6%	>13,2%	<12,7% (I) <10,3% (T)	G
	Solvency Ratio fully loaded	%	17.5%	17.3%	17.1%	18.1%	18.2%	19.1%	>15,2%	<14,7% (I) <12,3% (T)	G
	Economic Capital Adequacy	%	59,1%[5]	59.5%	59.9%	59.2%	49.4%	58.3%	<83%	>95%	G
	Total RWA Pillar I	EUR bn	114.8	117.0	117.7	115.4	117.2	117.7	121,8 bn	-	G
Leverage	Leverage Ratio	%	6.3%	6.4%	6.3%	6.6%	6.6%	6.8%	>4%	<3.5% (I) <3% (T)	G
Risk Return	Risk Earnings Ratio	%	0.0%	0.0%	0.0%	0.0%	0.0%	3.2%	<30%	>60% (I) >80% (T)	G
Credit Risk	Credit Risk RWA Pillar 1[1]	EUR bn	91.1	93.1	93.5	94.0	94.6	96.4	<101,3	-	G
	Credit Risk RWA Pillar 2[3]	EUR bn	106.3	108.2	107.7	109.0	109.0	89.2	<171,2	-	G
	Loans to Customers (Gross)	EUR bn	146,0	148.5	152.0	152.8	155.4	160.7	-	-	G
	Cost of Risk Ratio[8]	b.p.	-21	-11	-8	-3	1	14	<66	-	G
	NPL Ratio	%	3.7%	3.6%	3.5%	3.2%	3.0%	3.0%	<4,3%	>5,3% (I) >8,0% (T)	G
	NPL Coverage Ratio[4]	%	73.0%	72.5%	71.1%	73.4%	74.5%	73.9%	-	-	G
	Texas Ratio	%	28.1%	27.9%	27.1%	24.5%	23.2%	n/a	-	-	G
	New Retail FX Lending (quarterly)	%	1.4%	1.3%	1.2%	2.1%	2.49%	n/a	<2,5%	-	G

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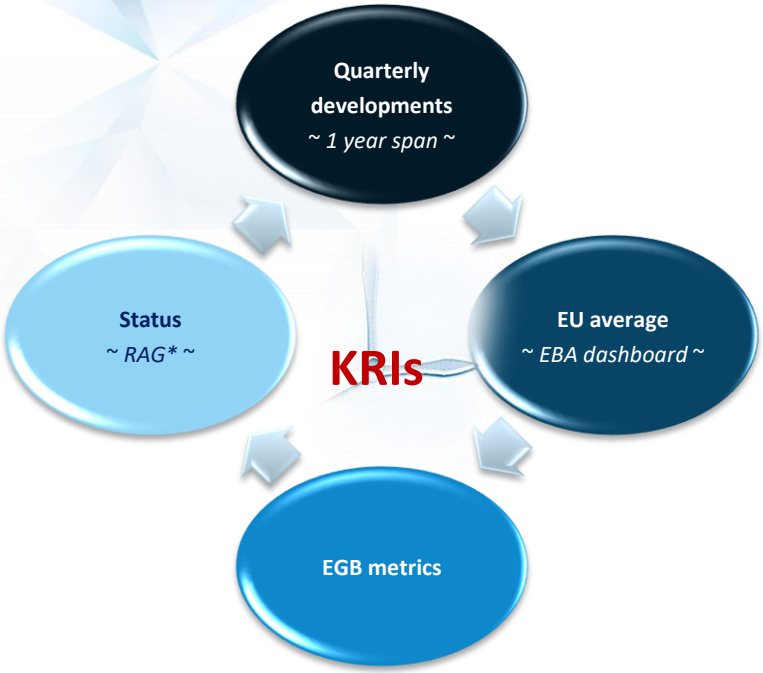
Converging multiple dimensions towards a holistic view without adding unnecessary complexity (3/3)

⇨ **EBA risk dashboard** used for **benchmarking Erste's performance** vs. European Union banking industry



KRIs in EBA focus:

- ⇨ CET 1 Ratio – fully loaded / transitional
- ⇨ Tier 1 Ratio
- ⇨ Solvency Ratio
- ⇨ Leverage Ratio
- ⇨ NPL Ratio
- ⇨ NPL Coverage Ratio
- ⇨ Liquidity Coverage Ratio
- ⇨ Asset Encumbrance Ratio

1 Management Summary and Risk Cockpit | 2 Capital Adequacy and REP | 3 Credit Risk | 4 Non-Financial Risk | 5 Market Risk | 6 Liquidity Risk | 7 Focus Topic | 8 Annexes and Glossary

Group Risk Report Q1 2019

Benchmarking EGB vs. EU - EBA Risk Dashboard

The EBA Risk Dashboard is part of the regular risk assessment conducted by the EBA and complements the Risk Assessment Report. The EBA Risk Dashboard summarizes the main risks and vulnerabilities in the banking sector in the European Union (EU) by looking at the evolution of Key Risk Indicators (KRIs) among a sample of 190 European banks across the EU

	Q1-18			Q2-18			Q3-18			Q4-18			Q1-19 *
KRIs in EBA focus	EU	EGB	Status	EU	EGB	Status	EU	EGB	Status	EU	EGB	Status	EGB
CET1 Ratio fully loaded	14.3%	12.5%	🔴	14.3%	12.5%	🔴	14.5%	12.4%	🔴	14.4%	13.5%	🔴	**13.2%**
of which CET1 ratio transitional	14.5%	12.6%	🔴	14.5%	12.6%	🔴	14.7%	12.5%	🔴	14.7%	13.5%	🔴	13.2%
Tier1 ratio fully loaded		13.3%			13.4%			13.3%			14.3%		**14.4%**
of which Tier1 ratio transitional	16.0%	13.4%	🔴	16.0%	13.5%	🔴	16.3%	13.4%	🔴	16.3%	14.4%	🔴	14.5%
Solvency Ratio fully loaded		17.5%			17.3%			17.1%			18.1%		**18.2%**
of which Solvency Ratio transitional	18.8%	17.6%	🔴	18.8%	17.4%	🔴	19.0%	17.2%	🔴	19.0%	18.2%	🔴	18.2%
Leverage Ratio	5.1%	6.3%	🟢	5.1%	6.4%	🟢	5.1%	6.3%	🟢	5.3%	6.6%	🟢	**6.6%**
NPL Ratio	3.8%	3.7%	🟢	3.6%	3.6%	🟡	3.4%	3.5%	🔴	3.2%	3.2%	🟡	**3.0%**
NPL Coverage Ratio		73.0%			72.5%			71.1%			73.4%		**74.5%**
NPL coverage with related CLA	46.7%	59.1%	🟢	46.0%	59.3%	🟢	45.7%	58.4%	🟢	45.1%	59.0%	🟢	**59.4%**
Liquidity Coverage Ratio	147.0%	149.0%	🟢	148.3%	148.0%	🔴	148.5%	139.4%	🔴	152.0%	150.3%	🔴	**151%**
Asset Encumbrance Ratio	28.4%	14.9%	🟢	28.0%	15.1%	🟢	28.7%	13.0%	🟢	28.0%	12.9%	🟢	**12.9%**

🟢 EGB displays **better** ratio than EU average
🟡 EGB displays **similar** ratio as EU average
🔴 EGB displays **lesser** ratio than EU average

* Due to the fact that EBA dashboard for Q1-19 is not yet published (expected in July 2019), only EGB figures are provided for Q1-19

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Status ~ RAG*:

- 🟢 EGB displays **better** ratio than EU average
- 🟡 EGB displays **similar** ratio as EU average
- 🔴 EGB displays **lesser** ratio than EU average

*RAG ~ Red, Amber, Green

Fulfilling the need to **synthesize information from different Risk areas** without getting bogged down in details (1/4)

⇨ Sections dedicated to Capital Adequacy, Credit Risk, Non-financial Risk, Market & Liquidity Risk, as well as to the monitoring of recovery indicators

Capital Adequacy and **RER:**

- ⇨ Pillar 1 - Regulatory Capital Adequacy - FL
  - ✓ CET1, AT1, T2 and RWA Pillar 1
  - ✓ Capital ratios: CET 1, Tier 1 & Solvency, including CST* results
- ⇨ Pillar 1 RWA – FL: CR, OpR, MR and Other Risks
- ⇨ Pillar 2 - Economic Capital Adequacy (ECA)
  - ✓ Coverage Potential
  - ✓ Economic Capital split on Credit, Market, Operational & Business Risk
  - ✓ ECA ratio, including Comprehensive Stress Test results
- ⇨ Pillar 2 RWA: CR, OpR, MR and Business Risks
- ⇨ Risk Earnings Ratio (RER)
  - ✓ Risk Cost
  - ✓ Credit risk related Income
  - ✓ RER

$$RER = \frac{Net\ Impairment\ Loss}{Credit\ risk\ related\ Income} * 100$$

- ⇨ Leverage Ratio
  - ✓ Leverage Exposure
  - ✓ Leverage ratio
- ⇨ ***Relevant aspects***
  - ✓ Drivers of significant developments and outlook
  - ✓ RAG and Mitigating Actions (if the case may be)
- ⇨ **Dimensions**

RAS / Risk Strategy limits & triggers

Budget / Forecast ~ Year End Metrics

Quarterly developments ~ 1 year span~

*Comprehensive Stress Test

Fulfilling the need to **synthesize information from different Risk areas** without getting bogged down in details (2/4)

⇨ Sections dedicated to Capital Adequacy, Credit Risk, Non-financial Risk, Market & Liquidity Risk, as well as to the monitoring of recovery indicators

Credit Risk:

⇨ Pillar 1 Credit RWA - FL
- ✓ Credit RWA, CCR, CVA, FL add-on

⇨ Pillar 2 Credit RWA - FL

⇨ Credit Risk Exposure / Loans to Customers (LtC) and Coverage
- ✓ Exposure / LtC (GCA as per IFRS 7)
- ✓ Provisions / CLAs
- ✓ Internal Collateral

⇨ Credit Risk Exposure / LtC - Portfolio Quality
- ✓ Risk Categories: Low Risk, Management Attention, Substandard & NPE
- ✓ NPE / NPL ratio & NPE / NPL coverage ratio
- ✓ NPE / NPL collateralization ratio

⇨ Credit Risk Exposure / LtC by Business Segment
- ✓ Retail, Corporates (*e.g. SME, LLC, PS, GLC, CRE*), Savings Banks & Other

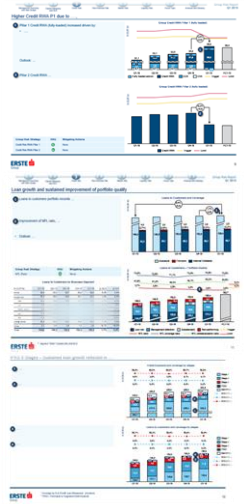
⇨ IFRS 9 Stages
- ✓ Credit Risk Exposure / LtC and coverage by stages (e.g. S1, S2, S3, POCI & non-IFRS 9)

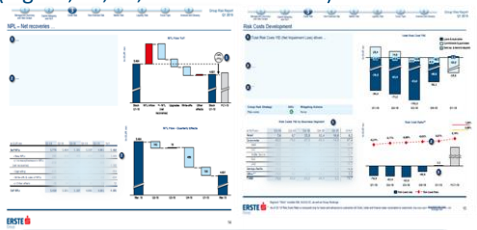
⇨ NPLs
- ✓ NPL flow QoQ, YoY, including quarterly effects
- ✓ NPL Sales
- ✓ NPL development by Entity

⇨ Risk Cost
- ✓ Total Risk Cost YtD
- ✓ Risk Cost Ratio
- ✓ Risk Cost by Business Segment

⇨ ***Relevant aspects***
- ✓ Drivers of significant developments and outlook
- ✓ RAG and Mitigating Actions (if the case may be)

⇨ **Dimensions** →





Fulfilling the need to **synthesize information from different Risk areas** without getting bogged down in details (3/4)

⇨ Sections dedicated to Capital Adequacy, Credit Risk, Non-financial Risk, Market & Liquidity Risk, as well as to the monitoring of recovery indicators

⇨ **Non-Financial Risk**
- ✓ Pillar 1 and Pillar 2 Operational Risk RWA split on AMA and BIA
- ✓ Loss volume by product
- ✓ Number of events by product
- ✓ KRIs (i.e. adequate, watch, attention) and number of RRDs (risk return decisions)

⇨ **Market Risk**
- ✓ Pillar 1 Market Risk TB RWA split on VaR, sVaR, Specific Risk STD, FX Risk STD & General Risk STD
- ✓ Pillar 2 Market Risk TB RWA split on VaR, Spread model, STD method
- ✓ Pillar 2 Market Risk BB RWA
- ✓ Δ EVE (Economic Value of Equity) as of Tier 1 (Tier 1, EVE/Parallel up)

⇨ **Liquidity Risk**
- ✓ SPA - Survival Period Analysis (all 6 scenarios, from 3Ms to 12Ms)
- ✓ LCR - Liquidity Coverage Ratio (HQLA, Net Liquidity Outflow, LCR Gap)
- ✓ NSFR - Net Stable Funding Ratio (Available SF, Required SF, NSFR Gap)
- ✓ Structural Liquidity Ratio (3 relevant time horizons: >1Y, >2Ys & >3Ys)
- ✓ Asset Encumbrance Ratio (Encumbered and Unencumbered Assets)
- ✓ Intra-group unsecured & secured Funding split on Resolution Groups in line with the MPE resolution strategy of Erste Group

⇨ **Focus Topic** - "hot topics" are highlighted in a dedicated "in focus" section, emphasizing the most impactful events towards the Bank's profile (e.g. expected overall improvements of CR RWA triggered by model changes during 2019, etc.)

⇨ ***Relevant aspects***
- ✓ Drivers of significant developments and outlook
- ✓ RAG and Mitigating Actions (if the case may be)

⇨ **Dimensions** →

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Fulfilling the need to **synthesize information from different Risk areas** without getting bogged down in details (4/4)

⇨ Sections dedicated to Capital Adequacy, Credit Risk, Non-financial Risk, Market & Liquidity Risk, as well as to the monitoring of recovery indicators

Recovery Indicators

- ✓ KRIs in focus
- ✓ Recovery red threshold & Recovery amber threshold
- ✓ Current period KRIs values & Status / mitigating actions (*if the case may be*)

Annexes & Glossary

⇨ **Credit Risk**

- ✓ Dedicated slide per Entity: Credit Risk Exposure and Coverage / LtC and Portfolio Quality / Risk Cost Ratio
- ✓ Forbearance exposure split on Performing and Non-performing, as well as on Entities
- ✓ FX Lending split on Retail, Corporates and Savings Banks, as well as on LCY and FX
- ✓ Repayment Vehicle Loans by
  - Risk Categories: Low Risk, Management Attention, Substandard & NPE
  - Business Lines & Entities, as well as portfolio development (*loans, collateral, provisions*)
- ✓ IFRS 7 figures (*exposure & LtC*) disclosed quarterly via Interim Report, breakdown by
  - Business segment and CCY; Business segment and risk category
  - Geographical segment and risk category
  - Region (*country of risk*) and risk category
  - Industry

- ✓ CCR (*counterparty credit risk*) and CVA (*credit value adjustments*) RWA Pillar 1 split on entities
- ✓ Top 10 single names / client groups by limits / MLL (*maximum lending limits*) per Corporates, Financial Institutions and Non-core Sovereigns

⇨ **Non-Financial Risk**

- ✓ High risk customers ratio & unacceptable clients
- ✓ Compliance metrics (e.g. personal account dealings, suspicious activity report, etc.)
- ✓ Security incidents; Customer phishing & Malware Infections

⇨ **Market & Liquidity Risk**

- ✓ Securities in Trading & Banking Book by Country and by Rating
- ✓ Interest Rate Sensitivities per Entity and per CCY
- ✓ NII Sensitivity

⇨ **Glossary**: indicator / abbreviation / definition - formula / reference

⇨ **Report Specification Details** in line with BCBS 239 requirements (*report owner, risk area, frequency, review and approved by, recipients, date of release, date of next release, source of data, distribution and confidentiality level*)

Serving as an **overarching framework for monitoring developments** and **outlook**

- **Overarching framework** for **monitoring developments and outlook**, supporting targeted audience with a basis for educated decisions, extending up to **trigger/limit breaches** and subsequent mitigating actions

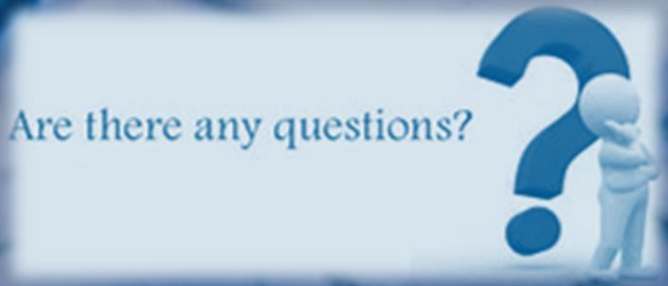
- Having in mind all dimensions encompassed at a glance in one single report, respectively:

Including the drivers of significant developments, as well as the outlook

Including the mitigating actions, if the case may be

We can conclude that the conferred Group Risk Report, designed to fulfill the elevated and partially contradicting expectations of all Erste Group stakeholders, should be considered as a comprehensive and intelligible risk steering report reinforcing the converging aspects of risk and business strategies & regulatory and risk management steering.

Thank you for your kind attention!



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