



COVID-19

# Industry Pulse Report: Banking

15 April 2020



## **COVID-19 Industry Pulse Report: Banking**

- ▶ What is the industry sentiment around the impact of COVID-19 on the Banking sector?
- ▶ How is COVID-19 expected to impact the Banking sector?
- ▶ What response measures have been taken to date to address the impact?



## Stelios Demetriou

Partner

Transaction Advisory Services Leader

### Foreword

“ The pandemic has caused global economic turmoil and has disrupted consumption and supply chains across the world.

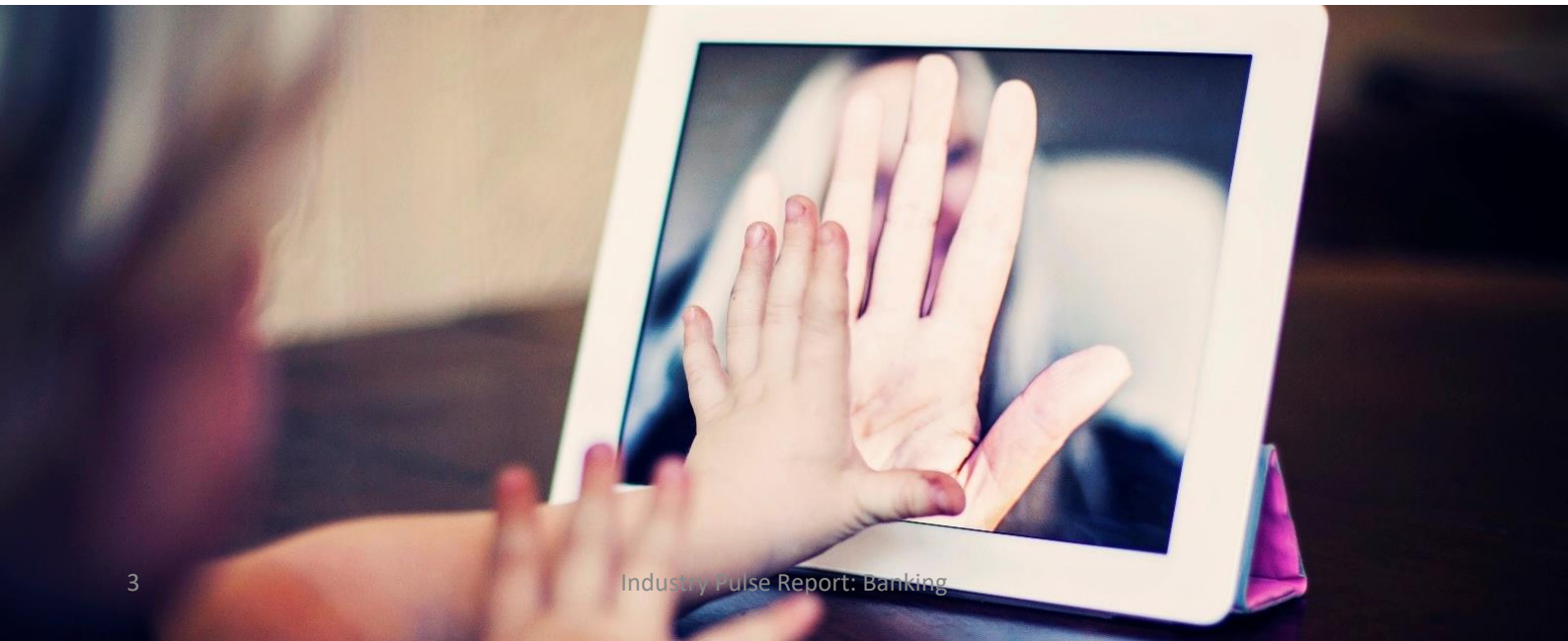
Cyprus is once again facing an immense challenge that is exacerbated by the global interconnectedness of its economy. The situation calls for ongoing monitoring to ensure proper understanding and sound decision-making.

At EY Cyprus, we have prepared three Industry Pulse reports for the Banking, Real Estate and Hospitality sectors. The reports aim to provide sector-specific perspective with regards to the impact of COVID-19, in conjunction with fiscal and monetary policy response, and include our own assessment of likely scenarios and trends. In this report, we focus on the Banking sector.

Our team has spoken with banking sector executives and leaders to obtain a realistic collective sense of their sentiment and expectations of this crisis, their views in relation to the response measures to date and their insights with regards to recovery scenarios and trends.

This publication will be updated periodically and shall incorporate the most updated publicly available information in relation to the impact of the virus on the aforementioned industries, the government and regulators' response actions as well as an updated economic assessment in accordance with our view.

We trust that this publication will become a reference document for discussion among stakeholders such as corporate executives, financial institutions and the government.



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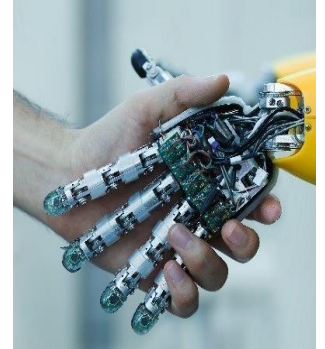


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# Executive Summary

The unprecedented humanitarian effect of the COVID-19 crisis comes along with a potential economic downturn. We are in uncharted territory that is beset with further shocks both to the local and the global economy, however what is clear is that the road to recovery will be an uphill one. Addressing a volatile situation like this requires coordinated actions across all levels and stakeholders. Banks will have a critical role to play as a conduit for liquidity into the economy.

It is noted that the rapid expansion of the outbreak may cause some of the perspectives in this report to quickly become out of date. This Pulse report reflects our perspective as of April 13, 2020; we aim to update the report regularly as the outbreak evolves, to capture the latest developments caused by the virus.

## Industry Sentiment - Key Takeaways of the EY Survey

EY has conducted a survey with regards to the potential impact of COVID-19 on the Cypriot Banking Sector. Key executives from the major Cypriot banks have been invited to provide their views, expectations and sentiment in relation to the impact of COVID-19 on various aspects of the banking operations and key financial metrics.

### View on key financial metrics

**New defaults and re-defaults** are expected to experience a modest increase in 2020, followed by a bigger uplift in 2021. It is anticipated that new defaults are mainly to arise from wholesale and retail trading, hospitality and RE construction portfolios. The supply chain effect is expected to increase unemployment and reduce household income, causing also defaults from individual borrowers.

**Loan losses** will increase, following a similar trend to new defaults in terms of timing. The level of provisions will be driven by the macro projections and the level of price adjustment in the real estate market.

**Interest income** will not be materially impacted in 2020 despite the moratorium. Low base rates driven at a European level as well as low margins to be driven by the potential application of the Government guarantee scheme are expected to impact interest income. However, **fee and commission income** is to be impacted in 2020 due to low economic activity. In 2021, interest income is likely to be impacted due to a wave of new defaults.

### View on Government measures to date

The view of Bank executives on the application of the **moratorium** on loan payments and the fiscal stimulus package was positive overall.

However, concerns are raised though around the final clauses of the **guarantee scheme** and whether it will allow the quick and effective transmission of funds to the real economy.

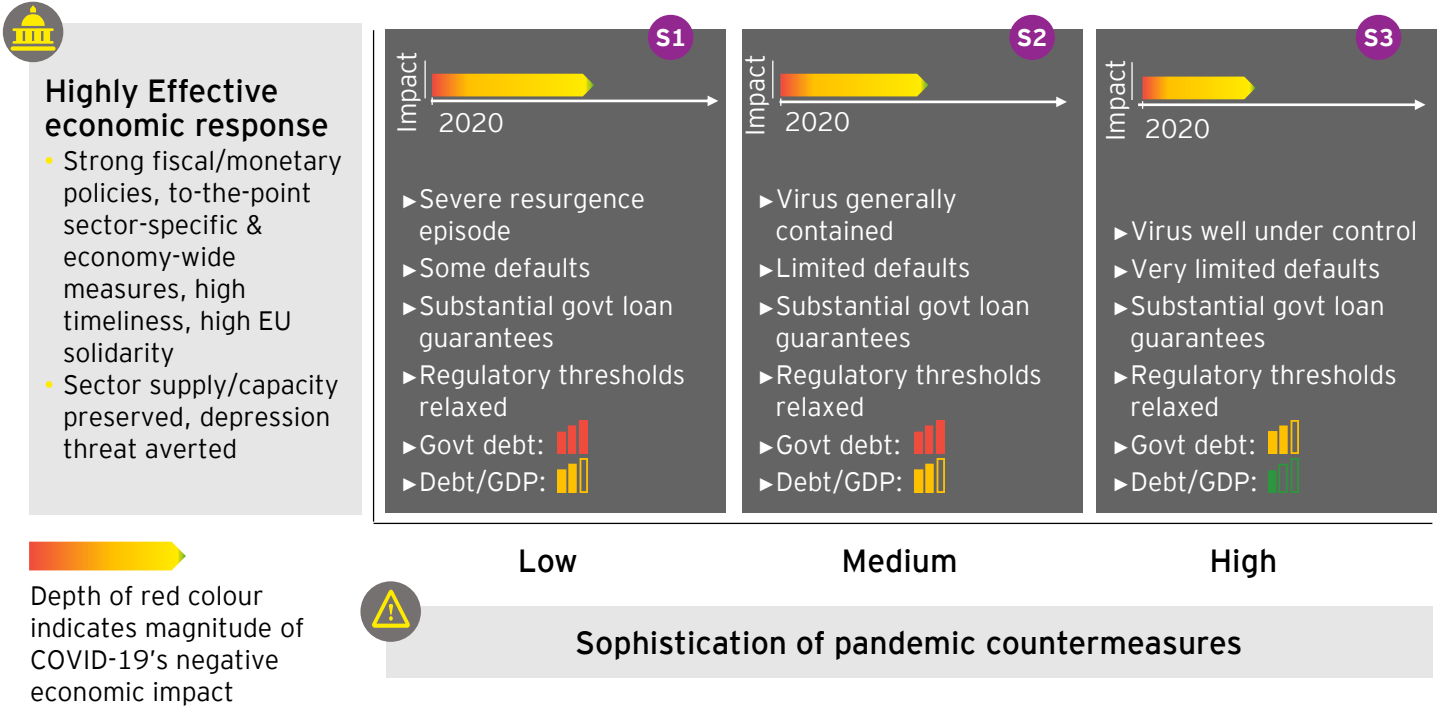
### Update on operational aspects

Usage of digital apps and credit card subscriptions	2x	since mid-March
Visits to branches	-50%	since mid-March
Employees working remotely	50%	since lockdown



# Executive Summary (cont'd)

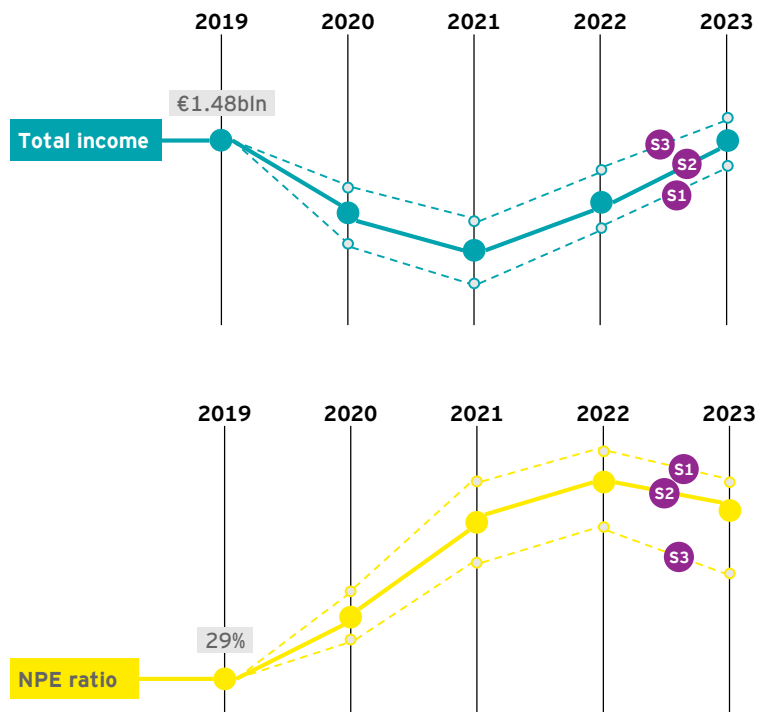
## Scenario Analysis for the Impact of COVID-19 on the Banking Sector



## Expected Impact of COVID-19 on key banking metrics

Banking is one of the few sectors of the economy that attracted immediate intervention by the Regulators and the Government through sector-specific measures. Taking into account the results of the EY Survey, we have analysed the shape of the curves for key banking metrics that we foresee to occur in the coming years.

- The **total income** in the banking sector is expected to follow a U-shape over the next 4 years, mainly driven by low interest rates (base and margin), the reduced fee and commission income expected in 2020 and a wave of new defaults likely to arise from 2021.
- The impact of reduced income is anticipated to increase the **Cost to Income ratio** since any attempts to reduce costs will not adequately cover for the expected lost income, at least in the first years. For the expected curve shape of cost to income, please refer to section "Impact of COVID-19 on the Banking Sector: Scenario Analysis" of this report.
- The **NPE ratio** is expected to rise in 2021 mainly, while it is anticipated to follow an inverted U-shape curve with longer recovery period than 4 years prior to returning back to 2019 levels.
- The expectation is that **loan losses** will increase as a result of the NPE increase, following an inverted V-shape, reaching a peak in 2021. Post 2021, loan losses are anticipated to follow a decreasing trend. For the expected curve shape of loan losses, please refer to section "Impact of COVID-19 on the Banking Sector: Scenario Analysis" of this report.

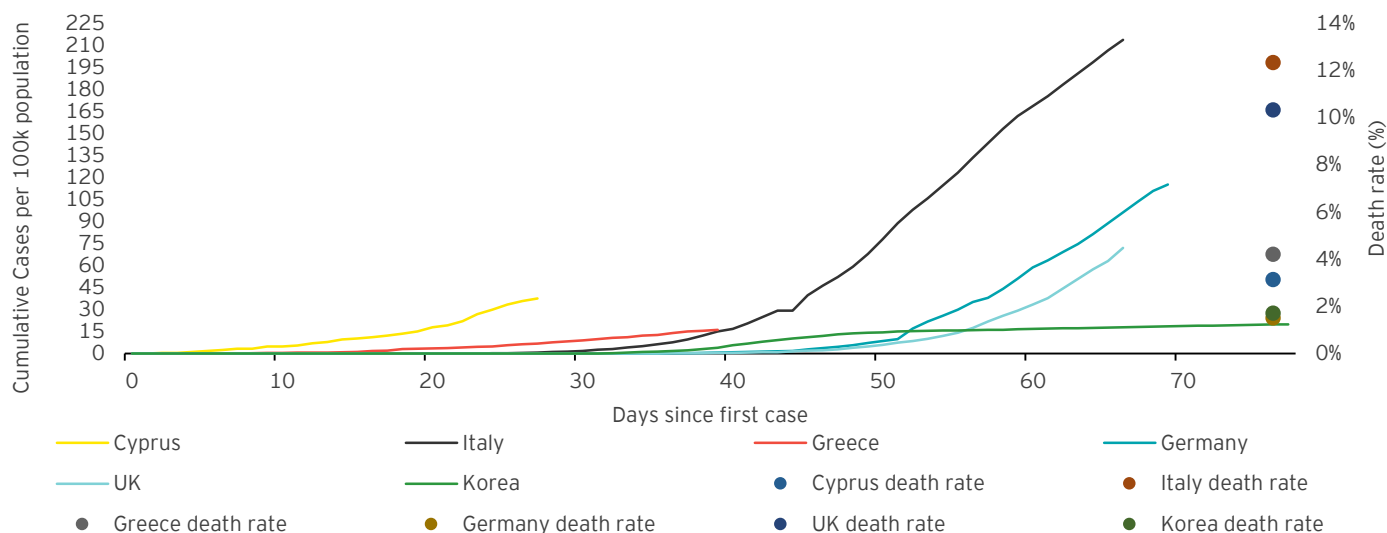


# COVID-19 Key facts & figures

## Introduction

The objective of the Industry Pulse report is to:

- ▶ Present a snapshot of the latest facts, figures, discussions and the industry sentiment around COVID-19
- ▶ Obtain the industry sentiment around the impact of COVID-19 on the Banking sector
- ▶ Estimate the potential impact of COVID-19 on the given sector
- ▶ Discuss effective fiscal and monetary measures for mitigating the adverse potential effects



## Governments' reaction

In response to the rapid spread of the virus to date (depicted in the adjacent graph) governments across the globe have adopted health-centric measures based on World Health Organisation's guidance<sup>1</sup>, with the aim to control the human-to-human transmission of the virus, and care for those affected. The measures focused on the below:

- ▶ Support the healthcare system through investment in necessary equipment & staff, protect health workers safety, ensure critical care of non-virus-related incidents;
- ▶ Enforcement of social distancing, closures of school & public spaces, lockdown, curfew, quarantine;
- ▶ Control points of entry into country, through strict border or travel bans;
- ▶ Contact tracing to identify cases, surveillance and monitoring of the spread;
- ▶ Testing ability, prepare capacity of national and private laboratories for rapid and reliable tests.

Health

The introduction of these health measures has necessitated the consideration of unprecedented fiscal and monetary interventions to limit the anticipated economic downturn<sup>2</sup>:

- |          |   |         |
|----------|---|---------|
| Fiscal   | <ul style="list-style-type: none"> <li>▶ Households: Income subsidisation and job guarantees, tax breaks, VAT reductions, extension of loan obligations and suspension of instalments.</li> <li>▶ Businesses: Salary payments to employees, suspension of financial obligations, favourable loan terms, tax breaks, deferral of VAT payments as well as sector-specific measures.</li> </ul>  | Economy |
| Monetary | <ul style="list-style-type: none"> <li>▶ ECB monetary support to governments such as additional asset purchases of €120bln until end-2020, an additional €750bln asset purchase program of private and public sector securities (Pandemic Emergency Purchase Programme), removal of issuer limits from bond-buying programs to allow central banks to push borrowing costs down, relaxation of collateral standards for Eurosystem refinancing operations.</li> <li>▶ ECB to facilitate banks' provision of the necessary liquidity to borrowers, temporary relaxation of: Pillar 2 Guidance and liquidity coverage ratio, as well as flexibility in classification requirements and expectations on loss provisioning for non-performing loans that are covered by public guarantees.</li> <li>▶ EU finance ministers have agreed on €540bln package of measures to support governments as they take on unprecedented debt burden: €100bln for joint employment insurance fund, €200bln for liquidity to companies through European Investment Bank instrument and €240bln for credit lines from European Stability Mechanism<sup>3</sup>. Possibility of an additional temporary fund to help hardest-hit economies and discussion of option for joint sovereign debt issuance (corona bonds).</li> </ul> |         |

1. <https://www.who.int/emergencies/diseases/novel-coronavirus-2019/technical-guidance>  
 2. <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19>  
 3. <https://www.bloomberg.com/news/articles/2020-04-09/eu-finance-chiefs-agree-on-590-bln-virus-rescue-package>

# COVID-19 Key facts & figures

## Wider implications of COVID-19

The social and economic ramifications in the aftermath of the pandemic are expected to be severe and widespread. These will likely include:

- ▶ Decline in consumption
- ▶ Drop in investment
- ▶ Structural changes as affected sectors shrink
- ▶ Spike in unemployment
- ▶ Potential banking crisis
- ▶ Overleverage as debt to GDP ratio spirals
- ▶ Sustained burden on the healthcare system
- ▶ Long-term loss in productivity
- ▶ Poverty increase
- ▶ Increased digitalisation

According to the latest worldwide research and discussions, expected timeframes for key medical solutions are:

- ▶ **Vaccination: 12-18 months**
- ▶ **Drugs/cure: 6 months ++ (timing highly uncertain)**
- ▶ **Antigen (polymerase chain reaction "PCR") tests that are cheap, mass-scalable and reliable : 1-3 months**
- ▶ **Antibody (immunity) tests that are cheap, mass-scalable and reliable : 1-3 months**





# Overview of the Banking sector

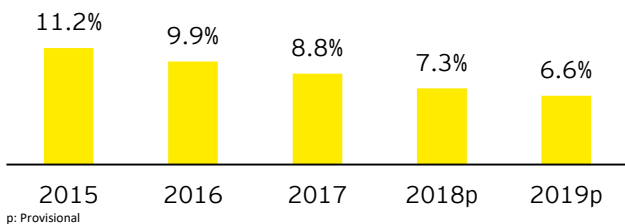
## Recent past performance (1/2)

COVID-19's impact is spreading relentlessly throughout the society causing health, social and economic pain affecting most, if not all, sectors and industries. This pandemic threatens to halt the overall macroeconomic growth of Cyprus and puts at risk significant improvements achieved in the banking sector over the last few years. Key indicators for the banking sector's historical performance are presented in this section.

### Contribution of the banking sector in the economy

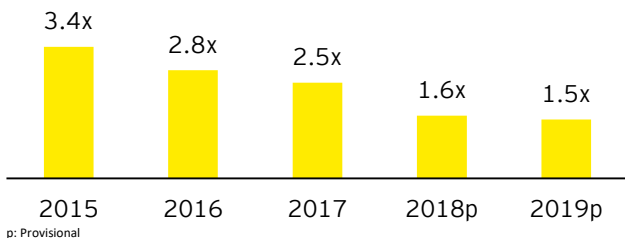
- ▶ Financial and insurance activities made up 6.63% of the GDP in 2019 (provisional results), compared to 11.2% in 2015. This is mainly attributed to a contraction of the banking sector due to deleveraging of problematic loans.
- ▶ According to CyStat, c.65% of the Financial and insurance activities is attributed to Banking.

Financial and insurance activities % of GDP



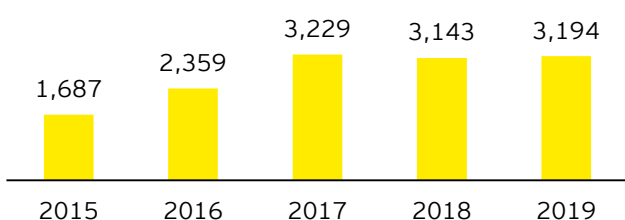
- ▶ In 2015, the domestic debt level stood at 3.4 times the GDP, signifying the over-leveraged state of corporates and households in Cyprus.
- ▶ Deleveraging decreased domestic debt to a more viable, healthy and sustainable level of 1.5 times the GDP in 2019, which is closer to the EU average of 1.4 times.

Domestic Debt to GDP



- ▶ Despite the contraction of the banking sector, new lending has been growing since 2015, driving the wider economic growth.
- ▶ Annual new lending jumped from €1.7bln in 2015 to €3.2bln in 2017. However, new lending has remained relatively stable since 2017 when it reached €3.2bln.

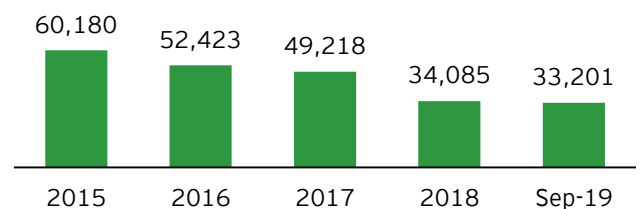
New lending (€mln)



### Financial and Capital position of the sector

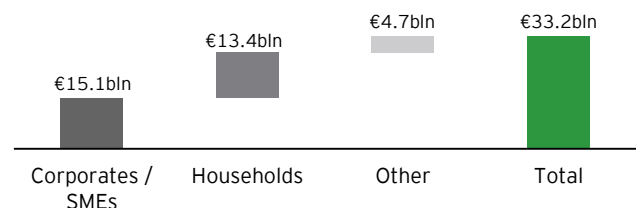
- ▶ Gross loans and advances to customers reduced by 45% from 2015 to September 2019, which was primarily driven by the resolution of NPLs. Although a large portion of the NPLs has been carved out of the banking sector, these loans still remain in the economy under the ownership of asset managers.

Gross Loans to Customers (€mln)

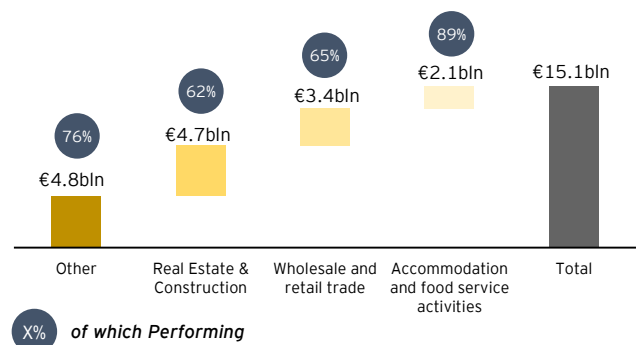


- ▶ Corporate and SME loans comprise the largest part (45%) of the Cypriot loan portfolio, followed by Household loans (41%).
- ▶ Out of the €33.2bln of gross loans as at 30 Sep-19, €15.1bln relate to Corporate and SME loans and €13.4bln relate to households (housing and other commercial loans).
- ▶ 68% of the Corporate and SME loans belong to borrowers operating in the 3 industries that are expected to be impacted the most during the COVID-19 crisis, namely Wholesale and Retail Trade, Real Estate and Construction, Accommodation and food service activities.

Breakdown of Gross Loans



Breakdown of Corporate / SME loans

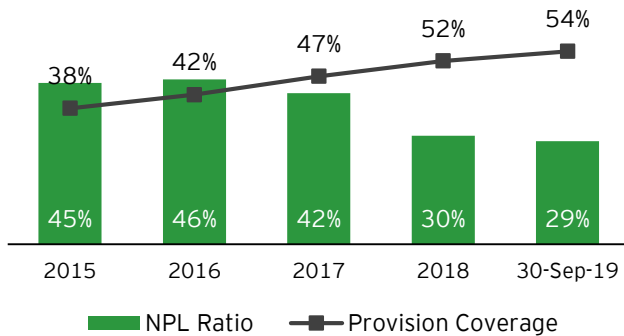


# Overview of the Banking sector

## Recent past performance (2/2)

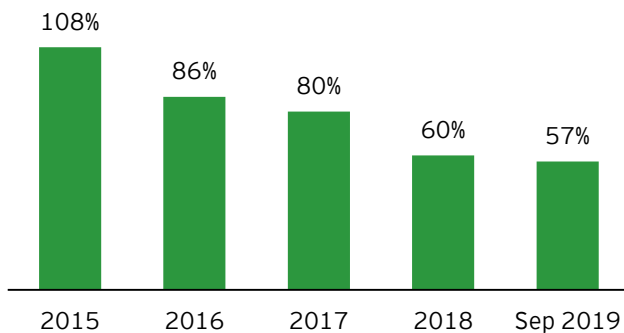
- ▶ The NPL ratio dropped from 45% in 2015 to 29% by September 2019. This reduction has been driven by the carve out and/or sale of NPLs to institutions operating outside of the banking sector.
- ▶ Provision coverage increased from 38% in 2015 to 54% by September 2019. Banks have been building their provision stock by utilising much of their operating profitability.

NPL ratio and Provision coverage



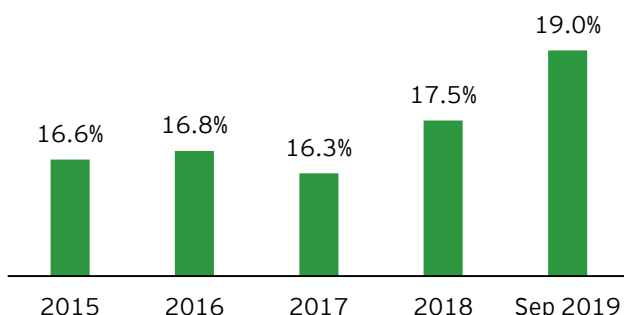
- ▶ Currently, there is excess liquidity in the sector, which is also evident from low Net loans to deposit ratio (57% as at Sep-19) as shown below.

Net loans to deposits



- ▶ In terms of capitalisation, the Cypriot banks have attracted fresh capital from investors since 2014 and, despite the big losses incurred due to heavy provisioning, they have managed to increase their capital adequacy ratio by 2.7% since 2015, reaching 19% in September 2019.

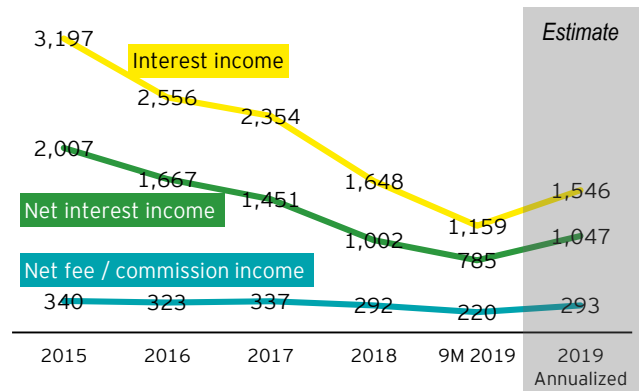
Capital Adequacy Ratio



### Financial performance of the sector

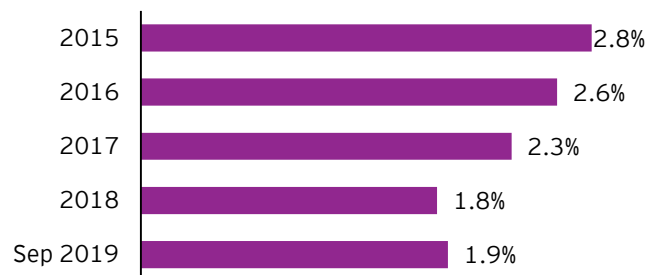
- ▶ Interest income decreased by 52% since 2015, driven by the high NPL stock which resulted in interest restriction. Consequently, net interest income decreased by 48% over the last 5 years. Net fee & commissions experienced a lower reduction of 14% since 2015.

Income (€mln)



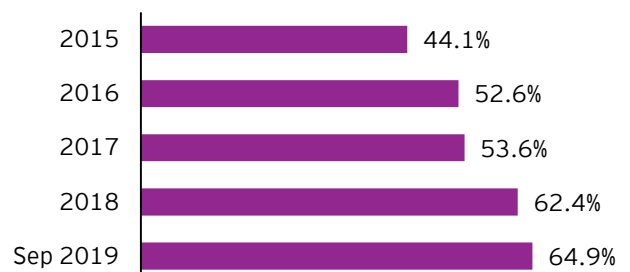
- ▶ Net interest margin stood at 1.9% as at September 2019 compared to 2.8% in 2015, mainly due to the decrease in interest income. Note that the EU Average NIM is equal to 1.43%

Net Interest Margin



- ▶ Cost to income ratio has increased in the past recent years, reaching 62.4% by September 2019. This is mainly a result of the reduction in interest income. Although the banks have attempted to reduce costs, this has been achieved to some extent and at a slower rate than income reduction to date.

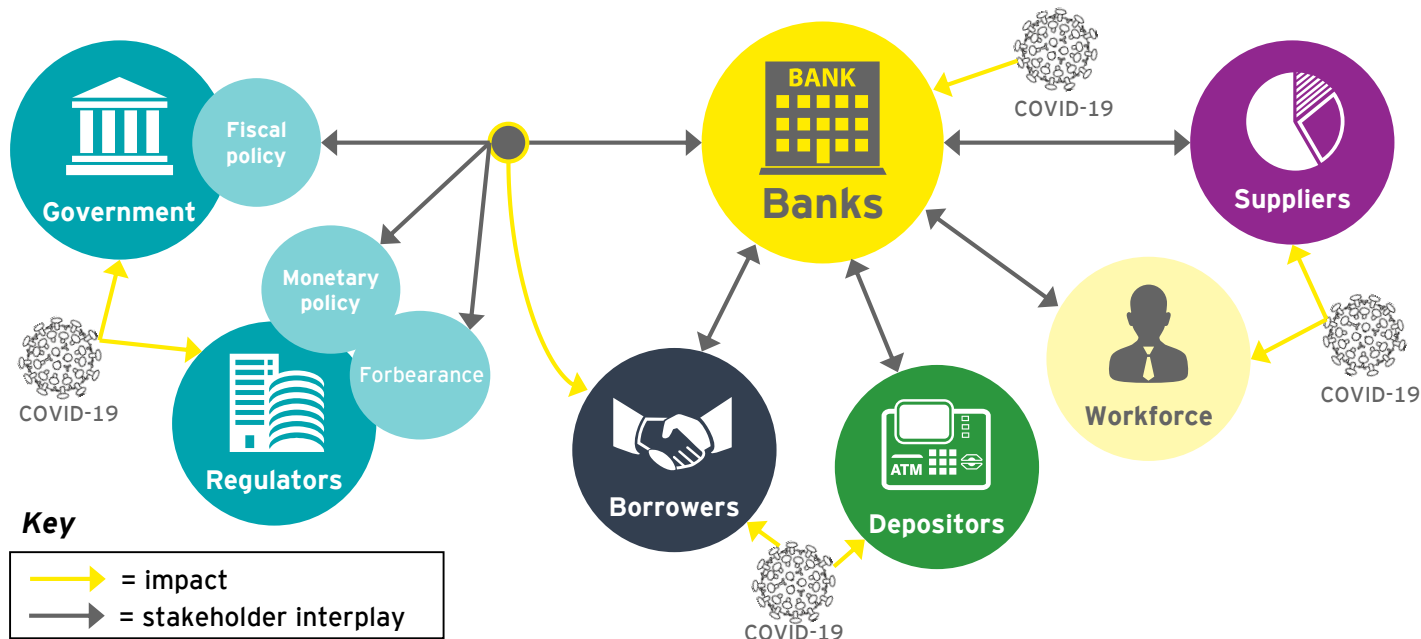
Cost to Income



# Banking sector stakeholder map and COVID-19 Impact

The banking sector stakeholder map covers a wide and diverse part of the economy and society. Banks are at the core of the real economy, by virtue of their role as the means of transmission of the Government's stimulus package and the link between fiscal and monetary policy. The customer base of the sector (borrowers and depositors) comprises the majority of the country's population.

The below map and explanatory notes present the impact of COVID-19 on each stakeholder, summarise the interplay and connectivity between stakeholders and the banks, and capture their main reactions in response to the crisis.



### Government

**COVID-19 impact**

- Operational disruption across the Government sector
- Limited availability of services (e.g. LRO, Tax)
- Compelled to secure the economy from potential collapse and deploy pandemic countermeasures

**Reaction**

- Suspended activity for many consumer-facing businesses
- Moratorium on debt payments
- Loan guarantee scheme (pending law to be voted)

### Banks

**COVID-19 impact**

- Increase in defaults / higher loan losses
- Reduced income and profitability
- Minimal loan repayments
- Postponement of NPL trades

**Reaction**

- Support performing borrowers survive the crisis through forbearance and liquidity injections
- Application of debt moratorium
- Transmission of stimulus package to the economy
- Cost-cutting initiatives

### Depositors

**COVID-19 impact**

- Rise in unemployment / loss of income
- Increased fear for face to face interaction

**Reaction**

- Avoid visiting bank branches
- Usage of digital banking services

### Suppliers (e.g. consultants)

**COVID-19 impact**

- Remote working creates inefficiencies
- Cutbacks on non-critical suppliers

**Reaction**

- Alternative service offerings relating to the impact of COVID-19
- Assistance with handling the substantial application volume for moratorium and guarantee schemes

### Regulators

**COVID-19 impact**

- Regulatory focus redirected towards the application of monetary policy for overcoming the crisis

**Reaction**

- Guidance on application of IFRS 9 during the COVID-19 crisis
- Allowance to operate below regulatory minimum capital and liquidity levels
- Reduction of interest rates

### Borrowers

**COVID-19 impact**

- Rise in unemployment / loss of income for households
- Liquidity issues for many businesses and viability concerns for others
- Need for liquidity support

**Reaction**

- Apply for moratorium of debt payments and for the Government guarantee scheme
- Request restructuring / forbearance
- Greater utilization of digital banking services

### Workforce

**COVID-19 impact**

- Possible own or family health issues / health & safety concerns for those unable to work remotely
- Operational slowdown and inefficiencies due to remote working
- Job security fear due to market uncertainty

**Reaction**







- Quick adaptation to remote working
- Utilisation of parental leave allowance

Further details on the measures and guidance announced by Governments and Regulators are described in the following pages.

# Measures and guidance announced by Governments and Regulators

European authorities and regulatory bodies, both at a local and supranational level, are also effecting change by announcing a series of guidelines and directives. The effort is to mitigate the impact of the virus on the wider economy, while at the same time governments have introduced measures to support local economies.

Examples of such measures and policies are briefly outlined below.

	<ul style="list-style-type: none"><li>▶ The European Commission has established a Temporary Framework that provides subsidized public loans to companies, state guarantees for bank loans to companies, safeguards for banks that channel state aid to the real economy etc.</li><li>▶ ECB announced a €750bn Pandemic Emergency Purchase Programme for the purchase of private and public sector securities.</li></ul>		<ul style="list-style-type: none"><li>▶ Establishment of the Economic Stabilization Fund which will, amongst other things, provide guarantees of up to €400bn and participate in the recapitalization of companies up to €100bn.</li></ul>
	<ul style="list-style-type: none"><li>▶ Introduction of an emergency decree of more than €400bn worth of liquidity and bank loans to companies hit by the coronavirus crisis.</li><li>▶ Government-backed loans of up to €340bn.</li></ul>		<ul style="list-style-type: none"><li>▶ Provision of £330bn government backed loans.</li><li>▶ The Monetary Policy Committee voted for a cut of 50 basis points of the Bank's base rate, reducing it to 0.25%.</li></ul>
	<ul style="list-style-type: none"><li>▶ Moratorium for the suspension of mortgage payments and accrual of ordinary and default interest.</li></ul>		<ul style="list-style-type: none"><li>▶ Aid package amounting to €6.8bn which includes a €800 benefit for 1.7 million private-sector employees who have been suspended from their employment contracts.</li><li>▶ The European Commission has approved a €2bn scheme to support the Greek economy, in the form of loan guarantees.</li></ul>



## Cyprus Government measures

Following the response at a European level, the Government of the Republic of Cyprus has also taken measures to help the local economy.

### **Moratorium for the suspension of loan payments**

On the 30<sup>th</sup> of March, the Minister of Finance announced the application of a moratorium under the issuance of a Decree, for the suspension of loan payments, the details of which are outlined below:

- ▶ The moratorium provides for the suspension of loan payments, including interest, of credit facilities granted and/or purchased and/or managed by financial institutions.
- ▶ The beneficiaries are natural persons, legal persons governed by public law, self-employed persons and businesses who had no more than 30 days of delay in paying their installments from the date provided for by existing contractual obligations as at 29 February 2020 and who have been adversely impacted in a financial manner by the pandemic.
- ▶ The moratorium is valid from the 30<sup>th</sup> of March 2020 and up to the 31<sup>st</sup> of December 2020 (9 months).
- ▶ The suspension of installments and interest shall apply from the 30<sup>th</sup> of March, provided that beneficiaries send the expression of interest form in writing or by mail or by e-mail or fax to the financial institutions as set out in the Annex to the relevant Decree.
- ▶ Financial institutions do not have the right to reject the form expressing interest submitted by the beneficiaries (unless the interested party does not meet the no more than 30 days delay criterion).
- ▶ The total of interest amount which will be suspended will be added to the loan balance at the termination date of the Decree and the total capital and interest amount suspended will not become immediately payable, unless the beneficiary and the financial institution agree otherwise.
- ▶ All other terms of the facility agreement apart from the repayment clause, as well as all collateral documents will continue be in force both during and post the payment suspension period.
- ▶ On the expiry date of the decree, the payment of installments and interest shall resume and the period of payment shall be deemed to have been automatically extended for any period required.

# Measures and guidance announced by Governments and Regulators (cont'd)

- ▶ If the beneficiary wishes, they can make any voluntarily payments for any amount that would be a part of their repayment schedule (under the facility agreement) if the Decree had not been enforced.
- ▶ Under no circumstances is the non payment of instalments during the suspension period a breach of the credit facility agreement between the beneficiary and the financial institution.
- ▶ The obligation for the submission of personal wealth/financial statements for the year ended 2019 of self-employed individuals and businesses eligible for the suspension of their loan payments, is suspended provided that a written request to the financial institutions is made.
- ▶ For new lending requests, all guidelines issued or any that will be issued by the Central Bank of Cyprus apply.

## Government Guarantee Scheme

The Government has proposed a guarantee scheme which is still pending to be voted by the Parliament. According to the latest version shared, the government will provide guarantees of up to €2bln to licensed credit institutions with the aim to:

- 1** Provide new lending to businesses and self-employed individuals affected by COVID-19 and the measures taken in response to COVID-19 (e.g. suspension of operations etc.); €1.75 bln
- 2** Subsidize part of the interest on performing loans of individuals, self-employed persons and businesses, according to criteria that will be set by Decree of the Minister of Finance; €250 mln
- 3** Government guarantees are to be provided for a period of no less than 3 months and no more than 6 years;
- 4** Any losses arising from new loans (secured or unsecured) given as part of the scheme will be borne by up to 70% by the Government and 30% by the credit institutions;
- 5** The beneficiaries include businesses, self-employed individuals with no financial difficulties as at the 31st of December 2019 and who had no more than 30 days of delay in paying their installments in accordance with the facility agreements and have entered a state of financial distress due to COVID-19;
- 6** Credit institutions are to provide new loans to the beneficiaries for the purpose of covering their liquidity, working capital and investment needs.

- ▶ We highlight the importance of approving the Guarantee Scheme by the Parliament as it is vital for providing liquidity to the real economy.
- ▶ It is also critical for the Guarantee Scheme to be passed with the right clauses in order to maximise the financial support to the economy and allow for quick and effective transmission of the funds.

**Government guarantees will be granted in an effort to inject liquidity into the real economy and will not be utilized for the repayment of any existing credit facilities.**

Sources: Government / Ministry of Finance



# Measures and guidance announced by Governments and Regulators (cont'd)

## Guidelines by the Central Bank of Cyprus ("CBC")



CBC has announced a series of guidelines in an effort to support both businesses and households, some of which are outlined below:

- ▶ Provision of overdraft facilities and short-term funding with full bullet repayment at maturity to enable businesses and households to meet their current needs. These loans should be given out with no charges;
- ▶ Banks are encouraged to proceed with restructurings of existing loans for historically healthy borrowers that are now experiencing difficulties as a result of COVID-19 and provide low interest rates;
- ▶ Relaxation of requirements for the provision of loans.

Sources: CBC

- ▶ We have seen coordinated effort to date by the Government, targeting to transmit liquidity in the real economy, and such coordinated actions must continue until this target is achieved. The banking system has a vital role to play in the stimulus transmission.
- ▶ The EU has also made it clear that any state guarantees by national governments to support banks, would not be considered as state aid.
- ▶ Regulators have offered several forms of regulatory forbearance, including removal of Counter-Cyclical Buffers and deferral of stress tests, which will all help to provide the playing field on which banks can extend further credit.
- ▶ We have also seen welcome moves to scale back more routine regulatory interactions to allow firms to focus on supporting customers.
- ▶ It is essential that the stimulus is transmitted to corporates, SMEs and citizens through the banks, as it is the only way to transmit more funds quickly to boost and help the real economy.



# Measures and guidance announced by Governments and Regulators (cont'd)

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## Regulatory measures and guidance



EBA, ESMA and other regulatory authorities have released guidelines on how banks should handle loan classification under these extraordinary circumstances, aiming for a consistent handling of the situation.

COVID-19 is causing shortage of liquidity to the economy, due to the suspension of business operations. Supply chain effects transfer the liquidity shortage to households grinding the economy to a halt.

Consequently, the key question that the banks are called to answer is which of their borrowers are likely to face long-term viability issues and which will survive the crisis with credit-worthiness issues, or not survive the crisis. This is particularly important concerning the application of IFRS9 and their assessments of expected credit losses.



### **Forbearance**

EBA has set out a number of criteria that public moratoria affecting loan payments must fulfil so that they do not lead to a forbearance reclassification.

1. **Moratorium launched in response to COVID-19 announced and applied prior to 30 June 2020.**
2. **Moratorium is broadly applied** and does not impose a tailored-made solution.
3. **Moratorium has to apply to a broad range of obligors** and not be limited to a specific exposure class or product. However, it is acceptable when the moratorium relates only to performing borrowers with no previous signs of payment difficulties prior to its application. Conversely, moratoria limited to borrowers who were being closely monitored or had experienced difficulties with their payment schedules are deemed to lead to forbearance classification.
4. **The same moratorium offers the same conditions**, noting that while the same conditions have to be offered to all borrowers, it is possible that different moratoria apply to different segments of exposures.
5. **Moratorium changes only the schedule of payments and not other conditions of the loan** unless these aim to neutralize the impact on the net present value of the loan. It is important to note that, any public guarantees provided in response to COVID-19 as well and associated to the moratorium, are not considered to change any loan terms or conditions.
6. **Moratorium does not apply to new loans granted after its launch**, highlighting the fact that the use of existing credit lines or renewal of revolving loans is not categorized as a new loan.

Sources: European Commission, EBA, ESMA



# Measures and guidance announced by Governments and Regulators (cont'd)

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## **Default**

These moratoria will inevitably impact the 90 days past due criterion as delays are counted based on the modified schedule of payments. Assessments with regards to the borrower's unlikelihood to pay in deciding their performing status, should take into account the modified payment schedule.

EBA states that, in the case where institutions face a substantial number of individual assessments, they should prioritize their analysis according to their risk-based approach and special attention should be given to borrowers who experience delays on their new payment schedules.



## **IFRS 9 ECL**

IASB emphasizes on the fact that IFRS 9 is based on a set of principles that are not mechanistic and require judgement, EBA stresses that in concluding whether there has been a significant increase in credit risk, the total expected life of the exposure should be taken into account rather than focusing on short-term shocks.

Institutions are encouraged to give greater weight to long-term stable outlook evidenced by past experience when estimating long-term expected credit losses for the purposes of IFRS 9 provisioning policies.

Moreover, to avoid any overestimations of the impact of such shocks, risk assessments should distinguish between obligors not significantly affected in the long term (temporary liquidity constraints) from those that would be unlikely to restore their credit worthiness.

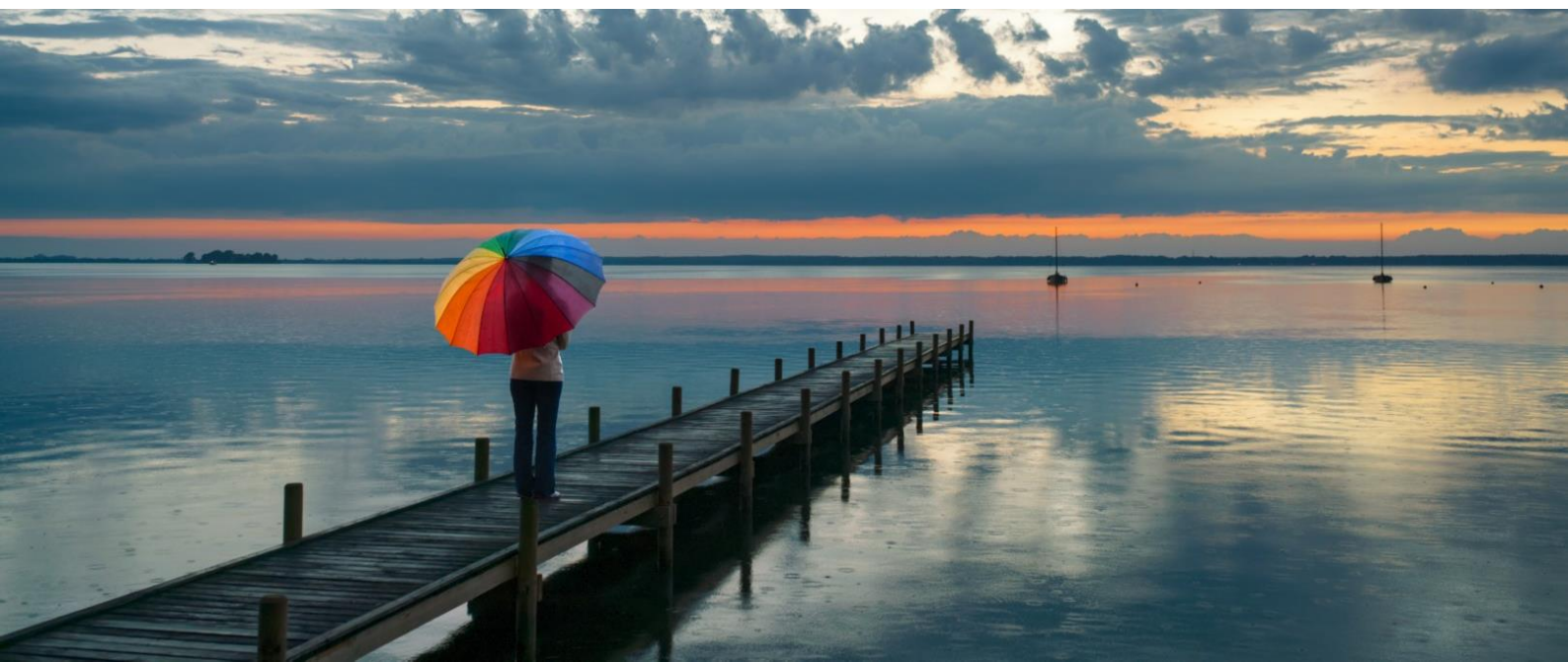


## **Relaxation of capital and liquidity buffers**

Apart from the aforementioned guidelines, regulatory bodies have also taken other measures to help banks continue to fulfil their role in funding the real economy as smoothly as possible. One major relief provided to European banks by the ECB is the relaxation of capital buffers. In its statement, ECB announced that:

- ▶ Banks will be allowed to operate temporarily below the level of capital defined by the Pillar 2 Guidance (P2G), the capital conservation buffer (CCB) and the liquidity coverage ratio (LCR).
- ▶ Banks will be allowed to partially use capital instruments that do not qualify as Common Equity Tier 1 (CET1) capital, for example Additional Tier 1 or Tier 2 instruments, to meet the Pillar 2 Requirements (P2R).

ECB highlights that: *"The above measures provide significant capital relief to banks in supporting the economy. Banks are expected to use the positive effects coming from these measures to support the economy and not to increase dividend distributions or variable remuneration."*





# COVID-19 impact on banks' capital and profitability

The coordinated approach of the Government and Regulators is expected to soften the impact of the COVID-19 crisis on the capital position and profitability of the banks.

The performing loan book is anticipated to experience the highest impact due to new defaults likely to arise. The income side is expected to reduce disproportionately compared to the cost base, which together with an increase in loan losses will impact profitability and the capital ratios. The below diagram describes the expected impact of the COVID-19 crisis on the key Balance Sheet and P&L line items of the banks, highlighting the impact on the performing loan book and on profitability.



An EY survey has been conducted with the aim to capture the views of bank executives for the impact of COVID on the banks' profitability and capital position, the results of which are described in detail on the following pages.

# Industry Sentiment

## EY Survey results

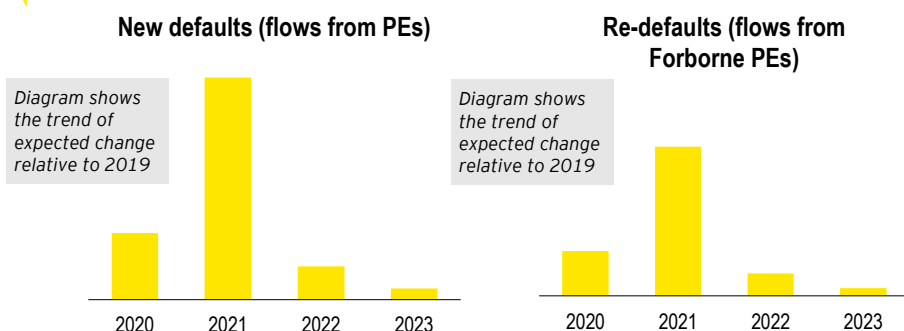
### Basis of the Survey

- ▶ EY has performed a survey during the period 6-13 April 2020, with regards to the potential impact of COVID-19 on the Cypriot Banking Sector.
- ▶ Key executives from the major Cypriot banks have participated and provided their views, expectations and sentiment in relation to the impact of COVID-19 on various aspects of the banking operations and key financial metrics.
- ▶ The areas covered during the EY Survey touched upon financial, asset quality, provisioning, liquidity, operational and strategy aspects. The results of the EY Survey are presented here.

## 1 Topic of discussion: Expectation of the COVID-19 impact on the banks' profitability, asset quality and liquidity in the short, medium and long term

### a New NPLs

#### Q What is the expectation for new defaults and re-defaults?



- ▶ Participants commented that, based on the Regulators' guidance for reporting new defaults in light of the COVID-19 crisis, the NPE inflow is likely to be deferred until after the 9-month moratorium.
- ▶ They unanimously agreed that defaults will mainly arise from borrowers who are unlikely to be able to restore their credit worthiness post the moratorium measures.
- ▶ They expect that NPEs will experience a modest increase in 2020, followed by a bigger jump in 2021.
- ▶ From 2022 onwards, no material defaults are expected.



“

*The most casualties are expected to arise from businesses that used to operate at thin margins and low equity levels. Restructuring those will be difficult and challenging.*

”

#### Q Which industries will drive the new defaults?

- ▶ Participants responded that the key industries to be affected the most and as a result drive the majority of new defaults and re-defaults are the Trading, Hospitality and Real Estate industries.
- ▶ Trading excludes consumer staples / FMCG businesses (e.g. supermarkets, pharmacies).



“

*Loans backed by operating assets which traditionally generated a strong revenue stream will likely return quickly back to normality after the crisis.*

”



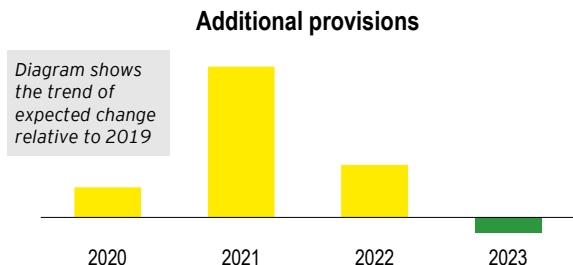
All participants agreed that the supply chain of each industry will also be impacted, leading to higher unemployment rates and reduced household income. As a result, they foresee that defaults in housing and consumer loans will rise.

# Industry Sentiment

## EY Survey results (cont'd)

### b Provisions

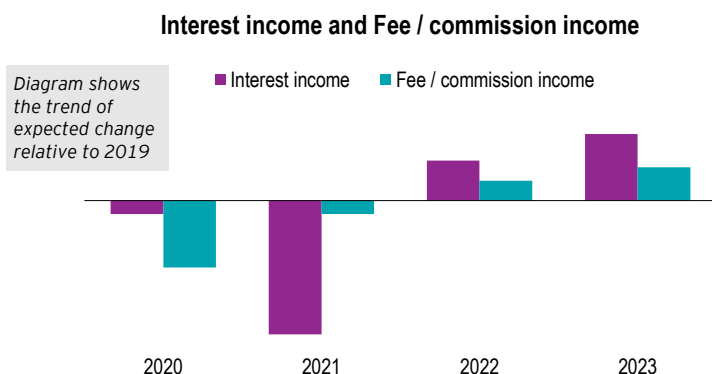
**Q Do you expect provisions to increase? What will be the timing and drivers of the increase?**



- ▶ Participants anticipate that additional provisions / loan losses will occur and these will follow a similar trend to new defaults in terms of timing.
- ▶ Participants agreed that the level of provisions will be driven by the macro projections and the level of price adjustment in the real estate market.
- ▶ Participants noted that, depending on the NPE cure rates by 2023, it might be the case that reversals of provisions could be recognised.

### c Income

**Q Do you anticipate income to reduce? What will be the main drivers for the reduction?**



- ▶ All participants agreed that interest income will not be materially impacted in 2020 due to the deferral of new defaults post the moratorium. Banks are expected to recognise the interest income as is for 2020, despite the low repayments expected.
- ▶ Low base rates (Euribor) driven at a European level as well as low margins to be driven by the application of the Government guarantee scheme are also expected to impact interest income.
- ▶ It has been stressed though, that interest income is likely to be highly impacted in 2021 due to a wave of new defaults and then rebound.
- ▶ Participants highlighted that fee and commission income is expected to be highly impacted in 2020.
- ▶ This will be driven by the low levels anticipated for new lending compared to 2019 and the minimal volume of transactions given the inactivity in the market due to the lockdown measures.



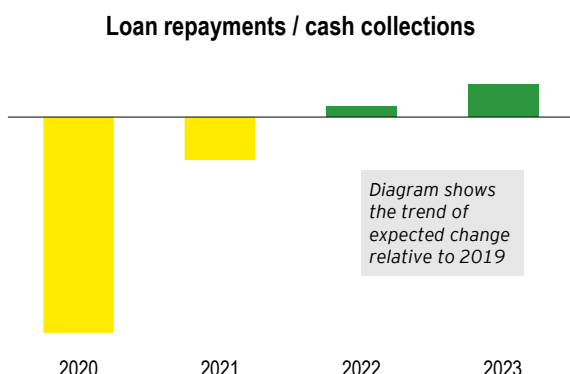
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Performing clients who have the capacity and ability to keep repaying are expected to push for interest rate reduction given the anticipated very low interest rates that the Government guarantee scheme will bring.

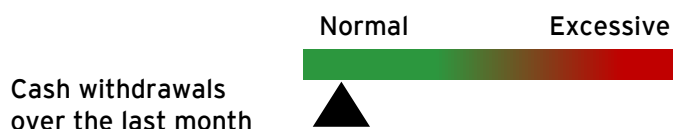
”

### d Liquidity

**Q What is the expected impact on loan repayments? Do you foresee the existing liquidity levels of the banks being threatened in the short to medium term?**



- ▶ Participants unanimously anticipate minimal repayments during the last 9 months of 2020, driven mainly by the moratorium of payments.
- ▶ It has been however highlighted that the excess liquidity provides the resilience required to tolerate the moratorium of payments and at the same time grant new loans with the aim to strengthen the liquidity of their customers.



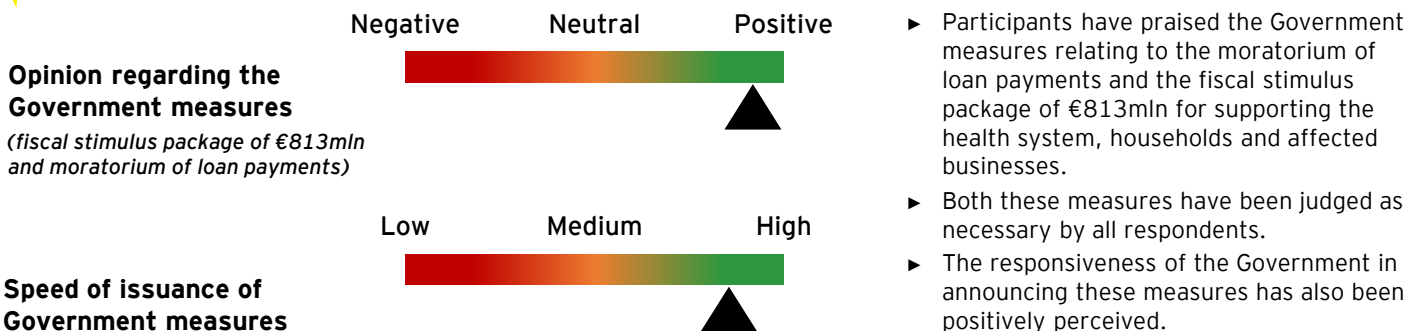
# Industry Sentiment

## EY Survey results (cont'd)

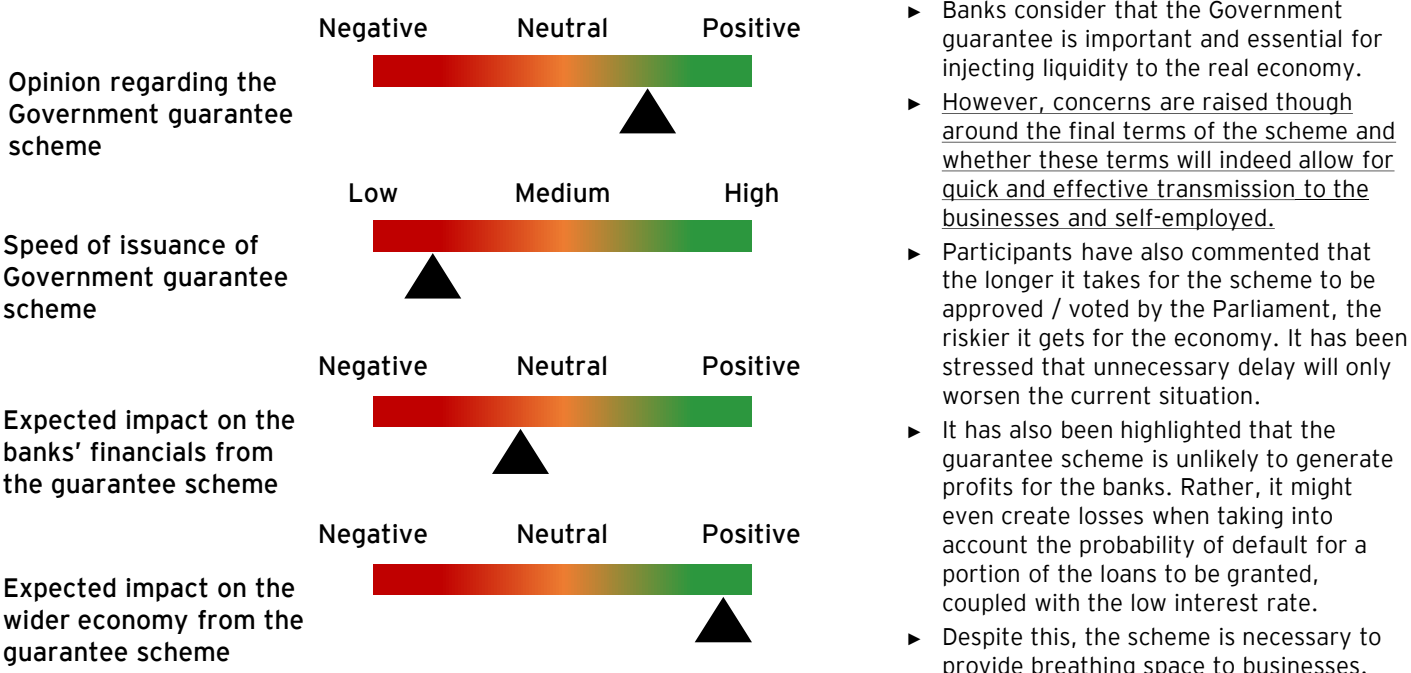
### 2 Topic of discussion: Opinion on the measures announced or pending to be announced by the Government and the Regulators

#### a Government measures

##### Q How did you perceive the measures announced by the Government to date?

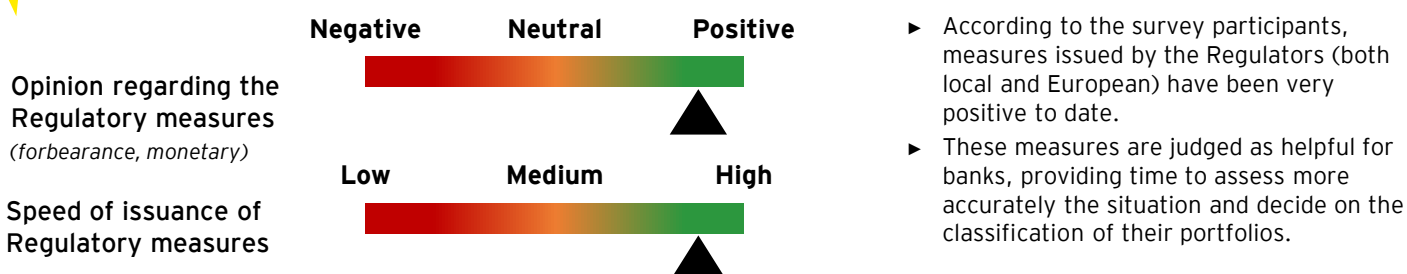


##### Q What is your opinion about the Government guarantee scheme being discussed at the Parliament?



#### b Regulatory measures

##### Q How did you perceive the measures announced by the Regulators to date?



# Industry Sentiment

## EY Survey results (cont'd)

### 3 Topic of discussion: Opinion on the NPL trades that were in progress prior to the COVID-19 crisis

#### Q What is the impact you see that COVID-19 will have on the NPL trades?

- ▶ Participants commented that the timing of COVID-19 was unfortunate given that significant NPL trades were close to completion.
- ▶ Completion of these trades would enable the banks to clean their balance sheets to a large extent
- ▶ The current situation is quite uncertain and does not allow any prediction on when the trades would likely recommence.



“

*The COVID-19 crisis is likely to create supply of distressed assets / new opportunities across Europe. This is likely to distract investors for some time prior to returning back to Cyprus.*

”

#### Q What do you see as the key drivers that could delay NPL trades from taking place?

Higher uncertainty in the real estate market, impacting the collateral values

90%

Limited cash collections during moratorium, resulting in poorer track record

50%

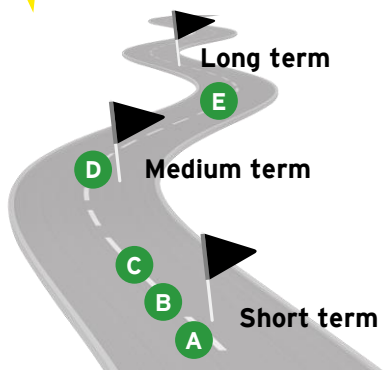
Limited resolutions expected during moratorium, especially after freezing the foreclosure procedures

25%

X% Denotes the % of respondents who included the specific answer in their response

### 4 Topic of discussion: Cost cutting

#### Q Does the bank plan to cut any costs? What are the planned to be cut first?



- A Marketing costs
- B Consultancy fees
- C Travelling costs
- D Branch optimisation
- E Staff cost

- ▶ Participants highlighted that amongst the first costs to be cut due to the crisis are marketing expenses, consultancy fees and travelling.
- ▶ In the medium to long term, banks are also considering to optimise their branch network but also to reduce the workforce through voluntary retirement schemes.

### 5 Topic of discussion: Interaction with customers

#### Q What changes have you seen so far in the customer interaction with the bank?

- ▶ Participants have expressed their satisfaction that an increasing number (double since last month) of customers have begun using the digital channels offered for carrying out their transactions.
- ▶ It has been noted that credit card subscriptions have also doubled since a month ago.
- ▶ Branch visits have halved since last month and this trajectory is continuing.
- ▶ Participants have highlighted that it would be crucial for banks to adapt accordingly so as to exploit this change of culture and maintain it after the crisis as well.

Usage of digital apps (mobile and internet subscriptions)



since mid-March

Visits to branches



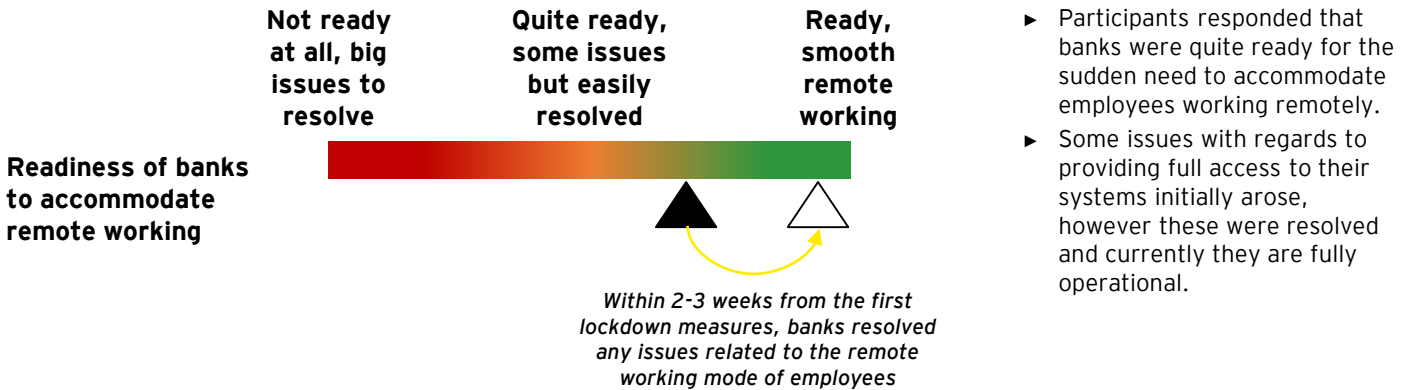
since mid-March

# Industry Sentiment

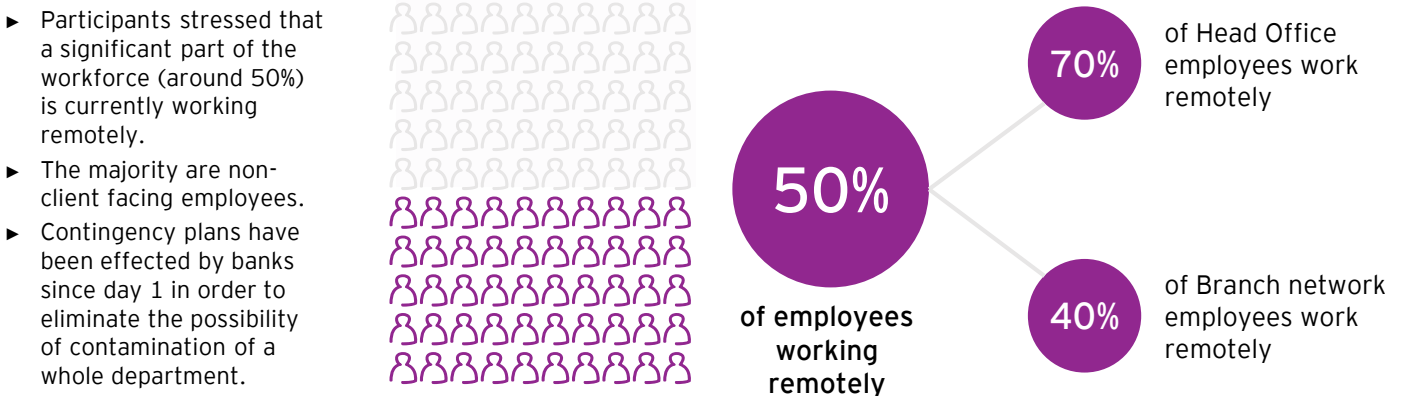
## EY Survey results (cont'd)

### 6 Topic of discussion: Operational aspects

#### Q Was the bank ready to accommodate a large number of people working remotely?

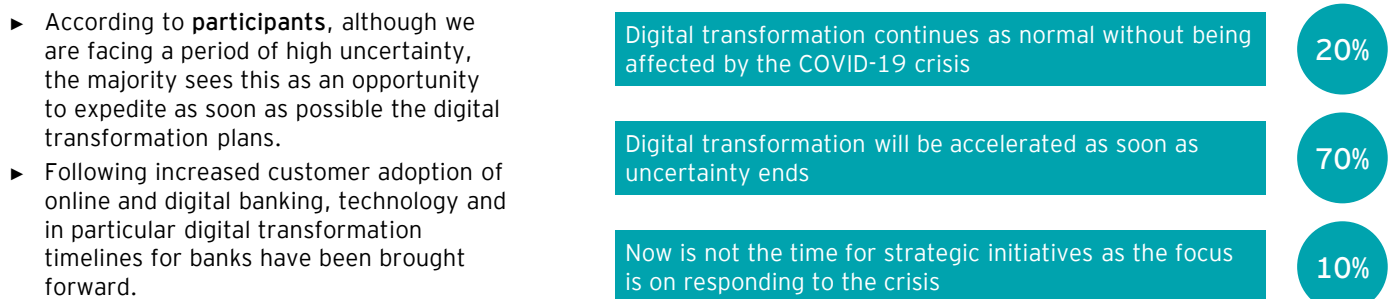


#### Q How many employees work remotely?



### 7 Topic of discussion: Digital transformation

#### Q Is the bank considering to postpone its digital transformation programme in light of the COVID-19 impact and the uncertain timeframe this could last?



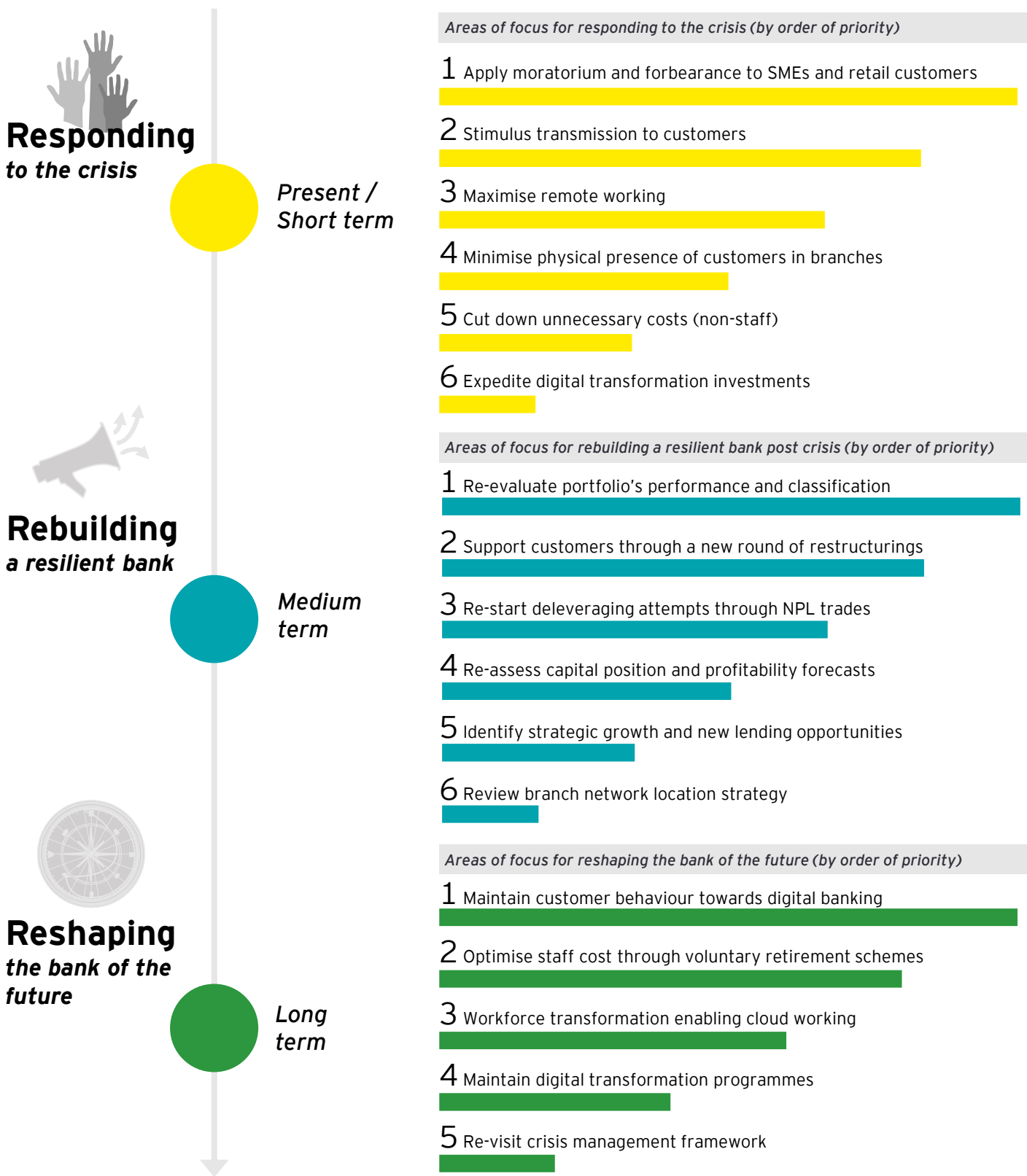
# Industry Sentiment

## Roadmap of banks' top priorities from present to future

The EY Survey has revealed the top priorities of the banks for the short, medium and longer term in light of the COVID-19 crisis, which are summarised in the below diagram.

Banks are rethinking how they operate as well as how they support customers through this period. The below diagram summarises the areas of focus, according to the participants' answers, in responding to the crisis in the short term, rebuilding a resilient bank in the medium term and reshaping the bank for the longer term.

The top priorities for now remain the forbearance and the stimulus transmission. In the medium to longer term, banks' concern relates to the evaluation and risk assessment of the performing portfolio, along with limiting physical presence in branches and optimising the cost structure.

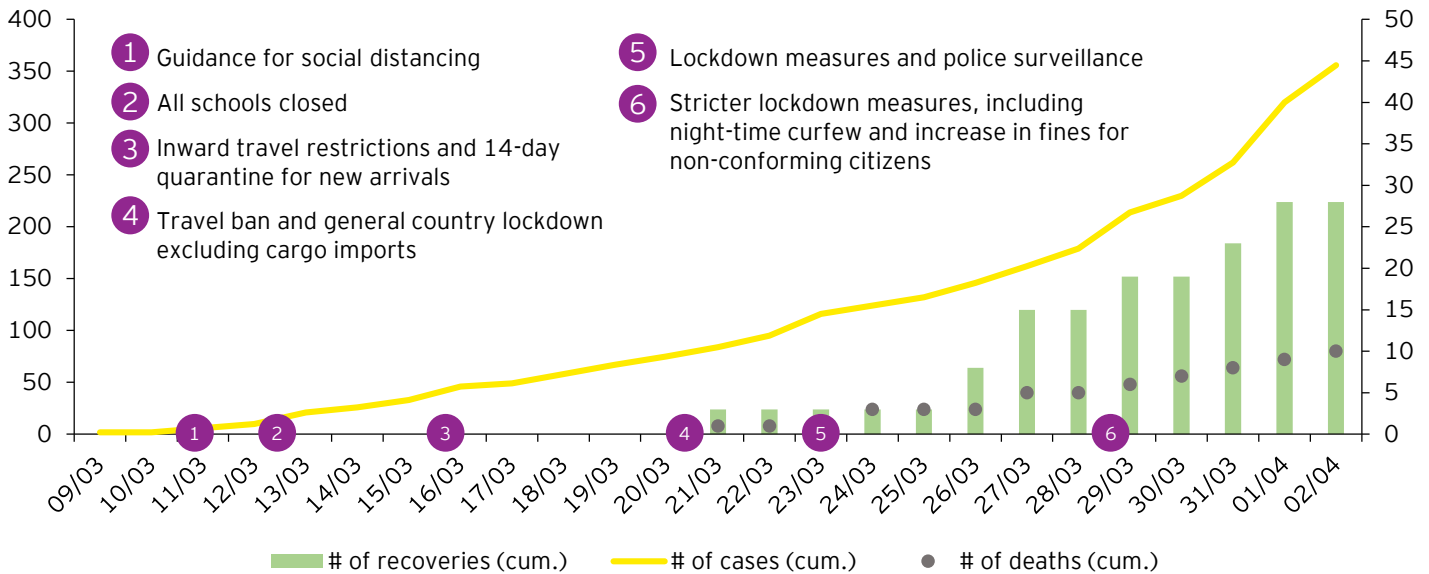


# Impact of COVID-19 on the Banking Sector

## Key considerations and scenarios

### Health measures and virus control

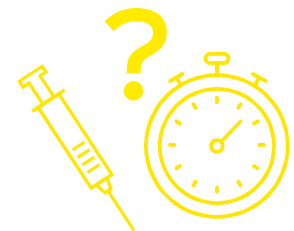
In alignment with WHO guidelines, the Cypriot government has imposed social distancing measures escalating to citizen lockdown and travel ban. The graph below illustrates the chronological escalation of these measures<sup>4</sup>.



These actions are estimated to reduce contact by 75%, which allows the virus to still spread albeit at a slower rate, alleviating the burden on the healthcare system and buying time until the threat passes<sup>5</sup>. Measures resemble those implemented in most other countries, especially in Europe and the US, but may vary in the future as each country decides to deal with the threat differently.

At current knowledge status, scientists speak of the following potential remedies:

- ▶ Development of vaccine in 12-18 months.
- ▶ Development of effective therapy protocol, based on existing (or new) drugs, to deal with acute symptoms and diminish mortality rate. Timing remains uncertain.
- ▶ Herd immunity through infection assuming immunity can last and no mutation.



In view of the uncertainty surrounding potential remedies, health-centric measures are developed with the understanding that the pandemic may last 12-18 months, that is the time needed for a vaccine to be developed and commercialized. Under this assumption, the government has the following toolkit at its disposal:

- A. Varying degrees of lockdown and border control** applied in accordance to the capacity of the health system to accommodate and treat the infected. Notably, relaxation of social distancing measures and travel ban but return to strict lockdown once the number of new cases exceeds a certain threshold. This swinging between the two strategies makes little difference for economic revival and comes at a great political cost.
- B. Upgrading and scale up of antigen (PCR) testing capacity.** This would enable proactive regular PCR testing for large samples of the population to provide a representative view of the spread of the virus. PCR tests produce very few false positives but there is an issue with false negatives resulting from problems with collecting and processing patient samples. They can be used to confirm the infection but are less reliable in confirming its absence. Mass testing is estimated to be possible in 1-3 months.
- C. Contact tracing.** Testing can be used to identify people who are infected and, with the use of app-enabled (location-based) technology, contact tracing serves to find those people who have come into contact with infected persons so as to monitor/ isolate them. This option can be viable in 1-3 months.
- D. Immunity passports with antibody tests.** Large-scale antibody testing, once approved by authorities, can be used to identify those who have had the virus and are therefore potentially immune and can return to work. Private manufacturers have played an outsized role in the development of antibody tests but products still need to be validated by authorities for their reliability. Roll out is estimated at > 3 months<sup>6</sup>.

4. <https://www.pio.gov.cy/en/press-releases/>

5. <https://www.imperial.ac.uk/media/imperial-college/medicine/sph/ide/gida-fellowships/Imperial-College-COVID19-NPI-modelling-16-03-2020.pdf>

6. <https://institute.global/policy/suppression-exit-strategies-options-lifting-lockdown-measures-uk>




# Impact of COVID-19 on the Banking Sector

## Key considerations and scenarios (cont'd)

### Health measures and virus control (cont'd)

Possible exit strategies are derived based on the above options and adjusted as the development of scientific remedies plays out. Such strategies vary in effectiveness in terms of how fast the country can begin exit from lockdown and travel ban (part exit) so that the economy can be resuscitated without risking a virus spread that spirals out of control and overwhelms the healthcare capacity.

We classify the ability of a country to respond to a pandemic into three levels of sophistication for the virus countermeasures. The higher the degree of sophistication, the more tools a country can deploy to respond to highly contagious pandemics and limit disruption to economy activity (more "exit" strategy options). It is evident that in the case of COVID-19, the benefit of utilizing the full suite of countermeasure tools outweighs the cost of deploying them until an effective therapy protocol or vaccine is developed, or until herd immunity is reached.

 <b>Strategy components:</b>	Sophistication of pandemic countermeasures		
	Low	Medium	High
▶ Govt applies various degrees of social distancing/border controls while keeping burden on healthcare system manageable.	✓	✓	✓
▶ Government performs mass scale & proactive sample PCR testing.		✓	✓
▶ Government employs app-based contact tracing.			✓
▶ Antibody tests used to allow immune people to exit isolation.			✓



# Impact of COVID-19 on the Banking Sector

## Key considerations and scenarios (cont'd)

### Economic measures and anticipated recovery

The Cypriot government has acted swiftly and with determination in both containing the virus spread and providing a soft cushion for the economy, for both households and businesses:

**Fiscal** Fiscal stimulus packages of total size €1.32bn<sup>7</sup> (5.4% of GDP) deployed to (a) aid the health sector in combatting the pandemic; (b) provide income support to households through leave allowance for parents/ vulnerable groups, unemployment benefits and banning of eviction in case of failure to pay rent; and (c) support to affected businesses by paying employee salaries and deferring VAT payments and GHS contributions. Government to guarantee up to €2bn to banks emergency lending, pending approval by Parliament.

**Monetary** Monetary measures at EU level include ECB's Pandemic Emergency Purchase Programme to buy government and corporate debt, removal of issuer limits from bond-buying programmes, release of capital and liquidity buffers for banks, government guarantees for new loans and suspension of loan installments for nine months. Eurozone agreement of €540bn package to help battle the economic fallout is a significant milestone, though not yet agreed by leaders.

The degree of effectiveness of government intervention depends on the combination, coordination and concerted implementation of fiscal and Eurozone monetary policy, that is timely, sufficient in magnitude, and targeted.

- ▶ **Monetary & fiscal measures.** Sophisticated combination and coordination of monetary and fiscal policies can maximize impact by reinforcing and providing financial backing to each other.
- ▶ **Coordination at Eurozone level.** The extent of quantitative easing, liquidity provision and relaxation of thresholds for banks are decided by the ECB, as are decisions affecting government debt and financing mechanisms. And while all Eurozone economies are affected, those countries relying more heavily on tourism and with a weak banking sector (such as Cyprus) are in a more dire situation with respect to the pace of recovery than countries with a hefty reliance on manufacturing. Solidarity between Eurozone states will be key in how effective the economic measures are for supporting Cyprus.
- ▶ **Timeliness.** Effective measures will curtail bureaucratic procedures and be delivered swiftly to households and corporations, be based on latest scientific evidence, and adaptable as the situation evolves.
- ▶ **Magnitude.** Effective measures will near in size the extent of the expected loss in output. Government to date has announced packages of €1.32bn, 5.4% of 2019 GDP figure (compared to 3% European average), but loss in economic output is set to exceed this number and disproportionately affect different sectors of the economy.
- ▶ **Economy-wide vs. sector-specific.** As some sectors are hit harder by the pandemic, or have different pain points, fiscal stimulus packages targeted specifically to those sectors can be more effective in preventing high rise in unemployment and permanent contraction of the sector.

We consider three key scenarios of government intervention in terms of their effectiveness to avoid a deflationary spiral leading into depression, and to lead to a quick economic recovery. The role of each policy component in each of the scenarios is depicted by the green bars. High effectiveness of intervention involves synchronized and sophisticated combination of monetary and fiscal policies, including sector-specific measures, careful planning to ensure that aid is transmitted to the appropriate recipients in a timely manner, monitoring to prevent misappropriation of aid, proactive expansion of fiscal stimulus package as needed. In terms of monetary policy, there is little space for maneuvering but EU-level solidarity matters.

Strategy components:	Effectiveness of intervention		
	Low	Partial	High
▶ Combination and coordination of monetary and fiscal policies.			
▶ Circumvention of bureaucracy in favour of timely transmission of financial aid.			
▶ Government expands fiscal stimulus package as needed.			
▶ Government successfully introduces sector-specific measures.			
▶ High EU-level solidarity/coordination/agreement and maintenance of ECB Quantitative Easing policy.			

The degree to which each policy component is successfully implemented is depicted by the green bars (mobile signal).

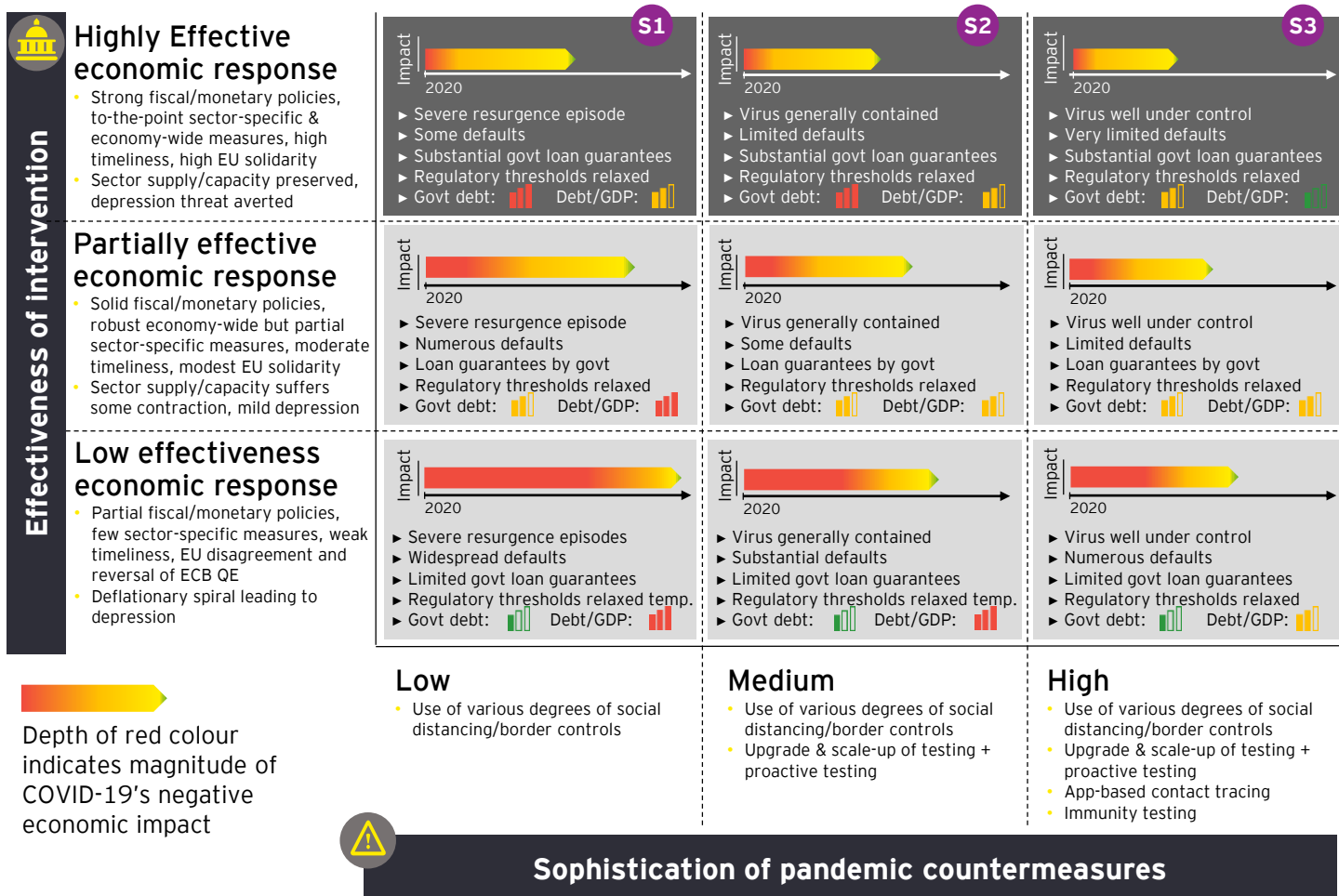
7. <https://www.pio.gov.cy/en/press-releases-article.html?id=13197#flat>

# Impact of COVID-19 on the Banking Sector

## Key considerations and scenarios (cont'd)

### Scenario summary

In the matrix below we summarise and combine the virus control strategies with the economic & fiscal strategies outlined previously, so as to derive various scenarios for COVID-19's economic impact (under the assumption that the pandemic will last for 12-18 months). For each scenario we provide a brief description in the respective matrix quadrant, along with an illustration of the magnitude of COVID-19' negative economic impact, and its longevity:



Depth of red colour indicates magnitude of COVID-19's negative economic impact

The banking sector horizon and impact is likely to move along the "Highly effective economic response" scenarios as presented in the above matrix. On the next pages we analyse the shape of the curves for key banking metrics that we foresee to occur in the coming years, based on the currently available information and the current situation.



# Impact of COVID-19 on the Banking Sector

## Scenario analysis

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### Effectiveness of economic intervention

The banking sector is one of the few sectors of the economy that attracted highly effective intervention by the Regulators and the Government through sector-specific measures. As the liaison between fiscal and monetary policy, it constitutes the means of transmission of funds to the real economy, thus the fast and effective economic response was undoubtedly very important. Further interventions and expansion of the fiscal stimulus package are likely to occur while assessing the situation going forward.

To date, ECB's relaxation of banking capital thresholds and Quantitative Easing (QE) policy, as well as the government's readiness to respond decisively by guaranteeing emergency loans, has provided much needed stability for the banking system during these turbulent times. But as the pandemic persists from a short into a longer exit horizon, both the likelihood of Eurozone policy to remain favourable as well as the depth of the government's pocket progressively decrease.

ECB QE policy is expected to support Eurozone economic recovery through the pandemic but no commitments have been made as to the time horizon of these measures. In the event that QE is halted at a premature time for some countries that may need longer to overcome the recession due to, for instance, major reliance of GDP in tourism as is the case for Cyprus, then the ability of the Cyprus government to finance its debt will deteriorate. Consequently, ability of the government to engage in expansionary fiscal policy to support households and businesses will weaken, and this will impact all stakeholders linked to the most affected sectors such as tourism and retail. This is likely to result in a progressive increase in defaults and a rise in the banks' NPLs portfolio.

### Sophistication of Pandemic countermeasures

The existing health measures for virus control enforced in Cyprus are expected to become more sophisticated as antigen (PCR) testing equipment and app-enabled technology for contact tracing becomes available. In addition, antibody testing is expected to help with the gradual revival of the economy through the creation of antibody passports for immune people. Uncertainty remains, however, regarding the pace at which the country will adopt these tools at large scale, to enable it to partly exit the lockdown. It is likely that the lockdown will continue to affect the economy at least for the short-term.

### Scenario analysis

Based on the above, and according to the existing available facts and figures, we believe that the most likely scenarios involve highly effective economic response in the banking sector and varying degrees of sophistication of pandemic countermeasures. This gives rise to the following scenarios:

- S1** Highly effective economic response - Low degree of sophistication of pandemic countermeasures - Long exit horizon
- S2** Highly effective economic response - Medium degree of sophistication of pandemic countermeasures - Medium exit horizon
- S3** Highly effective economic response - High degree of sophistication of pandemic countermeasures - Short exit horizon

The results of the EY Survey and the view of the banking experts and executives who participated in the survey have been interpreted and translated in an attempt to predict the shape of the curve for key banking metrics.

The shape of the curve for each metric takes into account the participants' sentiment of the market, the fiscal stimulus package and regulatory interventions and guidance issued to date.

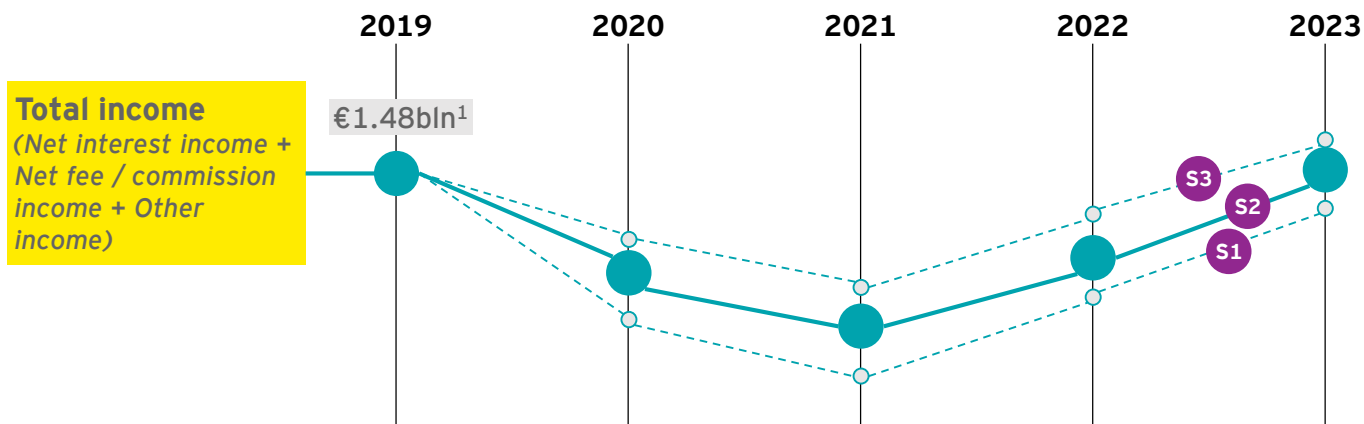
# Impact of COVID-19 on the Banking Sector

## Scenario analysis (cont'd)

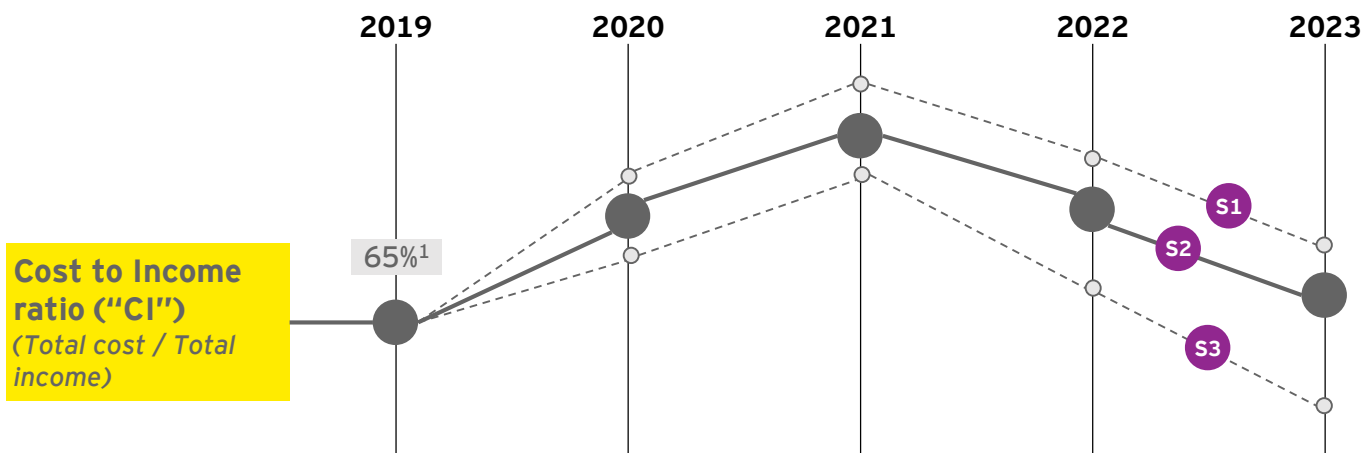
We highlight that the shape of the curves predicted are indicative. Besides the information and views collected from participants while conducting the EY Survey, the estimated trajectory of each metric was also based on relevant publications and literature including our industry experience and expertise.

The situation surrounding COVID-19 is dynamic and rapidly evolving on a daily basis and a lot is still unknown and uncertain. Therefore, the curve shapes should by no means be considered as accurate predictions.

The scenarios ran are for consideration purposes only as they depend on a number of assumptions and variable parameters pertaining a highly uncertain situation.



- ▶ Total income is expected to follow a U-shape.
- ▶ In 2020, the biggest impact is expected to arise from the low fee and commission income rather than new defaults.
- ▶ Low fee and commission income is expected to be driven from the smaller transaction volumes in the market and the lower new lending levels compared to 2019.
- ▶ The trough is expected in 2021 where the majority of new defaults is anticipated, following the end of the 9-month moratorium.
- ▶ Recovery close to 2019 figures is anticipated by 2023.

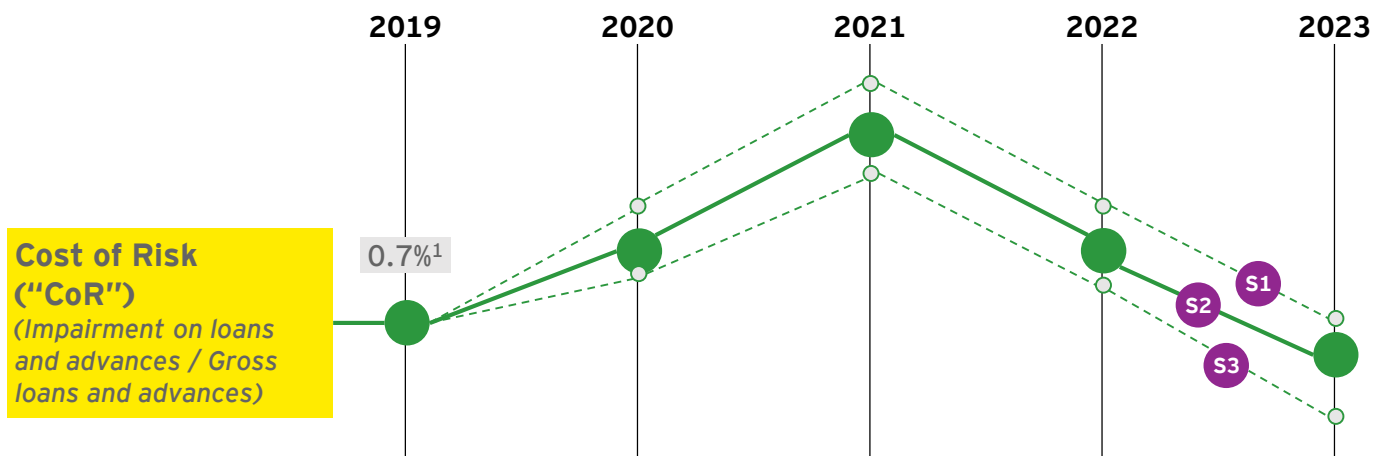


- ▶ Cost to income ratio is expected to increase given the anticipated decrease in total income.
- ▶ In 2020 and 2021, the ratio increases as the income reduction is expected to be larger compared to any cost savings that are likely to occur.
- ▶ Some savings are expected by banks in 2020 and 2021, which mainly relate to marketing fees and consultancy costs.
- ▶ From 2022 onwards, the ratio is expected to start declining as income will start bouncing back.
- ▶ Digital transformation investments are also expected to lead to further cost reduction in the longer term and help bank optimise their cost base.
- ▶ The effect and timing of the digital transformation initiative is expected to play an important role with regard to the shape of the curve. Effective and quick transformation could result in an inverted V-shape rather than an inverted U-shape, implying quicker restoration of the 2019 cost to income ratio.

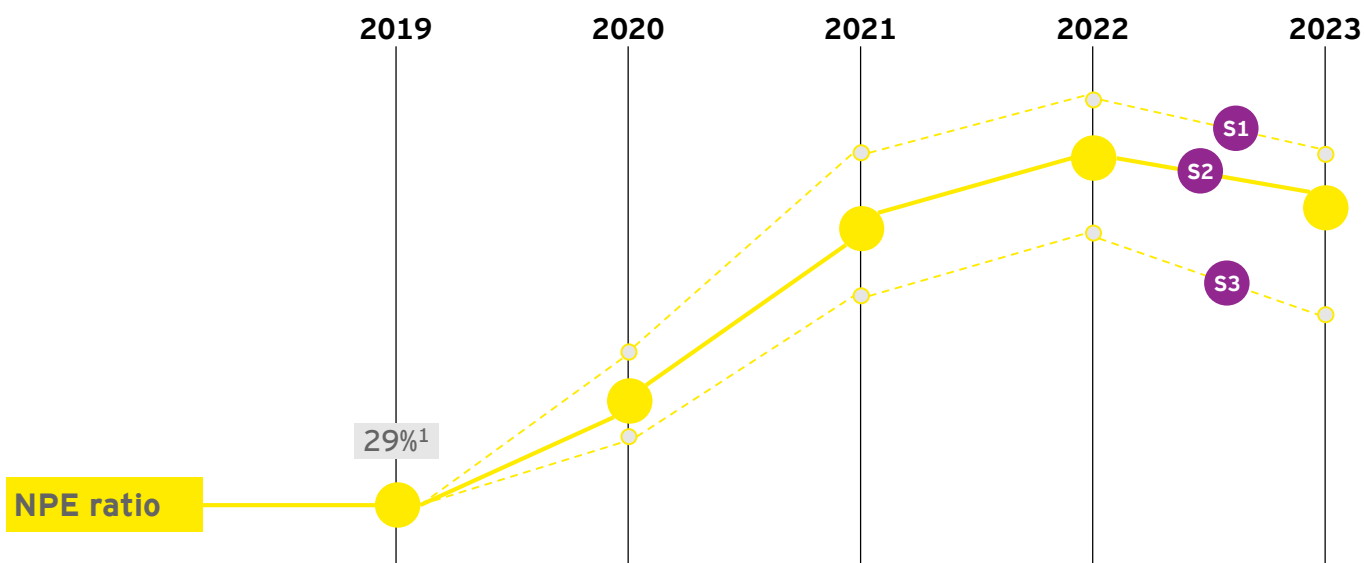
<sup>1</sup> Source: CBC, "2020\_02\_14 Aggregate Cyprus banking sector data\_30.09.2019.xlsx"; Figures represent the annualised of the 9 months of 2019.

# Impact of COVID-19 on the Banking Sector

## Scenario analysis (cont'd)



- ▶ Loan losses are expected to follow an inverted V-shape, highly affected by the expected increase in NPEs (refer below for the NPE ratio curve).
- ▶ An increase is anticipated in 2020 due to default inflows, however, a spike in cost of risk is anticipated in 2021, before it starts reducing from 2022 onwards. This is expected to be a result of the Regulators' guidance for periods of general moratorium, which will 'safeguard' the banks from NP classifications in 2020 until the uncertainty in the situation becomes clearer.
- ▶ In 2023, depending on macro performance, real estate prices and other market conditions, banks could also be targeting for loan loss reversals.
- ▶ It is stressed that loan losses, and consequently the cost of risk, is a metric driven by a number of different parameters and variables, such as the macroeconomic conditions, unemployment and real estate prices which drive the collateral valuation. Therefore, the peak point and the shape of the curve may vary significantly depending, amongst others, on the resilience of the wider economy, the borrower behaviours and the market conditions.

















- ▶ An increase is expected in NPEs in 2020, although a bigger wave of default inflows is expected in 2021, following the end of the 9-month moratorium.
- ▶ The level of the increase is still uncertain to predict. However, it is estimated that if the increase in defaults exceeds significantly a normal organic curing rate, then the NPE ratio is likely to follow a long inverted U-shape curve (as shown above) that would take post 2023 to return back to 2019 levels. If defaults in 2021 increase by a level that is close to a normal organic curing rate, it is likely that the curve will follow an inverted V-shape and the NPE ratio shall return to 2019 levels quicker than 2023.
- ▶ An alternative scenario where the NPE ratio could be reduced significantly entails the completion of the NPL trades that were in progress prior the commencement of the COVID-19 crisis.

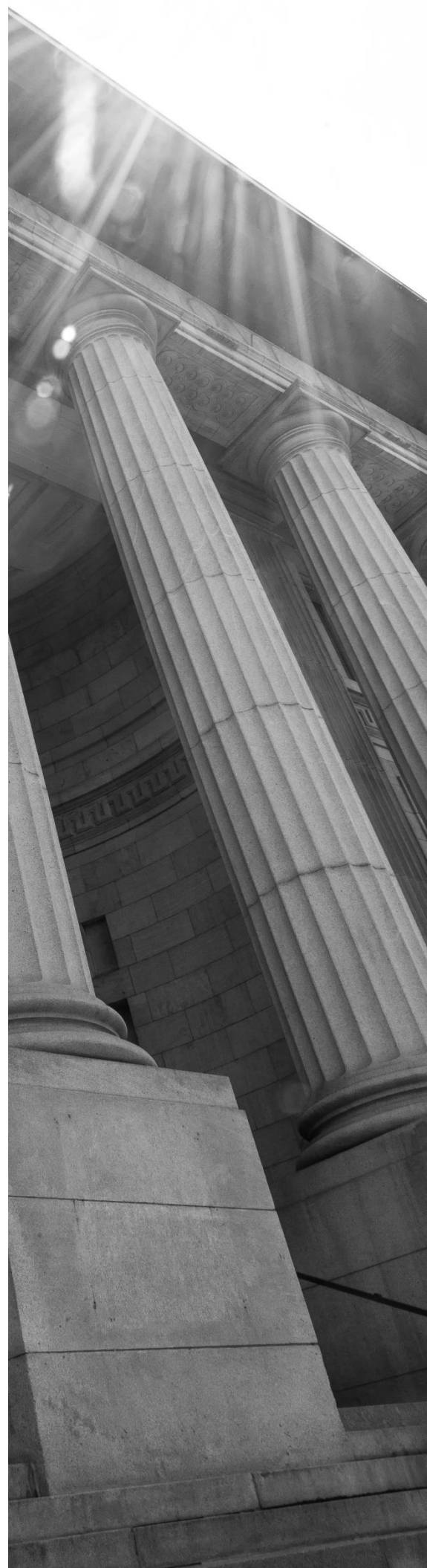
<sup>1</sup> Source: CBC, "2020\_02\_14 Aggregate Cyprus banking sector data\_30.09.2019.xlsx"; Figures represent the annualised of the 9 months of 2019.

# How EY can help

## Services that reshape your future

Our range of services span across the entire stakeholder framework of the banking sector, through our knowledge of the government operations, central banking operations, commercial banking and all industries within the real economy.

Government/ Regulator	<b>Economic Advisory</b> 	<ul style="list-style-type: none"> <li>▶ Economic Impact Assessments</li> <li>▶ Cost-Benefit Analysis</li> <li>▶ Regulatory economics</li> <li>▶ Ad-hoc advisory support on the terms of upcoming stimulus packages</li> <li>▶ Assessment of specific industries and close monitoring and reporting of the impact of COVID</li> </ul>
	<b>PMO for stimulus application</b> 	<ul style="list-style-type: none"> <li>▶ Lead Advisory / PMO role for the application of the stimulus transition framework</li> </ul>
Banks	<b>IBRs</b> 	<ul style="list-style-type: none"> <li>▶ Independent Business Reviews and detailed cash flow projection analysis</li> </ul>
	<b>Risk assessment</b> 	<ul style="list-style-type: none"> <li>▶ Scenario planning</li> <li>▶ Situation monitoring analysis</li> <li>▶ Industry assessment &amp; borrower risk analysis</li> </ul>
	<b>Strategy</b> 	<ul style="list-style-type: none"> <li>▶ Strategy update &amp; Robustness check</li> <li>▶ PMO for digital transformation implementation plan</li> </ul>
	<b>Stimulus package</b> 	<ul style="list-style-type: none"> <li>▶ PMO for stimulus package</li> <li>▶ Processes and procedures set up</li> <li>▶ Monitoring and reporting</li> </ul>
	<b>Data management</b> 	<ul style="list-style-type: none"> <li>▶ Remediation and validation of data</li> <li>▶ Information flow analysis</li> </ul>
	<b>Moratorium applications</b> 	<ul style="list-style-type: none"> <li>▶ PMO for moratorium applications</li> <li>▶ Processes and procedures set up</li> <li>▶ Monitoring and reporting</li> </ul>
Businesses	<b>Short-term cash &amp; liquidity management</b> 	<ul style="list-style-type: none"> <li>▶ Analysis of cash gaps</li> <li>▶ Identification of quick wins</li> <li>▶ Dynamic forecasting of cash needs under crisis scenarios and identification of mid-term solutions</li> </ul>
	<b>Financing options</b> 	<ul style="list-style-type: none"> <li>▶ Analysis of financing structure</li> <li>▶ Identification of alternative options</li> <li>▶ Securing non-bank / quick financing</li> </ul>
	<b>Negotiations with banks</b> 	<ul style="list-style-type: none"> <li>▶ Advice with bank negotiations</li> <li>▶ Lenders deck and banking presentation preparation</li> <li>▶ Preparation of financial projections</li> <li>▶ Capital structuring</li> </ul>
	<b>Working capital advisory</b> 	<ul style="list-style-type: none"> <li>▶ Supply and demand planning</li> <li>▶ Assessment of key WC drivers and cash release opportunities</li> </ul>
	<b>M&amp;A support</b> 	<ul style="list-style-type: none"> <li>▶ Divestment advisory</li> <li>▶ Real-estate sales</li> <li>▶ Quick direct sale process</li> <li>▶ Identification of opportunities</li> </ul>
	<b>Corporate Finance Strategy</b> 	<ul style="list-style-type: none"> <li>▶ Corporate strategy</li> <li>▶ Investment strategy</li> <li>▶ Feasibility &amp; business planning</li> <li>▶ Portfolio strategy</li> </ul>



## How EY can help (cont'd)

### People



**Stelios Demetriou**  
Partner / Transaction Advisory  
Services Leader

Stelios has over 20 years of corporate finance experience. He advises clients on transactions in the Banking sector and various other industries in Cyprus and South East Europe. During the last years, he has led various financial restructuring projects and NPL deals in the country, worked on IBRs on behalf of banks and corporates and acted as an advisor on government projects.



**Savvas Pentaris**  
Partner / Head of Financial  
Services

Savvas has more than 22 years of financial services experience gained in London, Cyprus and Southeast Europe, delivering professional services to banks, insurance and asset management companies. He is currently leading the Financial Services industry sector in EY Cyprus.



**Alexandros Pericleous**  
Director / Transaction Advisory  
Services

Alexandros focuses on strategy and corporate finance. He has helped clients reshape their results through regaining control of their cash and working capital, business planning and review, restructuring, renegotiating debt, and investing / divesting.



**Andreas Socratous**  
Senior Manager / Transaction  
Advisory Services

Andreas has over 7 years of experience in advising clients, primarily in the financial services industry. He was involved in sell and buy-side NPL transactions, fair valuation of loan portfolios, asset quality reviews, due diligences and valuations of banks and independent business reviews of big corporate groups across various industries.



**Renos Solomides**  
Manager



**Melina Moleskis**  
Assistant Manager



**Katerina Gregoriou**  
Analyst

**Transaction Advisory Services** are all about helping our clients get more for their capital. We provide comprehensive guidance on all aspects of transactions - understood as major corporate undertakings outside the ordinary course of operations - from inception to execution. In this way, we manage to support the flow of capital across borders, help bring new products and innovation to market, and enable organisations to reshape themselves for a better future, in a rapidly changing, increasingly digital and disrupted business environment.

### Why EY Transaction Advisory Services?

EY ensures the best outcome by combining:

- ▶ A highly experienced and entrepreneurial team
- ▶ Comprehensive solutions
- ▶ International network
- ▶ Sector expertise
- ▶ Digital expertise



## About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

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