# Additional Risk and Capital Management Disclosures

30 September 2016

## 1. Credit risk

The Central Bank of Cyprus (CBC) issued to credit institutions the Loan Impairment and Provisioning Procedures Directives of 2014 and 2015 (Directive), which provides guidance to banks for loan impairment policy and procedures for provisions. The purpose of this Directive is to ensure that credit institutions have in place adequate provisioning policies and procedures for the identification of credit losses and prudent application of IFRSs in the preparation of their financial statements.

The Directive requires certain disclosures in relation to the loan portfolio quality, provisioning policy and levels of provision. The disclosures required by the Directive, in addition to those presented in Notes 3 and 44 of the Consolidated Financial Statements for the year ended 31 December 2015 and on Note 27 of the Interim Condensed Consolidated Financial Statements for the nine months ended 30 September 2016 are set out in the following tables. The tables disclose non-performing exposures (NPEs) based on the definitions of the European Banking Authority (EBA) standards.

According to the EBA standards, NPEs are defined as those exposures that satisfy one of the following conditions:

(i) The debtor is assessed as unlikely to pay its credit obligations in full without the realisation of the collateral, regardless of the existence of any past due amount or of the number of days past due.
(ii) Defaulted or impaired exposures as per the approach provided in Regulation (EU) No 575/2013 Article 178.
(iii) Material exposures (as defined below) which are more than 90 days past due.
(iv) Performing forborne exposures under probation for which additional forbearance measures are extended.
(v) Performing forborne exposures under probation that present more than 30 days past due within the probation period.

Exposures include all on and off balance sheet exposures, except those held for trading, and are categorised as such for their entire amount without taking into account the existence of collateral.

The following materiality criteria are applied:

- When the problematic exposures of a customer that fulfil the NPE criteria set out above are greater than 20% of the gross carrying amount of all on balance sheet exposures of that customer, then the total customer exposure is classified as non-performing; otherwise only the problematic part of the exposure is classified as non-performing.

- Material arrears/excesses are defined as follows:
  - Retail exposures:
    - Loans: Arrears amount is greater than €500 or number of instalments in arrears is greater than one.
    - Overdrafts: Excess amount is greater than €500 or greater than 10% of the approved limit.
  - Exposures other than retail: Total customer arrears/excesses are greater than €1.000 or greater than 10% of the total customer funded balances.

NPEs may cease to be considered as non-performing only when all of the following conditions are met:

(i) The extension of forbearance measures does not lead to the recognition of impairment or default.
(ii) One year has passed since the forbearance measures were extended.
(iii) Following the forbearance measures and according to the post-forbearance conditions, there is no past due amount or concerns regarding the full repayment of the exposure.

## 1. Credit risk (continued)

The tables below present the analysis of loans and advances to customers in accordance with the EBA standards.

| 30 September 2016 | Gross loans and advances to customers | | | | Provision for impairment and fair value adjustment on initial recognition | | | |
|---|---|---|---|---|---|---|---|---|
| | Group gross customer loans and advances[1] | Of which NPEs | Of which exposures with forbearance measures | | Total provision for impairment and fair value adjustment on initial recognition | Of which NPEs | Of which exposures with forbearance measures | |
| | | | Total exposures with forbearance measures | Of which on NPEs | | | Total exposures with forbearance measures | Of which on NPEs |
| | €000 | €000 | €000 | €000 | €000 | €000 | €000 | €000 |
| **General governments** | **116.383** | 4.851 | 5.025 | 4.646 | **2.503** | 1.665 | 1.656 | 1.603 |
| **Other financial corporations** | **411.508** | 289.662 | 166.439 | 147.459 | **183.986** | 180.658 | 98.896 | 98.803 |
| **Non-financial corporations** | **12.044.121** | 7.557.313 | 5.546.508 | 4.282.243 | **3.241.569** | 3.151.385 | 1.349.178 | 1.314.098 |
| Of which: Small and Medium sized Enterprises[2] | **7.279.001** | 4.732.650 | 2.656.709 | 2.079.733 | **2.171.980** | 2.115.752 | 688.878 | 665.460 |
| Of which: Commercial real estate[2] | **9.487.849** | 6.233.304 | 4.882.592 | 3.801.307 | **2.442.435** | 2.369.571 | 1.107.471 | 1.075.734 |
| **Non-financial corporations by sector** | | | | | | | | |
| Construction | **3.180.514** | 2.569.374 | | | **1.089.515** | | | |
| Wholesale and retail trade | **2.121.711** | 1.087.101 | | | **458.829** | | | |
| Accommodation and food service activities | **1.343.302** | 780.361 | | | **267.712** | | | |
| Real estate activities | **2.901.900** | 1.600.081 | | | **709.356** | | | |
| Manufacturing | **687.847** | 415.545 | | | **162.970** | | | |
| Other sectors | **1.808.847** | 1.104.851 | | | **553.187** | | | |
| **Households** | **8.023.502** | 4.049.027 | 2.930.145 | 2.099.146 | **1.227.863** | 1.154.800 | 324.615 | 306.948 |
| Of which: Residential mortgage loans[2] | **5.460.371** | 2.780.661 | 2.269.467 | 1.602.318 | **603.145** | 550.011 | 184.686 | 173.094 |
| Of which: Credit for consumption[2] | **1.071.768** | 604.870 | 312.980 | 250.745 | **292.174** | 281.504 | 63.524 | 60.438 |
| **Total on-balance sheet** | **20.595.514** | **11.900.853** | **8.648.117** | **6.533.494** | **4.655.921** | **4.488.508** | **1.774.345** | **1.721.452** |

[1] Excluding loans and advances to central banks and credit institutions.
[2] The analysis shown in lines 'non-financial corporations' and 'households' is non-additive across categories as certain customers could be in both categories.

1. **Credit risk** (continued)

| 31 December 2015 | Gross loans and advances to customers | | | | Provision for impairment and fair value adjustment on initial recognition | | | |
|---|---|---|---|---|---|---|---|---|
| | Group gross customer loans and advances[1] | Of which NPEs | Of which exposures with forbearance measures | | Total provision for impairment and fair value adjustment on initial recognition | Of which NPEs | Of which exposures with forbearance measures | |
| | | | Total exposures with forbearance measures | Of which on NPEs | | | Total exposures with forbearance measures | Of which on NPEs |
| | €000 | €000 | €000 | €000 | €000 | €000 | €000 | €000 |
| **General governments** | **115.358** | 4.858 | 5.241 | 4.448 | **345** | 345 | 1.771 | 1.518 |
| **Other financial corporations** | **450.287** | 269.232 | 164.356 | 141.861 | **175.712** | 158.570 | 86.439 | 85.905 |
| **Non-financial corporations** | **13.687.340** | 9.447.487 | 6.250.424 | 5.101.675 | **3.938.616** | 3.852.385 | 1.651.274 | 1.618.835 |
| Of which: Small and Medium sized Enterprises[2] | **7.595.447** | 5.361.281 | 2.724.405 | 2.254.873 | **2.412.273** | 2.364.850 | 752.559 | 736.962 |
| Of which: Commercial real estate[2] | **10.998.641** | 8.009.181 | 5.684.179 | 4.661.835 | **2.996.289** | 2.931.498 | 1.418.013 | 1.390.942 |
| **Non-financial corporations by sector** | | | | | | | | |
| Construction | **4.023.260** | 3.440.287 | | | **1.391.760** | | | |
| Wholesale and retail trade | **2.286.348** | 1.308.725 | | | **552.581** | | | |
| Accommodation and food service activities | **1.484.868** | 975.111 | | | **329.840** | | | |
| Real estate activities | **3.034.255** | 1.789.356 | | | **705.072** | | | |
| Manufacturing | **809.277** | 510.071 | | | **219.188** | | | |
| Other sectors | **2.049.332** | 1.423.937 | | | **740.175** | | | |
| **Households** | **8.339.490** | 4.246.315 | 2.912.440 | 2.133.845 | **1.286.170** | 1.193.223 | 327.292 | 310.740 |
| Of which: Residential mortgage loans[2] | **5.565.680** | 2.879.120 | 2.168.251 | 1.622.346 | **614.752** | 553.454 | 181.776 | 172.587 |
| Of which: Credit for consumption[2] | **1.109.776** | 637.137 | 306.799 | 255.511 | **315.413** | 298.330 | 70.554 | 66.974 |
| **Total on-balance sheet** | **22.592.475** | **13.967.892** | **9.332.461** | **7.381.829** | **5.400.843** | **5.204.523** | **2.066.776** | **2.016.998** |

[1] Excluding loans and advances to central banks and credit institutions.
[2] The analysis shown in lines 'non-financial corporations' and 'households' is non-additive across categories as certain customers could be in both categories.

## 2. Liquidity risk and funding

### 2.1 Liquidity regulation

In addition to regulatory liquidity ratios disclosed in Note 29 of the Interim Condensed Consolidated Financial Statements for the nine months ended 30 September 2016, the Group has to comply with the Liquidity Coverage Ratio (EU) 2015/61 (LCR). It also monitors its position against the Basel Quantitative Impact Study (QIS) Net Stable Funding Ratio (NSFR). The LCR is designed to promote short-term resilience of a Group's liquidity risk profile by ensuring that it has sufficient high quality liquid resources to survive an acute stress scenario lasting for 30 days. The NSFR has been developed to promote a sustainable maturity structure of assets and liabilities.

The Capital Requirements Regulation (CRR) requires phased-in compliance with the LCR standard which started as from 1 October 2015 with an initial minimum ratio of 60%, increasing to 70% in 2016, 80% in 2017 and 100% by January 2018. In October 2014, the European Commission published a final Delegated Act for the LCR. During 2015, the monthly LCR was calculated as per the CRR and also quarterly as per the Delegated Act (as part of the Supervisory Review and Evaluation Process (SREP) Short Term Exercise). Starting from January 2016, the LCR is also calculated monthly based on the final published Delegated Regulation (EU) 2015/61. The Delegated Regulation was enacted in September 2016 and the LCR is only calculated under this Regulation (LCR as per Regulation (EU) 680/2014 has been abandoned).

In October 2014, the Basel Committee on Banking Supervision published a final standard for the NSFR with the minimum requirement to be introduced in January 2018 at 100%. The methodology for calculating the NSFR is based on an interpretation of the Basel standards published in October 2014 and includes a number of assumptions which are subject to change prior to adoption by the European Commission through the CRR.

Based on Regulation (EU) 2015/61 and Basel QIS standards respectively, as at 30 September 2016 the Group had a LCR of 0% (31 December 2015: 0%) and a Basel QIS NSFR of 88% (31 December 2015: 83%). Under the Delegated Regulation, the Emergency Liquidity Assistance (ELA) funding, as well as any other funding secured by non-LCR liquid assets and maturing within 30 days, is deducted from High Quality Liquid Assets, thus resulting in a zero LCR. It should be noted, however, that the Company considers that it has sufficient available liquidity to meet its day-to-day needs and the zero ratio is due to the above adjustment.

### 2.2 Liquidity reserves

| **Composition of the liquidity reserves** | **30 September 2016** | | 31 December 2015 | |
|---|---|---|---|---|
| | **Liquidity reserves** | **Liquidity reserves of which CRR (Delegated Regulation (EU) 2015/61) LCR eligible Level 1** | Liquidity reserves | Liquidity reserves of which Basel 3 LCR eligible Level 1 |
| | **€000** | **€000** | €000 | €000 |
| Cash and balances with central banks | **1.585.483** | **1.212.315** | 1.421.733 | 1.002.649 |
| Nostro and overnight loans and advances to banks | **620.118** | **-** | 537.722 | - |
| Other loans and advances to banks | **221.760** | **-** | 477.604 | - |
| Liquid investments | **43.630** | **49.729** | 19.594 | 2.421 |
| Available ECB Buffer | **47.963** | **-** | 178.792 | 178.792 |
| Other investments | **6.677** | **-** | 8.637 | - |
| **Total** | **2.525.631** | **1.262.044** | 2.644.082 | 1.183.862 |

## 2. Liquidity risk and funding (continued)

### 2.2 Liquidity reserves (continued)

Investments under Liquidity Reserve are shown at market value net of haircut (as prescribed by regulators) in order to reflect the actual liquidity value that can be obtained and include only the international issues of Government of Cyprus. Under LCR Liquidity Reserves, all Cyprus Government Bonds remain eligible for inclusion as Level 1 assets given that they are issued by a Member State. LCR does not require liquid assets to be eligible as collateral for central bank operations and are included at market value.

The Liquidity Reserves are managed by Group Treasury.

Cyprus exited its economic adjustment programme in March 2016. The credit ratings of the Republic of Cyprus by the main credit rating agencies continue to be below investment grade. As a result, the European Central Bank (ECB) is no longer able to include Cyprus Government bonds in its asset purchase programme, or as eligible collateral for Eurosystem monetary operations, as was the case when the waiver for collateral eligibility due to the country being under an economic adjustment programme existed. This resulted in the repayment of ECB funding at the end of March 2016 for an amount of €100 million which was collateralised by Cyprus Government bonds and materially reduced the available ECB buffer (this buffer represents the amount that could be drawn from the ECB based on the collateral pledged). However, any Cyprus Government bonds that remain unencumbered can be considered as ELA eligible collateral.

Although the Company has received no specific assurances, management expects that it will continue to have access to the central bank liquidity facilities, in line with applicable rules. In January 2014, the House of Representatives of Cyprus approved the issuance of up to €2,9 billion of guarantees. The European Commission announced in June 2016 the eighth extension of the bank guarantee scheme, which will see the scheme continue until 31 December 2016. At present, the Company does not expect to utilise the Government's guarantee scheme.

ELA is available to solvent Euro area credit institutions, and is therefore expected to remain available to the Company (subsequent to its repayment of existing ELA funds) if it were to face a 'stress event' that gave rise to temporary liquidity problems. If a stress event were to occur in the future, the Company would seek to utilise ELA funding, assuming it has sufficient available eligible collateral at the time.

In August 2016, the Company cancelled two own-issued bonds guaranteed by the Republic of Cyprus of €500 million each. The bonds bore an annual fixed interest rate at 5%. The bonds were guaranteed by the Republic of Cyprus and were issued in accordance with the relevant legislation and decrees on the 'Granting of Government Guarantees for the Conclusion of Loans and/or the Issue of Bonds by Credit Institutions Law'. No liability from the issue of these bonds was presented in debt securities in issue in the consolidated balance sheet as all the bonds were held by the Company. The bonds were listed on the Cyprus Stock Exchange and were pledged as collateral for obtaining funding from central banks. One of the bonds has been released in June 2016 from the ELA pool of collateralised assets. After taking into consideration the significant reduction of ELA funding, the Board of Directors of the Company at its meeting held on 16 August 2016, decided to proceed with the cancellation of the two bonds. Given the decision for the cancellation, the CBC released the second bond on 19 August 2016. The two bonds were cancelled on 25 August 2016, following the approval/consent from the competent authorities.

In May 2016, the Company raised new funding from ECB's Main Refinancing Operations using as collateral a pool of housing loans that satisfy the criteria of the Additional Credit Claims as set out in accordance with the Implementation of the Eurosystem Monetary Policy Framework Directives of 2015 and 2016.

Additionally, in May 2016 the Company has also concluded a repurchase transaction which is its first wholesale funding transaction since 2013. This was partially repaid in August 2016 and fully terminated by the Company in October 2016.

## 2. Liquidity risk and funding (continued)

### 2.2 Liquidity reserves (continued)

In 2014, the Group participated in the Targeted Long Term Refinancing Operations (TLTRO) of the ECB for an amount of €500 million. On 29 June 2016, the Company repaid the amount borrowed through the TLTRO amounting to €500 million and borrowed the same amount from the Main Refinancing Operations (MRO).

In August 2016 the CBC has released loans and advances with contractual value of €2 billion held as collateral for ELA and in October 2016 it has released additional loans and advances with contractual value of €2,5 billion.

## 3. Other risks

### Political risk

External factors which are beyond the control of the Group, such as developments in the European and the global economy, as well as political and government actions in Cyprus can affect the operations of the Group, its strategy and prospects, either directly or indirectly through their possible impact on the domestic economy.

Important political risk factors include the possible government intervention in the economy that may affect the Group's activities; social, economic and political developments in overseas countries where the Group operates or maintains exposure; and international developments particularly in the European Union (EU) and the Eurozone that may lead to payments crisis, changes in the regulatory and supervisory framework, or a Euro exit of a Eurozone member state. The exit of the United Kingdom (UK) following the EU referendum of 23 June 2016 may lead to an economic recession in the UK itself and to possible disruptions in the Eurozone with pressure to bear on the euro and the currency markets generally. Italy will hold a referendum on constitutional reform in December 2016. A rejection of the reforms may ignite a political uncertainty at a time when some Italian banks are trying to attract fresh capital and manage NPEs. France and Germany are facing elections in 2017.

An exit of the UK from the EU may impact Cyprus. Cyprus has trade, investment links with the UK, and it is a popular tourist destination for British tourists. In 2015 the UK accounted for 39% of all tourist arrivals and about 33% of tourist receipts as per the Cyprus Statistical Service. The possible loss of UK tourist arrivals may be mitigated at least in part, by increases in arrivals of tourists from other destinations, as tourist traffic may continue to divert away from other regional destinations. In total 9% of Cyprus imports and 7% of Cyprus exports are made with the UK. Additionally there is a relatively sizeable community of British expatriates in Cyprus, many of which have purchased homes and live permanently on the island.

Consequences for the Cyprus economy may potentially derive from the wider implications of the UK exit on the EU and the global economy. This may affect access to international markets and investment inflows.

Developments in other non-EU countries with which Cyprus maintains significant economic links, the unresolved Cyprus problem, and political and social unrest or escalation of military conflict in neighboring countries and/or other overseas areas may adversely affect the Cyprus economy.

The European Union is already stressed by economic crisis and by the refugee crisis that are creating insular reactions by member states. The UK exit from the EU may create other problems as other members choose to demand changes in the future in pursuing their own national priorities. These developments may be leading to a more fragmented Europe which may stop and sometimes reverse the process of integration. This may lead to slower growth, reduce intra-EU trade and aggravate the risk of recession.

Russia is an important economic partner of Cyprus both in terms of tourism and international business flows. Any developments that impact negatively on these linkages will have a negative impact on the economy and will thus affect the Group's operations. The standoff between Russia and the West over Ukraine continues and the United States and the EU maintain sanctions against Russia. Russia continues its military operations over Syria and relations with Turkey remain complicated despite the August 2016 rapprochement and the normalisation of diplomatic and economic relations.

**3. Other risks** (continued)

**Political risk** (continued)

As a result of sanctions and most importantly the steep decline in oil and commodity prices, Russia entered a steep recession in 2015 when the economy contracted by 3,7% and expected to contract further by 0,8% in 2016 according to the International Monetary Fund (IMF) (World Economic Outlook, October 2016). Adjusting to lower oil prices requires an ambitious fiscal consolidation programme over the medium term. Monetary policy has been on hold but normalisation can resume once underlying inflation is firmly on a declining path. Lower oil prices and necessary fiscal adjustment will keep the economy in recession in 2016 and growth is expected to resume in 2017 and reach about 1% as per IMF (World Economic Outlook, October 2016). However, with adverse demographics, and barring significant structural reforms that increase productivity growth, potential growth is likely to be at around 1,5% over the medium term. A fall in oil prices is the main risk to the outlook.

In relation to Greece, the economy contracted by 0,2% in 2015 and is expected to register a zero growth or slightly positive in 2016 before growing by 2,8% in 2017 according to the IMF (World Economic Outlook, October 2016). Greece signed a third Memorandum of Understanding (MoU) with the European Commission in August 2015 for further stability support accompanied by a third economic adjustment programme. The IMF was not part of the agreement. The Greek authorities also signed a Financial Assistance Facility Agreement with the European Stability Mechanism (ESM) to specify the financial terms of the loan.

It is now recognised that Greece will need debt relief and there is agreement on the methodology of how to assess debt sustainability. The IMF agreed that debt relief measures will be agreed at the end of the programme period and not upfront which was its initial position. In this context, the IMF is expected to support the Greek programme before the end of the year.

The Greek government has a slight majority in parliament but has so far been successful in passing important reforms. Unemployment is about 25% in Greece and youth unemployment is in excess of 50% as per Eurostat. With a shrinking labour force, low fertility rates and inefficient tax collection, the country will face considerable stresses meeting programme obligations and hence, discontent and social unrest may grow. Social unrest may remain a threat throughout 2016 and 2017, and with it, political instability will ensue. Early elections cannot be ruled out. In this context, the enforceability of the bailout programme and Greece's membership in the Eurozone may again come to be questioned.

Global economy risks remain elevated as highlighted by exceedingly easy monetary policies by most central banks, extremely low interest rates, which turned negative in many European countries and Japan, including in some cases, acceleration in credit expansion where credit outstanding is already elevated, as in China. Monetary policies have started to diverge between the Federal Reserve on the one hand, set on normalising interest rates, and most of the rest of the world on the other. These divergences are starting to put pressure on exchange rates at a time when the global financial system is particularly sensitive to a dollar appreciation. Changes in monetary policies therefore or loss of confidence in the ability of central banks to manage economic pressures, might lead to financial distress in the emerging world with broader consequences for economic activity in the advanced countries.

**4. Capital management**

The primary objective of the Group's capital management is to ensure compliance with the relevant regulatory capital requirements and to maintain strong credit ratings and healthy capital adequacy ratios in order to support its business and maximise shareholder value.

The Capital Requirements Regulation (CRR) and amended Capital Requirements Directive IV (CRD IV) became effective, comprising the European regulatory package designed to transpose the new capital, liquidity and leverage standards of Basel III into the EU legal framework on 1 January 2014. CRR establishes the prudential requirements for capital, liquidity and leverage that entities need to abide by. It is immediately binding on all EU member states. CRD IV governs access to deposit-taking activities, internal governance arrangements including remuneration, board composition and transparency. Unlike the CRR, CRD IV needs to be transposed into national laws, and allows national regulators to impose additional capital buffer requirements. CRR introduced significant changes in the prudential regulatory regime applicable to banks including amended minimum capital adequacy ratios, changes to the definition of capital and the calculation of risk weighted assets and the introduction of new measures relating to leverage, liquidity and funding.

**4. Capital management** (continued)

CRR permits a transitional period for certain of the enhanced capital requirements and certain other measures, such as the leverage ratio, which will be largely fully effective by 2019 and some other transitional provisions provide for phase in until 2024. The CBC has determined the extent of phasing-in of the transitional provisions relating to Common Equity Tier 1 deductions.

Since June 2016, the Pillar I CET1 minimum capital requirement applicable to the Group is 4,5%. The minimum Pillar I total capital requirement is 8,0% and may be met, in addition to the 4,5% CET1 requirement, with up to 1,5% by Additional Tier 1 capital and up to 2,0% by Tier 2 capital.

The capital conservation buffer is 2,5% of RWA over the minimum CET1 ratio and was fully phased in since 2015.

In addition to the above minimum capital requirements, the following capital buffer requirements are effective and are gradually being phasing-in and will become fully effective on 1 January 2022.

The level of the Countercyclical Capital buffer (CCyB) is set on a quarterly basis by the CBC in accordance with the provisions of the Macroprudential Oversight of Institutions Law of 2015 in accordance with the methodology set out in this law. The CCyB is effective as from 1 January 2016 and is determined by the CBC ahead of the beginning of each quarter. The CBC has set the level of the CCyB at 0% for the year of 2016.

Since 2015, the Group has been designated as an Other Systemically Important Institution (O-SII). The CBC set the O-SII buffer for the Group at 2%. This buffer will be phased-in gradually, starting from 1 January 2019 at 0,5% and increasing by 0,5% every year thereafter, until being fully implemented (2,0%) on 1 January 2022.

The Group is also subject to additional capital requirements for risks which are not covered by the Pillar I capital requirements (Pillar II add-ons). The Pillar II total minimum CET1 capital was determined by the ECB at 11,75% in November 2015. The Group's capital position at 30 September 2016 exceeds its Pillar I and its Pillar II add-on capital requirements. However, the Group's Pillar II add-on capital requirements are a point-in-time assessment and therefore are subject to change over time.

Following the SREP performed by the ECB in 2016, based on the pre-notification received in September 2016, the Group’s minimum phased-in CET1 capital ratio was set at 10,75%, comprising of a 4,5% Pillar I requirement, a 3,75% Pillar II requirement and the capital conservation buffer (CCB) which stands at 2,5% fully phased-in (in accordance with the prevailing CRD IV legislation in Cyprus). The ECB has also provided non public guidance for an additional Pillar II CET1 buffer.

The overall Total Capital Requirement has been set at 14,25%, comprising of a Pillar I requirement of 8% (of which up to 1,5% can be in the form of Additional Tier 1 capital and up to 2,0% in the form of Tier 2 capital), a Pillar II requirement of 3,75% (in the form of CET1), as well as the CCB of 2,5% fully phased in, which has been set for all credit institutions through the requirements of CRR/CRD IV.

The new SREP requirements will be effective as from 1 January 2017 and as at the date of the publication of these Additional Risk and Management disclosures, these requirements remain subject to ECB final confirmation, which is expected by end of 2016.

The Company’s overseas banking subsidiaries comply with the regulatory capital requirements of the local regulators in the countries in which they operate. The insurance subsidiaries of the Group comply with the requirements of the Superintendent of Insurance including the minimum solvency II ratio which is effective from 1 January 2016. The regulated investment firms of the Group comply with the regulatory capital requirements of the Cyprus Securities and Exchange Commission (CySEC) laws and regulations.

## 4. Capital management (continued)

### 4.1 Capital position

The capital position of the Group under CRD IV/CRR basis (after applying the transitional arrangements set by the CBC) is presented below.

| | **30 September 2016** | 31 December 2015 |
|---|---|---|
| **Regulatory capital** | **€000** | €000 |
| Transitional Common Equity Tier 1 (CET1)[3] | **2.736.004** | 2.747.772 |
| Transitional Additional Tier 1 capital (AT1) | **-** | - |
| Tier 2 capital (T2) | **20.990** | 30.290 |
| **Transitional total regulatory capital** | **2.756.994** | 2.778.062 |
| Risk weighted assets – credit risk[4] | **16.746.501** | 17.618.578 |
| Risk weighted assets – market risk | **6.433** | 7.811 |
| Risk weighted assets – operational risk | **2.050.325** | 2.039.888 |
| **Total risk weighted assets** | **18.803.259** | 19.666.277 |
| | | |
| | **%** | % |
| Transitional Common Equity Tier 1 ratio | **14,6** | 14,0 |
| **Transitional total capital ratio** | **14,7** | 14,1 |

During the nine months ended 30 September 2016, the CET1 was positively affected by the profit for the period and by the disposal of non-core assets and it was negatively affected by the phase in of transitional adjustments, mainly deferred tax asset. The reduction of risk-weighted assets is primarily due to the Group's ongoing efforts for risk-weighted assets optimisation. As a result of the above, the CET1 ratio increased by 60 bps during the period.

## 5. Internal Capital Adequacy Assessment Process (ICAAP), Internal Liquidity Assessment Process (ILAAP), Pillar II and Supervisory Review and Evaluation Process (SREP)

The Group prepared the ICAAP and ILAAP reports for year 2015. Both reports were approved by the Board of Directors and have been submitted to the ECB in April 2016.

The Group also undertakes a quarterly review of its ICAAP results. During the quarterly review, the Group's risk profile and risk management policies and processes are reviewed and any changes since the full ICAAP exercise are taken into consideration. The quarterly review identifies whether the Group is exposed to new risks and assesses the adequacy of capital resources in order to cover its risks, as these have evolved (compared to the full ICAAP exercise). Given completion of the full ICAAP report in April 2016, the first quarterly review for 2016, for the period up to the end of June 2016, has taken place in the third quarter of 2016.

A quarterly review is also performed for the ILAAP through quarterly stress tests submitted to the Assets and Liabilities Committee (ALCO) and Board Risk Committee, as from 2016. During the quarterly review, the liquidity risk drivers are assessed and, if needed, the stress test assumptions are amended accordingly. The quarterly review identifies whether the Group has an adequate liquidity buffer to cover the stress outflows.

[3] CET1 includes regulatory deductions, primarily comprising deferred tax assets and intangible assets amounting to €53.943 thousand and €35.193 thousand as at 30 September 2016 and 31 December 2015 respectively.

[4] Includes Credit Valuation Adjustments (CVA).

## 5. Internal Capital Adequacy Assessment Process (ICAAP), Internal Liquidity Assessment Process (ILAAP), Pillar II and Supervisory Review and Evaluation Process (SREP) (continued)

The ECB, as part of its supervisory role, has been conducting the SREP and onsite inspections on the Group. SREP is a holistic assessment of, amongst other things, the Group's business model, internal governance and institution-wide control arrangements, risks to capital and adequacy of capital to cover these risks and risks to liquidity and adequacy of liquidity resources to cover these risks. The objective of the SREP is for the ECB to form an up-to-date supervisory view of the Group's risks and viability and to form the basis for supervisory measures and dialogue with the Group. Additional capital and other requirements could be imposed on the Group as a result of these supervisory processes, including a revision of the level of Pillar II add-ons as the Pillar II add-on capital requirements are a point-in-time assessment and therefore subject to change over time.

Following the SREP performed by the ECB in 2016, based on the pre-notification received in September 2016, the Group's minimum phased-in CET1 capital ratio was set at 10,75%, comprising of a 4,5% Pillar I requirement, a 3,75% Pillar II requirement and the capital conservation buffer (CCB) which stands at 2,5% fully phased-in (in accordance with the prevailing CRD IV legislation in Cyprus). The ECB has also provided non public guidance for an additional Pillar II CET1 buffer.

The overall Total Capital Requirement has been set at 14,25%, comprising of a Pillar I requirement of 8% (of which up to 1,5% can be in the form of Additional Tier 1 capital and up to 2,0% in the form of Tier 2 capital), a Pillar II requirement of 3,75% (in the form of CET1), as well as the CCB of 2,5% fully phased in, which has been set for all credit institutions through the requirements of CRR/CRD IV.

The new SREP requirements will be effective as from 1 January 2017 and as at the date of the publication of these Additional Risk and Management disclosures, these requirements remain subject to ECB final confirmation, which is expected by end of 2016.