**Bank of Cyprus Group: Annual General Meeting**

**SPEECH: Mr. John Patrick Hourican, Group Chief Executive Officer**

**29TH NOVEMBER 2013**

*SLIDE 1*

## OPENING REMARKS

Good Morning. This is my first time to address the shareholders of the Bank as Chief Executive.

- I am pleased to have this opportunity to be in front of you and I am honoured to have been asked by the Chairman and the Board to lead The Group through this critical period of its history.
- I can assure you that The Board, the Management and all of the employees at Bank of Cyprus recognize our very real responsibility to re-build a financially sound, trusted and safe Bank.
- We recognize the size of the task and we will do all in our power and experience to restore the Bank to strength such that it can serve the Cypriot economy and be valuable to shareholders, customers and employees.

*SLIDE 2 – Progress So far*

I have only been at the Bank for four weeks now and I can confirm you that a number of very important steps towards our recovery have already been taken:

- The bank has been recapitalized through the regrettable bail in of its uninsured depositors. Its Core Tier 1 Capital ratio stands at 10.5% as at 30th June 2013;

- The bank has been reinstated as an eligible counterparty by the European Central Bank , indicating their satisfaction towards its current solvency position;
- A detailed restructuring plan has been formulated, agreed with the board and presented to and agreed with the Central Bank and the Troika;
- The integration of the former Laiki Bank operations is well advanced and will be completed by mid-2014.

*SLIDE 3- Immediate Priorities*

Of course there remains a huge amount of work to do beyond this good progress to restore the bank to strength. Our immediate priorities are clear and everyone across the Group is clear on what they are:

- We must tackle the very high level of arrears and non-performing loans. This can only be done through engaging directly and intensely with our customers and changing the way we operate. Our customers, from the very largest corporates through to our retail borrowers, need to recognize that the bank will not recover if we do not receive interest and capital repayment on outstanding loans. This will be an area of deliberate and clear focus over the coming weeks and months. It is an essential foundation for the recovery of our Group and, by extension, the Cyprus economy. We are, of course, sympathetic to the fact that some of our customers face real economic challenges and we will work with them to find viable solutions where possible. But it is important that our customers, large and smaller, recognize that, by necessity, the Bank will be more active in recovery and action around delinquent accounts, especially where the service ability of loans is clearly in question.
- We will focus on maintaining our Capital Adequacy and ensuring that our solvency throughout this journey is understood and managed. Our decisions on ownership, sale and structuring of our business interests will have an eye to ensuring we maximize solvency and balance sheet strength so as to

strengthen the foundations of trust, encouraging Cyprus' consumers and businesses to place their deposits in our care once again.

- We will continue to simplify the Group, disposing of non-core assets, both domestic and international, whilst maximizing capital. We will not fire-sale our business assets but rather manage all of the groups businesses and assets for value. We will clinically manage this process across the multiple years in our restructuring plan.
- We will complete the integration of the ex-Laiki business as swiftly and efficiently as we can. We recognize that this process is disruptive to our customers and we apologise for that. The Branch rationalization is almost complete. The systems integration is well underway and we will continue to communicate with our customers as we make progress to completion.
- Perhaps the biggest task we have is that of regaining trust with our customers. We recognize that the Bank has lost trust with its customers and the unprecedented bail-in of depositors makes this more acute. It is our intention to run this bank to better serve our customers, to raise our game in how we engage with them, to embrace transparency and adopt international best practices in risk management so as to instill confidence in our company. Ironically, the bank today belongs to the depositors and it is our job to make it valuable for them. I would appeal to our customers, you, to help us in this journey, engage with us, trust us with your money and help us make this bank valuable for you.

The last six months have been exceptionally difficult for the Group, our depositors, our customers, our shareholders and our employees. Following the Bank's failure to raise adequate capital from private investors during 2012 and its subsequent request for state support, Bank of Cyprus became the first financial institution in the European Union to be recapitalized primarily through the bail-in of depositors. We recognize the anger and the disappointment that our customers, shareholders, depositors and employees feel and the new management team will do all we can to ensure that, over time, we rebuild trust through action with each of these stakeholder groups.

**FIRST HALF OF 2013 FINANCIAL RESULTS**

I'd like to turn the Financial Results for the first half of 2013. Before I get started I'd like to point out that because of the various changes to the Group, including the sale of Greek assets to Piraeus Bank and the integration of the ex-Laiki Bank business with our Group, comparisons with the prior year period are not meaningful.

It will come as no surprise to anyone in the room that the results for this period reflect the difficulties in the Cypriot economy.

*SLIDE 4 – Profit and Loss Highlights*

Turning first to the Profit & Loss Account for the first six months of 2013

- Profit before impairment charges, restructuring and other charges for the six months to 30th June 2013 was E215 million;
- Provisions for impairment during the period was E539 million, reflecting a continued deterioration in in the loan book due primarily to worsening economic conditions and collateral values in Cyprus.
- As a result the "today" operations of Bank of Cyprus posted a loss after provisions of E324 million for the first six months of 2013;
- We incurred operating losses of E90 million from our discontinued Greek operations and a further loss of E1.4 billion on the disposal of these operations;
- We had restructuring charges amounting to E35 million during this period;
- The net loss posted to shareholder equity during the six month period was E1.8 billion.

*SLIDE 5 – Disposals*

The Group's balance sheet now reflects the consequences of the Eurogroup decisions in March 2013. Between 25th March 2013 and 30th July 2013 the Bank was under resolution and it was restructured and recapitalized as per the Decrees issued by the Central Bank of Cyprus in its capacity as The Resolution Authority.

I'd like to take a few moments to provide a little more detail on some of the key changes that occurred to the group's balance sheet during this period.

- The Group disposed of its Greek assets with a book value of E7.9 billion and Greek deposits with a book value of E7.7 billion to Piraeus Bank at an overall loss of E1.4 billion;
- The Group disposed the majority of its deposits and retail loans of its Romanian operations to Marfin Bank, with a loss on disposal of E4 million;

*SLIDE 6 – Acquisition of Laiki*

- The Group acquired the assets and liabilities of the Cypriot operations of ex-Laiki Bank, including insured deposits of E4.2 billion and Emergency Liquidity Assistance (ELA) funding of E9,1 billion.
- The Group also acquired the operations of Laiki Bank UK

*SLIDE 7 – Evolution of Deposits and Loans*

It is important for shareholders to understand the changes that have occurred to the Group's deposits and assets between 31st December 2012 and 30th June 2013. The loans and deposits of Bank of Cyprus were well balanced at the beginning of the year with E28.4 billion of deposits and E28.1 billion of loans.

- Group Deposits totaled E28.4 billion at 31st December 2012 but have been reduced to E17 billion at 30th June 2013. This change reflects:

- the disposal of E7.7 billion of deposits in Greece ;
- the acquisition of E4.2 billion of deposits from Laiki;
- the conversion of E3.8 billion of deposits into Equity;
- AND outflows of E4.1 billion of deposits during the period.

- Gross Loans totaled E28.1 billion as at 31st December 2012 and stand at E28.3 billion at 30th June 2013. Although the net change is small, it reflects the sale of gross loan exposures in Greece and the absorption of the Laiki portfolio in Cyprus.
- Bank of Cyprus is now the single largest provider of credit in Cyprus with a market share of 37% of loans at 30th June 2013.

*SLIDE 8 – A significantly different Group*

As result of these changes in our business, the Group's international footprint has been reduced, while operations in Cyprus, and exposure to the Cypriot economy, have been significantly increased. With the Cypriot operations accounting for about 85% of Group loans and deposits, respectively, the Bank's future financial performance and strength is therefore highly correlated with the economic activity in Cyprus.

*SLIDE 9 – Funding*

The funding profile of the Group has been severely weakened by the actions imposed on it by the resolution regime. Although customer deposits remain the primary source of funding, accounting for 51% of assets as at 30th June 2013, following the absorption of the assets of Laiki, the Group is now reliant on Central Bank and European Central Bank funding to the tune of E11.1 billion. Post the restoration of the Group's status as an eligible counterparty at the ECB, the Group's reliance on ELA funding has reduced by E1.3 billion to E9.8 billion and replaced with more normal ECB funding.

As has been much discussed, the decision of the Eurogroup to bail-in depositors significantly dented trust and confidence in the banking system in general and specifically in Bank of Cyprus. This resulted in large customer outflows during the immediate months following March 2013 but we are pleased to note that such outflows have significantly abated in recent weeks.

Our strategy is to continue to rebuild trust with Cyprus depositors and attract them back to the Bank. This will allow us reduce the ELA funding and, over time, restore the natural balance of loans and deposits at the Bank.

*SLIDE 10 – Loan Quality*

As I said at the opening of this presentation, we need to arrest the deterioration of the quality of our loan book in Cyprus and it will be the number 1 priority of the management team.

Loans past due for more than 90 days accounted for 38.8% of all loans outstanding at 30th June 2013, up from 27.4% at 31st December 2012. Provision coverage was at 42% at 30th June 2013 and deemed adequate at that point.

Again it will come as no surprise to anyone that, with economic conditions in Cyprus remaining challenged, the quality of the loan book continued to deteriorate into the second half of 2013. The provisions for impairment of loans are expected to remain elevated for the remainder of the year as more borrowers default and collateral values continue to decline. It is against this backdrop that I would repeat the intentions of the Bank to engage very actively in seeking repayment and recovery from its customers so as to arrest and reverse these trends.

SLIDE 11 – Capital Position

As a direct consequence of the actions carried out by the Resolution Authority, the bank's capital position has been normalized. Shareholders' equity supporting the bank's activities and risk now stands at E2.9 billion, while the Core Tier 1 capital ratio is 10.5% at 30th June 2013. We aim to preserve and enhance the capital adequacy of the Group by retaining internally generated capital and biasing our restructuring and disposal agenda to enhance capital where possible and toward making the Group financially safer.

*SLIDE 12 – Restructuring of Cypriot operations – Branches*

**RESTRUCTURING PROGRES**

Before handing back to the Chairman, I'd like to touch a few other areas which I think will be of interest to our shareholders.

- The Bank has proceeded to deal quickly with the integration of our Cyprus Banking operations and, in particular, the overlap in Branch network across the Island. The combined branch network amounted to 203 branches and personnel of 5,725.
- The total number of branches has already been reduced to 142 and we expect the rationalization plan to complete in early 2014 when the final complement will be closer to 125 branches.

*SLIDE 13 – Restructuring of Cypriot operations: Personnel*

- During the summer, the Group operated a Voluntary Retirement Scheme which was availed of by 1,370 people. This 24% reduction in our Cyprus staff to 4355 has reduced our annualized employee costs by approximately 34%.

SLIDE 14 – Restructuring Plan charts future strategic direction

As required by the Memorandum of Understanding for Cyprus, the Bank has completed and submitted a detailed restructuring plan. Our plans are detailed and we will be reviewing progress with the Authorities on a quarterly basis.

The plan was prepared with the assistance of our advisors, McKinsey & Co., and it defines the strategic objectives and actions required to create a smaller, safer and more focused institution capable of supporting the prosperity of the Cypriot Economy.

In simple terms, the key objectives of this plan are to:-

- Rebuild Trust and Confidence with depositors, customers and investors;
- Rebuild a resilient institution able to effectively manage its risk and being capable of withstanding external shocks or economic turbulence;
- Maximise synergies from a swift integration of the former Laiki businesses and orientate the branch network to best serve customers.
- Preserve the Bank's position in supporting the Cypriot Economy, supporting businesses and household;

*SLIDE 15 – Restructuring Plan: Key Pillars of Strategy*

These objectives are supported by real plans. The key pillars of our strategy can be simply articulated as follows:-

- We need to revamp and re-energise our core domestic operations to better serve our customers and protect (& grow) our deposit franchise. We want to focus our lending on promising cash generative business sectors and on lower-risk retail products.
- We will be deliberately looking at some of our largest exposures and managing them as part of a separate unit. The bank has overconcentrated exposures against some very large groups. We will be working with these customers to assess viability and to chart a course to reduce the bank's risk while supporting viable cash generative businesses.
- We are in the process of significantly increasing the capability and staffing of our delinquency and recovery teams. This is an essential part of our stabilizing the business and creating the capacity to provide credit to the Cyprus economy.

- We must (and will) change the risk profile of the Group and ensure that new business is written in way that sustains the business into the future. We will constrain the risk appetite of the group and strengthen our risk management routines.
- We will work to normalise our funding over time. We will need the trust of our depositors to achieve this.

As with any plan, our effectiveness will depend on a variety of internal and external conditions.

We are reliant on the Government implementing the reforms agreed with the Troika and we are, to a degree, a hostage of the economic trajectory of Cyprus. A deeper and more prolonged recession with all the consequent impacts on unemployment, real estate markets and customer confidence can be detrimental to our delivery.

I am encouraged by the fact that the economy is performing ahead of original expectations and that the recent visit by the Troika was a vote of confidence in measures taken by the government.

We will monitor and report on all aspects of our plan each time we meet and I look forward to building a transparent, direct and honest dialogue that I hope will be hallmarks of the New Bank of Cyprus Group over time.

I would like to close by acknowledging how difficult a time the past year has been for our employees, our customers and our shareholders. No one would have set out to create these conditions deliberately and I would ask for your support and encouragement in our plans to restore this Group to health and, in time, value.

Back to you Mr. Chairman.

END