



## ANNUAL GENERAL MEETING OF SHAREHOLDERS

24 November 2015

BOC Headquarters

Speech by the Chairman of the Board of Directors,  
Dr Josef Ackermann

Dear Shareholders,  
Distinguished guests,  
Dear Colleagues,

It is with great pleasure that I welcome each one of you to the Annual General Meeting of Shareholders of the Bank of Cyprus.

This is my first Annual Shareholder Meeting as Chairman of the Board of Directors of the Bank of Cyprus, but I believe that this is the 103rd such meeting for the Bank. As you know, the Bank was established in 1899 and was initially called “*Nicosia Savings Bank*.” But it was renamed “*Bank of Cyprus*” and recognized as a public company in 1912 with annual shareholder meetings taking place ever since.

Many things have happened to Cyprus and the Bank since then, particularly over the past few years, but the Bank has remained the island’s principal financial institution in the service of the Cypriot society.

It is with this sense of history and importance of the Bank of Cyprus for the Cypriot economy and the Cypriot people that my colleagues and I took our current duties as members of the Bank’s Board of Directors under its new shareholder structure at the last AGM in November 2014. We are very much aware that the ownership of the Bank is fairly unique, as more than 46% of the Bank’s shares are held by bailed-in former depositors. We are particularly cognizant of the dramatic circumstances that led to the restructuring of Cyprus’ two leading banks in March 2013 and of the painful consequences and suffering this restructuring and the overall economic and banking crises have caused for all Cypriot people.

But we are also convinced of the good prospects that lie ahead for both the Cypriot economy and the Bank of Cyprus, as their financial health and prosperity are closely interlinked. The Board of Directors has full confidence in the future of the Cypriot economy and of the Bank of Cyprus. It shares fully the sentiment of the new Bank shareholders who backed their views with an injection of €1 billion of new capital in late 2014.

I would like to assure you that the Board of Directors is dedicated to doing its utmost to advance the interests of all shareholders, both old and new, and together to help Cyprus achieve its full economic potential. From day one, the new Board has moved decisively to adopt the best practices in corporate governance, improve transparency, install proper delegation of responsibility for Board committees, and enhance the oversight and review of implementation of the Bank's strategy in order to both increase shareholder value and promote the interests of our clients and the Cypriot economy in general.

Dear Shareholders,

The financial position and performance of the Bank of Cyprus has improved dramatically since early 2013, but, as you well know, major challenges remain.

The Bank is getting stronger and so is the Cypriot economy. Much has been achieved, but also much more remains to be done.

Before I comment on the Bank's financial performance, I would like to discuss briefly the external and domestic economic environments in which the Bank operates.

#### **External economic environment**

The evolution of the Bank's financial performance over the past year took place in the context of a difficult global economic environment. Global growth has been hesitant and has recently been scaled back as a result of weaker prospects in China and other major emerging markets. The contraction of economic activity in Russia and Ukraine is of particular significance to Cyprus, affecting adversely tourist arrivals and spending, and non-resident financial transaction flows channelled through Cyprus. The renewed financial crisis and political and economic uncertainties in Greece for most of the year also raised concerns and potential risks.

#### **Domestic economic environment**

On the domestic front, economic conditions in Cyprus have continued to improve and to exceed expectations, even though there have been delays in the adoption of and postponements to the implementation of key structural reforms. Performance under the government's economic adjustment program has been kept on track, with better-than-planned fiscal outcomes and a stronger-than-expected recovery in output. Real GDP declined by less than expected in 2014 and has recorded increasing positive growth rates so far in 2015. The unemployment rate peaked at the end of 2014 and has since started to decline, albeit remaining still at high levels, particularly for young people. The remaining capital controls were lifted in early April 2015, and the government has returned to the international capital markets. The yields on sovereign bonds have declined to historically low levels, and international rating

agencies have upgraded both the Republic of Cyprus and the Bank of Cyprus. These are very welcome developments as they demonstrate the restoration of confidence in the banking system and the steady progress achieved under the government's program.

We welcome in particular the adoption of a new legal framework for foreclosures and insolvency, which became effective in August 2015, albeit much later than initially expected and with some complicated procedures and restrictions. This framework is very useful and we hope it will contribute to restoring more balance in the incentives of bank lenders and borrowers, reducing the incentives for strategic defaults, and facilitating the reduction of non-performing bank loans. However, the effectiveness of the new legal framework remains to be tested in practice, as cases come before the courts. We are pleased to note that the authorities stand ready to make reasonable amendments if necessary, as experience in the implementation of the new legislation is gained. We also welcome the recent adoption of the legislation on the sale of bank loans.

Going forward, the outlook for the economy is projected to improve further, with positive growth in output and employment projected for 2015 and 2016. Much remains to be done to consolidate the gains achieved so far and attain the true growth potential of the Cypriot economy. This will be critical, not only for lowering unemployment from its still very high levels, but also for facilitating the on-going deleveraging process by the household and corporate sectors, and for making it easier to accelerate the process of lowering on a lasting basis the high level of non-performing loans. This would also make it possible for banks in Cyprus to meet the likely increase in creditworthy demand for bank credit, and thus stimulate the expansion in output.

To this end, we very much hope that, as the Troika-supported program comes to an end in early 2016, the authorities guard against complacency and adopt instead the additional much needed structural reforms that are critical for promoting domestic and foreign investment, and thus boosting output growth. Many of these reforms are already envisaged under the government's program.

The Bank of Cyprus considers that a stronger growth than currently projected is possible provided there is government determination to sustain the reform momentum with the adoption and implementation of additional ambitious structural reforms. Such faster growth is necessary to reverse the increase in unemployment. The required reforms include *inter alia* a further improvement in the business environment; a much needed enhancement of the effectiveness of legal procedures so as to allow the timely delivery of justice and the adequate protection of investor property rights; the removal of rigidities in the labour market to allow modernization in human resource management and remove the disincentives for

hiring new employees; and the adoption and implementation of an appropriate growth strategy for the tourism sector where Cyprus has a tremendous unexploited comparative advantage. I note in this regard that, despite some modest gains over the past few years, the number of tourist arrivals and gross tourist receipts are today much lower than they were in 2001!

### Overview of BOC financial performance

Notwithstanding the broadly still difficult domestic and external economic settings, the Bank of Cyprus has achieved a major improvement in its financial performance, as demonstrated in the financial results for 2014 and the first three quarters of 2015. John Hourican will summarize the progress made in more detail in a few minutes, but allow me to highlight some of the key points:

- The Bank's restructuring strategy has been implemented successfully. The Bank has exceeded in many areas the performance targets established under the three-year restructuring plan agreed to with the authorities and the Troika in 2013.
- Financial performance during 2014, which is the main agenda item for today's shareholders' meeting, was a turning point for the Bank. It reflected the first annual effects of the new strategy of shrinking the Bank's balance sheet to strength, enhancing its capital base and rebuilding confidence. By the end of the year, the Bank recorded a small positive profit after tax and before the costs for restructuring and discontinued operations. More importantly, the decline in the Bank's deposits was arrested and a small increase in deposits was recorded in the last quarter.
- The Bank's financial performance improved further during the first nine months of 2015, as evidenced in the financial results released yesterday. The Bank recorded positive profits after tax and after the cost of restructuring and discontinued operations in each of the first three quarters of this year.
- The Bank has made enormous strides in deleveraging from high risk assets held outside Cyprus, including in Ukraine, Romania, and, more recently, Russia, as part of its strategy of de-risking and cutting its asset portfolio back to strength.
- The Bank has regained the confidence of both its resident and non-resident depositors, as deposits rose further during the first three quarters of 2015. The Bank has weathered well the lifting of capital controls last April, as

deposits by our non-resident clients have resumed their upward trend after a brief initial modest decline.

- The Bank's liquidity position has improved significantly. This, combined with the repayment ahead of schedule of government bonds held by the Bank and new innovative financing schemes, have facilitated a sharp reduction in ELA by €2,2 billion during 2014 and by €3,1 billion so far in 2015, at a much faster pace than initially envisaged. The ELA now stands at €4,3 billion.
- The Bank's capital position has remained strong, ranging between 14% and 15,6% based on the CET1 ratio, since the €1 billion recapitalization in late 2014. This is despite continued provisions against impaired and other non-performing loans.
- The stock of non-performing loans has levelled off and has begun to decline steadily since March 2015. The difficult domestic economic setting has contributed to further large new inflows of NPLs, but these have been more than offset by loan restructurings and cash collections. The NPL coverage ratio has increased steadily, and NPLs are more than 100% covered if account is taken of the current market value of tangible loan collateral.
- Bank new credit expansion has resumed at a slow pace. Such an expansion remains constrained, not so much by the availability of loanable resources, but by the continued limited creditworthy demand by the private sector, consistent with the new central bank documentation requirements for new loan origination.

But let me emphasize that the Bank strategy is not solely defined in terms of technocratic quantitative objectives and cold profitability metrics. Our fundamental objective remains to serve the needs of our customers and of the Cypriot economy, which are the core commercial priorities of the Bank. Ensuring that our customers are well served will also ensure that we create a valuable investment for our shareholders, as well as a rewarding environment for our staff to work.

We have strived to regain our customers' and shareholders' confidence and loyalty, to listen to your views about our current services and past practices and to meet fully your expectations. We believe we have made significant progress, but we also recognize that we still have some way to go. We are committed to reinforcing our efforts in this regard.

We are also very much committed to the Bank's broader role in the Cypriot society. The Bank has continued to contribute to the community at large by advancing further its activities in several areas of corporate social responsibility. Special mention could be made in this context of the Bank's assistance to cancer patients through our Oncology Centre, with cumulative funding in excess of €50 million since its inception in 1998, caring cumulatively for more than 30,000 patients. Equally important is the Bank's contribution to the island's cultural life and children's education and scholarship through the Bank's Cultural Foundation in Nicosia and the Pierides Museum in Larnaca.

### **Non-performing loans**

As many questions have been raised by shareholders, the authorities and the public at large about our efforts to deal with NPLs, particularly those concerning the Bank's largest borrowers, please allow me to provide some more detail on what the Bank has been doing and on the prospects for the period ahead.

A great deal has already been achieved in dealing with the large portfolio of non-performing loans through the implementation of customized strategies for the larger exposures and a range of more industrial options for the non-performing retail and SME loans. The restructuring process has been intensified over the past year and many of the negotiations with the largest borrowers are expected to be completed in the months ahead. I can assure you that the strategies we have followed seek to achieve a sustainable outcome for the borrower, better protection for the Bank and, importantly, better lending standards across the portfolio. We hope to see these efforts translate into an improvement in some of the statistics around non-performance over coming quarters.

More specifically, as regards the non-performing portfolio for major corporates of €4,5 billion, restructuring agreements have already been reached for two thirds of these loans, of which one quarter has already been executed. Loan restructurings so far in 2015 amounted to €2,7 billion, almost 20% of all NPLs, and affected 10,700 borrowers.

We are fully aware of the challenges the difficult economic situation has created for all bank borrowers, especially for individual households and SMEs. It is not our intention to resort to widespread foreclosures as now allowed under the new legal framework.

But to achieve accelerated progress in restructuring non-performing loans we need first and foremost a stronger commitment by individual borrowers, both large and

small, to cooperate with the banks and to the principle that borrowers should respect their financial obligations. An endorsement of this principle by the authorities is essential.

At the same time, in specific cases of genuine hardship by the borrowers, we recognize the need for a fair burden sharing, while always remembering that we are dealing with depositors' money.

### Change in Chief Executives

I would like now to address the issue of CEO succession.

We have informed this morning, before the beginning of the trading session, the Cyprus Securities and Exchange Commission and the Cyprus Stock Exchange that John Hourican will stay on as CEO under a new contract. You may have seen the news already on your mobile phones.

My colleagues at the Board of Directors and I are obviously very pleased and excited that John Hourican has agreed to stay on and continue the excellent work he has been doing over the past two years. I would like to express our thanks to Rioghnach Hourican who is sitting in the front seats for her support for John's decision.

As you know, the Board's Nominations Committee has launched a search for a new CEO since last April and we have actually made substantial progress in this regard by identifying a short list of well qualified candidates. At the same time, however, we have been working on John to encourage him to reconsider his earlier decision to step down and to remain instead on board. We are delighted at the end that John and his family have agreed to do so.

John has done a remarkable job in leading the Bank over the past two years. He has literally put Bank of Cyprus on the global financial map and justifiably earned the recognition of "*Banker of the Year*" bestowed on him by the *Euromoney Awards for Excellence* for 2015. His achievements are numerous and impressive. In a nutshell, he has, in a short period of time, instilled self-confidence and motivated a rather discouraged staff, established rigorous and effective management structures, empowered a team of talented young executives to respond to the new challenges and implemented a demanding restructuring plan, establishing a new, dedicated loan restructuring and recovery division. He has also secured a very successful and very timely recapitalization of the Bank from foreign investors, made major strides in deleveraging non-core assets in other countries and sharpened the focus of the Bank's core activities in Cyprus.

Overall, John has been instrumental in achieving the strong improvement in the Bank's financial performance. We are fully confident that, with him at the helm of the Bank, and with the support of the existing strong executive team, we will make further major strides in implementing the Bank's strategy.

### **The way forward**

Looking ahead, the Bank's strategy will remain focused on serving the needs of our clients and achieving value for our shareholders, while also aiding the recovery of the Cypriot economy. The Bank and the Cypriot economy are in the same boat and we need to work together with the whole Cypriot society.

Our immediate top priority remains the further enhancement of the quality of our assets through a steep reduction in the outstanding stock of NPLs and continued deleveraging of non-core assets.

At the same time, we will focus on advancing the core activities of the Bank through a broader range of financial products and services, better client-centred service, stepped up technological innovation, and enhanced operational efficiency. In addition, we will continue to explore options for the diversification of the Bank's funding sources and the potential listing of the Bank on more liquid, index-driven European stock exchanges.

### **AGM agenda items**

The business before today's AGM is mostly self-explanatory. Shareholders are asked to receive and approve the accounts for 2014, to reappoint the auditors, to fix the remuneration of the Board and, on this occasion, to authorize the Board to put in place a long-term incentive plan for key members of staff. I would like to add some specific comments on the last two of these agenda items.

It is important that our shareholders are well served by a professional, international and committed Board of Directors who are reasonably remunerated for the work they do. During 2015 we have carried out an extensive review of the Board and committee fee structures. We have concluded that the fees needed to be amended to reflect the level of work and commitment required of our Board. We are of course acutely conscious of the need to exercise restraint in all matters of remuneration and we have weighed this responsibility with the need to attract and retain the highest calibre board members. I believe that the proposals put before the AGM today reflect this balance.

We still have much to do to complete our journey back to full health and value. The Board believes that our shareholders will be best served through creating a targeted and aligned long-term incentive scheme for the senior management and key

employees at the Bank. Introducing this plan is an important step in creating a modern and progressive performance culture at the Bank, aligned with the interests of shareholders. Today, the Bank has no ability to pay short-term incentives or bonuses and we believe it is essential to have a long-term share-based scheme in place to better attract, motivate and retain the best talent. The plan will be designed to vest after 2019 and will only begin to accrue any value once a share price of 25 cents is exceeded and important safety metrics, such as the full repayment of ELA, have been achieved. We are seeking discretion from our shareholders to put this in place during 2016 and to engage with our regulators to approve such a scheme.

Dear Shareholders,

In conclusion, I would like to reiterate that, while the Bank has made substantial progress, exceeding initial expectations, many challenges remain. We believe we have the right strategy and a strong and dedicated senior management team to address these challenges, regain fully the trust of our customers, depositors and the Cypriot society more broadly, and play our traditional leading role in advancing the Cypriot economy. We would like to count on your support for achieving these objectives. I am fully confident that together we can meet them.

Thank you very much.