



COOPERATIVE  
CENTRAL BANK

# Key Performance Indicators and Overview of Progress in the Implementation of the Restructuring Plan of the Cooperative Credit Sector

FOR THE PERIOD ENDED  
31 MARCH 2017



## A. Key Performance Indicators

Following a consultation with the Central Bank of Cyprus, the following Key Performance Indicators (KPIs) have been selected for the Cooperative Credit Sector (CCS), including mid-term targets, which represent the priorities of the CCS. These Indicators are published on a quarterly basis, enabling the public to evaluate the progress of the Restructuring Plan (RP) and the financial performance of the CCS.

The following table presents the aforementioned Indicators, the mid-term targets for each Indicator as amended in accordance with the RP that was revised in December 2015, and the latest data for each Indicator.

Cooperative Credit Sector Key Performance Indicators		31.12.2016	31.03.2017	Medium-Term Target 31.12.2018
Loan portfolio Quality	Provisions to 90+ Days Past Due Loans	57,4%	58,3%	> 50%
	Provisioning charge ( <i>Cost of Risk</i> )	1,0%	1,0%	<2%
	90+ Days Past Due Loans (€ mln)	5.699	5.724	<4.500
	90+ Days Past Due Loans, excluding interest as of 01.01.2014 (€ mln)	4.439	4.359	
Funding	Loans (after provisions) to Deposits ratio	69,7%	70,0%	<85%
Capital	Common Equity Tier 1 capital ratio	15,4%	15,5%	>15%
	Leverage ratio ( <i>Assets/Equity</i> )	11,8 x	11,6 x	<12 x
Efficiency	Cost to Income ratio	50,5%	49,7%	<50%
	Net Interest Margin	2,1%	1,9%	>2,0%
	Cooperative Credit Sector branches	246	246	200
	Cooperative Credit Sector employees	2.677	2.671	2.700

## B. Comments on the evolution of the key performance indicators

### Loan portfolio quality

As at 31 March 2017, the Provisions to 90+ days past due loans ratio increased to 58,3%, compared to 57,4% as at 31 December 2016. The provisioning charge for the quarter ended 31 March 2017 remained stable to 1,0% (annualized), compared to the year ended 31 December 2016. The 90+ days past due loans did not show any substantial variation and remained below 50% of the loan portfolio.

### Funding

The loans (after provisions) to deposits ratio increased to 70,0% as at 31 March 2017 compared to 69,7% as at 31 December 2016.

### Capital

Capital adequacy ratio (Common Equity Tier 1 capital) for the quarter ended 31 March 2017 amounted to 15,5%, compared to 15,4% as at 31 December 2016 due to the decrease in risk weighted assets. The capital adequacy of the CCS is higher compared to the minimum regulatory requirements. The Leverage ratio for the quarter ended 31 March 2017 decreased to 11,6x compared to 11,8x as of 31 December 2016.

### Efficiency

Cost to income ratio decreased for the quarter ended 31 March 2017. Specifically, it decreased to 49,7%, compared to 50,5% for the year ended 31 December 2016. The decrease in total costs compensates the decrease in net interest income, mainly due to the decrease in interest income. The decrease in interest income resulted in the decrease in the net interest margin for the period ended 31 March 2017 to 1,9% compared to 2,1% during the prior year 2016.

The branch network as at 31 March 2017 remained stable to 246 branches maintaining the wide presence of the CCS throughout the island. The number of employees as at 31 March 2017 decreased to 2.671 compared to 2.677 as at 31 December 2016.

## C. Comments on the progress in the implementation of the Restructuring Plan

In December 2015, the Cooperative Central Bank (CCB) submitted an amended Restructuring Plan for the approval of the additional state aid of €175 mln with the purpose of meeting the supervisory capital requirements as assessed by the Single Supervisory Mechanism of the European Central Bank (SSM).

On 18 December 2015, the European Commission approved an additional state aid of €175 million in favor of the CCB and the affiliated CCIs in line with EU state aid rules. The recapitalization of CCB was completed through the increase of €175 million of equity and was fully covered by the independent Recapitalization Fund, in exchange for participation in the ownership structure of CCB. The Recapitalization Fund was set up as per article 3 of the Enactment and Operation of an Independent Recapitalization Fund Law of 2015.

The additional state aid is accompanied by a series of additional restructuring measures / actions that the CCB is committed to gradually implement throughout the restructuring period.

### IPO readiness assessment:

The final signed Prospectus was submitted to the Cyprus Securities and Exchange Commission (CySEC) on 22 December 2016. The CySEC sent a letter of approval of the CCB's Prospectus on 22 December 2016. Also, following the instructions of the Cyprus Stock Exchange (CSE), the Bank submitted the signed Annexes 4 and 7 for the application of the CCB, thus ensuring the pre-approval by the CSE.

### Legal merger of the CCIs with the CCB:

In December 2016, the management of the CCB decided to recommend the legal merger of the CCIs with the CCB as part of implementation of the strategy for restructuring of the CCS. The decision on the legal merger of CCIs with the CCB was approved by the General Meeting of the shareholders on 30 December 2016. The merger is expected to increase the value of the Organization and to strengthen its efforts to form a modern corporate governance framework, which will enable it to become more transparent, competitive and attractive for potential investors, in view of the forthcoming admission to the regulated market of CSE, through which it will be possible to restore the CCS to an enlarged and domestic ownership basis.

**Transfer of staff from the CCIs to the CCB:**

The transfer is expected to take place through the legal merger of the CCIs with the CCB while the provisions of the relevant law regarding the employees' rights in the transfer of business will be fully implemented (Law N.104 (I) / 2000).

**Comments on the overall progress of the implementation of the Restructuring Plan**

The responsibility for supervising the implementation of the Restructuring Plan has been assigned to the Strategy and Transformation Division of the CCB which reports directly to the General Manager. The planned actions for the implementation of the Restructuring Plan are divided into four basic pillars, as follows:

1. **Enhancement of Corporate Governance and Risk Management**
2. **Cost reduction and operational efficiency**
3. **Management of non-performing loans**
4. **Commercial and other non-core activities**

The progress achieved thus far is presented below:

**Corporate Governance and Risk Management**

The mergers of the 93 CCIs to 18 new entities were completed on 22 March 2014.

A new organizational structure became operational on 23 May 2016, as per the amended Restructuring Plan ('RP') of December 2015 with the target to improve the operational efficiency and internal processes and procedures of the CCB and the affiliated CCIs. According to the amended RP the Board of Directors ('BoD') of the CCIs shall be comprised of 2 executive managers of the CCI and 1 CCB manager. In this respect, the number of members of the BoD was reduced to three (3), they were appointed on 1 March 2016 and they have fully assumed their duties. Furthermore, the revised Terms of Reference of the BoD of the CCIs have been approved by the BoD of the CCB.

The CCB has appointed six advisory councils (one in each regional district of Cyprus and one for the professional CCIs).

More specifically the advisory councils shall operate at a regional level and will advise in writing the BoD of the CCB, on various issues such as the needs of the local community and innovative social programs that will enhance education, culture and sports.

According to the ministerial decree issued by the Ministry of Finance, Article 14 on the "Restructuring of Financial Institutions Laws 2011 to 2015", on the 6th of May 2016, the percentage shareholding the ownership structure of CCB is as follows:

<b>% shareholding, following the capital injection of €175m</b>	
Republic of Cyprus	<b>77.34%</b>
Recapitalization Fund	<b>21.88%</b>
CCB Holding Company	<b>0.78%</b>
CCIs Holding Companies	<b>0</b>
<b>Total</b>	<b>100%</b>

A Special Purpose Vehicle (SPV) was registered on 25 May 2016 with the name "CCSRE Real Estate Company Ltd" and CCB is the sole shareholder (as per the relevant ministerial decree issued by the Ministry of Finance). By the end of June 2016, the transfer of non-financial assets of CCB and CClIs to the SPV was completed.

A common Credit Policy has been prepared and implemented throughout the Cooperative Credit Sector. In addition, risk limits have been set and are being reviewed regularly on a consolidated Credit Sector basis, regarding all significant risks that the organization is exposed to.

The Internal Audit function was enhanced with emphasis given to the independence of the Internal Auditors. It is noted that the Internal Audit Unit has been centralized at the CCB level with a new structure that became fully operational on 31 December 2015. As per the centralized internal Audit Framework of CCB specialized Internal Audit software has been implemented and became fully operational from the end of March 2016.

By the end of January 2016, the operational merger of the CCB and SEM Ltd was completed. As a result SEM Ltd has been fully integrated in the organizational structure of the CCB as the Senior Technology Division. The final approval of the merger of SEM Ltd with the CCB was provided by the Supervisory Authorities on 26 August 2016.

The centralization of the Compliance Unit was completed on 31 March 2016 and the existing Compliance staff of the CClIs was transferred to the CCB's Compliance Unit. The CCB's Compliance Unit has full control and responsibility of the Compliance Framework of the CCS.

Moreover, the centralization the Risk Management Unit (RMU) has been completed within the deadline set for the end of May 2016. The Risk Charter of the CCB and the affiliated CClIs has been revised in order to reflect the new structure of the centralized RMU and has been approved by the Risk Committee.

According to the CCB's strategy framework the CCB proceeded with the implementation of the necessary reforms in order to upgrade the operations of the CCS and obtain prudent management and cost efficiency. The centralization of the following Divisions / Units of the CCB has been completed:

Description	Target Date
Internal Audit Unit	<b>31 December 2015</b>
Senior Technology Division	<b>31 January 2016</b>
Compliance Unit	<b>31 March 2016</b>
Risk Management Unit	<b>31 May 2016</b>
Credit Control Department	<b>31 May 2016</b>
Human Resources Division	<b>31 May 2016</b>
Organisation & Methods Division	<b>30 June 2016</b>
Documentation & Administration of Credit Facilities Division	<b>31 October 2016</b>
Movable and Immovable Property Department	<b>30 June 2016</b>
Senior Finance and Accounting Division	<b>31 October 2016</b>
Tenders Department	<b>31 December 2016</b>

A project for enhancing the framework of the Management Information Systems is in progress.

The policies and operational procedures manuals of the CCB are revised on a continuous basis in line with best - practice for banks and the requirements of the Supervisory Authorities.

### **Cost reduction / Efficiency improvement**

To meet the targets set out in the RP the following actions were taken:

The salaries were reduced by more than 15% on an annual basis.

A Voluntary Retirement Scheme was implemented in April 2014. The scheme was taken up by 297 employees, with an annual reduction in staff costs of €12,7 mln.

On 15 September 2016, the 2nd Voluntary Retirement Scheme was completed and as a result 78 employees exited the sector.

It is noted that the first phase of the CCIs branch network rationalization project, which was initiated on the basis of the provisions of the Restructuring Plan, has been completed. As a result, the branches had been reduced to 251 by the end of December 2015. On 31 December 2016, the number of branches has been reduced to 246. The second phase of the branch rationalization project is expected to be completed by the end of June 2017.

Overall, significant effort is being made for substantial reduction in the operational expenses of the CCB and the CCIs so as to maintain them to low levels in the coming years.

### **Managing Loans in Arrears**

The Non – Performing Loans Management Senior Division (SNPLD) of the CCB is at full operational capacity as from 1 May 2014. The SNPLD comprises of 4 Divisions (Early Arrears Management Division, Arrears Management & Restructuring Division, Debt Recovery Division, Asset Management & Real Estate Division) and its main aim and responsibility is to efficiently and effectively manage the delinquent portfolio of the CCS from early arrears to terminated accounts and foreclosures based on the Strategic Plan approved by the BoD of the CCB. This is achieved through common strategy and policies which have been prepared and implemented throughout the CCS. The arrears management strategy as well as all related policies are under continuous assessment and revision, in line with current market conditions. SNPLD has proceeded with the revision of the Arrears Management and NPE Strategy for the CCS, covering the three year period 2017 – 2019, aiming at the reduction in the absolute number of NPEs of the CCS.

Realizing the importance of the successful management of exposures in arrears and NPEs for the CCS and the economy in general, the SNPLD has been investing in the upgrade of both technology infrastructure and human resources.

Since September 2015, a well-known consultancy firm with international expertise in managing loans in arrears and NPEs has been engaged by the SNPLD to give support and offer knowledge in a number of issues. One area covered in collaboration with the above mentioned firm is the micro segmenting of the delinquent portfolio, with the main aim to adopt optimal and where applicable standardized approaches for each segment, aiming to increase both efficiency and effectiveness.

The Arrears Management & Restructuring Division through its network of regional offices has been proposing restructuring solutions to cooperating customers that face or are expected to face financial difficulties based on the Arrears Management Directive of the CBC, whilst demonstrating appropriate sensitivity to cases involving vulnerable groups of the population. It is noted that the CCS has managed to achieve the targets set by the CBC since Q3 of 2015 regarding the delinquent portfolio.

The Debt Recovery Division continues to intensively handle the terminated accounts through the implementation of the appropriate legal measures including foreclosures.

In March 2016, the Asset Management & Real Estate Division was set up to centrally manage the entire real estate and investment portfolio of the CCS and effectively support the NPL restructuring process. The transfer of all the real estate assets of the CCS has been completed. Information regarding the real estate properties of the CCS which are available for sale is listed on the website <http://www.realestate.coop.com.cy>.

The newly centralized call center aims to improve the effectiveness of early arrears management. It became operational in May 2016 and reports to the Early Arrears Management Division. The new Division aims to timely and proactively manage credit facilities in early arrears, so as to prevent performing exposures turning to non performing. The Early Arrears Management Division has been staffed with appropriately trained personnel and the required infrastructure has been set up.

SNPLD is currently evaluating available methods and strategic options with regards to NPL management, aiming to significantly improve performance and operational efficiency in managing the delinquent portfolio of the CCS.

**Commercial and other non-core activities***Commercial Non Credit Participations*

There is a commitment to divest the participations of CCS to commercial non credit companies by the end of 2018. In this respect, following the completion of valuations by independent valuation firms, divestment proposals have been submitted by the entities of the commercial cooperative sector for all the major commercial participations of the CCS, which have been approved by the BoD of CCB. The sale agreements for the agreed transactions, which involve all the major commercial participations, have already been drafted and are expected to be signed upon the approval of the Registrar of Cooperative Enterprises. The transaction of PEAL Troodos Ltd has already been completed.

*Commercial Activities*

Regarding the divestment of commercial activities, all activities have been divested during the year 2016, with the exception of two activities for which the transaction is still pending and whose divestment is expected to be completed within 2017.