ERSTE Group

Erste Group posts net profit of EUR 918.0 million in the first half of 2021 on the back of strong operating performance and low risk costs

Financial data

Income statement					
in EUR million	**Q2 20**	**Q1 21**	**Q2 21**	**1-6 20**	**1-6 21**
Net interest income	1,167.9	1,172.1	1,276.5	2,396.9	2,448.7
Net fee and commission income	452.5	540.0	559.0	956.7	1,099.0
Net trading result and gains/losses from financial instruments at FVPL	129.2	66.4	60.3	9.3	126.7
Operating income	1,808.9	1,828.6	1,962.1	3,471.9	3,790.7
Operating expenses	-1,003.5	-1,103.3	-999.7	-2,114.7	-2,103.0
Operating result	805.4	725.3	962.4	1,357.2	1,687.7
Impairment result from financial instruments	-613.7	-35.7	-47.2	-675.4	-82.9
Post-provision operating result	191.8	689.6	915.2	681.8	1,604.8
Net result attributable to owners of the parent	**58.5**	**355.1**	**562.9**	**293.8**	**918.0**
Net interest margin (on average interest-bearing assets)	2.04%	1.99%	2.13%	2.10%	2.07%
Cost/income ratio	55.5%	60.3%	51.0%	60.9%	55.5%
Provisioning ratio (on average gross customer loans)	1.48%	0.08%	0.11%	0.82%	0.10%
Tax rate	25.1%	22.0%	18.7%	27.5%	20.0%
Return on equity	0.2%	9.6%	13.0%	3.4%	11.3%

Balance sheet					
in EUR million	**Jun 20**	**Mar 21**	**Jun 21**	**Dec 20**	**Jun 21**
Cash and cash balances	18,433	53,954	48,421	35,839	48,421
Trading, financial assets	47,667	48,381	50,849	46,849	50,849
Loans and advances to banks	27,418	27,477	24,541	21,466	24,541
Loans and advances to customers	163,736	167,839	172,114	166,050	172,114
Intangible assets	1,331	1,332	1,342	1,359	1,342
Miscellaneous assets	6,106	5,985	6,168	5,830	6,168
Total assets	**264,692**	**304,969**	**303,435**	**277,394**	**303,435**
Financial liabilities held for trading	2,737	2,192	2,412	2,625	2,412
Deposits from banks	21,984	35,288	34,643	24,771	34,643
Deposits from customers	182,670	205,374	206,256	191,070	206,256
Debt securities issued	29,431	32,516	30,243	30,676	30,243
Miscellaneous liabilities	6,669	6,827	6,510	5,840	6,510
Total equity	21,200	22,771	23,371	22,410	23,371
Total liabilities and equity	**264,692**	**304,969**	**303,435**	**277,394**	**303,435**
Loan/deposit ratio	89.6%	81.7%	83.4%	86.9%	83.4%
NPL ratio	2.4%	2.6%	2.5%	2.7%	2.5%
NPL coverage ratio (based on AC loans, ex collateral)	91.1%	89.5%	91.4%	88.6%	91.4%
Texas ratio	18.8%	19.8%	18.9%	20.3%	18.9%
CET1 ratio (final)	14.2%	14.0%	14.2%	14.2%	14.2%

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HIGHLIGHTS

P&L 1-6 2021 compared with 1-6 2020; balance sheet as of 30 June 2021 compared with 31 December 2020

Net interest income increased to EUR 2,448.7 million (+2.2%; EUR 2,396.9 million), primarily due to one-off effects resulting from TLTRO III take-up in Austria and Slovakia. **Net fee and commission income** rose to EUR 1,099.0 million (+14.9%; EUR 956.7 million). Increases were posted across all fee and commission categories and core markets, with significant growth seen most notably in payment services as well as in asset management and in the securities business. **Net trading result** improved to EUR 43.1 million (EUR -19.2 million); the line item **gains/losses from financial instruments measured at fair value through profit or loss** rose to EUR 83.6 million (EUR 28.5 million). The development of these two line items was driven mostly by valuation effects. **Operating income** increased to EUR 3,790.7 million (+9.2%; EUR 3,471.9 million). **General administrative expenses** were reduced moderately to EUR 2,103.0 million (-0.6%; EUR 2,114.7 million). Personnel expenses declined to EUR 1,248.9 million (-1.3%; EUR 1,265.5 million). Other administrative expenses were slightly lower at EUR 581.3 million (-0.4%; EUR 583.3 million) despite a significant rise in payments into deposit insurance schemes to EUR 109.2 million (EUR 92.3 million). Most of the contributions expected for 2021 have already been posted upfront. Depreciation and amortisation rose to EUR 272.8 million (+2.6%; EUR 265.9 million). The **operating result** increased markedly to EUR 1,687.7 million (+24.4%; EUR 1,357.2 million) and the **cost/income ratio** improved to 55.5% (60.9%).

Due to net allocations, the **impairment result from financial instruments** amounted to EUR -82.9 million or 10 basis points of average gross customers loans (EUR -675.4 million or 82 basis points). Net allocations to provisions for loans as well as for commitments and guarantees were posted in all core markets, with the exception of Austria, but remained generally at a low level. A positive contribution came from income related to the recovery of loans already written off. In the comparative period, the updated risk parameters with forward looking information related to Covid-19 had resulted in a marked increase in net allocations to provisions for loans as well as for commitments and guarantees given. The **NPL ratio** based on gross customer loans improved to 2.5% (2.7%). The **NPL coverage ratio** increased to 91.4% (88.6%).

Other operating result amounted to EUR -172.4 million (EUR -169.9 million). Expenses for the annual contributions to resolution funds for the full year 2021 included in this line item rose – most strongly in Austria and Romania – to EUR 108.2 million (EUR 93.7 million). The decline in banking levies to EUR 52.2 million (EUR 83.0 million) is primarily attributable to the abolition of banking tax in Slovakia. At present, banking levies are payable in two core markets: in Hungary, banking tax for the full financial year amounted to EUR 14.9 million (EUR 14.3 million) and transaction tax for the first six months to another EUR 23.3 million (EUR 22.3 million). In Austria, banking tax equalled EUR 13.9 million (EUR 12.6 million).

Taxes on income increased to EUR 287.3 million (EUR 140.3 million). The minority charge rose to EUR 229.8 million (EUR 76.1 million) due to significantly higher earnings contributions of the savings banks. On the back of the strong operating result and low risk costs, **net result attributable to owners of the parent** rose to EUR 918.0 million (EUR 293.8 million).

Total equity not including AT1 instruments rose to EUR 20.6 billion (EUR 19.7 billion). After regulatory deductions and filtering in accordance with the CRR, **common equity tier 1 capital** (CET1, final) rose to EUR 18.0 billion (EUR 17.1 billion), as were total **own funds** (final) to EUR 23.8 billion (EUR 23.6 billion), both figures include interim profit. Total risk – **risk-weighted assets** including credit, market and operational risk (CRR, final) – increased moderately to EUR 127.1 billion (EUR 120.2 billion). The **common equity tier 1 ratio** (CET1, final) stood at 14.2% (14.2%), the **total capital ratio** at 18.7% (19.7%).

Total assets increased to EUR 303.4 billion (+9.4%; EUR 277.4 billion). On the asset side, cash and cash balances increased, primarily in Austria, to EUR 48.4 billion (EUR 35.8 billion), loans and advances to banks to EUR 24.5 billion (EUR 21.5 billion). **Loans and advances to customers** rose to EUR 172.1 billion (+3.7%; EUR 166.1 billion). On the liability side, deposits from banks grew significantly to EUR 34.6 billion (EUR 24.8 billion) as a result of increased ECB refinancing (TLTRO III). **Customer deposits** rose again in all core markets – most strongly in Austria and the Czech Republic – to EUR 206.3 billion (+7.9%; EUR 191.1 billion). The **loan-to-deposit ratio** declined significantly to 83.4% (86.9%).

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OUTLOOK

Erste Group's goal for 2021 is to increase net profit significantly. Among the factors that will support achievement of this goal are a recovery of the economies of all core markets – the Czech Republic, Slovakia, Hungary, Romania, Croatia, Serbia and Austria – and, on this basis, a reduction of risk costs and an improvement in the operating result. A continuation or further escalation of Covid-19 measures by governments as well as potential – and as yet unquantifiable – political, regulatory or economic risks may render meeting this goal more challenging.

In the past months the economic growth outlook for Erste Group's CEE core markets in 2021 was significantly upgraded from 2.8-4.5% to 3-7%. The development of other economic indicators should vary depending on Covid-19 policy measures imposed by authorities and/or the phasing out of state support. Unemployment rates are expected to rise slightly but, in the Czech Republic and Hungary, should remain among the lowest in the EU. Inflation rates are forecast to decline in the Czech Republic and Slovakia while the other core markets are likely to see an acceleration. In most countries, sustained competitiveness should again result in solid and, in Slovakia and Romania, stronger current account balances. The fiscal situation should likewise improve again after the significant budget deficits posted in the year 2020. Public debt is projected to remain largely stable, albeit at a significantly elevated level.

Against this backdrop, Erste Group expects net loan growth in the mid-single digits with upside potential. This performance should lead to a slight increase in net interest income despite negative interest rates in the euro zone. The second most important income component – net fee and commission income – is expected to rise in the high single digits. As in 2020, positive momentum should again come from fund management, the securities business, insurance brokerage as well as a recovery in payment services fees. Given the average result seen in 2020, the net trading and fair value result is expected to come in higher. This, however, will depend substantially on the financial market environment. The remaining income components are forecast to remain, by and large, stable. Overall, operating income should increase markedly in 2021. Operating expenses are expected to rise slightly in 2021, partly due to re-emerging wage pressure across all Erste Group markets. In addition, Erste Group will continue to invest in IT in 2021 and thus strengthening its competitive position, with a focus on progressive IT modernisation, back office digitalisation and expansion of the digital platform George. The rollout of George in Hungary and Croatia should be completed in 2021, as a result of which customers will be able to access George in the six largest core markets. Despite a hard to predict business environment, Erste Group expects solid positive jaws.

Based on the improved macro outlook described above, risks costs should decline significantly in 2021. While precise forecasting is hard in the current Covid-19 environment, Erste Group believes that in 2021 risk costs will not exceed 30 basis points of average gross customer loans. The NPL ratio is expected not to exceed 3%.

Other operating result is expected to remain unchanged in the absence of significant one-off effects. Assuming a lower tax rate of about 20% and despite higher minority charges than in the previous year, Erste Group aims to achieve a significant improvement in net profit resulting in a double-digit ROTE. Erste Group's CET1 ratio is expected to remain strong. As the ECB lifted its dividend recommendation, an additional EUR 1/share is expected to be paid in the fourth quarter of 2021 following approval by an extraordinary general meeting. For the 2021 fiscal year Erste Group targets a dividend of EUR 1.6 per share, thereby returning to its progressive dividend policy.

Potential risks to the guidance are besides other than expected (geo)political, economic (monetary and fiscal policies) and regulatory measures and developments also global health risks and changes to the competitive environment. In addition, given the Covid-19 governmental measures and their impact on the economic development, financial forecasts are still subject to an elevated level of uncertainty. Erste Group is moreover exposed to non-financial and legal risks that may materialise regardless of the economic environment. Worse than expected economic development may put goodwill at risk.

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