Bank of Cyprus Group

Bank of Cyprus Group: Extraordinary General Meeting

28 August 2014

Speech: Mr. John Patrick Hourican, Group Chief Executive Officer

OPENING REMARKS

Good Morning ladies and gentlemen, distinguished guests

This is my second time to stand in front of you, our shareholders, since taking on this role last year.

Our chairman has covered the majority of the points that we wanted to make at this meeting and I will limit my short remarks to areas not addressed by Dr. Hassapis or those where I believe additional emphasis is worthy.

I would like to start by also assuring you that the Board, the Management and every employee at The Bank of Cyprus have been working hard to rebuild a financially sound, trusted and safer bank. We have made some good progress but there remains a considerable amount to do before we can claim the job is done – this is still some way off.

I would also like to take this opportunity to thank each of you for bearing with us and for continuing to entrust us with your business dealings and your savings. We really do appreciate this trust and, importantly, we genuinely appreciate your patience with us as we work to rehabilitate your bank.

Today you are being asked to vote to accept new equity into the bank. This new equity is being raised to strengthen the bank's capital base to amongst the strongest in Europe. It will position us, not only to face the upcoming regulatory stress tests with greater confidence, but it will also instil improved confidence in our customers, future investors, depositors and International Markets such that we can begin to write a new and forward-looking chapter for the Bank, its customers, shareholders and our employees.

Raising this new and significant capital seeks to address the risk created by the very high level of non-performance in our Cyprus balance sheet, the idiosyncratic risk associated with Cyprus's economic situation and the emerging high level of capital standards required of Europe's systemic banks.

We are confident that this increase in capital will contribute to an accelerated recovery and improved prosperity in Cyprus itself – As Dr Hassapis said, this is a "page turning" moment not just for the Bank but also for Cyprus itself.

MAKING PROGRESS

Ensuring the recovery of Bank of Cyprus following the events that crystalized during 2012 and 2013 is a slow and incremental process. There are no quick fixes. The sustainable path to recovery is a deliberate and pain-staking one that involves implementing a large number of changes, on many fronts at the same time. We need to constantly re-calibrate our actions and take into account an evolving regulatory environment as well as a tough operating environment.

As Dr. Hassapis explained, and in line with the priorities I set out at last year's AGM, we have taken clear action to address our cost base, to sell unprofitable overseas businesses, to stabilize our deposit base, to reduce our reliance on Euro-system funding and to get a grip of and manage our very high non-performing loans. We are making incremental and steady progress on improving our capital adequacy and de-risking our business. We are fighting the constant tide of a rising underperforming domestic loan book which, of course, transmits the continuing recessionary conditions on the Cypriot economy today. We believe that all of the actions we are taking (and have taken) are slowly re-building confidence with each of our stakeholder groups.

We have worked closely with The Government of Cyprus, The Central Bank and The Troika to ensure that the implementation of our restorative measures are being done in tandem with the important policy objectives of the country. This good co-operation has resulted in, among other things, the complete lifting of domestic restrictive measures, the early release of blocked time deposits and good progress on deleveraging our own balance sheet – making the Bank safer. There remains much for the management team to do but the path to completing the journey is now very clearly set out and we will continue to work to deliver the Bank to safety and make it valuable for our shareholders.

The Board and the Management are extremely conscious of the Bank's fragile reputation with the people of Cyprus and we are genuinely working hard to recover society's trust. We recognize the financial pain that many of our customers' suffered as a result of this crisis and the fact that there are continuing recessionary conditions in Cyprus. We have implemented a number of measures such as reducing lending rates across a range of products, offering assistance to vulnerable citizens and proactively trying to protect viable businesses that are in need of debt restructuring. We will continue to do all we can to alleviate the short term financial distress of our customers and we will work with each of them to see how they can meet their financial obligations.

FORECLOSURE LAWS AND INSOLVENCY FRAMEWORK

It would be remiss of me not to comment on the important changes to the foreclosure laws and insolvency framework being discussed in the legislature. Bank of Cyprus has no intention of implementing mass-foreclosures on the homes of vulnerable or disadvantaged borrowers and we must move the debate back to the real issue. Banks essentially collect the savings of depositors and lend them to those who wish to borrow money to buy capital goods.

The current foreclosure laws and insolvency framework must be properly strengthened so as to ensure we can build a better and safer banking system. The current system has given rise to unacceptably high levels of delinquency, whether strategic or actual, and the remedies for this are wholly inadequate. It would be unreasonable to expect depositors to place their savings at the disposal of an economy that does not, at its core, morally and legally require the repayment of loans.

Cyprus needs a stronger legal framework which encourages the safe gathering of deposits and the regulated transformation of these savings into long term loans, allowing borrowers to consume their future earnings and generate economic prosperity. The country needs strong, simple and clear laws that impose the basic principle that "if you borrow money, you should pay it back". A breach of that principle should recognize that the offended party in that event is the lender (and indeed the depositor), not the borrower. The lending practices and the method of recovery of loans should of course be moderated and guided by good regulation which will ensure the lenders operate so as to "lend well" and "recover fairly". Enshrined in good regulation and indeed in the code of conduct at each of the lenders is a societal obligation to ensure we do not lend excessively to vulnerable groups and that we offer some better protection and assistance to vulnerable groups who fail to meet their obligations.

FINANCIAL RESULTS FOR FIRST SIX MONTHS OF 2014

Yesterday we announced the Group's results for the first six months of 2014. The results were satisfactory in the context of the plans we set ourselves and the Group posted a profit after tax attributable to shareholders for the first six months of the year amounting to Euro 81 million.

The positive progress we made in the first quarter of the year continued into the second quarter. We are not yet calling this a trend, but it is pleasing that we have recently arrested the run of negative results posted in consecutive quarters.

- Our Common Equity Tier 1 ratio, an important measure of our ability to cope with any further losses and risk, improved to 11.3% at the half year. This compares with 10.6% at the end of March 2104 and 10.4% at the end of December 2013. If this meeting should approve the equity placement today, this ratio will improve to 15.1% and position the Group amongst the best capitalized banks in Europe.

- During the second quarter of 2014 the balance sheet was de-leveraged by a further Euro 820 million. Emergency Liquidity Assistance (ELA) funding was also reduced in the second quarter by a further Euro 720 million, with total Eurosystem funding falling to Euro 10,2 billion. Our deposit base continued to stabilize.

- Loans in arrears for more than 90 days across the Group declined by Euro 165 million during the second quarter but still represent an unacceptable 49.8% of our gross loans. Loans in arrears for more than 90 days remains an area of critical management focus. The Group is to a large extent a hostage to the economic cycle of the Cypriot economy but, as Dr Hassapis intimated in his remarks, we expect that our balance sheet performance will be aided in 2015 by the combination of moderating economic conditions in Cyprus and the implementation of important changes to the legislative framework on foreclosures and insolvency that are currently being debated by the Cyprus legislature. The level of non-performing loans in Cyprus remains the worst in Europe and it is essential that every effort is made at a macro policy level and at an individual borrower level to remedy this. The risk pertaining to this persistent and unresolved issue is a primary reason why the Group is required to bolster its capital levels at this juncture.

CONCLUDING REMARKS

Ladies and Gentlemen and distinguished guests, as Dr Hassapis said, one year ago our Bank was staring down the barrel of great uncertainty. We suffered the indignity of being the only Bank and Eurozone Sovereign nation to bail in its depositors and impose capital controls. We lost the confidence of our customers, our investors, our staff and all stakeholders.

Today the picture is much more positive. A year ago we devised a restructuring plan. We picked up the broken pieces and we set out to reshape the bank so that it could have the best chance of success. We have begun to deleverage the balance sheet. We have completed the integration of the two predecessor banks. We have shrunk the cost base. We have made progress in selling overseas assets. We have stabilized the deposit base and we have improved the solvency of the company.

But the world requires more of us. The Bank is one of Europe's systemic banks and it must stand the comparison against its new peer group despite the continued economic difficulties in Cyprus. We continue to carry a large level of risk on the asset side of our balance sheet which manifests itself in our non-performing loan statistics. We continue to have an excessive reliance on Eurosystem funding and a lower level of deposits than we would naturally wish. It is prudent and right to raise capital to protect against the inherent risks in our business and to ensure that we can move the debate from survival to value.

Strengthening our bank now and placing its survival in no doubt will allow us accelerate its recovery. We will be able to engage with the wholesale markets more easily. Our stock will shortly be relisted and hopefully become a desirable and improving investment. We will be better positioned to play our part in rehabilitating the Cyprus economy and we will have a much better platform from which to create a future for our employees, customers, investors and Cyprus more generally.

Back to you Mr. Chairman.

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