

7th Capital Markets Day – **4 October 2010, Dubrovnik, Croatia**

Taking stock after 20 years of transformation –

Croatia: Prospect of EU membership will further boost the economy

Tomislav Vuić, Deputy CEO, EB Croatia



– Long-term economic development patterns

- Economic and political timeline
- Economic scorecard: real economy, fiscal performance & monetary policy
- Social indicator scorecard: backing up economic progress
- Focus topic: charting the development of residential real estate

– Evolution of the banking market

- The emergence of retail banking
 - Moving away from the cash economy
 - The loan growth story
 - Wealth creation: from deposits to fund management
- The transformation of corporate banking
 - From financing the state sector to financing private enterprise

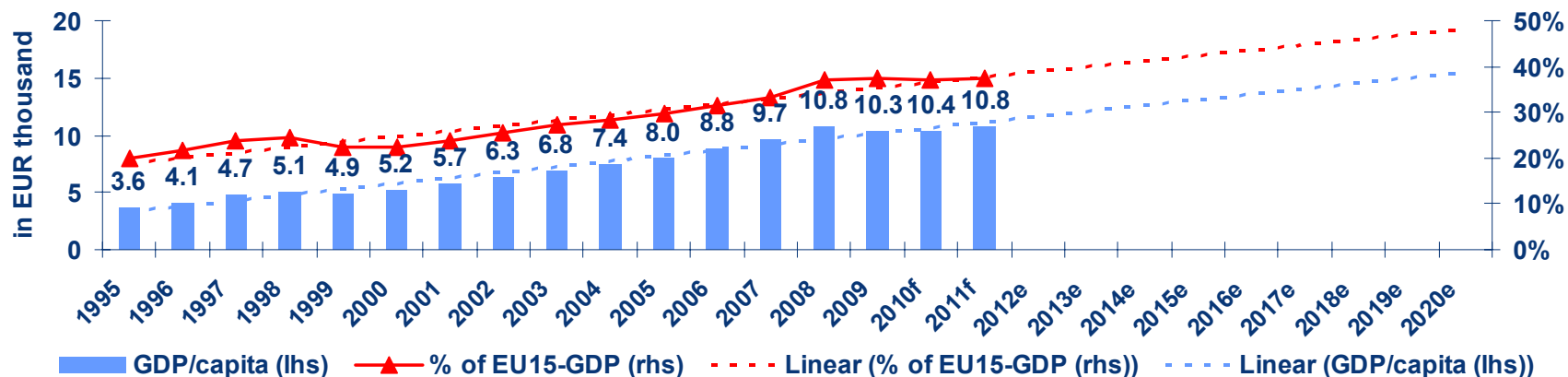
– Post-acquisition track record of EB Croatia

- Long-term financial performance
- Analysing credit risk
- Conclusion

Economic and political timeline –

From independence to the prospect of EU membership

Croatia - GDP/capita vs % of EU15 GDP/capita



1992-99 Christian democrats

- » Croatia recognised as an independent country
- » IMF membership
- » War ends in 1995
- » Stabilisation programme – tightly managed exchange rate float – inflation moderated
- » Recovery during post-war years
- » VAT introduction
- » Slowdown and recession in 1998-99
- » Banking sector crisis

2000-03 Social democrats - big coalition

- » Pension reform – 3 pillar system
- » Economy returns to strong growth
- » GDP boosted by large scale public investments – highways construction
- » Fiscal gap and external imbalances widened
- » Strong presence of foreign banks in the Croatian market
- » Croatia applied for EU membership

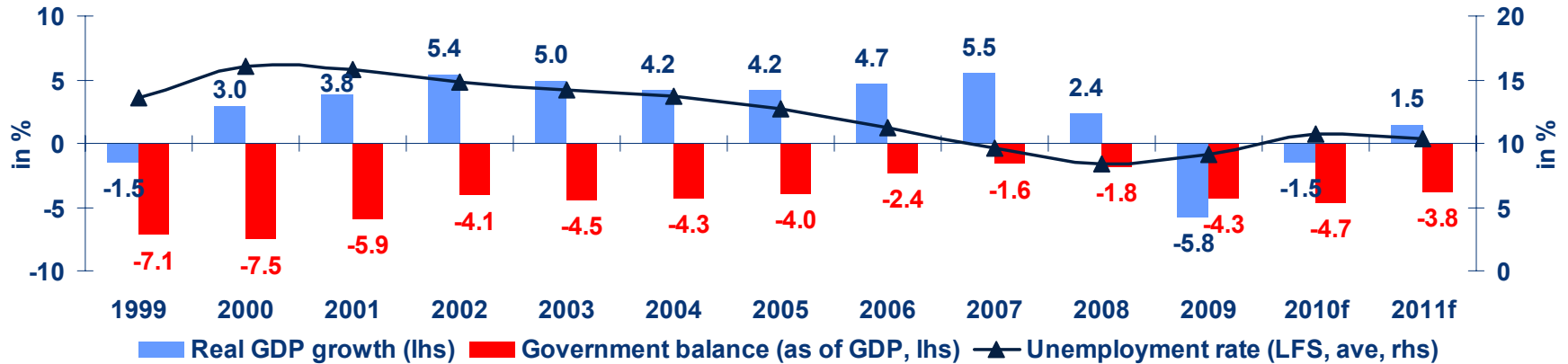
Since 2003: Christian democrats

- » Croatia gained EU candidate status
- » EU negotiations started (2005)
- » GDP growth remained robust prior to the global crisis – domestic demand remained strong growth driver
- » External imbalances remain pronounced – accumulation of foreign debt
- » Unemployment rate declined
- » NATO membership
- » EU negotiations – all chapters opened – negotiations to be finished in 2010/11

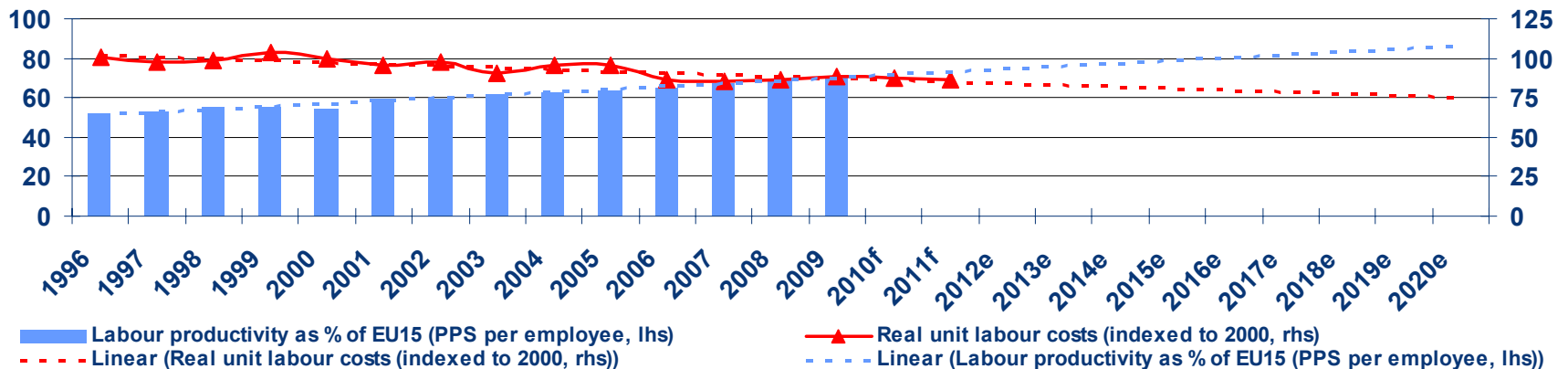
Source: Eurostat, Erste Group Research

Economic scorecard: the real economy – Successful convergence story

Croatia - Real GDP growth vs fiscal balance vs unemployment rate



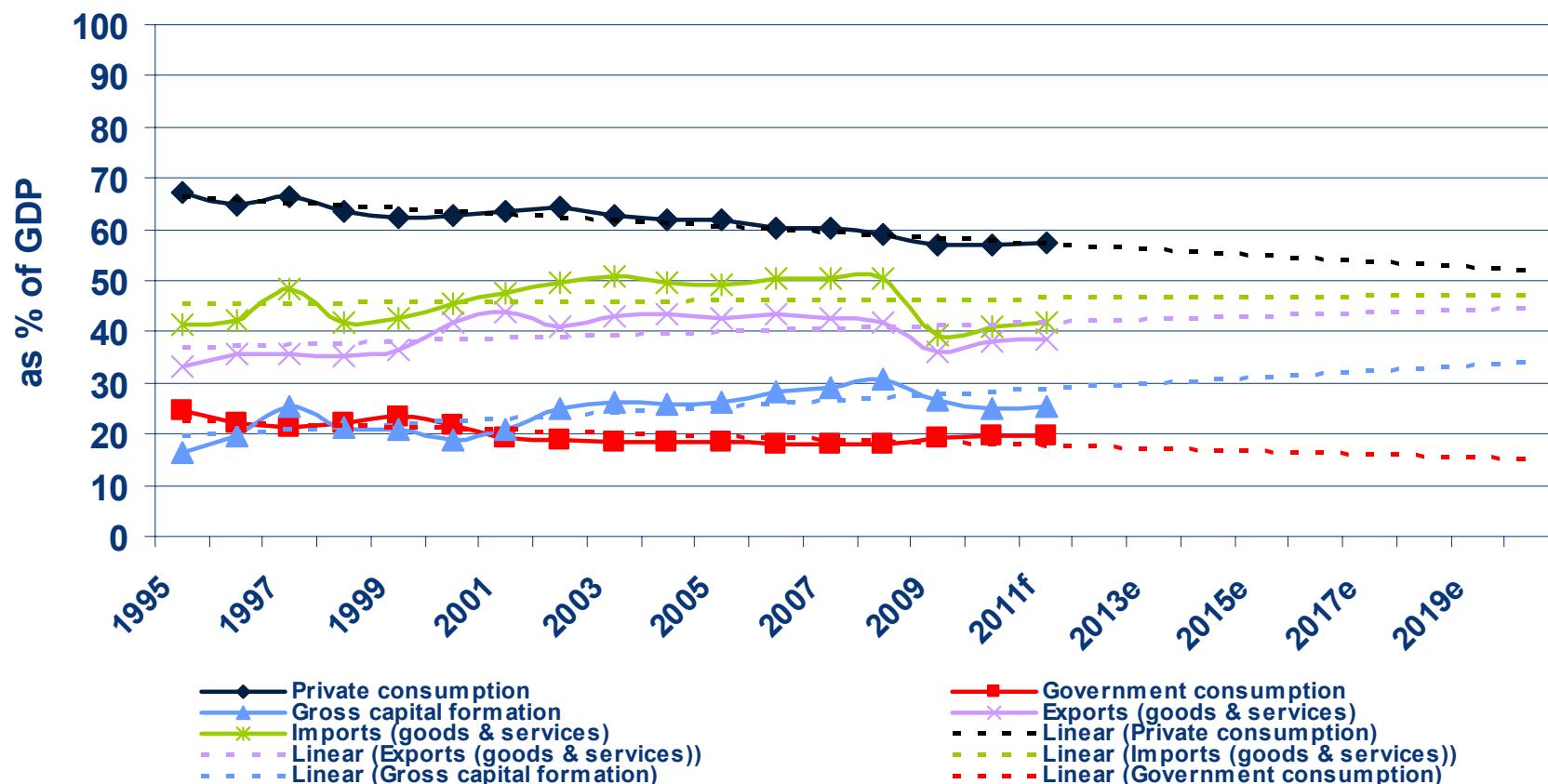
Croatia - Labour productivity vs real unit labour costs



Source: Eurostat, Erste Group Research. LFS = Labour Force Survey.

Economic scorecard: GDP composition – Consumption to remain the key contributor to GDP

Croatia: Composition of GDP - expenditure approach



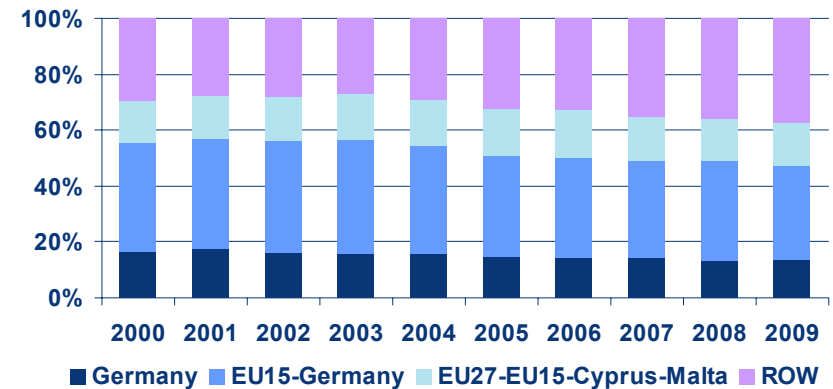
Source: Eurostat

Economic scorecard: trade drilldown –

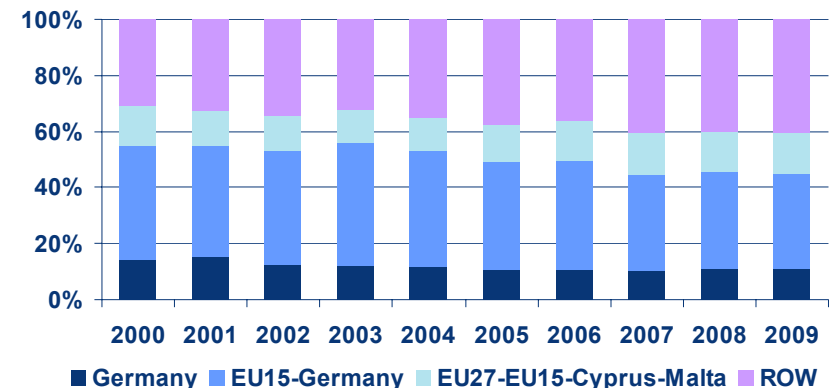
Biggest markets: EU and former Yugoslav nations

- **Economic openness in Croatia is smaller than in other CEE countries**
 - Exports of goods account for 17% of GDP
- **Main trading partners are European Union countries and former Yugoslavia**
 - Italy, Germany, Austria
 - Bosnia and Herzegovina
- **Main trading commodities are transport equipment, machinery and textile**
- **Well developed tourism industry is an important source of income and has been a major pillar of economy**
 - Among the top 20 most visited countries in the world
 - More than 10 million foreign visitors per year

Croatia - Goods import distribution



Croatia - Goods export distribution

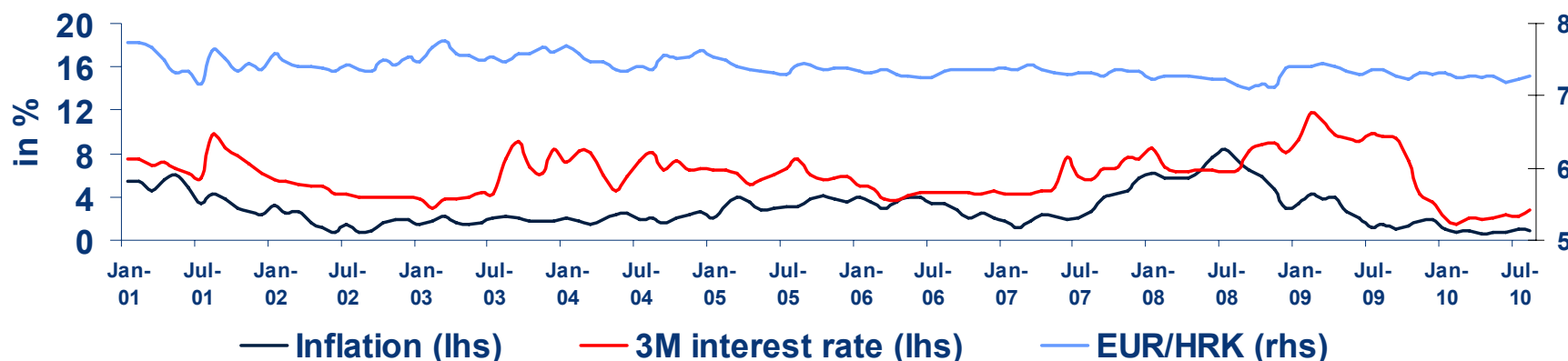


Source: Eurostat

Economic scorecard: monetary policy –

Exchange rate remains the monetary policy anchor

Croatia: Inflation, interest rate, exchange rate



1992-99 Christian democrats

- » Stabilisation programme – nominal exchange rate set as monetary policy anchor aiming to curb inflationary pressures
- » Program has been successful in taming inflation
- » 1998-99 banking sector crisis accompanied by exchange rate crisis
- » Credit activity decelerated
- » CNB was able to maintain exchange rate stability

2000-03 Social democrats - big coalition

- » Foreign owned banks intensified activity on Croatian market, leading to credit growth
- » Exchange rate remained the main monetary policy tool in keeping inflation at low levels
- » CNB started to introduce prudential regulation to curb excessive credit growth

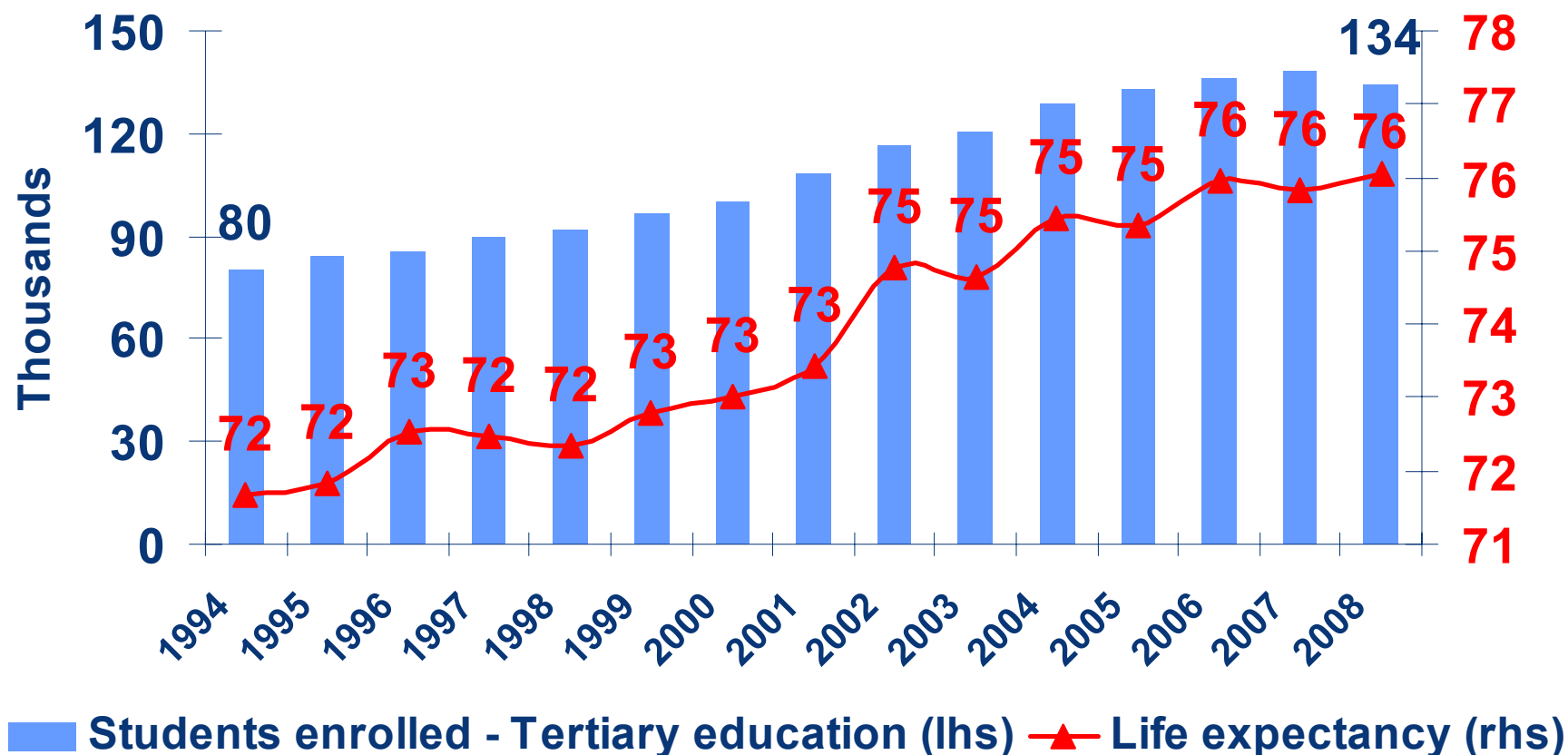
Since 2003: Christian democrats

- » Tightly managed float remained CNB top priority – CNB in comfortable position given hefty capital inflows, thus fighting appreciation pressures
- » CNB introduced harsher prudential framework i.e. marginal reserve requirement and 12% limit to credit growth, aiming to curb credit growth and control external imbalances and the rise in foreign debt
- » CNB eased the stance during global crisis to support external stability, exchange rate stability and debt refinancing
- » Credit activity slowed down – inflation subdued on weak demand

Source: Eurostat, Bloomberg

Social indicator scorecard – Improvements in most indicators

Croatia - Social indicators



Source: Eurostat

Focus: residential real estate development –

Market characterised by gradual growth

Croatia - Residential property prices



– Sustainable growth of residential real estate prices until 2008

- Wide availability of housing loans supported the market development as did favourable labour market conditions
- Overall high demand for residential property due to fast economic catch-up

– Slightly lower prices since 2008

- Conditions have changed since the economic downturn
- Pace of economic recovery will be key factor in market revival

– CAGR (2002-2009): 5.6%

Source: Croatian Central Statistics Office

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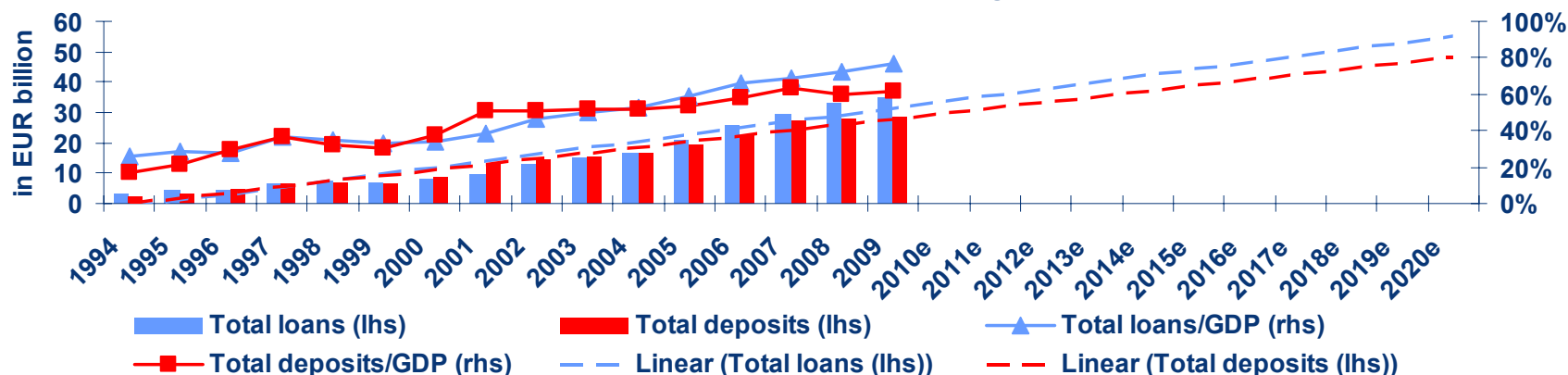
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Evolution of the banking market –

From one state-owned bank to developed financial system

Croatia - Development of banking sector



1990-1998 Forming the banking sector

- » Croatian National Bank established
- » Banks involved in privatisation process
- » Recovery and rehabilitation of largest national banks → state intervention
- » Banking sector crisis
- » 60 banks on the market
- » Banks had problems with insolvency
- » 1998: total assets of the banking sector amount to EUR 13bn

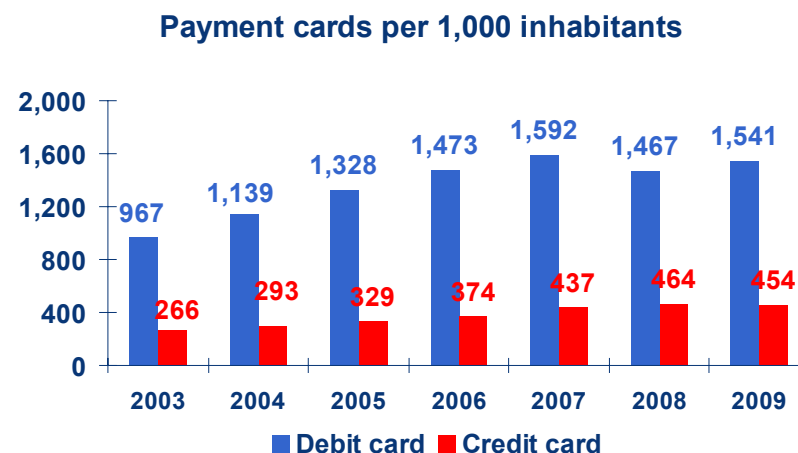
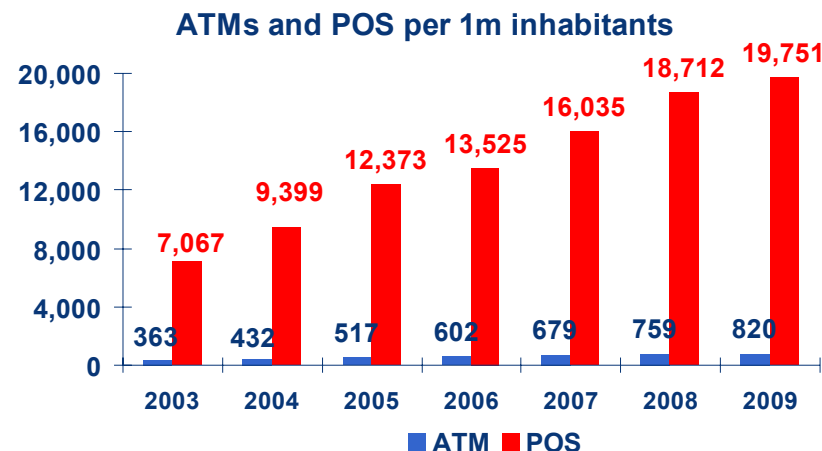
1999-2009 Consolidation of the banking sector

- » Beginning of the privatisation of banks
- » Banking sector becomes more international with foreign players entering the market
- » Beginning of reform of banking sector
- » Consolidation of banking sector – 36 banks on the market in 2009
- » Stable banking sector with high profitability
- » Major banks well prepared for crisis – stable position thanks to excellent capitalisation
- » 2009: total assets of the banking sector amount to EUR 53bn

Source: National Bank of Croatia

The emergence of retail banking – Moving away from the cash economy

- Croatia has been among the most developed CEE countries based on financial intermediation figures
- Croatia's cashless economy has developed rapidly in the last decade
 - 3,600 ATMs
 - 87,000 POS
 - 6.8m debit cards and 2m credit cards
- Number of ATMs and POS has continued to grow even during the crisis
 - Reflecting growing number of transactions and volume
- Number of payment cards declined in recent years due to the recessionary environment



Source: Croatian Chamber of Economy

The emergence of retail banking – The loan growth story

– Lending has been the main driver of the retail segment

- Retail loans grew every year between 1994 and 2008
- Since 2008 lower demand for loans and higher risk awareness by banks led to a slowdown in retail lending
- CNB started to relax lending restrictions in 2008

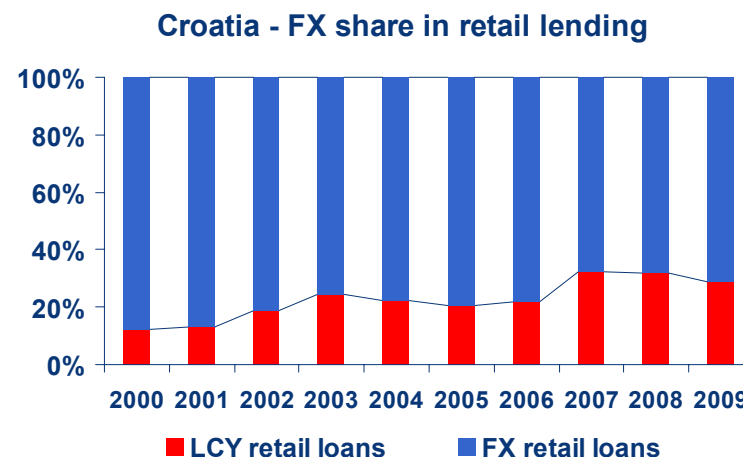
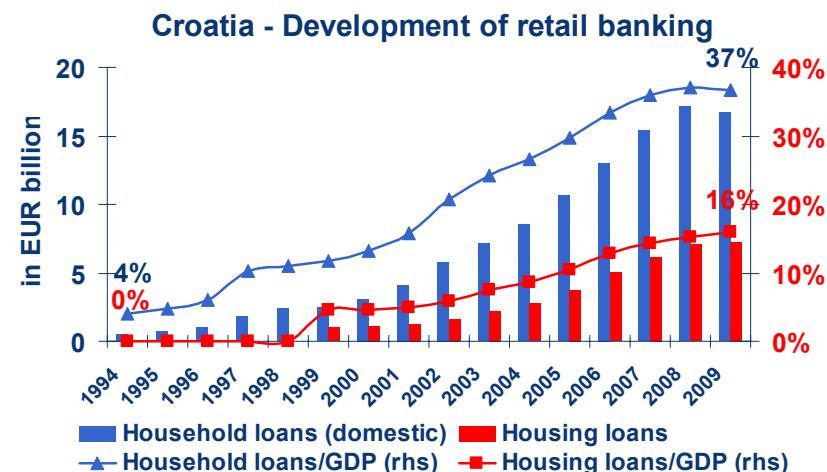
– Development of housing loans has been impressive since 1998

- Housing loans have outgrown consumer loans and represented 43% of total retail loans in 2009 (up from 33% in 2004)

– Foreign currency lending has always accounted for the majority of retail loans

- EUR and CHF
- Many households have income in euro

Source: National Bank of Croatia

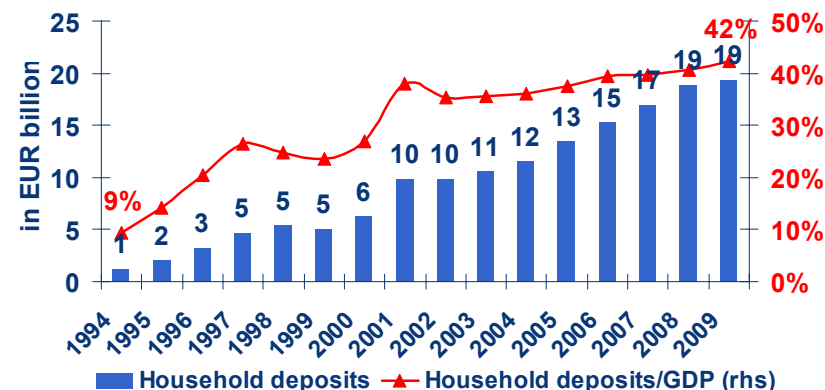


The emergence of retail banking –

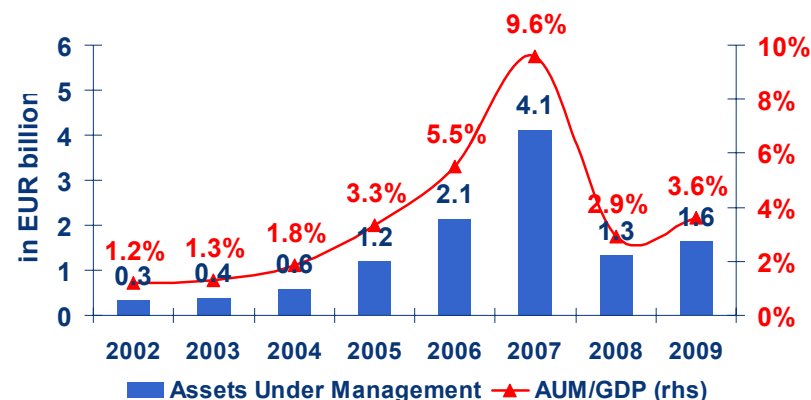
Wealth creation: from deposits to fund management

- **Well developed retail deposit market compared to other CEE markets**
 - Household deposits against GDP are in line with those of the Czech Republic
- **Constantly growing retail deposit market**
 - Amount of retail deposits has doubled within the last decade
 - Majority of retail deposits are in FX - households have historical habit to save in euro
- **Asset management development is a reflection of market environment**
 - Rapid growth until 2007
 - Market took a big hit in 2008 due to economic downturn
 - Gradual recovery since 2009

Croatia - Development of household deposits



Croatia - Development of asset management

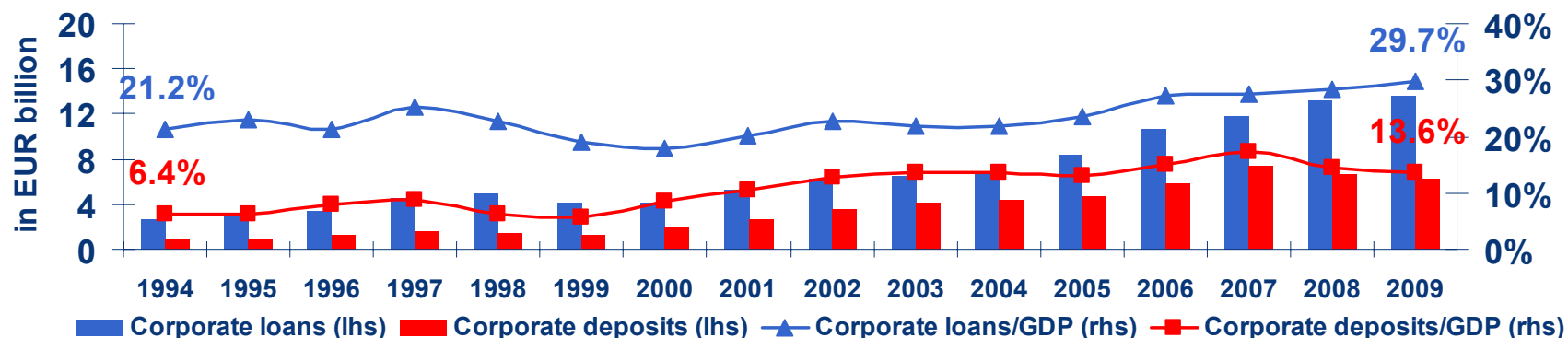


Source: National Bank of Croatia

The transformation of corporate banking –

Economic growth drives corporate market

Croatia - Development of corporate banking



- In the 1990's corporate loans were mostly used for financing the state sector
- **Croatian corporate loan market entered into a constant growth period in 2000**
 - Corporations enjoyed the favourable economic environment – real GDP grew every year between 2000 and 2008
 - Major driver of growth was the re-emerging Croatian tourism industry
 - Role of private enterprise grew compared to the state sector
- **Corporate deposits grew continuously between 1999 and 2007**
 - Decline in 2008 and 2009 due to more unfavourable macroeconomic conditions

Source: National Bank of Croatia

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Post-acquisition track record of EB Croatia – Long-term financial performance *

– 2003: Successful merger of the Croatian subsidiaries, Erste & Steiermärkische Banka and Rijecka Banka

- EB Croatia bought Opportunity Bank, Montenegro, in March 2009

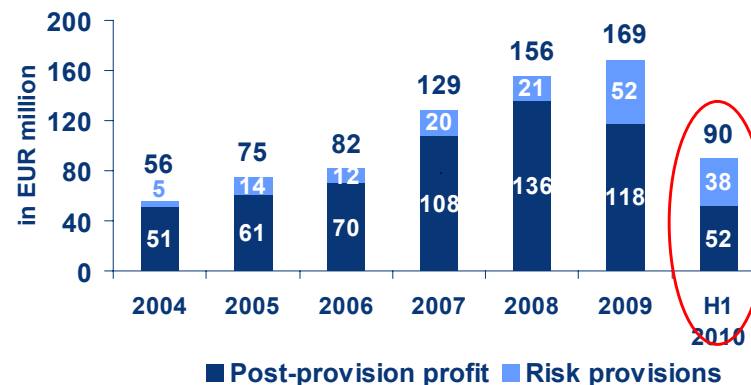
– Erste Bank Croatia today is one of the major banking institutions in Croatia

- Double-digit market shares in main product categories
- 832 thousand customers, 140 branches

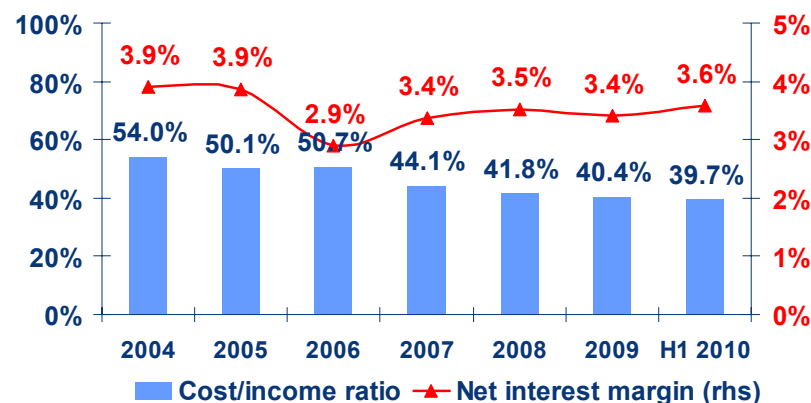
– Operating profit has always increased compared to previous year

- Higher revenues coupled with cost control
 - CIR under 40%
- NIM has been very stable for last four years
 - Between 3.4% and 3.6%

EB Croatia: operating profit history
(pre-provision profit)



EB Croatia: CIR and NIM

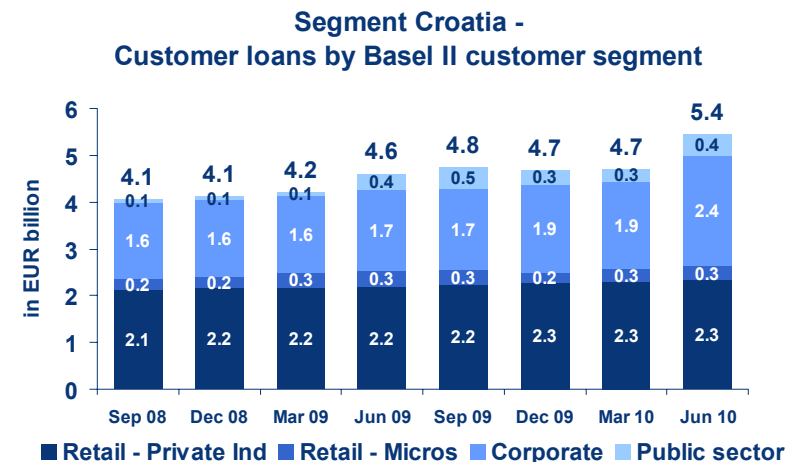


*) Based on local consolidated IFRS data

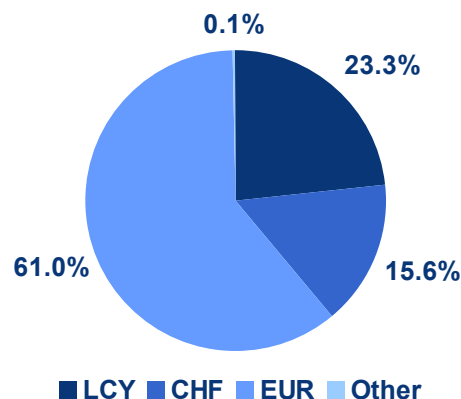
Post-acquisition track record of EB Croatia –

Analysing credit risk *

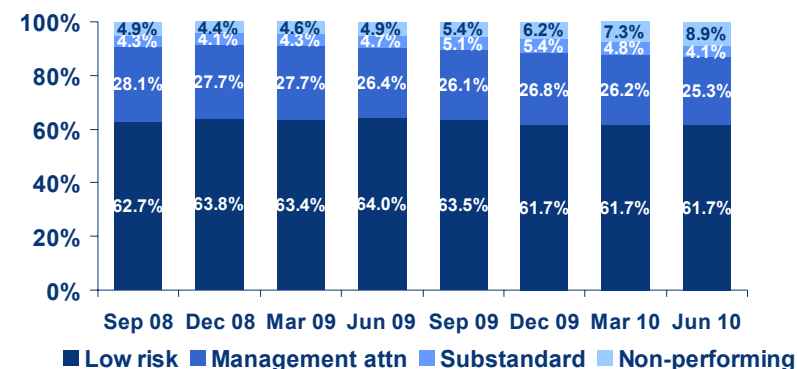
- **Loan growth moderated since economic downturn**
 - One-time impacts contributed to volume growth
 - Impact of acquisition of Opportunity Bank and full inclusion of factoring subsidiary
 - Majority of loans are EUR-based (61% of loans)
- **Still accelerating new NPL formation in Q2 2010**
 - NPL ratio at 8.9%
 - Deterioration in loans to the self-employed and small business has been disproportionally high
- **Risk costs still elevated**
 - Despite stabilisation on low risk category



Segment Croatia - Loan book by currency (30 June 2010: EUR 5.4bn)



Segment Croatia - Migration analysis



*) Based on segment figures

-
- **European Union accession in 2012-2013 to lead to economic boost**
 - Economy, however, to remain sluggish in 2010 due to weak domestic demand
 - EU accession process further facilitating structural reforms
 - Focus to remain on boosting exports and to keep imbalances under control

 - **Banking sector to slowly return to growth during the second half of 2010**
 - CNB abandoned former law on limiting lending growth, as expected
 - Growth will initially be driven by recovery in corporate lending
 - Low single-digit growth expected for 2010

 - **EB Croatia to maintain its very strong market positions**
 - Number 3 in the Croatian market with retail market shares of 13%
 - Stabilisation expected in the NPLs in the coming quarters
 - Strong operating performance to continue in the coming years