Management report

ECONOMIC ENVIRONMENT

In 2017, the global environment was characterised by a strong increase in world trade with improvements relatively well synchronised across advanced economies and emerging markets. Main economic and political topics were diverging monetary policies among central banks of the world's leading economies, the continued migration into Europe – though at a lower level – and intensified geopolitical tensions related to North Korea. Global trade activity was supported by a gradual recovery in commodity prices, continued rapid growth in China and India, a return to positive growth in formerly distressed economies such as Brazil and Russia, which benefitted from higher oil prices and growing demand among advanced economies. Among the advanced economies, Canada, New Zealand and dynamic Asian economies, such as Singapore, showed particularly strong performances in 2017. The United States and the economies of the euro zone were supported by favourable labour market developments and muted inflation. In Europe, negotiations regarding the withdrawal of the United Kingdom from the European Union continued. Among major central banks, policies continued to diverge. While the Swiss National Bank, the European Central Bank (ECB) and the Bank of Japan left key interest rates untouched throughout 2017, the Bank of England and the Federal Reserve (Fed) hiked their key rates by 0.25% and by 0.75% in 2017. Overall, global economic growth accelerated from 3.2% in 2016 to 3.7% in 2017.[1]

The US economy benefitted from solid private consumption growth, which was significantly supported by elevated consumer sentiment and higher investment activity reflecting strong increase of manufacturing output. Negotiations regarding the future of the North American Free Trade Agreement (NAFTA) continued throughout 2017 after the announcement that the United States might withdraw from the 23-year-old accord. Employment growth was solid throughout 2017, resulting in both a higher labour-force participation rate and a further decline in the unemployment rate to 4.1%[2] at the end of 2017. Despite increasing energy and moderately rising real estate prices, inflation remained muted. Based on the strong economic performance, the Fed decided to wind down its asset purchase scheme and raised its key rate three times, to 1.50% during 2017. Overall, the US economy grew by 2.3%[3] in 2017.

The pace of economic growth also accelerated in the euro zone in 2017, propelled by resilient private consumption, more investment activities, increasing support from the global upswing, loose financing conditions and further improvements in the labour market. When looking at the bigger economies of the euro zone, Germany and Spain again outperformed Italy and France. Despite the uncertainties triggered by the Catalan independence movement, economic growth in Spain was particularly strong mainly driven by excellent investment activity. Elections in some of the continent's biggest economies, such as Germany and France were mainly in line with expectations. The continued negotiations regarding the United Kingdom exiting the European Union did not significantly impact economic performance. Most of the euro zone's economies continued to show increasing employment rates throughout 2017. Unemployment, however, still varied substantially among the member states, with southern countries having significantly higher rates than those in the north. Consumer prices increased but remained well under control across the region. The ECB maintained its expansionary monetary policy by keeping the base rate unchanged in 2017. The adaptions of the ECB's monthly asset purchase programme reflected growing confidence of the central bank to reach its inflation target of less than 2%. Overall, real GDP growth in the euro zone was 2.5%[4].

After several years of moderate growth, the Austrian economy achieved a solid performance in 2017. The real GDP growth of 2.9%[5], the highest in six years, was supported by the rapid recovery of exports, strong investment activity and solid domestic consumption. The economic sentiment indicators also showed a clear upswing throughout the year. In addition, the traditionally strong service and tourism sectors continued to perform well. The favourable economic performance led for the first time since 2012 to the decline of the unemployment rate. Average consumer prices remained well under control with an increase of the inflation rate of 2.2%[6]. Following the parliamentary elections held in October, a new government was formed in December. With EUR 42,000 GDP per capita[7], Austria remained one of the most prosperous economies in the euro zone characterised by its well-educated workforce, stable institutional framework and strong international competitiveness.

The economies of Central and Eastern Europe continued to outperform the euro zone and achieved strong economic performance in 2017. Domestic demand remained the main growth driver, while exports also contributed to economic growth. The rising convergence of the region was demonstrated by significant wage inflation, most pronounced in the Czech Republic, Slovakia, Hungary and Romania. Consumption was further supported by higher consumer confidence, improving labour markets and relatively low interest rates across the region. The automobile

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[1] IMF: http://www.imf.org/en/Publications/WEO/Issues/2018/01/11/world-economic-outlook-update-january-2018 (Download on 21 February 2018)

[2] Bureau of Labor Statistics: https://www.bls.gov/news.release/archives/empsit_01052018.htm (Download on 21 February 2018)

3 Bureau of Economic Analysis: https://www.bea.gov/newsreleases/national/gdp/gdpnewsrelease.htm (Download on 21 February 2018)

[4] Eurostat: http://ec.europa.eu/eurostat/documents/2995521/8662991/2-14022018-BP-EN.pdf/ccf970c0-bb55-4a22-b8ea-d50d5a92586d (Download on 21 February 2018)

5 WIFO: http://www.wifo.ac.at/jart/prj3/wifo/resources/person_dokument/person_dokument.jart?publikationsid=60911&mime_type=application/pdf (Download on 21 February 2018)

6 Statistik Austria: http://www.statistik.at/web_de/statistiken/wirtschaft/preise/verbraucherpreisindex_vpi_hvpi/022835.html (Download on 21 February 2018)

7 Statistik Austria: http://www.statistik.at/web_de/statistiken/wirtschaft/volkswirtschaftliche_gesamtrechnungen/index.html (Download on 21 February 2018), adjusted for economic growth and inflation for 2017

industry, which was one of the main contributors to exports, again supported the Czech, Slovak, Romanian and Hungarian economies. In addition, European Union fund absorption rates improved in 2017. Consumer price inflation remained well under control and with the exception of the Czech Republic, central banks kept the base rates at historic low levels. The strong fundamentals of the Czech economy were also demonstrated by the strengthening of the Czech koruna following the decision of the Czech National Bank to depeg the currency from the euro. Unemployment rates in the region declined further. The Czech Republic and Hungary were among the countries showing the lowest unemployment rates in the European Union. In addition, public deficits in the region remained low. Overall, CEE economies grew in 2017, between 7.0%[8] in Romania and 1.8%[9] in Serbia.

PERFORMANCE IN 2017

In the consolidated management report P&L data of 2017 is compared with data of 2016, balance sheet data as of 31 December 2017 is compared to data as of 31 December 2016.

Acquisitions and disposals in Erste Group in 2017 did not have any significant impact and therefore had no effect on the rates of change stated below. Details are provided in the notes to the consolidated financial statements.

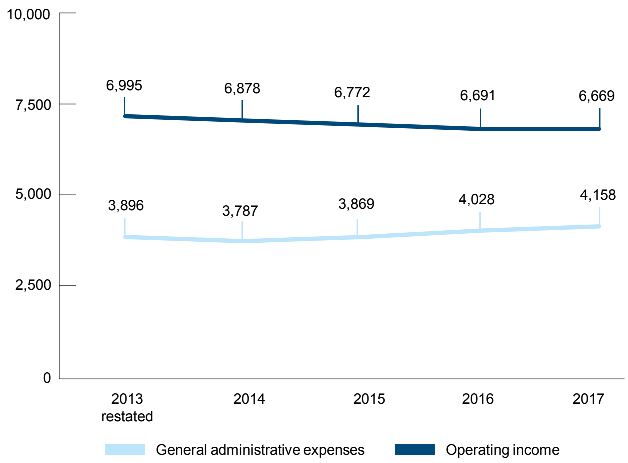
Overview

Net interest income declined to EUR 4,353.2 million (EUR 4,374.5 million) despite lending growth, mostly due to lower interest income from the government bond portfolio and a lower unwinding effect. Net fee and commission income increased to EUR 1,851.6 million (EUR 1,783.0 million). Income from the securities business, from asset management and from brokerage was up substantially, while income from the lending business declined. **Net trading result** decreased significantly to EUR 222.8 million (EUR 283.8 million). **Operating income** was nearly stable at EUR 6,669.0 million (EUR 6,691.2 million).

General administrative expenses rose to EUR 4,158.2 million (EUR 4,028.2 million). This was attributable to an increase in other administrative expenses and in depreciation and amortisation as well as higher personnel expenses of EUR 2,388.6 million (EUR 2,339.3 million). This line item also included deposit insurance payments in the amount of EUR 82.2 million (EUR 88.8 million). Consequently, the **operating result** decreased to EUR 2,510.8 million (-5.7%; EUR 2,663.0 million). The **cost/income ratio** rose to 62.4% (60.2%).

Net impairment loss on financial assets declined even further to EUR 132.0 million or 9 basis points of average gross customer loans (EUR 195.7 million or 15 basis points) and thus to a historical low. This was attributable to the substantial decline in the balance of the allocation and release of provisions for the lending business, mostly in Austria and in the Czech Republic. The **NPL ratio** improved further to 4.0% (4.9%). The **NPL cover ratio** was stable at 68.8% (69.1%).

Operating income and operating expenses in EUR million



Other operating result amounted to EUR -457.4 million (EUR -665.0 million). The improvement was largely due to the significant reduction of Austrian banking taxes to EUR 23.0 million (EUR 306.7 million, including a one-off payment of EUR 200.9 million under the Austrian Bank Tax Act). Overall, banking and transaction taxes declined to EUR 105.7 million (EUR 388.8 million). This line item includes the annual contributions to resolution funds in the amount of EUR 65.8 million (EUR 65.6 million) and EUR 45.0 million in expenses for losses from loans to consumers incurred as a result of supreme court rulings regarding negative reference interest rates in Austria.

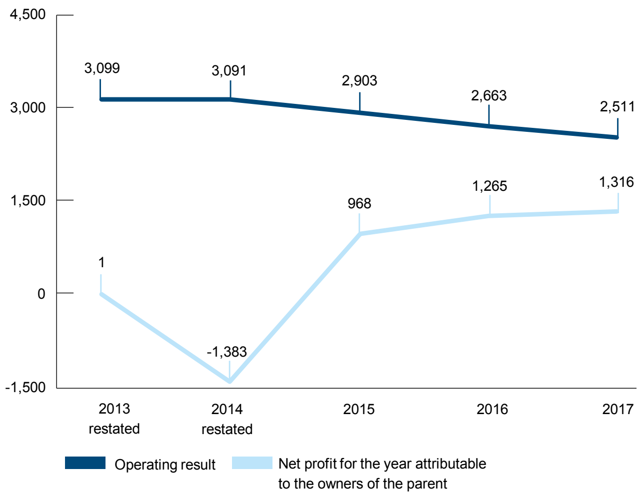
The minority charge rose to EUR 351.5 million (EUR 272.0 million) due to a rise in the earnings contributions of the savings banks. The **net result attributable to owners of the parent** rose to EUR 1,316.2 million (EUR 1,264.7 million).

Cash return on equity (see glossary for definition), i.e. return on equity adjusted for non-cash expenses such as goodwill impairment and straight-line amortisation of customer relationships, stood at 10.2% (reported ROE: 10.1%) versus 11.4% (reported ROE: 10.8%) in the previous year.

[8] National Institute of Statistics: http://www.insse.ro/cms/sites/default/files/com_presa/com_pdf/pib_tr4e2017.pdf (Download on 21 February 2018)

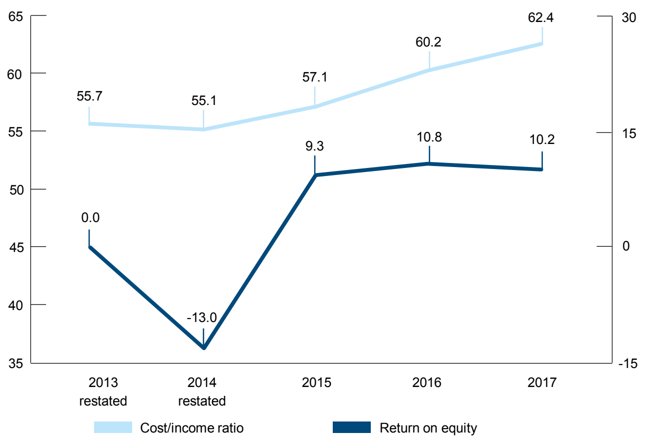
9 Statistical Office of the Republic of Serbia: (http://www.stat.gov.rs/WebSite/repository/documents/00/02/68/18/NR40_-_ENG-327.pdf (Download am 21 February 2018), adjusted by estimates for the fourth quarter 2017

Operating result and net profit/loss for the year attributable to owners of the parent in EUR million



Cash earnings per share (see glossary for definition) amounted to EUR 2.96 (reported EPS: EUR 2.94) versus EUR 3.08 (reported EPS: 2.93) in the previous year.

Key profitability ratios in %



Total assets increased to EUR 220.7 billion (EUR 208.2 billion). On the asset side, cash and cash balances rose to EUR 21.8 billion (EUR 18.4 billion), loans and receivables to credit institutions increased to EUR 9.1 billion (EUR 3.5 billion). **Loans and receivables to customers** rose to EUR 139.5 billion (EUR 130.7 billion). On the liabilities side, deposits from banks increased to EUR 16.3 billion (EUR 14.6 billion) and **customer deposits** continued to grow – most notably in the Czech Republic and in Austria – to EUR 150.9 billion (EUR 138.0 billion). The **loan-to-deposit ratio** stood at 92.4% (94.7%).

The **common equity tier 1 ratio** (CET1, Basel 3 phased-in; see glossary for definition) remained stable at 13.4% (13.4%), the **total capital ratio** (Basel 3 phased-in; see glossary for definition) at 18.5% (18.5%).

Dividend

A dividend distribution of EUR 1.20 per share will be proposed at the annual general meeting (2016: EUR 1.00 per share).

Outlook

Erste Group targets a return on tangible equity (ROTE) of more than 10% in 2018. The expected very solid macro-economic development in the core markets Czech Republic, Slovakia, Hungary, Romania, Croatia, Serbia and Austria, rising interest rate levels in several of our markets and still historically low risk costs should be supportive factors to achieve this target. On the other hand, a global or regional slowdown of economic growth as well as potential – and as yet unquantifiable – political or regulatory risks might jeopardise achieving the target.

In 2018, the positive development of the economy should be reflected in growth rates (real GDP growth) of around 3% to 5% in the Erste Group's CEE core markets. All other economic parameters are currently expected to be similarly robust. Unemployment rates should remain at historic lows – in the Czech Republic and in Hungary they are already among the lowest in the EU. Inflation is forecast to rise but remain subdued by historical standards and strong competitive positions should again lead to current account surpluses. The fiscal situation and public debt levels are also projected to remain sound. Austria should see accelerating economic growth at a rate of close to 3%. Overall, growth continues to be driven by domestic demand across all economies. The contribution of exports is forecast as neutral.

Against this backdrop, Erste Group expects mid-single digit net loan growth. In 2018, net interest income should also be slightly up on the back of rising short and long-term interest rates, primarily in the Czech Republic and Romania, but also globally, and therefore declining margin pressure from sovereign bond reinvestments. The second key income component, net fee and commission income, is also expected to increase moderately in 2018. As in 2017, some positive momentum should again come from the securities business, fund management and the insurance business. The other income components are expected to remain stable, by and large, despite the volatility of the net trading and fair value results. Consequently, operating income should grow slightly in 2018.

Operating expenses are expected to decline marginally in 2018, mainly due to the fact that in 2017 higher IT expenditure was incurred for regulatory projects, which will not recur on the same scale in 2018. However, Erste Group will continue to invest in digitalisation and thereby its future competitiveness in 2018. The focus will be on product simplification, process standardisation or the group-wide implementation of the digital platform George. After its rollout in Austria, George will be fully up and running in the Czech Republic, Slovakia and Romania in 2018. Overall, the operating result is projected to rise in 2018.

Risk costs should support net profit again in 2018. Amid a moderate rise of interest rates, risk costs should go up only slightly. Further improvements in asset quality, however, should have a dampening effect. Overall, Erste Group does not expect a recurrence of the historically low risk cost level of 2017 of just 9 basis points of average gross customer loans. While precise forecasts are difficult in the current environment, Erste Group projects for 2018 risk costs of up to 20 basis points of average gross customer loans. The implementation of accounting standard IFRS 9 is not expected to materially impact financial results in 2018.

Assuming a tax rate of around 22% and a similar level of minority charges, Erste Group aims to achieve a return on tangible equity (ROTE) of more than 10%.

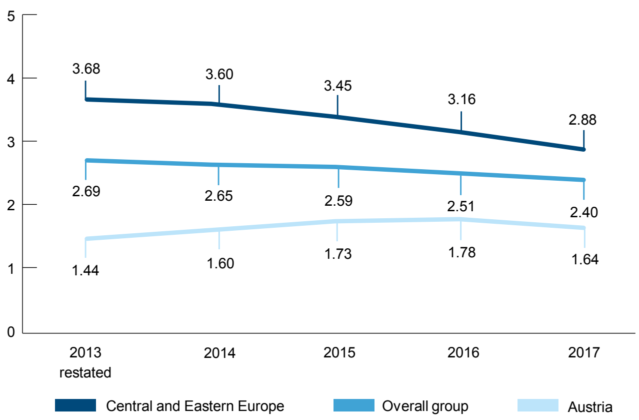
Potential risks to the guidance are interest rate trends that differ from expectations, political or regulatory measures targeting banks as well as geopolitical and global economic developments.

ANALYSIS OF PERFORMANCE

Net interest income

Net interest income declined to EUR 4,353.2 million (EUR 4,374.5 million) on the back of a persistently challenging market interest rate environment, which resulted in lower interest income from the government bond portfolio and customer loans, and a lower unwinding effect owed to continued asset quality improvements. The implementation of supreme court rulings regarding negative reference interest rates for consumer loans also had a negative impact on net interest income in Austria. Solid net customer loan growth did not fully offset the pressure on net interest income. As a result, the net interest margin (net interest income as a percentage of average interest-bearing assets) declined from 2.51% to 2.40%.

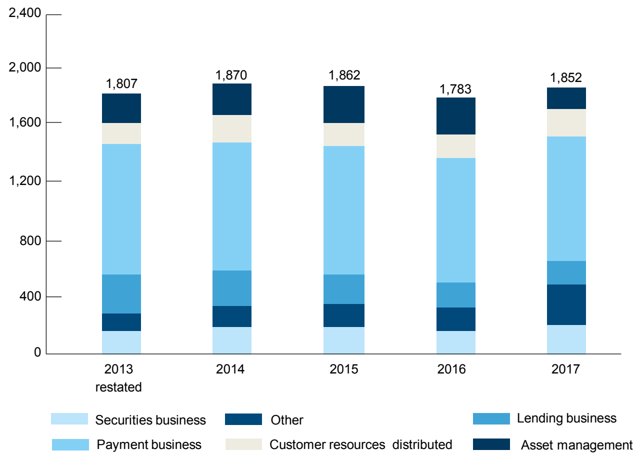
Net interest margin in %



Net fee and commission income

Net fee and commission income rose to EUR 1,851.6 million (EUR 1,783.0 million). While income from the securities business, from asset management and from brokerage saw significant growth, income from lending declined, most notably in the Czech Republic and in Slovakia.

Net fee and commission income, structure and trend in EUR million



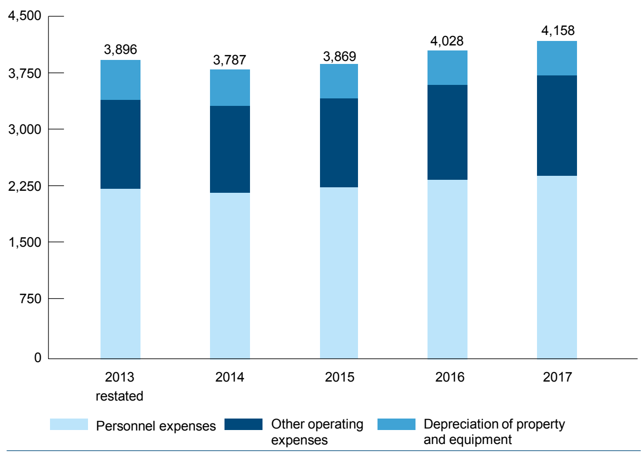
Net trading result

Net trading result decreased to EUR 222.8 million (EUR 283.8 million). This was attributable to losses from securities and derivatives trading as well as negative contributions from hedge accounting.

General administrative expenses

General administrative expenses amounted to EUR 4,158.2 million (EUR 4,028.2 million).

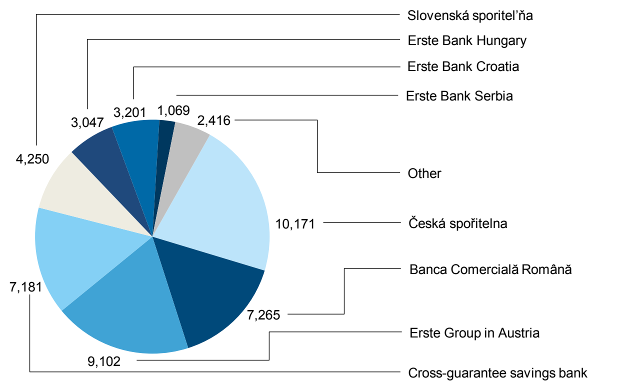
General administrative expenses, structure and trend, in EUR million



Personnel expenses increased to EUR 2,388.6 million (EUR 2,339.3 million), **other administrative expenses** to EUR 1,309.6 million (EUR 1,235.8 million). IT expenditure rose to EUR 425.9 million (EUR 339.3 million), mainly due to increased regulatory requirements and the implementation of new systems in Austria. Consulting expenses were up at EUR 165.7 million (EUR 151.7 million). Deposit insurance contributions declined to EUR 82.8 million (EUR 88.8 million) as lower contributions of EUR 2.2 million (EUR 14.5 million) in Romania and EUR 0.8 million (EUR 2.5 million) in Slovakia offset higher payments in other core markets. **Depreciation and amortisation** increased to EUR 460.0 million (EUR 453.1 million).

The **average headcount** increased marginally by 1.5% to 47,659 (46,955).

Headcount as of 31 December 2017



The number of employees is based on full-time equivalents. The data regarding subsidiaries in Central and Eastern Europe refer to partial groups.

Operating result

Operating income was nearly stable at EUR 6,669.0 million (EUR 6,691.2 million) on the back of improved net fee and commission income, moderately declining net interest income and lower net trading result. General administrative expenses rose to EUR 4,158.2 million (EUR 4,028.2 million), driven by an increase in other administrative and personnel expenses and depreciation and amortisation. The operating result accordingly declined to EUR 2,510.8 million (EUR 2,663.0 million). The cost/income ratio stood at 62.4% (60.2%).

Gains/losses from financial assets and liabilities not measured at fair value through profit or loss (net)

Gains from financial assets and liabilities not measured at fair value through profit or loss (net) amounted to EUR 156.4 million (EUR 148.0 million). This item includes mostly gains from the sale of securities in Austria, in the Czech Republic and in Hungary shown in income from financial assets – available for sale. In the comparative period, the item reflected a gain from the sale of shares in VISA Europe in the amount of EUR 138.7 million.

Net impairment loss on financial assets

Net impairment loss on financial assets amounted to EUR 132.0 million (EUR 195.7 million) or 9 basis points (15 basis points) on the average volume of gross customer loans and hence remained at a historically very low level. This was mostly attributable to the decline in the balance of the allocation and release of provisions for the lending business together with lower costs of direct loan write-offs, which also offset the decline in income received from the recovery of loans already written off. In addition, this line item included a net impairment loss on financial assets – held to maturity and financial assets – available for sale in the amount of EUR -27.0 million (EUR -11.4 million), which was mostly a net impairment loss on participations.

Other operating result

Other operating result improved significantly to EUR -457.4 million (EUR -665.0 million) mostly due to reduced **levies on banking activities** of EUR 105.7 million (EUR 388.8 million). Following last year's one-off payment of EUR 200.9 million, banking tax rates have been reduced in Austria from 2017 onwards. This resulted in lower Austrian banking levies of EUR 23.0 million (EUR 306.7 million). In addition, the Hungarian banking tax was further reduced. Due to a lower tax rate and an adjustment of the assessment base, the tax charge declined to EUR 12.8 million (EUR 19.4 million). Including financial transaction tax of EUR 42.4 million (EUR 37.6 million), bank levies in Hungary totalled EUR 55.2 million (EUR 57.0 million). In Slovakia, bank levies rose to EUR 27.4 million (EUR 25.1 million).

Allocation/release of other provisions, including for commitments and guarantees given, amounted to EUR -116.2 million (EUR -125.9 million). This included EUR 45.0 million in provisions for losses from loans to consumers resulting from supreme court rulings regarding negative reference interest rates in Austria. In addition, other operating result also reflected impairments (EUR 31.1 million for IT projects and EUR 26.7 million for branches in the Czech Republic) as well as the annual contributions to resolution funds in the amount of EUR 65.8 million (EUR 65.6 million) shown in the line item result from other operating expenses/income. In Romania, these increased to EUR 14.2 million (EUR 4.5 million) and, to a lesser extent, also in the Czech Republic and Hungary, but declined marginally in Austria, Slovakia and Croatia. In the previous year, the partial impairment of goodwill in Slovenská sporitel'ňa had a negative effect of EUR 61.3 million.

Profit/loss for the year

The pre-tax result from continuing operations amounted to EUR 2,077.8 million (EUR 1,950.4 million). The minority charge rose to EUR 351.5 million (EUR 272.0 million) due to continued solid earnings contributions of the savings banks. The net result attributable to owners of the parent rose to EUR 1,316.2 million (EUR 1,264.7 million).

Tax situation

Pursuant to section 9 of the Austrian Corporate Tax Act ("KStG"), Erste Group Bank AG and its main domestic subsidiaries constitute a tax group. Due to the high proportion of tax-exempt income – particularly income from participating interests – and tax payments for the permanent establishments abroad, no Austrian corporate income tax was payable for the financial year 2017. The current tax loss carried forward increased in 2017.

Taxes on income are made up of current taxes on income calculated in each of the Group companies based on the results reported for tax purposes, corrections to taxes on income for previous years, and the change in deferred taxes. The reported total income tax expense amounted to EUR 410.1 million (EUR 413.6 million).

Balance sheet development

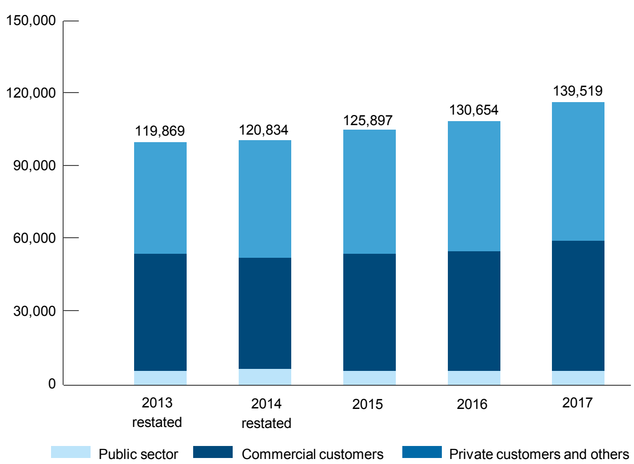
The rise in **cash and cash balances** to EUR 21.8 billion (EUR 18.4 billion) was primarily due to larger cash balances held at central banks on the back of continued strong customer deposit inflows and lower reinvestments.

Trading and investment securities held in various categories of financial assets declined to EUR 42.8 billion (EUR 47.6 billion), driven by sales of available-for-sale securities.

Loans and receivables to credit institutions (net), including demand deposits other than overnight deposits, increased to EUR 9.1 billion (EUR 3.5 billion).

Loans and receivables to customers (net) rose – mainly in the Czech Republic, but also in Austria and in Slovakia – to EUR 139.5 billion (+6.8%; EUR 130.7 billion) on the back of growth in retail and corporate lending as well as a temporarily expanded money market business.

Loans and advances to customers, structure and trend, in EUR million



Allowances for loans and receivables to customers declined to EUR 4.0 billion (EUR 4.6 billion), mostly due to the continuing improvement in asset quality.

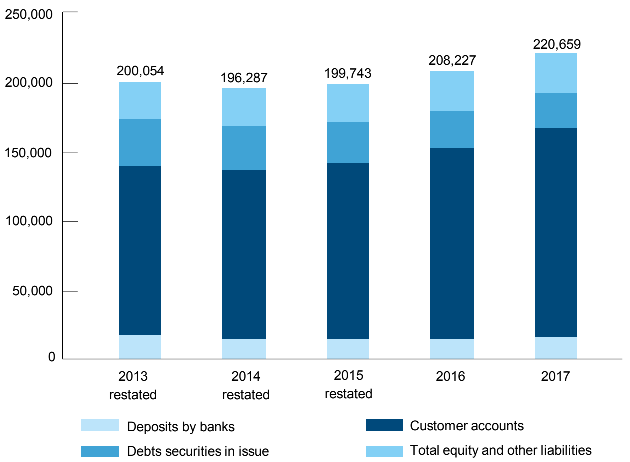
Intangible assets increased to EUR 1.5 billion (EUR 1.4 billion).

Miscellaneous assets declined to EUR 5.9 billion (EUR 6.8 billion).

Financial liabilities – held for trading decreased to EUR 3.4 billion (EUR 4.8 billion).

Deposits from banks, primarily in the form of term deposits, rose to EUR 16.3 billion (EUR 14.6 billion); **deposits from customers** increased to EUR 151.0 billion (EUR 138.0 billion), due to the strong growth in overnight deposits mainly in Austria and in the Czech Republic. The **loan-to-deposit ratio** stood at 92.4% (94.7%).

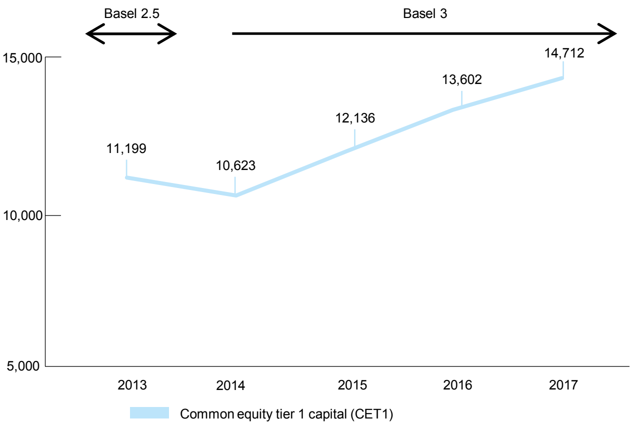
Balance sheet structure/liabilities and total equity in EUR million



Debt securities in issue declined to EUR 25.1 billion (EUR 27.2 billion). Miscellaneous liabilities were almost unchanged at EUR 6.5 billion (EUR 7.0 billion).

Total assets increased to EUR 220.7 billion (EUR 208.2 billion). Erste Group's **total equity** increased to EUR 18.3 billion (EUR 16.6 billion). Following two issuances in June 2016 and April 2017, this has included AT1 instruments in the amount of EUR 993 million. After regulatory deductions and filtering according to the Capital Requirements Regulation (CRR) the **common equity tier 1 capital** (CET1, Basel 3 phased-in) increased to EUR 14.7 billion (EUR 13.6 billion). **Total own funds** (Basel 3 phased-in) rose to EUR 20.3 billion (EUR 18.8 billion). **Total risk** (risk-weighted assets (RWAs) including credit, market and operational risk, Basel 3 phased-in) increased to EUR 110.0 billion (EUR 101.8 billion).

Common equity tier 1 capital (CET 1) according to CRR in EUR million

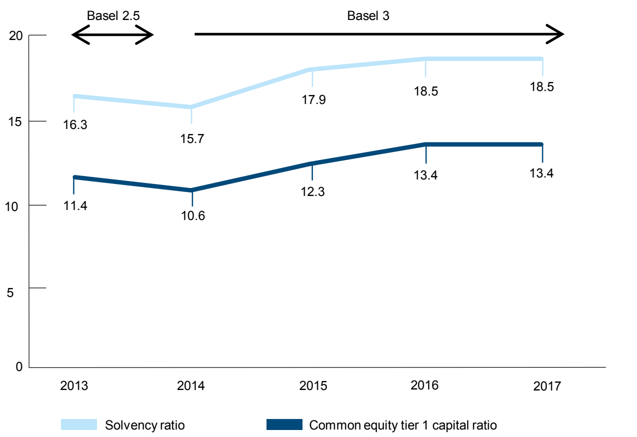


In Basel 2.5: Core tier-1 capital excluding hybrid capital pursuant to section 23 (4a and 4b) of the Austrian Banking Act
Basel 3 values are based on CRR transitional rules.

Consolidated regulatory capital is calculated in accordance with CRR taking into consideration transitional provisions as defined in the Austrian CRR Supplementary Regulation and the regulation 2016/445 of the European Central Bank on the exercise of options and discretions. These define the percentages applicable to eligible capital instruments and regulatory deduction items as well as filters. The **total capital ratio** (Basel 3 phased-in), total eligible qualifying capital in relation to total risk pursuant to CRR, remained stable at 18.5% (18.5%), well above the legal minimum requirement.

The **tier 1 ratio** (Basel 3 phased in) stood at 14.0% (13.4%), the **common equity tier 1 ratio** (Basel 3 phased-in) at 13.4% (13.4%).

Solvency ratio and common equity tier 1 capital ratio in %



In Basel 2.5: Core tier-1 capital excluding hybrid capital pursuant to section 23 (4a and 4b) of the Austrian Banking Act
Basel 3 values are based on CRR transitional rules.

EVENTS AFTER BALANCE SHEET DATE

There were no significant events after the balance sheet date.

RISK MANAGEMENT

With respect to the explanations on substantial financial and non-financial risks at Erste Group as well as the goals and methods of risk management, we would like to draw the reader's attention to the information in Notes 44, 45 and 50 to the consolidated financial statements.

RESEARCH AND DEVELOPMENT

Erste Group does not engage in any research activities pursuant to section 243 (3) no. 3 UGB, but in 2017 development costs in the amount of EUR 139 million (EUR 45 million) were capitalised in connection with software developed in-house.

In order to drive improvements for retail customers and in the ongoing services, Erste Group launched the Innovation Hub. Its purpose is to initiate and coordinate across-the-board initiatives with a strong focus on customer experiences. As a multi-disciplinary team consisting of marketing, product and IT as well as design experts, the Innovation Hub is tasked with creating innovations and managing new programme initiatives.

CAPITAL, SHARE, VOTING AND CONTROL RIGHTS

Disclosures pursuant to section 243a (1) UGB (Austrian Commercial Code)

With regard to the statutory disclosure requirements related to the composition of the capital as well as the class of shares, special reference is made to Note 36 in the consolidated financial statements.

As of 31 December 2017, together with its syndicate partners, DIE ERSTE oesterreichische Spar-Casse Privatstiftung (Privatstiftung), a foundation, controlled approximately 29.62% of the shares in Erste Group Bank AG and with 15.62% the most important shareholder. The Privatstiftung holds 6.50% of the shares directly, the indirect participation of the Privatstiftung amounts to 9.12% of the shares held by Sparkassen Beteiligungs GmbH & Co KG, which is an affiliated undertaking of the Privatstiftung. 1.00% is held directly by Austrian savings banks respectively saving banks foundations acting together with the Privatstiftung and affiliated with Erste Group Bank AG through the Haftungsverbund. 9.92% of the subscribed capital is controlled by the Privatstiftung on the basis of a shareholder agreement with Caixabank S.A. 3.08% are held by other partners to the shareholder agreement.

Furthermore, it should be noted that Erste Group Bank AG – just as nearly all Austrian savings banks – is a member of the Haftungsverbund of Sparkassengruppe. Sparkassengruppe sees itself as an association of independent, regionally established savings banks that strives to bolster its market position by strengthening common product development, harmonising its market presence and advertising concepts, pursuing a common risk policy, engaging in co-ordinated liquidity management and applying common controlling standards.

In addition, the purpose of this scheme is:

_ to identify any business issues of its member banks at an early stage and to provide effective assistance to its members in the resolution of business issues – this can range from offering technical assistance or giving guarantees to providing borrowed or qualifying capital and
_ to provide customers with a deposit guarantee system that goes beyond the legal deposit guarantee requirement (section 93 et seq. of the Austrian Banking Act (BWG), which only guarantees certain types of customer deposits, by creating a suitable obligation to service the liabilities of other participating savings banks if the need arises.

Haftungsverbund GmbH is responsible for implementing such measures and analysing the business situation of every member bank of the Haftungsverbund. Overall, the participating savings banks hold a maximum stake of 49% (assuming all savings banks participate) in Haftungsverbund GmbH and Erste Group Bank AG always holds a minimum stake of 51%.

As required by the BWG, individual members of the Haftungsverbund may need to provide assistance to other members (by giving liquidity assistance, granting loans or guarantees and providing equity capital, for instance) and, in any other protection case (insolvency), to service the guaranteed customer deposits of a Haftungsverbund member. The scope of the individual services to be provided by individual Haftungsverbund members where needed is subject to an individual and general maximum limit. Any contributions made by Haftungsverbund members under the statutory deposit guarantee system pursuant to section 93 et seq. BWG are likewise counted. The corresponding amounts are determined by Haftungsgesellschaft and communicated to members liable for contributions.

In 2013, collaboration with savings banks was further strengthened by way of an additional agreement. The purpose of the agreement concluded in 2013 and effective as of 1 January 2014 is not only to broaden the regulatory options available to Erste Group Bank AG but also to ensure compliance with point 127 of Article 4 (1) CRR and Article 113 (7) CRR with a view to allowing recognition of minority interests at consolidated level in accordance with Article 84 (6) CRR. Savings banks that are party to the agreement concluded in 2013 also include Allgemeine Sparkasse Oberösterreich, which forms an institutional protection scheme as defined under Article 113 (7) CRR with the other members of the Haftungsverbund. Owing to the new legal and supervisory requirements, the maximum limits for support mechanisms of the individual members were raised and an ex ante fund was set up. Payments to the ex-ante fund are made on a quarterly basis over a period of 10 years. In the financial statements, the payments by the individual members are recognised as participations in IPS GesbR – which has been charged with managing the ex-ante fund. There was a shift in retained earnings from untied reserves to tied reserves. On the basis of the contractual provisions, these retained earnings represent a tied reserve. These tied retained earnings may be released only if the ex-ante fund is used due to a contingency. Internally, this reserve may therefore not be used to cover a loss and, at member level, it does not qualify as capital under the definition of CRR; on a consolidated level, however, the ex-ante fund qualifies as capital.

Additional disclosures pursuant to section 243a (1) UGB

All restrictions on voting rights or the transfer of shares, even if they are included in agreements between shareholders, insofar as they are known to the management board pursuant to section 243a (1) no. 2 UGB:

In shareholder agreements, the Privatstiftung agreed with its partners the following: Concerning the appointment of the members of the supervisory board, the partners are obliged to vote as required by the Privatstiftung. The partners can dispose of shares according to a predefined sale procedure and can purchase shares only within the quotas agreed with the Privatstiftung (of in total a maximum of 2% within 12 months); with this regulation an unwanted creeping-in according to the Takeover Act shall be prevented. In addition, the partners have committed themselves not to make a hostile takeover bid, nor to participate in a hostile takeover bid, nor to act together with a hostile bidder in any other way.

Under article 15.1 of the articles of association, for the duration of its assumption of liability for all current and future debts in the event of their default on payment, the Privatstiftung is entitled, pursuant to section 92 (9) of the Austrian Banking Act, to delegate up to one-third of the supervisory board members to be elected at the annual general meeting. Until now, the Privatstiftung has not exercised this right.

Article 15.4 of the Articles of Association concerning the appointment and dismissal of members of the management board and the supervisory board is not directly prescribed by statutory law: A three-quarters majority of valid votes cast and a three-quarters majority of the subscribed capital represented at the meeting considering the proposal are required to pass a motion for removal of supervisory board members. The Articles of Association contain no restrictions in respect of voting rights or the transfer of shares. Article 19.9 of the Articles of Association concerning amendments to the Articles of Association contains a provision that is not prescribed directly by statutory law: Amendments to the Articles of Association, in so far as they do not alter the business purpose, may be passed by a simple majority of votes cast and a simple majority of the subscribed capital represented at the meeting considering the amendment. Where higher majority votes are required by individual provisions of the Articles of Association, these provisions can only be amended with the same higher majority vote. Moreover, amendments to Article 19.9 require a three-quarters majority of the votes cast and a three-quarters majority of the subscribed capital represented at the meeting considering the proposal.

Additional disclosures pursuant to section 243a (1) no. 7 UGB

Pursuant to the following provisions, members of the management board have the right to repurchase shares, where such a right is not prescribed by statutory law.
As per resolution of the annual general meeting of 17 May 2017:

- The management board is entitled to purchase up to 10% of the subscribed capital in treasury shares for trading purposes according to section 65 (1) no. 7 Austrian Stock Corporation Act (AktG). However, the trading portfolio of these shares must not exceed 5% of the subscribed capital at the end of any calendar day. The consideration for the shares to be purchased must not be less than 50% of the closing price at the Vienna Stock Exchange on the last trading day prior to the purchase and must not exceed 20% of the closing price at the Vienna Stock Exchange on the last trading day prior to the purchase. This authorisation is valid for a period of 30 months, i.e. until 11 November 2017.
- The management board is entitled, pursuant to section 65 (1) no. 8 as well as (1a) and (1b) Stock Exchange Act and for a period of 30 months from the date of the resolution, i.e. until 11 November 2017, to acquire own shares of up to 10% of the subscribed capital, subject to approval by the supervisory board, with the option of making repeated use of the 10% limit, either at the stock exchange or over the counter, likewise to the exclusion of the shareholders' right to tender proportional payment. The authorisation may be exercised in whole or in part or in several instalments and in pursuit of one or more purposes. The market price per share must not be below EUR 2.00 or above EUR 120.00. Pursuant to section 65 (1b) in conjunction with section 171 Stock Corporation Act, the management board is authorised, from the date of the resolution, i.e. until 11 May 2020, on approval by the supervisory board, to sell or use the company's own shares, also by means other than the stock exchange or a public offering for any purpose allowed by the law, particularly as consideration for the acquisition and financing of the acquisition of companies, businesses, business divisions or shares in one or more businesses in Austria or abroad to the exclusion of the shareholders' proportional purchase option. The authorisation may be exercised in whole or in part or in several instalments and in pursuit of one or more purposes. The management board is authorised to redeem own shares subject to the supervisory board's approval without requiring the annual general meeting to adopt any further resolution.

The management board is authorised until 28 June 2017, with the consent of the supervisory board, to issue convertible bonds, which have the conversion or subscription right for shares of the Company, observing or excluding the subscription rights of the shareholders. The terms and conditions may, in addition or instead of a conversion or subscription right, also provide for the mandatory conversion at the end of the term or at any other time. The issuance of the convertible bonds is limited to the extent that all conversion or subscription rights and, in the case of a mandatory conversion stipulated in terms and conditions, the mandatory conversion, are covered by conditional capital. The issue amount, the terms and conditions of the issue of the convertible bonds and the exclusion of the subscription rights for the shareholders will be determined by the management board with the consent of the supervisory board.

Concerning the authorised and conditional capital we refer to the information given in Note 36 to the consolidated financial statements. All sales and purchases were carried out as authorised at the annual general meeting.

Significant agreements pursuant to section 243 a (1) no. 8 UGB

The following paragraphs list important agreements to which the company is party and which become effective, are amended or are rendered ineffective when there is a change in the control of the company as a result of a takeover bid, as well as their effects:

Haftungsverbund

The agreement in principle of the Haftungsverbund provides for the possibility of early cancellation for good cause. Good cause allowing the respective other contracting parties to cancel the agreement is deemed to exist if

- one contracting party harms grossly the duties resulting from present agreement
- the ownership structure of a party to the contract changes in such a way – particularly by transfer or capital increase – that one or more third parties from outside the savings banks sector directly and/or indirectly gain a majority of the equity capital or voting rights in the contracting party or
- one contracting party resigns from the savings banks sector irrespective of the reason.

The Haftungsverbund agreement in principle and supplementary agreement expire if and as soon as any entity that is not a member of the savings bank sector association acquires more than 25% of the voting power or equity capital of Erste Group Bank AG in any manner whatsoever and a member savings bank notifies the Haftungsverbund steering company and Erste Group Bank AG by registered letter within 12 weeks from the change of control that it intends to withdraw from the Haftungsverbund.

Directors and officers insurance

Changes in controlling interests
In the event that any of the following transactions or processes occur during the term of the insurance policy (each constituting a "change of control") in respect of the insured party:

_ the insured party ceases to exist as a result of merger or consolidation, unless the merger or consolidation occurs between two insured parties, or
_ another company, person or group of companies or persons acting in concert who are not insured parties, acquire more than 50% of the insured party's outstanding equity or more than 50% of its voting power (giving rise to the right to control the voting power represented by the shares, and the right to appoint the management board members of the insured party), then the insurance cover under this policy remains in full force and effect for claims relating to unlawful acts committed or alleged to have been committed before this change in control took effect. However, no insurance cover is provided for claims relating to unlawful acts committed or allegedly committed after that time (unless the insured party and insurer agree otherwise). The premium for this insurance cover is deemed to be completely earned.

In the event that a subsidiary ceases to be a subsidiary during the insurance period, the insurance cover under this policy remains in full force and effect for that entity for the remainder of the insurance period or (if applicable) until the end of the extended discovery period but only in respect of claims brought against an insured party in relation to unlawful acts committed or alleged to have been committed by the insured party during the existence of this entity as a subsidiary. No insurance cover is provided for claims brought against an insured party in relation to unlawful acts committed or allegedly committed after this entity ceased to exist.

Cooperation between Erste Group Bank AG and Vienna Insurance Group ("VIG")

Erste Group Bank AG and Vienna Insurance Group AG Wiener Versicherung Gruppe (VIG) are parties to a General Distribution Agreement concerning the framework of the cooperation of Erste Group and VIG in Austria and CEE with respect to bank and insurance products. In the event of a change of control of Erste Group Bank AG, VIG has the right to terminate the General Distribution Agreement and, in the event of a change of control of VIG, Erste Group Bank AG has a reciprocal right. A change of control is defined, with respect to Erste Group Bank AG, as the acquisition of Erste Group Bank AG by any entity other than DIE ERSTE österreichische Spar-Casse Privatstiftung or Austrian savings banks of 50% plus one share of Erste Group Bank AG's voting shares and, with respect to VIG, as the acquisition of VIG by any entity other than Wiener Städtische Wechselseitiger Versicherungsverein-Vermögensverwaltung-Vienna Insurance Group of 50% plus one share of VIG's voting shares. If VIG elects to terminate the General Distribution Agreement after a change of control of Erste Group Bank AG has occurred, it may choose to ask for a reduction of the original purchase price that it and its group companies have paid for the shares in the CEE insurance companies of Erste Group. The rebate corresponds to the difference between the purchase price and the embedded value and is reduced to zero on a linear scale from 26 March 2013 to 16 March 2018.

Erste Group Bank AG and VIG are furthermore parties to an Asset Management Agreement, pursuant to which Erste Group undertakes to manage certain parts of VIG's and its group companies' securities assets. In the event of a change of control (as defined above), each party has a termination right. If Erste Group Bank AG elects to terminate the Asset Management Agreement following such a change of control of VIG because the new controlling shareholders of VIG no longer support the Agreement, it may choose to ask for a full refund of the purchase price that it has paid for 95% of Ringturm Kapitalanlagegesellschaft m.b.H., the asset management company performing the services under the Asset Management Agreement. The refund decreases on a linear scale down to zero from October 2013 to October 2018.

INTERNAL CONTROL AND RISK MANAGEMENT SYSTEM FOR THE GROUP FINANCIAL REPORTING PROCEDURES

Control environment

The management board is responsible for the establishment, structure and application of an appropriate internal control and risk management system that meets the company's needs in its group accounting procedures.

The management in each group unit is responsible for implementing group-wide instructions. Compliance with group rules is monitored as part of the audits performed by internal and local auditors.

Consolidated financial statements are prepared by the Group Consolidation department. The assignment of powers, the process description and the necessary control procedure are defined in the operating instructions.

Risks relating to the financial reporting procedures

The main risk in the financial reporting procedures is that errors or deliberate action (fraud) prevent facts from adequately reflecting the company's financial position and performance. This is the case whenever the data provided in the financial statements and notes is essentially inconsistent with the correct figures, i.e. whenever, alone or in aggregate, they are apt to influence the decisions made by the users of financial statements. Such a decision may incur serious damage, such as financial loss, the imposition of sanctions by the banking supervisor or reputational harm.

Furthermore, especially estimates for the determination of the fair value of financial instruments for which no reliable market value is available, estimates for the accounting of risk provisions for loans and advances and for provisions, complex measurement requirements for accounting as well as a difficult business environment bear the risk of significant financial reporting errors.

Controls

Group Accounting and Group Performance Management are responsible for group reporting and report to Erste Group's CFO.

Erste Group issues group policies used for preparation of consolidated financial statements in accordance with IFRS. A summary description of the accounting process is provided in Erste Group's IFRS Accounting Manual. All transactions have to be recorded, posted and accounted for in accordance with the accounting and measurement methods set out in this manual. The management of each subsidiary is responsible for the implementation of group policies. The basic components of the internal control system (ICS) at Erste Group are:

- Controlling as a permanent financial/business analysis (e.g. comparison of target and actual data between Accounting and Controlling) and control of the company and/or individual corporate divisions.
- Systemic, automatic control systems and measures in the formal procedure and structure, e.g. programmed controls during data processing.
- Principles of functional separation and checks performed by a second person (the four-eye principle).
- Internal Audit – as a separate organisational unit – is charged with monitoring all corporate divisions in an independent yet proximate manner, particularly with regard to the effectiveness of the components of the internal control system. The Internal Audit unit is monitored and/or checked by the management board, the audit committee/supervisory board, by external parties (bank supervisor, in individual cases also by an external auditor) as well as through audit's internal quality assurance measures (self-assessments, peer reviews).

Group Consolidation

The data provided by the group entities is checked for plausibility by the Group Consolidation department. The subsequent consolidation steps are then performed using the consolidation system (TAGETIK). These include consolidation of capital, expense and income consolidation, and debt consolidation. Lastly, possible intragroup gains are eliminated. At the end of the consolidation process, the notes to the financial statements are prepared in accordance with IFRS, BWG and UGB.

The consolidated financial statements and the group management report are reviewed by the audit committee of the supervisory board and are also presented to the supervisory board for approval. They are published as part of the annual report, on Erste Group's website and in the Official Journal of Wiener Zeitung and finally filed with the Commercial Register.

Information and communication

Each year, the annual report shows the consolidated results in the form of a complete set of consolidated financial statements. In addition, the management summary provides verbal comments on the consolidated results in accordance with the statutory requirements. Throughout the year, the group produces consolidated monthly reports for group management. Statutory interim reports are produced that conform to the provisions of IAS 34 and are also published quarterly in accordance with the Austrian Stock Corporation Act. Before publication, the consolidated financial statements are presented to senior managers and the Chief Financial Officer for final approval and then submitted to the supervisory board's audit committee.

Reporting is almost fully automated, based on source systems and automated interfaces, and guarantees up-to-date data for controlling, segment reporting and other analyses. Accounting information is derived from the same data source and is reconciled monthly for reporting purposes. Close collaboration between accounting and controlling permits continual target/actual comparisons for control and reconciliation purposes. Monthly and quarterly reports to the management board and the supervisory board ensure a regular flow of financial information and monitoring of the internal control system.

Responsibilities of Internal Audit

Internal Audit is in charge of auditing and evaluating all areas of the bank based on risk-oriented audit areas (according to the annual audit plan as approved by the management board and reported to the audit committee). The main focus of audit reviews is to monitor the completeness and functionality of the internal control system. Internal Audit has the duty of reporting its findings to the group's management board, supervisory board and audit committee several times within one year.

According to section 42 BWG, Internal Audit is a control body that is directly subordinate to the management board. Its sole purpose is to comprehensively verify the lawfulness, propriety and expediency of the banking business and banking operation on an ongoing basis. The mandate of Internal Audit is therefore to support the management board in its efforts to secure the bank's assets and promote economic and operational performance and thus in the management board's pursuit of its business and operating policy. The activities of Internal Audit are governed in particular by the currently applicable Rules of Procedure, which were drawn up under the authority of all management board members and approved as well as implemented by them. The Rules of Procedure are reviewed on a regular basis and whenever required and adapted should the need arise.

Audit activities of Internal Audit

In its auditing activities, Internal Audit puts a special focus on:

- Operating and business areas of the bank;
- Operating and business processes of the bank;
- Internal bank standards (policies, guidelines, operating instructions), also with regard to their compliance and up-to-dateness;
- Audit areas stipulated by the law as they inter alia result from the rules of the Austrian Banking Act (BWG) and the Capital Requirements Regulation (CRR).

Internal Audit performs its responsibilities based on its own discretion and in compliance with the annual audit plan as approved by the management board. Once approved, the audit plan is also reported to the audit committee.

CORPORATE GOVERNANCE

The (consolidated) corporate governance report is part of the annual report of Erste Group (http://www.erstegroup.com/investor-relations).

(CONSOLIDATED) NON-FINANCIAL DECLARATION

Erste Group decided to prepare and publish a separate non-financial report – integrated in the annual report– in line with an option provided for in the Austrian Sustainability and Diversity Improvement Act (NaDiVeG).

Management board	
Andreas Treichl mp, Chairman	Willibald Cernko mp, Member
Peter Bosek mp, Member	Gernot Mittendorfer mp, Member
Petr Brávek mp, Member	Jozef Síkela mp, Member

Vienna, 28 February 2018