



## Erste Bank becomes leading Central European bank

### Czech Government accepts Erste Bank's bid for Ceska Sporitelna

"The acquisition of Ceska Sporitelna, the second largest bank in the Czech Republic, is not only a major step forward for Erste Bank in the implementation of its Central European strategy, but makes us into the most important retail bank in the region", said Andreas Treichl, CEO of Erste Bank der oesterreichischen Sparkassen AG ("Erste Bank") following the Czech Government's announcement that it decided to accept Erste Bank's offer to buy a 52 % stake in Ceska Sporitelna a.s. (CS).

With total assets of around CZK 351 billion (EUR 9.8 billion(1)) as at 30.9.1999, CS is the second largest bank in the Czech Republic. It is the clear leader in retail business with market shares of 35 % in primary deposits, 50 % in lending business, 30 % in mortgage loans and 75 % in ATM and credit cards. A further core business is in services for small and medium-sized enterprises in the Czech Republic. The CS group includes the investment fund company Sporitelni investicni spolecnost a.s., the building society CS - stavebni sporitelna a.s., the insurance company CS - Zivnostenska pojistovna, a.s., the pension fund company "Sporitelni penzini fond, a.s." and the leasing company Corfina a.s. Selected group subsidiaries are market leaders in their respective sectors.

The acquisition of Ceska Sporitelna is in line with Erste Bank's Central European strategy. There is an excellent fit between CS and Erste Bank, and CS provides a means for Erste Bank to fulfil its strategic objective of becoming the leading retail bank in the region. Together with CS, Erste Bank will have a network of around 1000 branches spread across Central Europe, including the following potential candidates for EU entry - the Czech Republic, Hungary and Croatia. For the enlarged Erste Bank Group including CS, the share of Eastern European business in total group assets and profits is expected to rise to between 20 % and 30 % over the next three to five years.

#### Purchase price

The purchase price for the 52.07 % stake (56.22 % of the voting rights) is CZK 19 billion (EUR 529 million). This represents a premium of 29 % over the closing price on 1 February 2000.

Erste Bank is committed to conducting capital increases with a combined value in the amount of CZK 4 billion (EUR 111 million). The new capital is expected to be used for expansion in important areas of business, including insurance, asset management, leasing and venture capital financing. In addition, it is planned to merge Erste Bank Sparkassen (Prague) into CS.

#### Financing

The financing of the deal is currently being evaluated by Erste Bank and a range of approaches to structuring the financing are being discussed. Through the EUR 100 million issue of Sub Tier 1 capital in January 1999 and authorised capital with a nominal value of EUR 43.6 million the bank has substantial latitude with Tier 1 funds. However, the Erste Bank Group will in any case ensure that its Tier 1 ratio remains at a level of at least 6 %.

#### Protection against credit risks

The quality of the loan portfolio of CS has been substantially improved through a November 1999 "Bail-Out-Programme" of the Czech Government in the amount of about CZK 50 bn (EUR 1.4 bn).

A significant part of the agreement with the Czech National Property Fund (NPF) deals with securing Erste Bank against CS's remaining credit risks in the form of a guarantee by the Czech Government ("Ring Fencing").

The governmental guarantee for the risk assets of CS lasts for five years. After the acquisition the remaining credit portfolio will be the subject of a detailed review. Non-performing loans that are identified can be transferred from CS to Konsolidacni banka within this five year period.

"These agreements ensure that Erste Bank will not inherit problem risks stemming from credit decisions taken in the past, and will also give us sufficient time to reappraise the credit portfolio and offload non-performing loans", said Treichl, highlighting a key element of the four month long negotiations.

#### Additional support programmes for the Czech economy

As part of an additional support programme for the Czech economy, CS in conjunction with Erste Bank will offer financing worth CZK 20 billion (EUR 557 million) at subsidised interest rates to Czech companies and private households. These programmes are to be targeted at boosting growth in areas which are of importance to the wider economy, and are also aimed at diminishing the current tight credit conditions in the Czech Republic. In addition this will provide CS with access to new customers.

The financing to be offered is as follows:

- A housing construction and renovation programme worth CZK 10 billion (EUR 278 million), tailored specifically for private households. These loans will have a term of up to 20 years
- A programme tailored for SMEs and the agricultural sector worth CZK 10 billion (EUR 278 million). These loans will have a term of up to 10 years
- A venture capital fund with a volume of CZK 1 billion (EUR 28 million) will be established to provide capital for Czech SMEs and start-ups

### **The privatisation process**

"During the four months of negotiations we found the Czech Government to be a professional player and tough negotiating partner. We are grateful to the Government and the Czech National Bank. With this decision they have demonstrated immense confidence in Erste Bank and in the Austrian economy. We will ensure that this confidence is rewarded, not least because the Government has stood its ground against some very unusual challenges from the fringes of this privatisation process", said Andreas Treichl, commenting on the privatisation process and the Government's decision on the sale.

As the largest Austrian investment to date in the Czech Republic, that carries with it responsibility for billions in customer funds in both countries, it will create the strongest link yet between the Czech and Austrian economies.

"Through a cross border presence the Austrian economy and in particular the banks and insurance companies have for years been strong advocates of EU membership for our neighbouring countries", Treichl added. "In my personal opinion, every Austrian Government will persistently support the principle of enlargement of the EU to include our neighbours".

### **Continuing the modernisation of the Czech banking industry**

The sale of CS to Erste Bank underscores the Czech Government's commitment to the ongoing modernisation of the banking industry in line with western practices and standards. Together with the management of CS, Erste Bank will inject expertise, products and, in particular, customer focus into the CS strategy. The goal is to keep CS in the forefront of Czech financial services with all the benefits of being part of an integrated regional powerhouse.

The restructuring costs associated with achieving this clear improved focus are put at around CZK 8 billion (EUR 223 million) over the next three years. This includes investments in software and in the branch restructuring programme. A significant proportion of the expenditure is to be on training programmes for employees, in order to deliver a customer orientation in line with western standards as soon as possible. Not only the customer focus, but also the customer segmentation is to be brought into with Erste Bank's standards.

The envisaged investments in software are to be primarily aimed at enabling marketing information, the cross-selling of financial products among CS group subsidiaries and process reengineering. Better use is to be made of CS's widely spread branch network, particularly with regard to the sale of insurance products. In view of the modern equipment in place at CS, no investments are expected to be required in IT hardware.

### **Earnings targets and timetable**

Erste Bank's earnings targets for 2000 (an ROE of over 12 % and a cost/income ratio of 65-67 %) will be delayed by a maximum of one to two years as a result of the Ceska Sportelna acquisition. The preliminary business plan for the enlarged Erste Bank Group, drawn up in the course of acquisition negotiations, supports this forecast by predicting an average increase in Group profits of around 15 % per annum. The restructuring and support program costs are included in the Business Plan.

As soon as the acquisition contract is signed, Erste Bank has the right to appoint a member of the Management Board of CS and two members of its Supervisory Board. By hiring Jack Stack, a former Executive Vice President at Chase Manhattan, Erste Bank has secured a leading international retail banker, and Erste Bank will put him forward to the CS Supervisory Board for an appointment to the Management Board of CS.

After the closing of the deal, when the CS shares will be transferred to Erste Bank, and which is scheduled to follow the submission of audited results in Q2 2000, Erste Bank will hold 56 % of the voting rights and therefore a controlling majority stake in CS. This means that Erste Bank will assume management responsibility for CS.

The other major shareholders are the EBRD (which holds a 6 % stake) and the insurer Ceska Pojistovna (8 %). In addition, 7 % of the total share capital comprises preferred stock without voting rights held by Czech municipalities. Ceska Sportelna is listed on the stock exchange - the free float accounts for about 28 %.

(1) EUR 1 = CZK 35.85

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