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Implications of COVID-19 crisis for the Turkish banking sector

Client briefing

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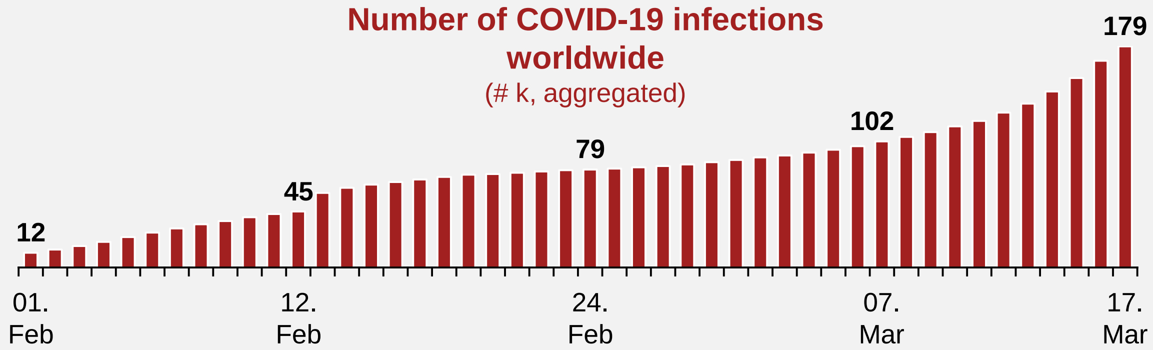
pwc

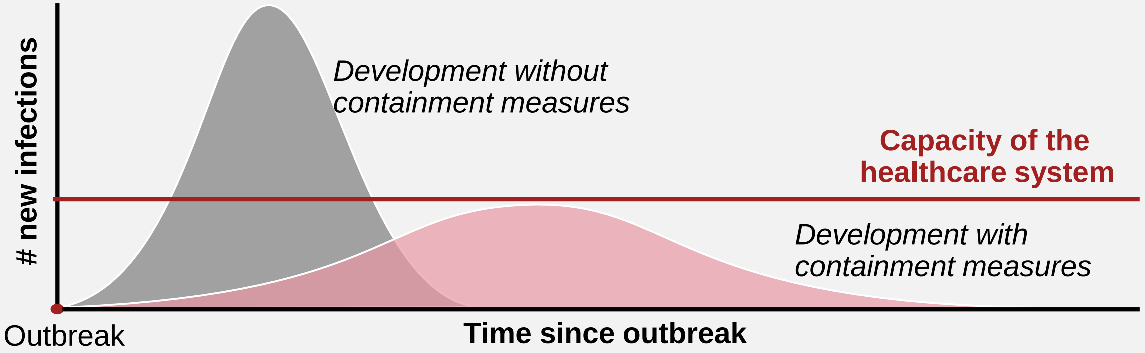
After severe market disruptions, a long-term pandemic might put the economic system under severe stress

COVID-19 pandemic: Initial situation

COVID-19 continues to spread in over 170 countries



Containment could lead to a long-term pandemic



Perspective

- Global COVID-19 pandemic currently causing **significant market disruptions**
- **External shock** hits a fragile global economy – limited headroom for responses of central banks
- Containment is the best solution for society, but fatal for the economy – **the longer the pandemic persists, potentially the deeper the recession**
- **Liquidity shock due to decline in sales** already impacting SMEs and specific sub-industries
- Disruption of supply chains and production stops could soon potentially lead to **more widespread liquidity shortages** in many industries
- Rising expectations of the society and regulators from banks to **continue supporting the economy** and **acting responsibly**

Source: European Centre for Disease Prevention and Control, World Health Organization; Strategy& analysis

European banking sector already hit by first negative effects of the crisis – likely affecting Turkish banking sector as well

Impact on the European and Turkish banking market

Challenges before the crisis

Macroeconomic pressure on asset quality	*Concerns over bank's **asset quality** due to **worsening macroeconomic environment** continue to rise*
Profitability slump	*Difficulties to compensate **for declining net interest income***
Pressure on fees & commissions	*Regulatory **pressure** to **fee & commission income***
End of the economic cycle	***Key risk indicators** are at an **increasing trend***

COVID-19: First effects in the banking sector

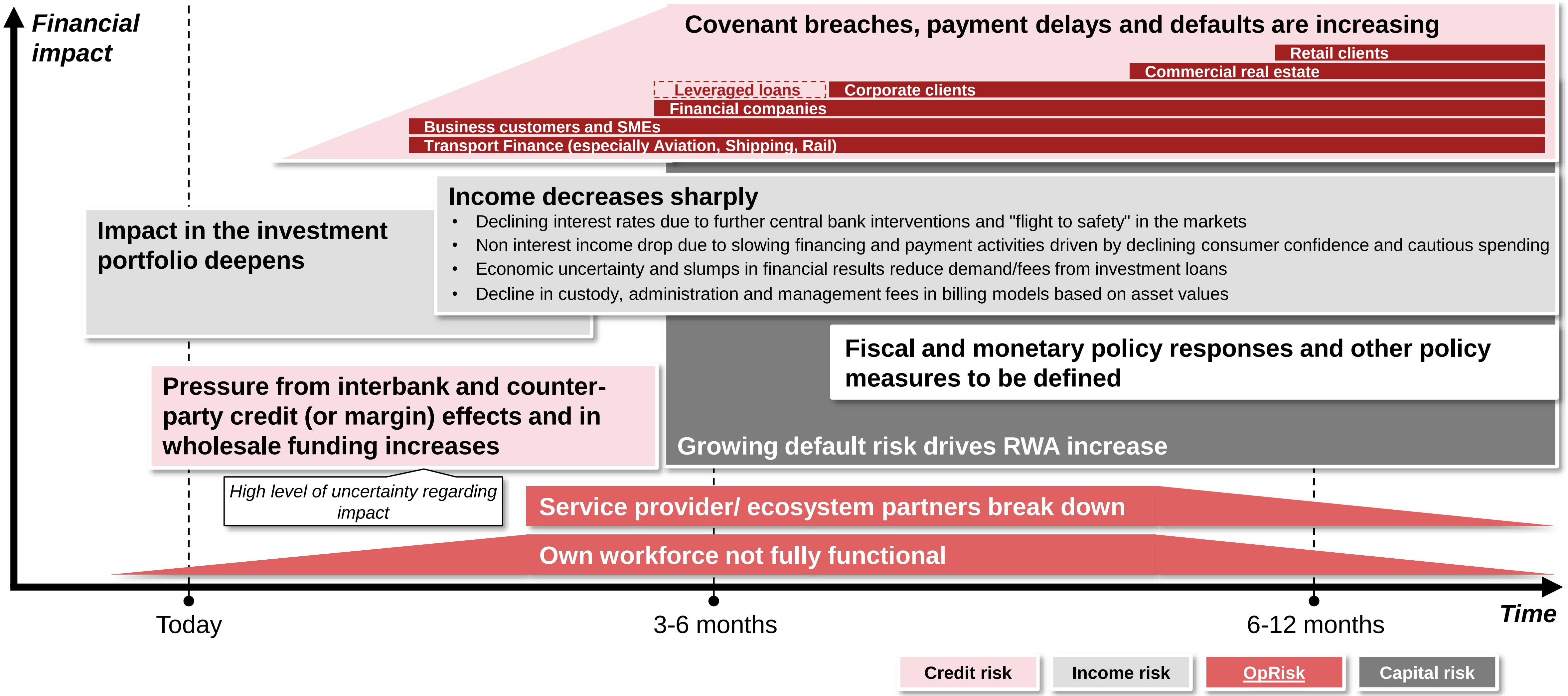
- **Corporate customers draw their undrawn credit facilities to increase liquidity buffer**
- **Importance of operational resilience increased, burden over alternative distribution channels surged**
- **Government and regulator taking action to minimize impact of COVID-19**
- **Increasing pressure to make decisions in dealing with covenant breaches and unprofitable customers**
- **Securing regional and overseas wholesale funding potentially becoming more difficult**

New business already in slow-down during 2019 due to asset quality concerns – what will be banks' reaction to the crisis in 2020?

Source: Strategy& analysis

COVID-19 has the potential to infect banks at various levels and lead to losses

Risks for banks in case of a long-term pandemic



This is important now: to prepare as best as possible for the economic storm of the COVID-19 crisis

Management priorities

1

Ensure operational and funding resilience

- Activation of crisis or business continuity plans and teams
- Ensuring operational resilience (internally) and checking readiness of customers, channels, partners as well as managing operational and security burden on alternative distribution channels
- Ensure funding resilience going forward
- Crisis communication with stakeholders including own workforce

2

Perform scenario analysis of credit portfolios

- Rapid, model-driven review of loan portfolios
- Focus on exposure of particularly affected industries/ regions/ products (e.g. project financing activities and covenant breaches)
- Implementation of scenario analyses (e.g. worst case) and stress testing
- Identification of particularly critical loans

3

Adapting market strategies

- Assess potential impact on different business (e.g. payments volume decrease)
- Derive potential options (business as usual, origination stop, balanced approach)
- Analysis of options per market area / client segment (client profitability, acceptable level of covenant breaches)
- Accelerate digital sales and service enablement in preparation for «social distancing» and reduced branch footfall

4

Develop portfolio strategies

- Identification of critical loans and / or group of loans that require action
- Development of potential options to mitigate risks (e.g. sale, restructuring, maturity / limit extension, exit)
- Analysis of options and development of guidelines to handle possible scenarios going forward
- Implement portfolio strategy

5

Cost and liquidity management

- Based on scenario and other analyses, estimation of potential balance sheet and P&L impact of current situation
- Identification of cost reduction (e.g. expense and channel optimization) and liquidity management levers to ensure business continuity and profitability
- Implement levers

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Three to six months remaining until impact of income, credit and capital risks become fully visible

Source: Strategy& analysis

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