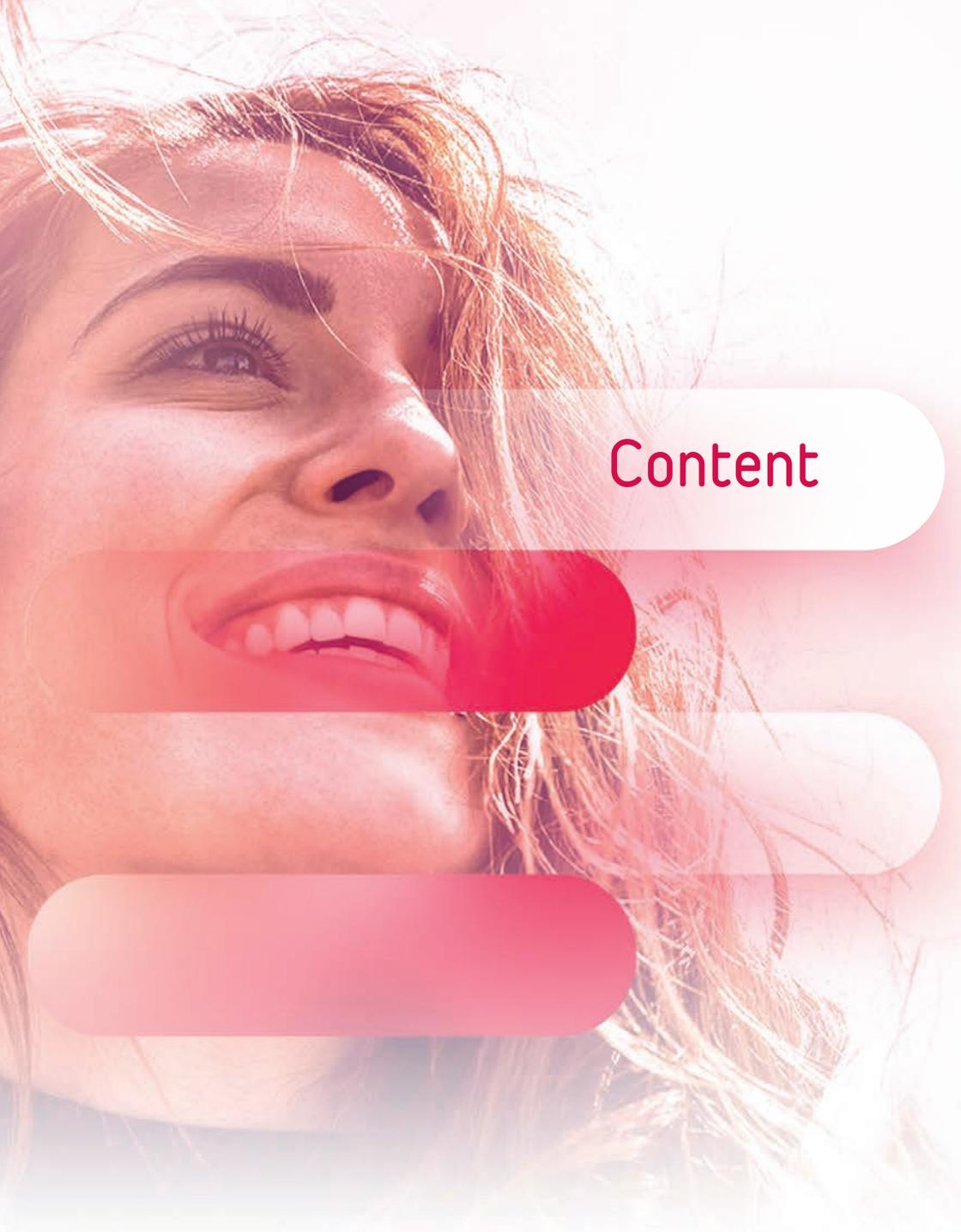




# RISK REPORT 2020



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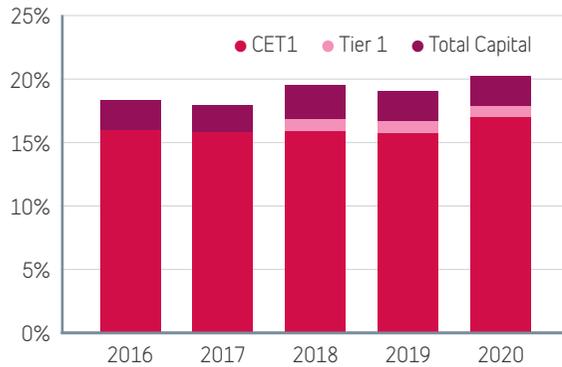


# 2020 – key figures

CET 1 RATIO	CAD RATIO	LCR	COST OF RISK	ASSET QUALITY RATIO	COVERAGE RATIO	LEVERAGE RATIO
Percent	Percent	Percent	EUR Million	Percent	Percent	Percent
<b>17.1</b> (15.9)	<b>20.4</b> (19.2)	<b>158</b> (130)	<b>453</b> (111)	<b>2.02</b> (1.96)	<b>60</b> (62.3)	<b>6.85</b> (5.95)

## CAPITAL RATIO

Percent



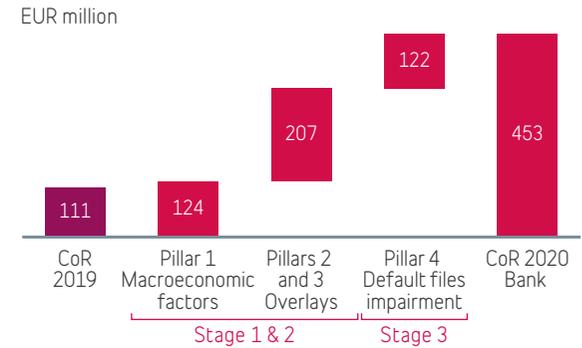
## DEVELOPMENTS IN RISK-WEIGHTED ASSETS

EUR Billion



## EVOLUTION COST OF RISK

In EUR Million





# Summary of risk profile

## An unexpected and unprecedented crisis

The Covid-19 pandemic was an unprecedented shock. It was called a 'Crisis like no other' as soon as 15 April 2020 when the International Monetary Fund warned that the 'Great Lockdown' recession would be the worst in almost 100 years. The crisis had a worldwide impact and was characterized by huge uncertainties about duration and intensity. One year later, the pandemic is still not under control and economic recovery prospects remain subject to a high degree of uncertainty.

In Belgium, the surge in reported Covid-19 cases in February and March led the Belgian governments to impose strict containment measures. As the number of Covid-19 cases decreased in May, authorities gradually lifted restrictions. Nonetheless, infections have rapidly increased again in a new wave of the pandemic and containment measures have resumed in the second part of 2020.

Although the monetary, fiscal and prudential policy responses to limit the impacts on the economy and financial institutions have been in many ways much more supportive than in the previous crises, the lockdowns affected large to small corporates as well as individuals and public sector entities and led to sharp Gross Domestic Product contractions (-6.3% in Belgium<sup>(1)</sup>).

Beside the Covid-19 sanitary and economic crisis, the year was also characterized by an unstable geopolitical environment, namely with high uncertainties by year-end relating to the Brexit and the turmoil of the US elections.

Therefore, we can conclude that the bank and the insurance company had to manage a real-life stress test exercise, dealing with challenges and uncertainties reaching levels never seen before and events impacting intensively all areas of financial and non-financial risk management.

As further detailed in the next sections, the Risk & Compliance department proved agile in 2020 and promptly reacted to adjust the risk management practices to the Covid-19 situation in all key

(1) NBB Economic Review December 2020.

risk areas and with intensive collaboration with the 1st and 2nd lines of defence (Business lines, Information Technology, Human resources, Finance department,...). This allowed to maintain the risks, measured by financial and non-financial metrics, under control and globally in line with our risk appetite framework.

## Prompt policy response to Covid-19

The disruption from the Covid-19 pandemic led to the adoption of extraordinary policy measures to support economies. The responses included monetary measures, fiscal stimulus and ad-hoc regulatory packages to support credit markets and banks' lending to households and corporates.

In Belgium, measures providing liquidity support to the economy included:

- A guarantee scheme (EUR 50 billion) made available for new credits and new lines of credit to viable non-financial businesses, viable independents and non-profit organizations, initially for a maximum of 1 year and in a second stage, 20% of the envelope of the guarantee scheme up to 3 years for loans to Small and Medium Enterprises (SMEs).
- Moratoria to viable companies on loans and advances and to individuals on mortgage and consumer loans as well as payment of premiums on mortgage protection insurance, if they could prove Covid-19 related issues.
- The Belgian insurance sector also committed to extend cover, with no further formalities, for pension, death, disability and hospitalisation under group insurance (contracted by employers) for all persons in temporary unemployment. The payment of premiums due by employers in this context is deferred until 31 March 2021. It is up to the employers to decide whether or not to use this possibility.

Monetary support from the ECB was strong too with many measures taken to keep liquidity flowing and give support to credit markets (Asset Purchase Program reinforcement, introduction of the Pandemic Emergency Purchase Program, easing conditions TLTRO-3 and additional TLTRO's,...).



EU prudential and supervisory measures were also taken to guarantee banks' continued support of the economy, including the following measures:

<b>Cost of risk and non-performing loans</b>	<ul style="list-style-type: none"><li>→ EBA and ECB guidance in the way to compute stage 1 &amp; 2 impairments. The purpose was to use a long term "through-the-cycle" view and avoid the negative impact from procyclicality of the IFRS 9 methodology that would otherwise require to give greater weight to the point-in-time stress data</li><li>→ Regulatory guidance was given to the banks with respect to the treatment of exposures covered by public and private moratoria related to Covid-19, both from a prudential (forbearance as unlikely-to-pay classification) and an accounting perspective (as an indication of significant increase in credit risk)</li></ul>
<b>VaR overshootings</b>	<ul style="list-style-type: none"><li>→ The ECB smoothed the negative impact on Market RWA from financial market turmoils by temporarily reducing penalizing factors in the calculations</li></ul>
<b>TRIM requirements</b>	<ul style="list-style-type: none"><li>→ TRIM and non-final decisions at the time of crisis burst have been put on hold until Q3 2020</li><li>→ Existing deadlines for remedial actions imposed in the context of on-site inspections, TRIM inspections, internal model investigations and SREP qualitative measures were postponed</li></ul>
<b>Stress testing</b>	<ul style="list-style-type: none"><li>→ Postponement of the EU-wide 2020 stress test exercise to 2021</li></ul>
<b>Basel III finalization</b>	<ul style="list-style-type: none"><li>→ Implementation of Basel III finalisation has been postponed by one year to 1 January 2023</li></ul>
<b>Capital relief</b>	<ul style="list-style-type: none"><li>→ Capital requirements were lowered through various adjustments (countercyclical capital buffers; possibility to partially cover the Pillar 2 Requirement with own funds other than CET 1, etc)</li><li>→ Transitional arrangements were offered to mitigate the impact of IFRS 9 on solvency</li><li>→ A more favourable prudential treatment was allowed for SMEs</li><li>→ Publication of a statement on dividends distribution and variable remuneration policies in the context of Covid-19 inviting prudent approach in capital management by the ECB</li></ul>
<b>SII regulatory measures</b>	<ul style="list-style-type: none"><li>→ Some countercyclical regulatory measures (like the volatility adjustment on spread movements and the symmetric adjustment on equities) have supported the European insurers' SII ratio during the first semester of 2020</li></ul>
<b>NBB/EIOPA measures for insurers</b>	<ul style="list-style-type: none"><li>→ Implementation of NBB LAC DT circular was postponed to the end of year 2020</li><li>→ Delay in application of some reporting deadlines</li><li>→ Publication of a statement on dividends distribution and variable remuneration policies in the context of Covid-19 inviting prudent approach in capital management</li></ul>



## Belfius adjusted immediately its governance...

The crisis, very soon in the year, led to governance adjustments, namely through the set-up of a daily Group Crisis committee and new dashboards & tools:

### Crisis committee

- The crisis committee was the cornerstone of the crisis management. It is a group (Bank and Insurance) committee that met to deal with all important Covid-19 related topics (financial markets evolution, Profit & Loss (P&L) impact of measures taken, liquidity situation, Human Resources (HR) situation, follow-up of use of moratoria and State guarantee loans, internal & external communication, impact on Belfius Insurance financials & loan portfolios, assessment of business continuity plans (BCP), etc.
- The members include the Bank's management board, key people of the Insurance company's management board and experts from various departments.
- The minutes and decisions were shared instantaneously a.o. with the Board of Directors Chairman and the other Belfius Insurance' management board members.
- Frequency of the meetings was initially daily, before being progressively reduced to ad-hoc meetings.

Besides the Crisis committee, more specific committees were set up temporarily for Belfius Bank and Belfius Insurance, including a weekly management board dedicated to P&L and solvency situation, a cost of risk committee, a liquidity committee, an ALCO committee, etc.

### Dashboards and tools

The number and frequency of a wide-range of dashboards and reports have been revised to monitor the situation closely for Belfius Bank and Belfius Insurance (e.g. E&E committed lines, HR dashboard, liquidity cockpit, liquidity dashboard, liquidity reporting, daily P&L FM, daily mortgages, weekly solvency, weekly anti-fraud, weekly outsourcing, weekly corona requests, weekly PBR, weekly WEP, Credit risk dashboard, weekly NBB Covid-19 report, daily Solvency II (SII) dashboard and economic indicators, specific Covid-19 liquidity and credit stress tests for Belfius Insurance, weekly ALCO Belins, ad-hoc Covid-19 ORSA stress testing exercise, etc).

Despite these changes aiming at closer and timely monitoring, the fundamentals of existing governance remained in place:

- The existing committees (Management Boards, Risk Committees, Board of Directors) were also used as means to monitor the situation. They met on a more frequent basis than usually due to the extraordinary circumstances.
- The standard governance process (sequence and precedence of committees) was left unchanged.

## ...and took additional risk measures

### Non-financial risks

Operational measures with regard to staff and customers' safety and increased vigilance regarding operational and business continuity were implemented very early:

1. Implementation of BCP strategies to protect people's health and ensure business continuity. For instance, massive staff teleworking for long duration was decided before the start of the confinement together with increase of IT capacity.
2. Regular Anti-Fraud Steering Committee and Information Steering Committee addressing new risks and monitoring adapted Covid-19 processes which could impact the effectiveness of existing internal controls.
3. Dedicated (SARIC/RCSA-based) surveys about potential impacted controls and additional risks were conducted and internal controls were re-enforced, when needed.
4. As external risks increased sharply, specific attention was devoted to:
  - new fraud schemes and risks (a.o. spoofing and impersonation);
  - cyber risk scan round-ups;
  - outsourcing and third-party risks;
  - proper change management through the New Product Approval Process (NPAP).

These actions contributed to a successful business continuity (>99.9% applications availability, >95% of staff working remote, >99% open branches) and a strong resilience to increasing cyberattacks and fraud risks.



## Credit risk

Unlike the 2008-2009 financial crisis, the Covid-19 pandemic directly hit the real economy affecting drastically goods and services production and distribution in key sectors such as primarily, but not exclusively, accommodation and food services, entertainment activities, (non-food) retail sales and some segments of transportation. The companies directly or indirectly hit by the lockdowns, especially small and medium-sized enterprises, rapidly made use of available loan commitments and moratoria to secure liquidity and operational continuity. Credit demand was also driven, to a limited extent, by government guaranteed loans.

The credit risk management team adapted to the new situation and set up several operational processes to manage Covid-19 impacts, including:

- Set up and roll-out of a portfolio screening process, organized in waves, and aiming at the identification of vulnerable sectors/counterparties as a complementary approach to the IFRS 9 mechanical expected credit losses calculations (= Covid-19 overlays).
- Close cooperation with Business & Corporate bankers to define a priority list of credit reviews and to assess customers' vulnerability and implement risk mitigation action plans (line reductions, additional collateral, etc).
- Integration of Covid-19 impacts in IFRS 9 impairment models: revision of macro-economic factors and scenarios based on a long-term average for all the relevant macroeconomic factors with a backward and a forward looking part, revision of the scenario weights, definition of Covid-19 overlays, inclusion of ECB/EBA relief measures.
- Definition of analyst guidance for rating assignment to ensure a uniform approach when integrating Covid-19 impacts and sensitivities in the (re-) rating process.
- Regulatory watch of risk management texts and guidances related to the effects of the Covid-19-crisis.
- Development of new detection and early warning tools (a.o. transactional data to better capture the ongoing evolution).
- Creation of a detailed Credit Risk Dashboard (rating evolutions, use of credit lines, use of Covid-19 loans, payment arrears, watchlist, defaults,..).
- Regular reporting to the Management Board and Board of Directors.

These measures led to a strong and as accurate as possible cost of risk approach taking into account the specific nature of the crisis with sufficient forward-looking elements and portfolio granularity to avoid severe cost of risk impacts in the coming years and at the same time, avoid excessive pro-cyclicality.

For 2020, the CoR amounts to EUR 453 million of which EUR 331 million resulting from ex-ante provisioning (stage 1 & stage 2) and EUR 122 million in stage 3, only part of which can be attributed to the Covid-19 crisis.

## Market risk

The market risks teams reacted promptly to the Covid-19 crisis by developing new detection and monitoring tools and by taking actions to protect the P&L and solvency:

- The Covid-19 crisis was particularly hard for counterparty credit spreads (translated into Fair Value through P&L via Credit Value Adjustment (CVA)) and generated huge equity drops, equity volatility, interest rate and FX swings. Starting the first week of the Covid-19 crisis, actions were taken to further reduce the credit spread sensitivity. The other remaining risk sensitivities, although well within internal limits at the beginning of the crisis, were reduced to a maximum extent.
- Permanent monitoring between Risk and Front office was put in place including intraday estimates of risks and results as well as a daily reporting to the Management Board.

The actions taken throughout the year led to the implementation of new limits to align with Management Board risk appetite, significant improvement of sensitivity analysis (including cross-effects) and proposal for new hedges.

## Strategic risk

The crisis led to:

- The development of new methodologies to assess Cost of risk and Risk Weighted Asset (RWA) impact from Covid-19. Multiple stress tests were run during the year to update the Cost of risk and RWA forecasts on a five-year horizon.
- The Risk appetite framework has been adjusted:
  - To reflect the regulators' additional capital flexibility;
  - To introduce a floor Net Income Before Tax (NIBT) in some key risk indicators to ensure Belfius would be able to continue to fully support the real economy and execute its core business.
- Some reports were enhanced, e.g. with the implementation of weekly capital dashboards, with detailed assessment of the capital and RWA evolution and sensitivities.



These actions gave progressively a full view and comfort about Belfius' capacity to financially bear such a crisis and on the fact that Belfius was solid enough to play an active role in supporting the real economy in these crucial times, with CET 1 of 17.1% and LCR of 158% at the end of Q4 2020.

## Insurance

Regarding the crisis management and business continuity, Belfius Insurance was fully included in the entire Belfius Group exercise. During the first semester of 2020, after concerns for employees and the business continuity have first been addressed, the business impacts have been tackled.

As anticipated, the claims turned out to be very moderate in Life and Health thanks to the typology of our policyholders which are proportionally much less vulnerable to the virus. In Non-Life, the contractual conditions preserved the company against massive losses in business interruption and the economic slowdown which followed the lock-down even led to a loss experience below the normal on branches such as motor and workers' compensation. The effect of the crisis on production was more noticeable, but it returned to better fortune as the de-containment progressed and the production bounced back to levels close to normal, except in Life.

Finally, the most important effect at short term for Belfius Insurance comes from the financial markets causing huge volatility of the Solvency II ratio requiring close monitoring and management actions. All along the year, considering the deep uncertainty, the priority at Belfius Insurance was to protect the solvency and the P&L of the company. Hence, actions have been taken proportionate to the risk bearing capacity:

- Dynamic management of balance sheet as de-risking of the balance sheet;
- Capital management with allocation of the results 2019 in the retained earnings;
- Duration gap - investing on long duration bonds.

At the end of the year 2020, Belfius Insurance continues to rank amongst the best capitalized Belgian Insurers with a SII ratio of 200%.

Moreover, all along the year, specific monitoring and stress tests were regularly performed to assess the Belfius Insurance' resilience. Results were positive and didn't require additional actions. The latest "Covid-19" stress tests assessing the sustainability of the Belfius Insurance financial plan 21-25 (forward-looking view) concluded that the risk exposure is commensurate to the risk appetite of the company.

## Belfius fulfilled its mission statement and proved highly resilient

Belfius Group being firmly anchored in all the segments of the Belgian economy and society, it was of utmost importance to be able to rely on strong solvency and liquidity positions and on our capacity to adjust rapidly our internal and external processes to unusual situations to absorb the shocks and be able to uninterruptedly remain one of the driving forces of the Belgian economy. In this objective, the unfailing commitment of the Belfius' staff operating in a resilient operational and collaborative environment allowed to continuously support the Belfius' customers and thereby the whole Belgian society.

Particular attention has been given to finding the right balance between our responsibility towards the Belgian society and economy on the one hand, and preserving our financial position on the other hand (in particular the quality of the loan book and the potential capital impacts thereof).

At the end of 2020, Belfius proved it has a very resilient business model and financial profile and was able to fulfil its mission statement. Risk appetite has been respected in most dimensions, despite the unprecedented crisis which has affected both financial and non-financial risks.

### Risk appetite framework

Our risk appetite framework (RAF) has not been significantly modified by the Covid-19 crisis and we maintained a very high compliance degree throughout the year.

The changes brought to the framework due to the Covid-19 crisis were limited to:

- adjusting the solvency minimum requirements to bring them in line with evolving regulatory requirements and getting a temporary approval for managing solvency ratios at a lower level if needed, a precaution which proved unnecessary;
- flooring the Net income before tax that is used as a base to determine acceptable Profit & Loss volatility in order to avoid loan granting constraints in a context in which the Bank had and was willing to support the real economy

The number of Key Risk Indicator (KRI) breaches did not change materially compared to previous years and kept stable quarter on quarter. As required by the RAF policy, each breach is being addressed through the implementation of action plans to bring the measured risk in the safe zone within a reasonable timeframe.



The annual review of the risk appetite framework by year-end led to a further improvement of risk coverage with a fine-tuning of the existing risk indicators or the introduction of new ones such as broader IT risks/access management, NPAP, compliances topics, etc. In particular, Belfius invests in structural programs as part of the 20-25 strategy whose successful achievement is closely monitored in the risk appetite framework especially through new areas covered such as “transformation/project risk” for anticipating any deviation or “resource risk” for maintaining an enabling staff environment. A new area related to “outsourcing and third-party risk” has also been deeply developed to monitor our exposure to partners’ failure or non-respect of contractual obligations.

## Asset quality

Belfius maintained a historically strong asset quality with a stable asset quality ratio of 2.02% in 2020 vs 1.96% in 2019. The Covid-19 crisis did not have a significant impact on non-performing loans so far, which is attributable to the intrinsic resilience level of the portfolio, but also to a wide range of support measures such as debt moratoria, guarantee scheme, relaxation of insolvency laws and general fiscal measures.

The strong asset quality is also maintained for the portfolios Corporate and Business which presents average PD levels that remain in line with the historical averages (PD of 1.41% for the Corporate Banking portfolio and 2.06% for the Business Banking portfolio). In the Retail segment, the average PD of the mortgage portfolio remains also solid and in line with levels recorded over the last years (PD of 0.50%).

After years of decline, non-performing loans (NPL) started to rise slightly for the first time, but the asset quality ratios remain well within tolerance limits. The deterioration materialized as from Q2 2020 especially in the Corporate and Business Banking segments. However, the number of new defaults remains within reasonable boundaries.

The cost of risk increased markedly in 2020 (EUR 453 million or 35bp in 2020 vs EUR 111 million or 9bp in 2019), reflecting higher expected credit losses and anticipating on a possible worsening of the credit portfolio quality. The significant amount of ex-ante provisions taken by Belfius in 2020 (EUR 331 million) will help alleviate the P&L impact from expected non-performing loans increase as from 2021 if support measures come to an end. The coverage ratio was still a high 60.0% at year-end 2020 vs 62.3% in 2019.

Over the year, Belfius has granted EUR 8.1 billion of moratoria (EUR 4.7 billion to Corporate banking & Business banking customers, EUR 0.4 billion to Public sector customers and EUR 3.0 billion to mortgages loans). The pick-up rates on moratoria that expired on 31 December 2020 are very high (>99%) for each segment, which highlighted the efficiency of the measure.

Even in crisis time, Belfius continued to monitor potential de-risking opportunities in its run-off portfolios and large exposure concentrations. The management decided at the end of 2020 to sell Italian Government Bonds (total fair value of EUR 885 million) considering the market window with low credit spreads and a possible increasing risk profile in the future. The transaction was done with a positive up-front P&L impact of EUR 4.2 million and translated into a RWA gain of EUR 968 million. Still in the ex-Legacy portfolios, one of the major transactions was the novation of EUR 305 million uncollateralized derivatives into collateralized deals (P&L EUR -5.5 million, RWA gain EUR 464 million). In total, the active balance sheet management resulted in a significant RWA reduction of EUR 1.8 billion (-50 bps CET 1).

The overall market value of the portfolio of the insurance company decreased in 2020 because of the turnaround in the challenging environment (macroeconomic and societal) and the context of volatile financial markets marked by the Covid-19 crisis. This was dampened by the continuous growth of the mortgage production. This balance sheet evolution was strictly monitored through a sound risk management.

In terms of asset management, the asset allocation of the insurance company is bound by limits to absorb severe stresses as foreseen by the approved risk appetite of the company. The specific limits applied on the assets are defined in the investment risk framework and the counterparty limit framework (which is aligned with that of the bank in the context of the conglomerate) and are regularly monitored. This resulted in a high asset quality with an average credit rating at A-. Due to the persistent decline in rates, the duration gap required more active management. An investment plan was implemented in the first half of the year reducing the duration gap and the basis point value of the insurance company.

Considering the current economic situation, Belfius will, more than ever, closely monitor its portfolios’ asset quality to quickly identify possible deterioration and (pro)actively manage assets and non-performing loans in the balance sheet.

## Solvency and liquidity

Active loan growth and support to the real economy in a Covid-19 context were done without jeopardizing the solvency and liquidity ratios that improved over the year and remained strongly above the regulatory requirements.

Based on their 2020 solvency metrics, Belfius Bank and Belfius Insurance continued to rank amongst the best capitalized European banks and insurance companies.



The Bank CET 1 ratio reached 17.1% at the end of 2020 (vs 15.9% at YE 2019). This solid capital base still compares very favourably with Belfius' minimum SREP requirement (9.625%) and internally defined operational target (>13.5%). The lower CET 1 supervisory requirement compared to last year follows (i) decisions of national supervisor to release the countercyclical buffer due to the Covid-19 crisis and (ii) implementation of the ECB measure whereby pillar 2 requirement (P2R) can be partially met with capital instruments that do not qualify as Common Equity Tier 1 (Additional Tier 1 (AT1) and Tier 2 instruments).

The CET 1 ratio of 17.1%, 126 bps up compared to December 2019, results from higher CET 1 capital (EUR 10.1 billion in 2020 vs EUR 8.8 billion in 2019, +214 bp) and higher RWA (EUR 59.3 billion in 2020 vs EUR 56.4 billion in 2019, -88 bp).

The positive impact at CET 1 level is namely attributable to:

- net income (+55bp CET 1 ratio);
- a change regarding the option given to the financial conglomerate on the way to include of the value of Belfius Insurance' equity in the Bank's RWA calculation (Danish Compromise under the equity method, +40bp);
- the implementation of the IFRS 9 transitional measures (+75 bp) and
- management actions including the above-mentioned sale of Italian Government bonds and derivatives novation (+48bp). The main negative impact came from the RWA increase related to high production volumes during the year, without significant materialization of credit quality deterioration due to Covid-19 crisis so far (-89bp CET 1 ratio).

Belfius Insurance has been able to maintain a sound risk profile too. The Solvency II ratio is solid (200%) and stable compared to 2019 as the result of financial conditions offset by management actions (+14pp of which no dividend paid for 2019), fine-tuning on model and assumptions including regulatory changes (-2pp). This enables to foresee a dividend of EUR 140 million (-12pp) for the year 2020.

In an abundant ECB funding environment and with a quickly recovering wholesale market, the liquidity and funding profiles of Belfius remained strong in 2020 with a Liquidity Coverage Ratio (LCR) of 158% (2019: 130%) and a Net Stable Funding Ratio (NSFR) of 128% (2019: 116%). Liquid assets represented 13.6x (2019: 4.9x) one-year wholesale refinancing needs at year-end 2020, partly supported by additional (retained) covered bonds. Loan to deposit ratio (for commercial balance sheet) decreased strongly from 94% in 2019 to 89% in 2020.

These strong solvency and liquidity positions, largely respecting all regulatory minima, allowed Belfius to cope with unprecedented economic and geo-political uncertainties and to keep playing

an active positive role for the Belgian society. The current buffers are large and make Belfius strong enough to absorb a possible deterioration of the loan portfolio due to Covid-19 additional effects, face regulatory requirements (e.g. TRIM, Basel III finalization) and support the ambitious growth strategy.

## Non-financial risks

While non-financial risks have been part of the Belfius risk management for many years, the efforts for integrating the non-financial risk culture in Belfius have been paying off in 2020: the Covid-19 crisis has actually been a life stress test for non-financial risks, where Belfius has shown its resilience to a combination of multiple operational risks, including IT (security), human capital, business continuity, fraud, cyber and outsourcing risks. Despite the Covid-19 crisis management and situation, all NFR-related processes have been successfully executed and the NFR management framework has also been consolidated in a concern of continuous improvement, in particular:

- Set up of a project risk framework which has been applied to Core Banking Renewal;
- Highlighting a clear overview on NFR roles and responsibilities and laying down the foundation for a sound conglomerate NFR management framework;
- Review of the NPAP process to ensure adequate process, governance and implementation of new process/activities/products;
- Structural integration of the privacy workflow (GDPR) in the NPAP process, working out advises for strategic files;
- Strengthening of the outsourcing risk management by strengthening risk framework for outsourcing (initial requirements, enhanced audit review,...), by extending the initial scope to other material arrangements and by paying special attention that Belfius' providers are fully complying with their contractual obligations (including GDPR compliance); or
- Major steps for improving the NFR tooling.

## Compliance

Compliance risks remain in our top priorities in order to manage the increasing number of files and increasing files complexity, to deal with evolving regulatory requirements and with ambitious internal targets set to ensure compliance risks remain within our low risk appetite.

In 2020, this translated namely into further progress in the enhancement of the Anti-Money Laundering (AML) framework and oversight (including development of Artificial Intelligence/Big Data models to enhance transactions detection), further awareness and controls enhancement (Know Your Customer (KYC), Know Your Transaction (KYT)) and RAF development.



## Risk management organisation, governance, tools and processes

In this particular year, additional improvements were realized at risk governance level either as a deployment of previous initiatives or to embed the lessons from the 2020 crisis.

The organisation of Credit Risk Management and Strategic Risk Management teams was revised. The organizational adjustment of Credit Risk Management, initiated pre-Covid-19, has put its core responsibilities in the centre of its organization, i.e. building powerful credit rating and decision models and a pro-active monitoring and management of portfolios. In the Strategic Risk Management team, changes included the creation of a RWA competence centre and the reinforcement of the Asset & Liability Management (ALM) & Liquidity second line of defence.

The Conglomerate dimension has been further developed with a closer oversight of subsidiaries, especially those with lower risk culture and further alignment of major Risk policies in a conglomerate approach. This included taking the first steps to implement in 2021 specific risk appetite frameworks at subsidiary level that will reflect and monitor their own (financial and non-financial) vulnerabilities and risks. A first AML risk assessment was performed on conglomerate level, as well as an inventory of all AML risks and policies in the subsidiaries.

Regarding tools and processes, Belfius continues to work on different initiatives to further improve the quality of data and increase efficiency of risk processes.

Amongst those, the project aiming at the creation of a common data platform with specific attention for Risk and Finance data concepts will enable further automation within Risk and Finance and share a common view within the group. In 2020, Belfius has further implemented some technical components that will enable the onboarding of Risk & Finance data in the course of 2021 into that common data platform.

A bank-wide analysis has been achieved and will lead to further centralisation and specialisation of data management and reporting production activities in the Data & Digital department as well as a strengthening of the data governance department within the Finance department. Implementation is foreseen as from 1 March 2021.

Belfius also pursues the implementation of a broad Core Banking Renewal program, a first release will address the credit risk processes from an end-to-end perspective and the risk engines. Lessons from the crisis have fed these project streams with many relevant information.

Belfius also started an initiative regarding RegTech solutions to further automate the production of regulatory reports and investigate opportunities to streamline the Risk and Finance calculation engines.

All these steps aim at putting Belfius in a position to face ever more complex and rapidly evolving risks with strong, comprehensive but also agile risk management processes and practices.

## Belfius' strong profile is confirmed by external sources

### SREP

Due to the Covid-19 pandemic, the EBA and ECB have decided to apply a pragmatic approach towards the SREP for the 2020 cycle. A focus was therefore given to the management of the challenges issued from this crisis. Based on this alternative approach, no supervisory decision was issued regarding pillar 2 requirement that remained unchanged compared to 2019 (as a reminder, the 2019 SREP translated into a 25bp decrease of pillar II requirement to 2%).

### Rating agencies

The rating agencies view positively the group's credit quality as reflected by the rating actions taken during 2020. S&P affirmed the A- long term rating with a stable outlook on April 23, 2020. Fitch initially attached a negative outlook to the A- rating in March 2020, at the time of the Covid-19 outburst, before revising it to A- stable on 21 October 2020. Moody's long-term rating has been left unchanged at A1 with a stable outlook.



# Belfius is ready for the next challenges

The Covid-19 crisis emphasized the group's risk and financial resilience which is key to face the next challenges.

## Covid-19

There remains tremendous uncertainty around the macroeconomic outlook with both downside and upside risks. The outlook will largely depend on the health situation and the timeline for the implementation of an effective medical solution. Depending on the evolution of the sanitary situation, the crisis' additional severity for specific sectors/counterparties and/or the extension or transformation of support measures/recovery plans, banks can be confronted to default flows or negative rating migrations in their loan portfolios.

Although, we are strongly convinced that the approach adopted as a reaction to the Covid-19 crisis has been a very effective way to design a comprehensive cartography of potential risk pockets, to build responsive action plans and execute them in a consistent way, this approach will require further refinement in 2021 both in credit risk detection (e.g. industrialization of early warning signals and monitoring tools including the use of alternative data) and in NPL follow-up and management.

## Profitability

The year 2020 confirmed the importance and validity of the diversification strategy, with strongly resilient pre-provision results in all segments.

Yet, profitability will remain a key attention point in the coming years due to the continuous decrease of interest rates and the steady increase of non-maturing deposits, both trends being reinforced by the Covid-19 crisis and pressuring the Bank's net interest margin. We are tackling this challenge by continuously enhancing our risk-based pricing framework and by enriching the interest rate risk framework (e.g. deep review of models and assumptions, inclusion of additional scenarios that also cover tail risk,...).

Beside the attention to our core business' profitability, we aim at diversifying revenue sources. This part of the strategy requires additional controls (operational, compliance,...) to ensure risks remain within the risk appetite. The management has decided to enhance controls and set-up specific corporate offices responsible for the required internal controls. Strategy-related risks will need to be closely monitored to ensure the reinforcements are sufficient in view of the increasing activities' complexity.

## ESG (Environment, Social & Governance)

The troubled period of 2020 demonstrated the validity of the Belfius' strategy: the ambitions of diversification, digitalization and prudent risk appetite. This sets Belfius in a good position to further deploy its strategy and further meet its mission statement of being meaningful and inspiring for the Belgian society, including dealing with the structural changes that we may expect from the pandemic. This process will be supported by national and European recovery programs, with a focus on long-term investments aimed at enabling the green and digital transition of the economy. Internally, this will deploy through the roll-out of a well-defined ESG strategy.

Belfius has started to develop an ESG risk framework in 2020 that is part of the Belfius Sustainability strategy. A dedicated ESG Committee was set up in 2020, supervised by the CEO and monitoring ESG topics at conglomerate level. Additional committees, transversal workgroups and competence centres have been set up throughout the organisation to achieve the sustainability objectives. The aim with ESG considerations is to first address climate-related risks.

From a risk perspective, a first step was taken by including ESG qualitative statements in the Risk appetite framework (quantitative approach to be developed in 2021-2022).

Next steps are to define roadmaps and action plans to manage physical and transition climate risks, both direct and indirect. The process will encompass risk identification and measurement, impact quantification, risk management/mitigation and transparent disclosure. Within the top priorities, embedding ESG considerations in our credit-granting and underwriting process is key, with a special focus on the real estate portfolio.

In 2020, we started screening the balance sheet based on available information, implemented a Transition Acceleration Policy restricting activities in 8 sensitive sectors, developed new products to promote sustainability and took various initiatives to gather external support in developing our ESG strategy.

## Regulatory developments

Belfius is putting many efforts to meet the requirements of the newest EBA guidelines and technical standards covering the models used to estimate probability of default (PD) and loss given default (LGD). The roadmap of model development is well on-track at end of the 2020.

Regulatory developments also include the National Bank of Belgium supervisory expectations regarding the lending standards for mortgage loans, requiring banks and insurance companies to strengthen their underwriting criteria. These measures, which entered into force in 2020, have



translated into revised credit standards at origination and are monitored through a specific Risk Appetite Framework in application since 1 January 2020 and a dedicated reporting to the NBB.

Main challenges from the EU banking reform entail the new method for the measurement of counterparty credit risk (SA-CCR), the minimum loss coverage mechanism for new non-performing exposures (backstop provisioning) and revision of the large exposure framework. All these topics are addressed actively, and we expect no material obstacles to the implementation of the new regulatory requirements.

Belfius is also preparing for upcoming regulatory developments from Basel III finalisation and the EU Banking reform, including the revised market risk framework (Fundamental Review of the Trading Book). Based on current assessments, Belfius expects a moderate impact from the Basel III finalisation package on its solvency and considers the solvency position as sufficiently robust, as demonstrated above, in normal market circumstances to successfully comply with the requirements of this new regulatory landscape in 2023. Yet, the regulation still entails some uncertainties that would need to be clarified, such as the transposition of the international agreements in the EU legal framework or the discretion of the macro prudential authority to adjust some measures.

During 2020 several regulatory changes and reporting requirements were implemented by the insurance company. Amendment to the LAC DT NBB circular was published in March 2020 and were applicable as from 2020 Q4, having a negative impact on its Solvency II ratio.

All over the year 2020, the NBB was closely following up the crisis on the Belgian insurance market, with demand of dedicated reports on both BCP and financials situations. The NBB took actions as delay in application of some circulars, delay in the EIOPA and NBB stress tests or reporting deadlines.

EIOPA and NBB published a statement on dividends distribution and variable remuneration policies in the context of Covid-19 inviting prudent approach in capital management.

The NBB has also published a circular asking insurers for an in-depth update of the capital planning considering two Covid-19 stress tests determined by the companies themselves. They have been used to assess company policies relating to their future dividends. These stress tests were performed in line with the update of our Financial plan 2021-2025 and demonstrate that Belfius Insurance is resilient to severe but plausible stress tests and that the business plan is globally sustainable from a solvency perspective.

The insurance company is also actively preparing the upcoming regulatory and accounting developments. On the one hand the EIOPA Solvency II 2020 review is currently focusing on the calibration of the Solvency II, while on the other hand IFRS 17 will bring an entirely new system of accounting for insurance contracts.

**Marianne Collin**  
CRO Belfius Bank

**Emmanuel Michiels**  
CRO Belfius Insurance



# I. Regulatory framework and Pillar 3 disclosure

## I.1. Regulatory framework

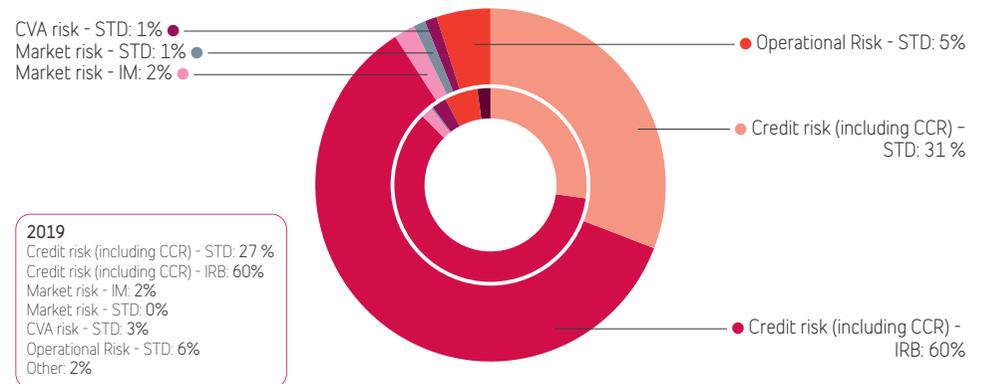
The capital adequacy regulations consist of three pillars.

- The first pillar – minimum capital requirements – defines the way banking institutions calculate their regulatory capital requirements in order to cover credit risk (including counterparty credit risk), market risk, operational risk and credit valuation adjustment (CVA). The framework provides different approaches for calculating credit risk (3 approaches: Standardised, Foundation Internal Rating-Based and Advanced Internal Rating-Based), market risk (2 approaches: Standardised Approach and Internal Model Approach), operational risk (3 approaches: Basic Indicator Approach, Standardised Approach and Advanced Measurement Approach) and CVA (2 approaches: Standardized Approach and Internal Model Approach). The Pillar 1 also encompasses the leverage requirement which is a non-risk-based ratio serving as backstop to the risk-based minimum capital requirements.
- The second pillar – supervisory review – provides the European regulators acting under the Single Supervisory Mechanism (SSM) with a framework to help them in assessing the adequacy of banks’ capital to be used to cover either risks identified in the first pillar but not sufficiently covered by the Pillar 1, or other risks such as among others concentration or interest rate risks.
- The third pillar – market discipline – develops a set of qualitative and quantitative disclosures allowing market participants to make a better assessment of capital, risk exposure, risk assessment processes, and hence the capital adequacy of the institution. The requirements of the third pillar are met by this publication.

### I.1.1. Pillar 1 implementation

Belfius uses different approaches for the determination of its minimum regulatory capital requirements under Pillar:

#### Reporting methods used (Outside 2020 – Inside 2019)



#### I.1.1.1. Credit Risk

Since 1 January 2008, Belfius has been authorised to use the Advanced Internal Rating-Based Approach (AIRB Approach) for the determination of its minimum regulatory capital requirements (see as well IV.2.2.1).

Belfius has also decided to maintain a Standardised Approach for some portfolios for which this approach is specifically authorised by the Basel framework, such as small business units, non-material portfolios, portfolios corresponding to activities in run-off, to be sold or portfolios and entities for which Belfius has adopted a phased roll-out of the AIRB Approach.

In total, credit risks (including CCR) capital requirements represent 91% of total requirement.



### I.1.1.2. Counterparty Credit Risk and CVA risk

Belfius calculates its exposures based on the Mark-to-Market method (also known as Current Exposure Method). Capital requirements are calculated according to the same principles as for credit risk.

The additional charge to cover the risk of Mark-to-Market losses due to a deterioration in the creditworthiness of their counterparties, the CVA risk, is calculated according to the Standardised Method, and represents 1% as compared to 3% in 2019 as a result of the unwind of uncollateralised derivatives.

### I.1.1.3. Market Risk

Since 25 June 2013, Belfius has been authorized to use its historical VaR model for the determination of its regulatory capital requirements. This Internal Model Approach is currently granted for general interest rate risk and foreign exchange risk. Belfius applies the Standardised Approach for specific interest rate risk, equity risk and commodity risk (see as well V.3.6.).

In total, market risks requirements account for 2% of total requirements.

### I.1.1.4. Operational Risk

For operational risk, Belfius Bank applies the Standardised Approach, which accounts for 5% of total capital requirements

## I.1.2. Pillar 2 implementation

The Internal Capital Adequacy Assessment Process (ICAAP), applicable since the end of 2008, requires banks to demonstrate to the supervisors the adequacy of their risk profile and their capital aiming at providing an overview of the internal consolidated Belfius Bank process for assessing its Capital Adequacy in relation to its risk profile and organisation. In this context, appropriate governance has been put in place for the calculation and management of the risks and the assessment of the economic capital needs from a Risk Appetite perspective (see section III.4.3.1.). A Capital Adequacy Statement (CAS), endorsed and signed by the management body, has been communicated to supervisors. Next to this ICAAP, an ILAAP (Internal Liquidity Adequacy Assessment Process) describing how Belfius Bank monitors and assesses the adequacy of its liquidity and funding risk management has been designed. Similarly, a Liquidity Adequacy Statement (LAS), endorsed and signed by the management body, demonstrating that Belfius Bank has an adequate management and monitoring of its liquidity and funding positions and risks, has also been communicated to the supervisors. A detailed description of the Belfius liquidity and funding risk management framework can be found in the chapter Risk management of the Belfius' Management Report (see section on liquidity risk).

The SSM imposes as well additional requirements above the first pillar. The P2R has remained constant at 2%, while the P2G is 1% (see section III.1. for more detail).

## I.1.3. Pillar 3 – Disclosure policy & disclosure map

### I.1.3.1. Pillar 3

The current report contains information about risk management, risk measurement and capital adequacy in accordance with the Capital Requirement Regulation (CRR) and the Capital Requirement Directive (CRD IV) of the European Union.

The current report contains information on all subjects included in the directives and implementing regulations, insofar as they apply to Belfius Bank SA:

- Part eight of CRR;
- EBA guidelines for pillar 3 disclosures (EBA/GL/2016/11);
- Disclosure of own funds requirements (EU No. 1423/2013);
- Disclosure of countercyclical capital buffer (EU No. 2015/1555);
- Disclosure of the leverage ratio (EU No. 2017/200);
- Disclosure of encumbered and unencumbered assets (EU No. 2017/2295);
- Disclosure of liquidity coverage ratio (LCR) (EBA/GL/2017/01);
- Disclosure of remuneration policy (EBA/GL/2015/22);
- Disclosure of NPL (EBA/GL/2018/10);
- EBA guideline on disclosures of exposures subject to measures applied in response to the Covid-19 crisis (EBA/GL/2020/07);
- EBA guideline on IFRS 9 transitional arrangements (EBA/GL/2020/12).

The pillar 3 disclosures under the CRD IV/CRR framework only deal with parent companies, subsidiaries and associated companies in the financial sector, and exclude insurance companies. This means that disclosures of requirements for Belfius Insurance are generally not included in this report. Belfius Insurance prepares its own Solvency Report, which will be published on 20 May 2021.

However, in order to give a representative view of Belfius Group's risk profile, Belfius Insurance figures have been included in some sections, when relevant. In this case, the reporting scope is always clearly indicated.

The information provided in this report has not been subject to an external audit, but the quality of information is guaranteed by a strong process of validation within the Belfius Bank SA Management Board.



The Risk report 2020 and its templates have been signed off by Belfius' Chief Risk Officer. The report was also presented to the Risk Committee and Audit Committee (in joint session) on 19 March 2021 and to the Board of Directors on 25 March 2021.

The decision not to disclose specific information, under circumstances set out in article 432 (1) and (2) of the CRR, i.e. where the information is regarded as not material, proprietary or confidential is finally taken by the Board of Directors.

Information exempted from disclosure due to being non-material, proprietary or confidential can be found in Appendix XI. 1.

The Risk report is presented in euros (EUR), which is Belfius' presentation currency, rounded to the nearest million (unless otherwise stated). Certain figures in this report may not tally exactly due to rounding. Furthermore, certain percentages in this document have been calculated using rounded figures.

The Risk report is released on an annual basis. The next report's update is scheduled for April 2022. Nevertheless, intermediate updates will be published if considered relevant by Belfius due to significant changes in its risk profile.

This Risk report  
and the Risk report  
annex are published  
in English on  
the Belfius website  
[www.belfius.be](http://www.belfius.be)



### I.1.3.2. Pillar 3 disclosure map

If information is already available in the Management report of Belfius or Belfius Insurance and if Belfius believes it is equivalent in nature and scope to the disclosure requirements, the Risk report 2020 clearly refers to it, without repeating this information. For this purpose, a Disclosure map is established.

#### Mapping with Pillar III disclosure

Article CRR	Disclosure requirement	Reference to the chapter in present document	Risk report annex	Reference to external documents: Management report (MR) / Financial statements (FS)
435	Risk Management objectives and policies	II. Risk management governance	■	Coporate governance (MR)
436	Scope of application	I. Regulatory framework and Pillar III disclosure	■	
437	Own funds	III. Equity and capital adequacy	■	
438	Capital requirements	III. Equity and capital adequacy	■	
439	Exposure to counterparty credit risk	IV.4. Counterparty credit risk	■	
440	Capital buffers	III. Equity and capital adequacy	■	
441	Indicators of global systemic importance		Not applicable for Belfius	
442	Credit risk adjustments	IV.3. Credit risk management and governance	■	Accounting policies - section 6.5 Impairment of financial instruments
443	Unencumbered assets	VI.3. Encumbered assets	■	Risk management - Section Liquidity Risk (MR)
444	Use of ECAs	IV.2.3. Standardised approaches		
445	Exposure to market risk	V.3. Trading market risk	■	
446	Operational risk	VII.2. Non-financial risk - operational risk		
447	Exposures in equities not included in the trading book	IV.5. Focus on Equity exposure	■	Accounting policies - section 6.2.3 Financial assets measured at fair value through other comprehensive income (FS)
448	Exposure to interest rate risk on positions not included in the trading book	V.2. Structural &ALM risk		Risk management - Section Market Risk (MR)
449	Exposure to securitisation positions	IV.6. Securitisation risk VI.2. Securitisation activity as originator	■	
450	Remuneration policy			Coporate governance (MR)
451	Leverage	III. Equity and capital adequacy	■	
452	Use of the IRB Approach to credit risk	IV.2.2. Internal rating based approaches XI.2. Risk methodology	■	
453	Use of credit risk mitigation techniques	IV.3.2. Credit risk mitigation techniques	■	
454	Use of the Advanced Measurement Approaches to operational risk		Not applicable for Belfius	
455	Use of Internal Market Risk Models	V.3. Trading market risk	■	



### I.1.3.3. Pillar 3 - Risk report annexes with all tables

As EBA encourages institutions to disclose the quantitative templates in an editable format, the tables listed in the Reference table are not included in the Risk report itself but published in a separate excel file referred as the Annex of the Risk report (Risk report Annex.xls) published on the same level as the Risk report itself. You will find this reference table here beneath.

#### Risk report annex reference table

Disclosure reference	Title
<b>GROUP STRUCTURE AND SCOPE OF APPLICATION</b>	
EU LI1	Differences between accounting and regulatory scopes of consolidation and mapping of financial statements with regulatory risk categories
EU LI2	Main sources of differences between regulatory exposure amounts and carrying values in financial statements
EU LI3	Outline of the differences in the scopes of consolidation (entity by entity)
<b>CAPITAL BASE AND CAPITAL REQUIREMENTS</b>	
CCA	Capital instruments main features. Disclosure according to article 3 in the Commission implementing regulation (EU) No 1423/2013
CC1	Own Funds: disclosure template. Disclosure according to article 5 in the Commission implementing regulation (EU) No 1423/2013
LRSum	Summary reconciliation of accounting assets and leverage ratio exposures
LRCom	Leverage ratio common disclosure
LRSpl	Split-up of on balance sheet exposures
KM1	Key metrics
EU OV1	Overview of RWAs
EU INS1	Non-deducted participations in insurance undertakings
IFRS9	IFRS 9 transitional arrangements
CCyB1	Geographical distribution of credit exposures used in the countercyclical capital buffer
<b>CREDIT RISK AND CREDIT RISK MITIGATION GENERAL INFORMATION</b>	
EU CRB-B	Total and average net amount of exposures
EU CRB-E	Maturity of exposures
EU CR1-A	Credit quality of exposures by exposure class and instrument
EU CR1-B	Credit quality of exposures by industry or counterparty types
EU CR1-C	Credit quality of exposures by geography
Template 1	Information on loans and advances subject to legislative and non-legislative moratoria
Template 2	Breakdown of loans and advances subject to legislative and non-legislative moratoria by residual maturity of moratoria
Template 3	Information on newly originated loans and advances provided under newly applicable public guarantee schemes introduced in response to COVID-19 crisis
EU CQ1	Credit quality of forborne exposure
EU CQ3	Credit quality of performing and non-performing exposures by past due days
EU CR1	Performing and non-performing exposures and related ECL provisions
EU CR2-A	Changes in the stock of ECL provisions
EU CR3	CRM techniques - Overview

Disclosure reference	Title
<b>CREDIT RISK AND CREDIT RISK MITIGATION STANDARDISED APPROACH</b>	
EU CR4	Standardised approach - Credit risk exposure and CRM effects
EU CR5	Standardised approach - Credit risk exposure by regulatory portfolio and risk weight
<b>CREDIT RISK AND CREDIT RISK MITIGATION IRB APPROACH</b>	
EU CR6	IRB approach - Credit risk exposures by exposure class and PD range
EU CR9	IRB approach - Backtesting of PD per exposure class
EU CR10	IRB (specialised lending under slotting approach and equities)
<b>COUNTERPARTY CREDIT RISK</b>	
EU CCR1	Analysis of CCR exposure by approach
EU CCR8	Exposures to CCPs
EU CCR3	Standardised approach - CCR exposures by regulatory portfolio and risk weights
EU CCR4	IRB approach - CCR exposures by portfolio and PD scale
EU CCR5-A	Impact of netting and collateral held on exposure values
EU CCR5-B	Composition of collateral for exposures to CCR
EU CCR6	Credit derivatives exposures
EU CCR2	CVA capital charge
<b>MARKET RISK</b>	
EU MR1	Market risk under the standardised approach
EU MR2-A	Market risk under the IMA
EU MR3	IMA values for trading portfolios
<b>(UN)ENCUMBERED ASSETS</b>	
Template A	Encumbered and unencumbered assets
Template B	Collateral received
Template C	Source of encumbrance
<b>LIQUIDITY REQUIREMENTS DISCLOSURE</b>	
LIQ1	Quantitative disclosure on LCR
LIQ2	Qualitative disclosure on LCR
<b>SECURITISATION</b>	
SEC 1	Securitisation exposures in the banking book
SEC 3	Securitisation exposures in the banking book and associated capital requirements



## I.2. Declaration approved by the management body on the adequacy of risk management arrangements

Belfius Bank is a Belgian banking and insurance group fully owned by the Belgian Federal State through the Federal Holding and Investment Company (FHIC). Belfius Bank shares are not listed.

Belfius Bank is a locally anchored autonomous banking and insurance group serving individuals, professionals, companies, social profit institutions and public authorities in Belgium.

With a mainly Belgian balance sheet in its commercial Businesses and customers from all segments, Belfius is committed to deliver value-added products and services through a modern proximity model. It aims at a healthy financial profile, reflected in a prudent investment strategy and a carefully managed risk profile, resulting into sound liquidity and solvency positions.

The Belfius risk management framework is based on the 3 Lines of Defence (3 LoD's) model with a set of adapted and effective guidelines, policies and internal controls. Belfius Bank has centralised risk data and systems supporting regulatory reporting and disclosures as well as internal management reporting on a regular or ad-hoc basis for the various risk types (credit risk, market risk, liquidity risk, non-financial risk...). The various reports are presented to the appropriate committees as indicated in the risk governance structure. The most relevant key ratios and figures are incorporated in the "Summary of risk profile".

In accordance with Article 435 of Regulation (EU) No. 575/2013, the Management Board is of the opinion that the risk management system is adequate regarding Belfius' risk profile and strategy.

The Management Board considers that this Risk report demonstrates the assurance of the adequacy of the risk management system.

This declaration is also approved by Belfius Bank's Board of Directors of 25 March 2021.

# II. Risk management governance

## II.1. Governance arrangements

For the global governance arrangements at Belfius Bank and Belfius Insurance, we refer to the respective Annual Reports (see chapter Corporate governance).

## II.2. Risk governance model at Belfius Bank

### II.2.1. Three lines of defence model

The Belfius risk management framework is based on the 3 Lines of Defence (3 LoD's) model with a set of adapted and effective internal controls.

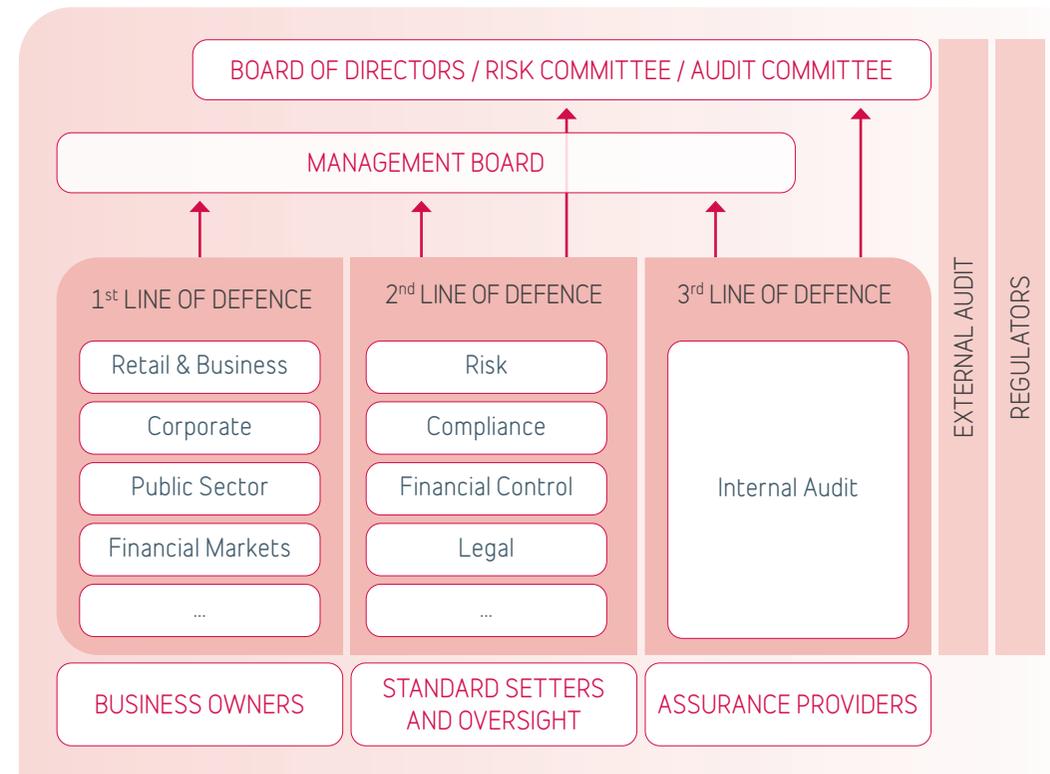
The first line of defence is the responsibility of the business (and support lines when applicable) and their management as this is where the risks are taken (handled) or where the risks occur and where risks are potentially mitigated.

The second line of defence is the responsibility of the (transversal) control functions assured mainly but not exclusively by Risk and Compliance, which are independent from the business.

The third line of defence is the responsibility of the internal audit function, which provides an independent review of the first two lines of defence.

In concrete, the different roles are:

- 1<sup>st</sup> LoD: own, manage and control risk (Business Lines/Front) within the framework designed by the 2nd LoD;
- 2<sup>nd</sup> LoD: define the risk management framework (policies, guidelines, Risk Appetite Framework...), monitor and control risk in support of the 1st line (Risk, Financial control, Legal, Compliance) and keep global risk oversight;



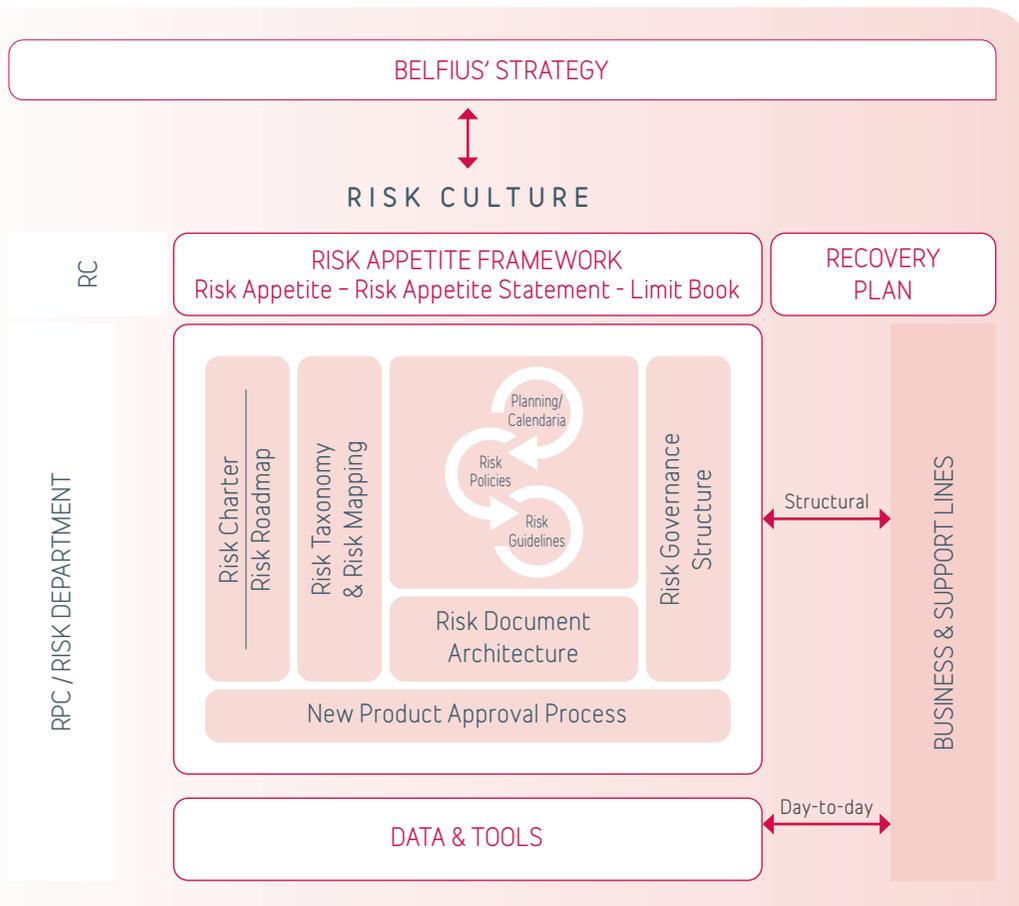
- 3<sup>rd</sup> LoD: provide independent assurance to the Board of Director and the Management Board of the effectiveness of Risk Management and Control (Internal audit).

With regards to the 3 LoD model, the Risk Mapping enables a good risk coverage as well as an enhanced ability to spot gaps and define action plans. This risk mapping has been updated in 2019, integrating all newly identified risk categories in accordance with the adapted Belfius' Risk Taxonomy.



## II.2.2. Risk management framework

The risk management framework aims to implement sound, prudent and effective risk management and corporate governance (see figure below). It aims to cover in a coherent way all elements needed for a sound risk management.



### II.2.2.1. The Risk Appetite Framework (RAF)

(see also Equity and Capital Adequacy – III.3.3.1. Risk Appetite)

The Risk Appetite Framework (RAF) is the expression, at the highest consolidated level, of the risks Belfius is prepared to take or not to take as a stand-alone group pursuing its own strategy and financial targets. It applies group-wide and all (sub-)limits and risk guidelines must be consistent with it. It is composed of 3 levels:

- Level 1 includes high level risk indicators and qualitative statements;
- Level 2 includes more detailed KRI's on a broad range of key risks;
- Level 3 concerns the operational limit book and activity or entity specific risk indicators.

The RAF is coherent with Belfius Group strategy and financial targets. The construction of the RAF is an evolutive process where Key Risk Indicators (KRI's) and limits are checked against business strategies to see if it allows to meet financial targets. One of the key process is to ensure that the Financial Plan, which translates bank strategies into financial figures, respects the RAF limits, both in base case and in case of stress scenarios.

The RAF covers both qualitative and quantitative indicators. Qualitative indicators are embedded in the RAF under the form of statements, while quantitative indicators are based on regulatory requirements (CET 1, LCR, NFRS, MREL,...) and other type of indicators which are deemed relevant to monitor Belfius' risk profile (EaR, operational losses, data breaches, internal fraud indicators, compliance indicators, ..).

These indicators cover a wide range of risks Belfius wants to assess and control. In recent years, non-financial risk indicators (fraud, outsourcing risks, IT risks, HR,..) - including compliance indicators, have been added to the RAF in view of the increasing importance of these new risks in the financial landscape.

For all quantitative indicators, the Board of Directors defines tolerance levels which need to be respected at all times. In case of breaches, an action plan needs to be submitted to the Board of Directors.

### II.2.2.2. The Risk Charter

Belfius Bank has determined the main risk principles and guidance for all stakeholders and departments involved and more specifically for Belfius risk management, in a Risk Charter.

It gives guidance permitting management and staff members to prepare/take decisions, even when specific and adapted policies, guidelines or procedures have not yet been worked out.



### II.2.2.3. The Risk Roadmap

Via its risk roadmap, Belfius Bank sets and communicates the overall objectives for the Risk department, its team members and its main stakeholders (Finance & Business).

The risk roadmap expresses the overall and the risk management objectives, actions and priorities of the Risk department (1 to 2-year time horizon).

### II.2.2.4. The Risk Taxonomy and Risk Mapping

The Risk Taxonomy is a common set of risk categories, used within Belfius, presented following a tree structure in which risks higher up in the hierarchy are decomposed into more specific risk categories. The Belfius Risk Taxonomy is integrated and standardized:

- 1 basic classification: same risk types and classification
- 1 description for each risk category & risk type.

The Belfius Risk Mapping:

- defines clear roles and responsibilities for all risk types and tasks in the Bank;
- ensures better Risk, Compliance and Audit coordination based on common risk assessment and coordinated roadmap;
- constitutes an optimised framework, guaranteeing full risk coverage and redundancy avoidance;
- enhances the ability to spot gaps and optimise risk coverage through increased stakeholder confidence and better targeted resources on key risks (while avoiding redundancy);
- is reviewed regularly to cover all risks.

The general Risk Taxonomy & Risk Mapping have been updated in 2019. The NFR risk taxonomy has been refined in 2020.

### II.2.2.5. The Risk Governance Structure

The Risk Governance Structure

- defines a robust set-up of Risk Committees incorporating effective communication and reporting lines with clear and consistent assignment of responsibilities and authorities;
- consistently assigns roles and responsibilities to both Risk/Risk & Business Committees;
- positions decision taking (and their monitoring) at an adequate management level in a coherent way (Strategic/Tactical - Operational Committees); and
- optimises committees and encourages a double signature process whenever possible.

### II.2.2.6. Risk Policies & Guidelines

The Risk Policies and Guidelines

- constitute an aggregated set of specific risk policies and guidelines to concretize the desired global risk management governance and culture;
- define strategies, roles and responsibilities, concepts and objectives of an activity; and
- give clear instructions for stakeholders to be applied in a day-to-day business context.

### II. 2.2.7. Risk Document Architecture

The Risk Document Architecture describes the main Risk types of document on a high level, together with the responsible issuer, the validation instance and the frequency of update.

### II.2.2.8. New Product Approval Process (NPAP)

The process of developing a “product, activity, process or system” involves several steps that must be completed before the new (or changed) function can be implemented. The policy establishes the overall process and the accountability of the parties involved in this process. Therefore, it defines the governance and describes the new product approval process.

The objectives of the process are the following:

- ensure that the development of a “product, activity, process or system” fits within the strategy of Belfius;
- ensure the risk acceptance (in function of the risk tolerance/appetite);
- ensure that necessary resources are available;
- ensure customer satisfaction;
- avoid unknown or unwanted risks in the future.

We also refer to VII.2.3.3. of this report.

### II.2.2.9. The Recovery Plan

Following the implementation of the Bank Recovery and Resolution Directive (BRRD) and the Belgian Banking Law, Belfius Bank has to prepare a recovery plan, which is updated on a yearly basis. As part of the crisis management framework, the recovery plan outlines how the Bank can react to a financial stress to avoid resolution. In this context, it aims at preparing the Bank to develop recovery measures to restore the financial strength under various types of stress scenarios. The plan is fully integrated in Belfius’ Risk management framework.

For further information about the Resolution Plan, we refer to III.4.3.2.4.



### II.2.2.10. The Risk Culture

The Risk Culture

- is a policy approved by Belfius Bank which sets out the vision, strategy and responsibilities;
- is about standards, attitudes, behaviours and judgements, playing an important role in influencing the actions and decisions taken by individuals within the Bank, related to risk awareness, risk taking and risk management all within a strong risk governance;
- determines the collective ability to identify, understand, openly discuss and act on the current and future risks.

Risk culture is extremely important within Belfius. Risk culture is embedded at all levels of the Group and starts with the tone at the top. The risk culture is developed via multiple complementary processes (trainings, messages from CRO in the QRR, awareness campaign and communication, introduction of permanent controls in the first lines,...), which are continuously enhanced.

### II.2.2.11 Data & Tools

Regarding tools and processes, Belfius continues to work on different initiatives in order to further improve the quality of data and increase efficiency of risk processes. Amongst those, the project aiming at the creation of a common data platform with specific attention for Risk and Finance data concepts will enable further automation within Risk and Finance and share a common view within the group.

In 2020, Belfius has further implemented some technical components that will enable the onboarding of Risk & Finance data in the course of 2021 into that common data platform. Belfius also pursues the implementation of a broad Core Banking Renewal program, a first release will address the credit risk processes from an end-to-end perspective and the risk engines. Lessons from the crisis have fed these project streams with many relevant information. Belfius also started an Initiative regarding RegTech solutions in order to further automate the production of regulatory reportings and Investigate opportunities to streamline the Risk and Finance calculation engines.

## II.2.3. Risk governance structure

A performant risk governance structure is considered as a central cornerstone to sound risk management. A robust risk committee set-up incorporates effective communication and reporting lines and a clear delineation of responsibilities and competences. Such a set-up ensures a two-way process of risk management instructions and feedback enabling senior management to execute its management and supervisory obligations.

### II.2.3.1. Risk Committee operating within the Board of Directors: Risk Committee (RC)

For a more extensive description of the Risk Committee (including remit and functioning), we refer to the Belfius Management report, chapter Corporate governance.

BOARD OF DIRECTORS

Risk Committee

The Risk Committee (RC) is one of the advisory committees operating within the Board of Directors. It has been established in accordance with Article 27 and Article 29 of the Belgian Banking law.

When deemed necessary and without restrictions, the CRO can directly access the chairman of the Risk Committee and/or the Audit Committee.

### II.2.3.2. Risk Committees on strategic level operating within the Management Board

Three risk committees have been set up within the Management Board of Belfius Bank, prepared by the Risk department and meeting 2 to 4 times<sup>(1)</sup> a year:

- the **Risk Policy Committee (RPC)** surveys the definition and the implementation of the Bank's principal risk management and measurement policies, processes and methodologies, and supervises their validation status;
- the **Risk Appetite Committee (RAC)** surveys Belfius' risk appetite, capital adequacy and capital allocation;
- the **Non-Financial Risks (NFR) Committee** ensures a well-governed and coordinated non-financial risk framework for an effective Non-financial risk management.

(1) This is not a fixed number. As the composition of these committees is equal to the Management Board, the specified topics may be presented in a management board without the specific set-up of these dedicated committees.



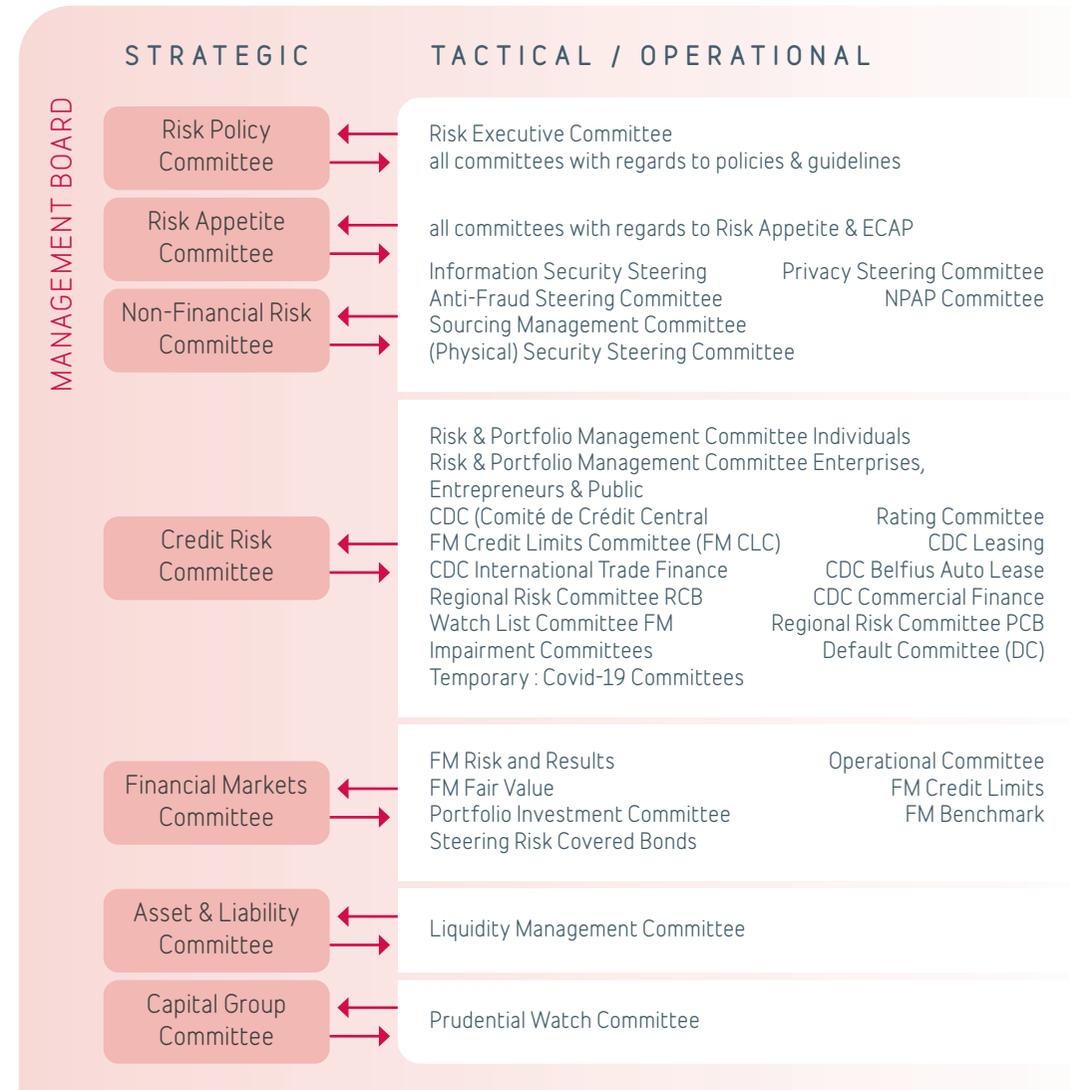
In addition to these three risk committees, four functional areas also report to the Management Board without a separate committee being set up for them:

- the **Credit Risk Committee (CRC)** centralizes, in a strategic and end-to-end process view, all credit risk related topics (origination, monitoring, impairment) into one committee with presence of the Management Board members who are directly involved (CRO, Head of PBR & WEP);
- the **Financial Markets Committee (FMC)** has as prime function the effective risk management oversight and steering of the Financial Markets activities. It is held once a month with a strict quorum including members of the Management Board (CRO, CFO and Head of WEP);
- the **Assets & Liabilities Committee (ALCo)**: while the Management Board and the Board of Directors have the ultimate responsibility for setting the strategic risk appetite and business objectives, they delegate to the ALCo the effective ALM management within the regulatory framework. The Liquidity Management Committee has been mandated by the ALCo to take care of all aspects relating to liquidity management and steering as well as the reporting on the liquidity situation;
- the **Capital Group Committee (CGC)** anticipates, understands, prepares, analyses & monitors all capital aspects on a conglomerate level (Bank, Insurance & related subsidiaries) in compliance with regulatory, legal and economic constraints. It also acts as Prudential Watch Committee (PwaC) to enable Belfius to anticipate, to understand, to steer and to follow-up on prudential reforms, guidelines, proposals and evolutions thereof impacting Belfius and its entities.

### II.2.3.3. Risk Committees on tactical/operational level

The Management Board delegates certain decisions to a tactical/operational level. The details of this delegation are set out in the applicable committee charters. For matters that fall outside this delegation, the tactical/operational level provides information or puts forward opinions to the Management Board, which then decides.

The committees that are part of the tactical/operational level are committees on which the Risk department generally participates alongside business divisions. Risk committees which are steered by the Risk department focus mainly on risk appetite and methodology. Risk/Business committees which are steered jointly by the Risk department and Business focus mainly on guidelines, transactions and risks on counterparty level. The Risk department has a veto right in many of these committees, as well as the right to bring files for decision to a higher governance level.





### II.2.3.3.1. At a general level

The **Risk Executive Committee (Risk ExCom)** is responsible for the day-to-day deployment of the Risk Appetite Framework of Belfius Bank as defined by the Board of Directors and/or the Management Board (RPC, RAC, & Non-Financial Risk Committee) and bears the ultimate responsibility of the implementation of Belfius Bank's risk roadmap.

### II.2.3.3.2. Financial Markets Risk Management

As mentioned above, the **Financial Markets Committee (FMC)** - at strategic level - has as prime function the effective risk management oversight and steering of the Financial Markets activities. This committee is the main committee for Financial Markets Management. The committee is divided into sub-committees which are responding to the main FMC.

The sub-committees are:

- **FM Risk and Results (FM RR)** reviewing business, risks, P/L reports and providing for an appropriate risk management and governance framework aligned to the risk appetite and business objectives set forward by the Management Board;
- **FM Fair Value (FM FV)**, in its capacity of Fair Value assessor, acts as a body in charge of "Fair Value Validation" with a focus on validation of market parameters and models;
- **FM Benchmark**: follow-up of obligations of the Bank as panel bank for the contribution of Euribor and ESTR following the Code of Conduct of Panel Banks and the internal policy;
- **Operational Committee (FM OC)** makes the follow up of operational issues;
- **FM Credit Limits (FM CLC)** approves credit limits requests related to all FM activities, Belins and WEP Trade Finance and monitors the associated credit risk for all the counterparties in the scope of FM RM - Research Analysis;
- **Portfolio Investment Committee (PIC)** acts as the central supervisory and decision body on all matters regarding the management of legacy portfolios (ALM Yield portfolio and Credit Derivatives portfolio). The PIC also receives delegation from the ALCo for the follow-up of the ALM Liquidity portfolio;
- **Steering Risk Covered Bonds (SRCB)**: common Risk forum in order to communicate and to discuss regarding the Covered Bonds programs.

### II.2.3.3.3. Credit Risk Management

Besides the **Credit Risk Committee (CRC)** - at strategic level - the following committees at tactical/operational level cover credit risk:

- the **Risk & Portfolio Management Committee Individuals** is a platform for structural consultation and dialogue, in order to increase the involvement of all stakeholders in the strategy and the functioning of risk management regarding individuals;
- the **Risk Portfolio Management Committee Entreprises, Entrepreneurs & Public (E&E&P)** is a platform for structural consultation and dialogue, in order to increase the involvement of all stakeholders in the strategy and the functioning of risk management regarding E&E&P;
- the **CDC (Comité de Crédit Central)**: the main Credit Committee, the CDC Central (specific delegations have been given to various lower credit committees): approves new credit transactions PC and RC and annual reviews of existing credit files (based on updated financial statements, i.e. without any adjustment of the current risk), that do not exceed its delegation limits and/or that do not lead to an exceeding of the prevailing credit limits; advises on new deals or limits that must be presented to the Management Board;
- the **FM Credit Limits Committee (FM CLC)** is described above under the Financial Market Risk Committees;
- the **CDC International Trade Finance** makes decisions with regard to transactions managed by the International Trade Finance department of Distribution ITF;
- the **Rating Committee**: the main purpose of the Rating Committee is to supervise the correct and coherent application of the various Internal Rating Systems within Belfius Bank and its subsidiaries, together with an assessment of their performance;
- the **CDC Leasing** and the **CDC Belfius Auto Lease** handle new credit applications, extension of lines with a specific duration as well as the periodic review of files;
- the **CDC Commercial Finance** handles new credit applications, extension of lines with a specific duration as well as the periodic review of files;
- the **Regional Risk Committee PBR** monitors the regional loan portfolio, with a special focus on the counterparties whose credit profile is weakened (watch list). It is organised by region (NO, NW, SE, SO and Centrum & Branches);
- the **Regional Risk Committee WEP** monitors the regional loan portfolio, with a special focus on the counterparties whose credit profile is weakened (watch list). It is organised by region (NO, NW, SE, SO and Centrum);
- the **Default Committee (DC)**: the objective of the DC is to decide on and follow up the default status of counterparties, i.e. being a necessary condition for an impairment to be recognised;



- the **Impairment Committees**: the need of Belfius to oversee and govern IFRS 9 impairments resulted in a committee structure, consisting of one Expert Panel and three dedicated Impairment Committees (Stage 1, Stage 2 & Stage 3);
- additional **Covid-19 committees** have been created since the Covid-19 crisis. These are temporary committees.

#### II.2.3.3.4. Non-Financial Risk Management

Besides the **Non-Financial Risks Committee (NFRC)** - at strategic level - the following committees at tactical/operational level cover specific NFR risk:

- the **Information Security Steering (ISS)** ensures a well governed and coordinated information security strategy whereby an adequate “prevention”, “detection”, “protection” and “reaction” in line with regulatory requirements towards information security is guaranteed;
- the **Anti-Fraud Steering Committee** is a platform for the internal control functions (Risk/ Compliance/Internal Audit) and a forum to reflect and organize a dialogue between the internal control functions and all the stakeholders (mainly operating in the decentralised expert units) regarding fraud risk management;
- the **Privacy Steering Committee** ensures a well governed and coordinated privacy strategy in line with regulatory requirements regarding privacy and personal data protection;
- the **(Physical) Security Steering Committee** oversees the (physical) security risk management in order to prevent and provide appropriate protection for all organizational assets of Belfius, with focus on people, from crime incidents and damaging natural elements such as fire;
- the **NPAP Committee** oversees the “New Product Approval Process” (NPAP) management, implementation and execution in order to ensure appropriate risk analysis to any new or changed function. In particular, the committee delivers a final opinion based on the advices of risk experts;
- the **Outsourcing Management Committee** defines and monitors Outsourcing Management. It is organised by Strategic Planning and Performance Management.

## II.3. Risk governance model at Belfius Insurance

For the Risk Governance model at Belfius Insurance, we refer to the Belfius Insurance Annual Report, chapter Risk management.

## II.4. Risk department organisation, role and responsibilities

### II.4.1. General mission

The mission and role of the Risk department are to define and implement a robust risk management framework based inter alia on the following cornerstones:

- an acceptable risk appetite in line with the commercial and financial objectives;
- a set of independent and integrated risk measures for different types of risk, enhanced by internal limits, themselves consistent with the approved risk appetite;
- an effective process to identify, measure, monitor, assess and mitigate risks to which Belfius Bank is or might be exposed, enhanced by timely and accurate reporting to make management aware of all the material risks and the overall risk profile, in order to ensure appropriate decision-taking.

The Risk department has the responsibility to establish a set of risk policies and guidelines defining the risk governance structure and management.

The overall objective of the Risk department is to ensure the implementation of sound, prudent and effective risk management based on a full understanding of the risks relying on swift and proactive risk identification and alerting processes.

### II.4.2. Risk organisation

#### II.4.2.1. At Belfius’ level

In line with Art. 194 of the Banking Law, Belfius is managing risks based on a group-wide<sup>(1)</sup>, consolidated and integrated risk management framework. It assumes a risk-based approach to further strengthen the conglomerate dimension.

The overall objective is to have a risk management coordination, ensuring consistency while respecting the entities’ specificities, responsibilities and legal/regulatory obligations. The main pillars of this risk management are an appropriate risk governance structure, a robust and aligned risk framework, risk monitoring and decision-taking process.

(1) Belfius Bank, Belfius Insurance, Belfius Investment Partners.



The conglomerate dimension of Belfius' Risk Governance includes:

- At the level of the Board of Directors, joint RC/RUC's (Risk Committee / Risk & Underwriting Committee) are scheduled.
- At the level of the Management Board (strategic level):
  - A Group Management Committee (GMC), with potential conflicts dealt with at the level of Mediation Committee
  - A joint Non-Financial Risk Committee (NFRC), related to all NFR topics
  - A Group Financial Conglomerate Review Committee (GFCR), assuring an overview of all subsidiaries. It tackles amongst other the risk management framework of each subsidiary.
- At a general risk level (tactical/operational level), several committees are 'joint' or 'Belfius Together' (BB: Belfius Bank; BI: Belfius Insurance & BIP: Belfius Investment Partners):
  - The Conglo Risk Executive Committee (Conglo Risk ExCom) with participation of the CRO of Belins and the CRO of BIP
  - The Capital Group Committee (CGC) is a joint BB and BI committee
  - The Investment Conviction Committee (ICC) is a joint BB, BI and BIP committee (including Candriam as well)
  - The Assets & Liabilities Committee (ALCo) of Belins in which BB participates
  - The BIP Pricing & Methodology Committee BIP in which BB participates.
- At specific risk level, several subdomains have a common governance with 'Belfius Together' sub-committees for various risks:
  - The Information Security Committee
  - The Anti-Fraud Steering Committee
  - Recent initiative to have a cross committee for ESG/Climate Risk.

The 3 entities have similar risk policies, guidelines framework and approach. They use similar and/or common tools ensuring consistency and enabling coherence as well as an integrated management of risks and internal controls:

- Risk Appetite Framework: defined and validated group wide by Belfius Bank and cascading down to subsidiaries; as such a RAF roll-out for the subsidiaries is further foreseen in 2021.
- Risk Management & Control executed through the "Senior Management Report on the Assessment of the Internal Control".
- ICAAP (Belfius Bank & BIP), Recovery Plan (Belfius Bank) and ORSA (Own Risk and Solvency Assessment; Belfius Insurance).

The Conglomerate dimension has been further developed with a closer oversight of subsidiaries, especially those with lower risk culture, and further alignment of major Risk policies in a conglomerate approach. This included taking the first steps to implement in 2021 specific risk appetite frameworks at subsidiary level that will reflect and monitor their own (financial and non-financial) vulnerabilities and risks. A first AML risk assessment was performed on conglomerate level, as well as an inventory of all AML risks and policies in the subsidiaries.

#### II. 4.2.2. Belfius together

The Risk department has further enhanced the conglomerate dimension in the Risk department, in line with the strategy of the Group (Bank & Insurance).

As from January 2019, the Risk Management implemented organisational changes, following the "Belfius Together" approach. This new Risk Management organisation takes more systematically a conglomerate vision while ensuring quality, efficiency and expertise in both entities at all times.

3 new departments were created for a future-proof Risk Management: the Strategic Risk Management team, the Risk Services team, while the Operational Risk Management team evolved towards Non-Financial Risk Management on a group level.

#### II.4.2.3. At Belfius Bank's level

This risk organisation considers:

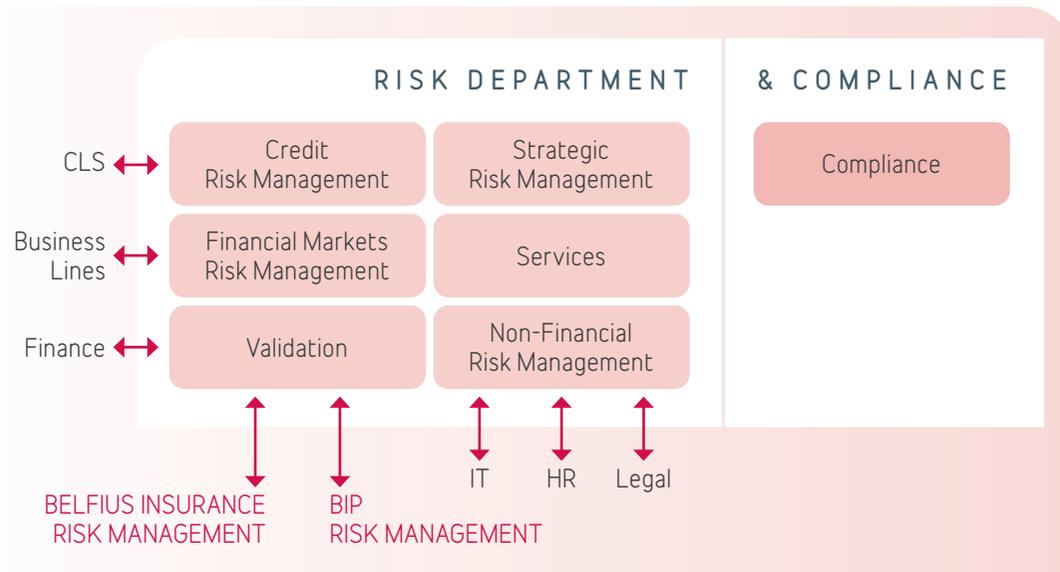
- Belfius as a major actor in the Belgian financial sector/context serving Belgian society/economy;
- the size of Belfius;
- the strategic objectives of Belfius;
- the needed cooperation between methodological and operational risk teams;
- the extension and reinforcement of regulations (Basel III and beyond) and additional (inter) national regulatory frameworks;
- the liquidity, solvency and profitability challenges;
- the necessary promotion of a risk culture within Belfius.



More information regarding the risk governance of Belfius Insurance can be found in the Annual Report of Belfius Insurance, chapter Risk management.



These are the main missions of the various divisions of the Risk department:



#### II.4.2.3.1. Credit Risk Management

The goal pursued by Credit Risk Management is the development and maintenance of an efficient and robust risk management framework for the Retail, Business & Corporates and Public Sector credit activities, based on proactive risk control and risk-challenger view.

#### II.4.2.3.2. FM Risk Management

The focus of FM Risk Management is to develop and to maintain an efficient and robust risk management framework for treasury, portfolio management and financial markets activities, in strict compliance with the risk appetite and the business strategy of Belfius Bank.

#### II.4.2.3.3. Strategic Risk Management

The Strategic Risk Management team enhances the strategic dimension of risk management, increases consistency within the group and ensures a relevant and consistent risk approach.

Strategic Risk Management includes a.o. the "Rate & Liquidity" team (Risk -ALM), exercising the second line of defence on the ALM function.

#### II.4.2.3.4. Validation

The primary task of Validation is to independently ensure quality, reliability, proper functioning and adequate use of the models developed by Belfius Bank as well as their compliance with regulatory requirements during their entire life cycle. Validation also plays an important role in the assessments/communication of the strengths and weaknesses of models to help all stakeholders to improve their use and understanding.

#### II.4.2.3.5. Risk Services

The Risk Services division is responsible for the calculation, analysis and reporting of risk figures consistent with Finance in view of both internal and external communications.

The Risk Services ensures a lean and efficient Risk Management including the centralisation of IT & projects and the production of standardized reporting (regulatory...).

The Risk Services team acts on behalf of Bank and Insurance entities.

#### II.4.2.3.6. Non-Financial Risk

The Non-Financial Risks department acts as the 2<sup>nd</sup> line of defence for the main non-financial risks and acts as a corporate crisis, BCP manager within Belfius. The division includes a Transversal NFR team, the DPO (Data Privacy Officer) as well as the CISO (Chief Information Security Officer). The Non-Financial Risks team acts on behalf of Bank and Insurance entities.

#### II. 4.2.3.7. Compliance

The Compliance department acts as the 2<sup>nd</sup> line of defence for the management of the Compliance Risks, as defined in the 2012 circular of the BNB and FSMA. The department consists of a team of Compliance Business Advisors, a Compliance Risk Monitoring teams, as well as an Anti-Money Laundering team.

#### II.4.2.4. At Belfius Insurance level

More information regarding the risk organisation of Belfius Insurance can be found in the Annual Report of Belfius Insurance, chapter Risk management.

## II.5. Belfius Risk Cartography

The RICAP (Risk Identification and Cartography Assessment Process) was implemented in 2011. The RICAP consists of a series of meetings with key business representatives to ensure all risks are identified.



The following table illustrates the risk identification process within Belfius. It represents the risk cartography of Belfius at 31 December 2020, which aims at screening all risks to ensure they are identified, quantified and monitored.

All risk types are classified as Financial, Non-Financial or Conglomerate risks (further segmented into financial or non-financial risk types).

Financial risks are capitalised with the exception of Liquidity Risk for which no capital is set aside as Belfius perceives that capital is not the adequate answer to cover this risk. It is actively monitored and managed through gap limits and stress tests.

Most of Non-financial risks are not capitalized but will generally be contained by adequate procedures and monitored through appropriate processes.

Business Risk, even if not covered by capital will be considered through Earnings at Risk and Stress Testing framework.

Conglomerate risks can be further broken down into financial and non-financial risks.

Credit risk, market risk and operational risk are subject to the Pillar 1 framework and are also included in the Pillar 2 framework.

The Pillar 1 and Pillar 2 approaches to the same risks might differ at four levels:

- the perimeter;
- the methodology;
- the risk parameters used;
- the level of severity.

The perimeter of Pillar 2 risks is larger as Pillar 2 aims for exhaustiveness. Other risks than those included in the Pillar 1 framework are then specifically included in the Belfius Pillar 2 framework i.e. settlement risk, residual/recovery risk, interest rate risk (Structural Market and ALM Risk), currency risk (Structural Market and ALM Risk), funding risk (Structural Market and ALM Risk), liquidity risk, behavioural risk, insurance specific risks, pension plan risk, business risk, strategic risk, execution risk, compliance risk, reputation risk, external risk and legal risk.

Methodologies and risk parameters used by Belfius lead to the calculation of economic capital. It is defined as the potential deviation of the Group's economic value from its expected economic value at a determined interval of confidence and time horizon. The choice made by Belfius is to

		Pillar 1	Pillar 2	Covered by Capital	
Financial Risks	Credit Risk	Solvency Risk	■	■	Yes
		Country Risk	■	■	Yes
		Counterparty Credit Risk	■	■	Yes
		Residual/Recovery Risk		■	Yes
		Settlement Risk		■	Yes
	Structural Market and ALM Risk	Interest Rate Risk		■	Yes
		Price Risk <sup>(1)</sup>	■	■	Yes
		Currency Risk		■	Yes
		Spread Risk		■	Yes
		Liquidity Risk		■	No
		Funding Risk		■	Yes
	Trading Market Risk	Interest Rate Risk	■	■	Yes
		Spread Risk	■	■	Yes
		Price Risk	■	■	Yes
		Currency Risk	■	■	Yes
		Liquidity Risk		■	No
		Other Market Risks <sup>(2)</sup>		■	Yes
Other Risks	Insurance Specific Risks (incl. Life, Non-Life and Health)		■	Yes	
	Behavioural Risk (incl. Prepayment Risk)		■	Yes	
	Pension Plan Risk		■	Yes	
	Model Risk <sup>(3)</sup>	■	■	Yes	
Operational Risk	Operational Risk	■	■	Yes	
	Business Risk		■	No	
Non Financial Risks	Other Risks	Strategic Risk		■	No
		Execution Risk		■	No
		Reputation Risk		■	No
		External Risk		■	No
		Compliance Risk		■	No
		Legal Risk		■	No
		Conglomerate risks	Conglomerate Risk		■

(1) price risk includes risk on Equity exposure and Property exposure in the Banking Book.

(2) including volatility / correlation, carbon and commodities risks.

(3) consisting of Additional Value Adjustments (AVA) considered for Market and Credit Risks.

estimate its risks at a severity level of 99.94% on a 1-year horizon) instead of, respectively 99.9% and 1-year for Credit and Operational risks and 99% and 10-day for Market Risk as required by the Pillar 1 requirements.

Several risks such as business, reputation, strategic, liquidity, compliance, execution, conglomerate, external and legal risks are part of the Pillar 2 but are not capitalised, either because they are considered as non-material (currency risk) or because they are managed through appropriate processes.

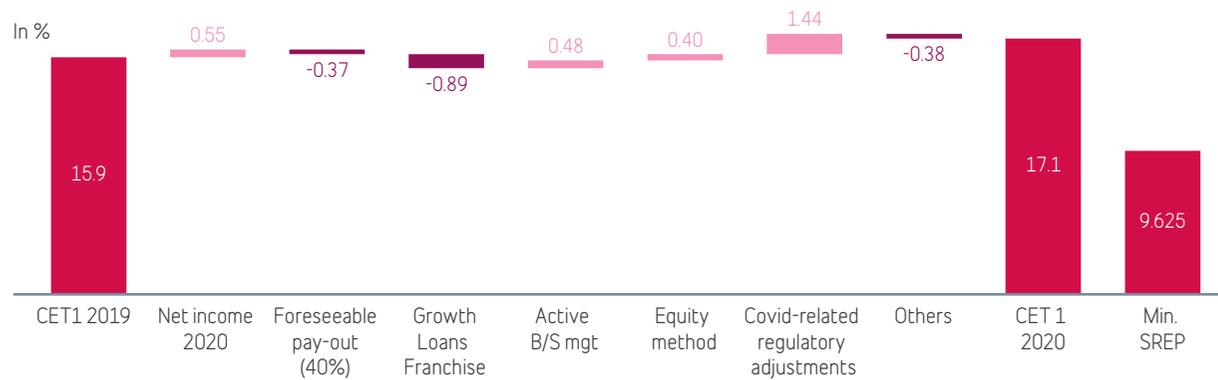


# III. Equity & Capital adequacy

A strong CET1 ratio is enabling Belfius to continue to support the Belgian economy and to execute its commercial strategy

## CET 1: FROM 15.9% IN 2019 TO 17.1% END 2020

This solid capital base compares comfortably with Belfius' minimum SREP level and internally defined minimum operational zone



## MREL

MREL compliant as of Dec 2020

EUR bn





# III.1. Equity

## III.1.1. Prudential supervision

### III.1.1.1 Minimum Requirement

Belfius Bank reports on its solvency position on consolidated level and on statutory level in line with CRR/CRD IV regulations:

- the minimum capital requirements (“Pillar 1 requirements”) as defined by Article 92 of Regulation (EU) No 575/2013 (CRR);
- the capital requirements that are imposed by the decision following the SREP pursuant to Article 16(2)(a) of Regulation (EU) No 1024/2013 and which go beyond the Pillar 1 requirements (“Pillar 2 requirements”);
- the combined buffer requirement as defined in Article 128(6) of Directive 2013/36/EU (CRD IV).

As a result of the annual “Supervisory Review and Evaluation Process” (SREP) finalised by the ECB at the end of 2019, Belfius must comply for 2020 with a minimum CET 1-ratio of 10.57% (including the countercyclical capital buffer), composed of:

- a Pillar 1 minimum of 4.5%;
- a Pillar 2 Requirement (P2R) of 2%;
- a capital conservation buffer (CCB) of 2.5%;
- a buffer for (other) domestic systemically important institutions (O-SII buffer) of 1.5% (imposed by the National Bank of Belgium); and
- a countercyclical capital buffer (CCyB) of 0.07%.

Belfius has to respect the full combined buffer requirements (capital conservation buffer, countercyclical capital buffer, buffer for systemically important institutions and systemic risk buffer) and the Pillar 2 buffer requirements. Note that the ECB also notified Belfius of a Pillar 2 Guidance (P2G) of 1% CET 1 ratio for 2020, a recommended buffer to be held over the minimum requirements set out above.

On 11 March 2020, the Financial Policy Committee (FPC) of the Bank of England reduced the UK countercyclical buffer rate to 0% of bank’ exposures to UK borrowers with immediate effect, to support further the ability of banks to supply the credit needed to bridge a potentially challenging period due to the economic shock from Covid-19.

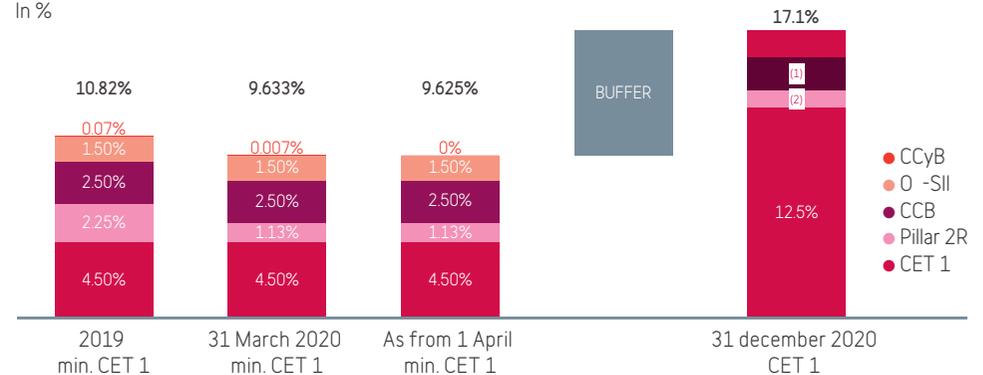
For similar reasons, and on the same day, the National Bank of Belgium decided to reduce the Belgian countercyclical buffer rate of banks’ exposures to Belgian borrowers, formerly set at 0.5% and announced on 28 June 2019 for implementation as from 1 July 2020, to 0% until further notice and on 18 March 2020, the French Comité de Stabilité Financière followed suit and set its countercyclical buffer at 0%.

Following these measures, the countercyclical capital buffer requirement for Belfius is now below 0.5bp, relating to Belfius’ very limited exposures under the countercyclical buffer requirements of Luxembourg, Hong Kong, Slovakia, Norway, Bulgaria and the Czech Republic.

Further details on the countercyclical buffer are provided in the Risk report annex (Table CCyB1).



**Belfius’minimum CET 1 requirements vs. Belfius’ 2020 CET 1 capital position and target**  
In %



(1) target zone in normal times : 15.0% - 15.5%

(2) minimum operational zone during the Covid-19 crisis : 12.5% - 13.5%

Due to ECB measures, notified to Belfius on 8 April 2020, banks are able to use capital instruments that do not qualify as Common Equity Tier 1 (such as Additional Tier 1 or Tier 2 instruments) to partially meet Pillar 2 Requirements (P2R - Article 104-a of CRD IV). As a result, the P2R total capital buffer of 2% can be split into 1,125% to meet with CET 1 instruments, 0,375% to meet with Additional Tier 1 instruments and 0.5% to meet with Tier 2 instruments.



Since 2Q 2020, Belfius has therefore had to comply with a minimum CET 1-ratio of 9.625%, which is composed of:

- a Pillar 1 minimum of 4.5%;
- a Pillar 2 Requirement (P2R) of 1.125%;
- a capital conservation buffer (CCB) of 2.5%;
- a O-SII buffer of 1.5%; and
- a total countercyclical capital buffer of 0%.

The ECB has also confirmed the Pillar 2 Guidance (P2G) for Belfius of 1% CET 1-ratio for 2020, setting the minimum requirement at 10.625%.

At the end of 2020, the ECB informed Belfius that the ECB is not issuing a SREP decision for the 2020 SREP cycle and that the previous '2019 SREP Decision' from the end of 2019 and its amendments remains into force. As a result, Belfius must comply for 2021 with an unchanged minimum CET 1 ratio of 9.625%.

The consolidated CET 1 ratio of Belfius at the end of 2020 stood at 17.11%, well above the 2020 applicable CET 1 capital requirement mentioned above.

Further to these regulatory requirements, Belfius stated in its Risk Appetite Framework that, in normal market circumstances and under stable regulations, it would strive to respect a minimum operational CET 1 ratio of 13.5%, on solo and consolidated levels – this was, evidently, defined before the Covid-19 pandemic.

Even during the Covid-19 pandemic, Belfius continued its support for the Belfius economy, in line with the request of the regulators. As a result, a temporary exemption was decided upon by the Board of Directors in H1 2020, to reduce the minimum operational CET 1 ratio to a range of 12.5% - 13.5% to cover any credit risk deterioration and loss provisioning and/or absorption purposes only. The former minimum operational CET 1 ratio level of 13.5% will be restored once the economical and financial context has normalised again.

### III.1.1.2 Applied methodology

The regulator authorised Belfius to apply Article 49 of the CRR and to monitor and report solvency within the prudential scope, where Belfius Insurance is accounted for.

Following the amendments of CRR article 473a in 2020, Belfius requested and was granted by the ECB the application of transitional measures for the first time adoption impact and all subsequent impacts of IFRS 9 on the expected credit loss model from 31 December 2020.

As a result, the solvency metrics of 2020 are referenced as “transitional” for both the CET 1 capital and the risk exposure amounts.

For a detail of the other CRR 2 Covid-19-related regulatory relaxations and their impact on the CET 1 capital and the risk exposure amounts, please see Section III.3.

In addition to the CRR/CRD IV regulations, Belfius is considered as a financial conglomerate with significant banking and insurance activities and is required to comply with the Financial Conglomerate Directive (FICO 2002/87/EC). For this purpose, specific reporting requirements with financial statements, regulatory capital, risk concentration and leverage ratio are sent to the regulator. These calculations and reports are made on the consolidated position of the bank and insurance group.

At the end of 2020, Belfius complied with all requirements requested from a financial conglomerate point of view.

## III.1.2. Regulatory own funds

CET 1 capital amounted to EUR 10,150 million, compared with EUR 8,941 million at the end of 2019. The increase in CET 1 capital of EUR 1,209 million resulted mainly from:

- the inclusion of the net consolidated result of EUR 532 million;
- the inclusion of the equity reserves of the Belfius Insurance group of EUR 146 million;
- the impact of the add-back of IFRS 9 provisions thanks to the transitional arrangements stated in the CRR of EUR 413 million;
- the increase of the “gains and losses not recognised in the statement of income” for EUR 281 million;
- the decreased deduction for software and other intangible assets of EUR 79 million resulting from the Covid-19-related relaxations provided by the ECB, partially offset by;
- the correction for a probable dividend of EUR 210 million (based on a 40% pay-out ratio); and
- a decrease of the remeasurement of pension plans of EUR 21 million.



Please note that following the Covid-19 pandemic, the Board of Directors decided not to pay out any dividend on the result of 2019 (beyond the interim dividend of EUR 100 million already paid in August 2019), in line with the recommendation of the ECB. Regarding the dividend distribution on the result of 2020, the Board of Directors decided, in line with the ECB restrictions on the dividend distribution (ECB/2020/62 of 15 December 2020), to propose an ordinary dividend on the 2020 result of 77 million EUR, corresponding to the lower of (a) a pay-out ratio of 15% on the 2020 adjusted net profit and (b) 0.20% of the 2020 year-end CET 1 ratio.

However, for prudential purposes, a deduction of the probable dividend of EUR 210 million had to be made in 2020, determined based on the pay-out ratio as defined by the dividend and capital policy:

- a calculation of the probable dividend for ordinary shares based on a pay-out ratio of 40% multiplied by the 2020 consolidated net result reduced by the full year 2020 coupon cost after tax (treated for accounting purposes as dividend) on the AT1 instrument, rounded by the million; and
- the remaining AT1 instrument coupon cost after tax (treated for accounting purposes as dividend) since the last coupon date, which has not yet been paid out to AT1 holders (i.e. EUR 2.9 million, which for accounting purposes has not yet deducted from equity, for the period between 16 October and 31 December 2020).

The transitional measures regarding the first time adoption impact and all subsequent impacts of IFRS 9 on expected credit losses (Covid-19-related relaxation) amounted to EUR 413 million. As of 31 December 2020, Belfius is allowed to apply transitional measures to add back to its prudential CET 1 capital a portion of the increase of IFRS 9 expected credit loss provisions for the static component (relating to the FTA IFRS 9 on 1 January 2018) and the dynamic components (from 1 January 2018 until 31 December 2020), with the adjusted phasing-in timetable. These transitional measures will be applied until 31 December 2023, unless Belfius requests and is granted an exemption.

The increase in “gains and losses not recognised in the statement of income” of EUR 260 million stemmed from the increase in the revaluation of the portfolios of debt and equity instruments of EUR 281 million, mainly of the Belfius Insurance group, partially offset by declining stock markets following the Covid-19 pandemic and a decrease in the remeasurement of defined benefit plans of EUR 21 million due to the effect of a reduction in the discount rate, partially offset by the positive return on plan assets.

The deductions and prudential filters decreased by EUR 77 million, mainly following a decrease in the deduction of software and other intangible assets of EUR 79 million due to a Covid-19-related relaxation, offset by an increased deduction for regulatory additional valuation adjustments of EUR 3 million due to market movements, partially offset by temporary mitigation. The deductions for the goodwill for Belfius Insurance and for the irrevocable payment commitment (IPC) with regard to resolution funds remain stable.

Note that the significant and non-significant investments in own funds instruments of financial entities and the stock of temporary differences in the not recognized deferred tax assets remain below the thresholds for deduction of the regulatory own funds and are included in the credit risk exposure amount.

Tier 1 capital amounted to EUR 10,647 million, compared with EUR 9,438 million at the end of 2019 as it includes the additional Tier 1 issue of EUR 500 million (nominal value) dated February 2018.

Tier 2 capital increased to EUR 1,433 million compared with EUR 1,391 million at the end of 2019. The increase of EUR 42 million was mainly related to the integration of credit risk adjustments determined by a standardised approach (EUR 73 million), partially offset by the decrease of EUR 31 million of the useful prudential value of subordinated Tier 2 instruments. At the end of 2020, total regulatory own funds amounted to EUR 12,080 million, compared with EUR 10,830 million at the end of 2019.

The composition of capital is detailed further in the Risk report annex (Table CC1). 

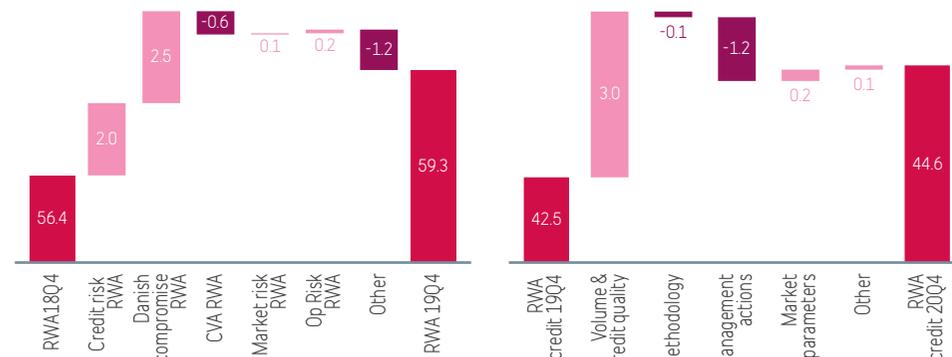
For more information on regulatory own funds on a consolidated level, please refer to the capital management section of the Annual Report.



## III.2. Capital requirements by type of risk

Total Risk Weighted Assets (RWA) includes risk-weighted exposures for credit risk including counterparty credit risk, CVA risk, market risk and operational risk. Each of the underlying risks is detailed elsewhere on in this report (section IV, V & VII). The risk exposure amount also stems from the Danish Compromise, whereby the capital instruments issued by Belfius Insurance and held by Belfius Bank are included in the RWA via a weighting of 370%.

RWA evolution by type of risk



Drivers RWA credit



At the end of 2020, Belfius RWA amounted to EUR 59,309 million, an increase of EUR 2,911 million compared with EUR 56,398 million at the end of 2019.

The credit risk exposure amount including counterparty credit risk increased by EUR 2,017 million to EUR 44,559 million due to:

- volume and credit quality (EUR +3 billion);  
new loan production remained strong during the period, mainly in the business banking and corporate segments. The Covid-19 crisis has not yet significantly materialised at a bank level;
- methodological changes and regulatory measures (EUR -0.1 billion);
- since Q1 2020, Belfius is subject to a regulatory add-on due to the new definition of default, which was, however, offset by the Covid-19-related regulatory measures: extension of the SME supporting factor, IFRS 9 transitional measures and new treatment of software assets;
- management actions (EUR -1,15 billion), with the sale of Italian bonds being the main driver;
- market parameters (EUR +0.2 billion).

The RWA for the Danish Compromise increased by EUR 2,522 million to EUR 9,391 million, due mainly to the change in the valuation method used for the participation in Belfius Insurance.

The CVA RWA decreased with EUR 642 million due to active management of counterparty credit risk including additional CVA hedges, the unwinding of uncollateralised swaps with financial counterparts and an increased use of CCP clearing.

The market RWA increased by EUR 59 million as a result of market evolutions.

Operational RWA slightly increased (EUR +105 million) over the period, in line with the increase in income.

In total, regulatory measures had an impact of EUR -0.5 billion, while management actions contributed to reducing the RWA by EUR 1.8 billion.

In anticipation of a more stringent regulatory framework applicable from 2020 onwards, Belfius had included in its 2019 Q4 solvency requirements an additional Risk exposure amount of 1,150 million. Due to the Covid-19 crisis, this anticipation has been removed. As of the end of 2020, Belfius cancelled these additional regulatory RWA as there was assessed to be - for the time being - not appropriate during the Covid-19 crisis.

Further details are provided in the Risk report annex (Tables OV1, INS1, MR1, MR2-A, MR3, CCR2).





### III.3. Application of Covid-19-related regulatory adjustments

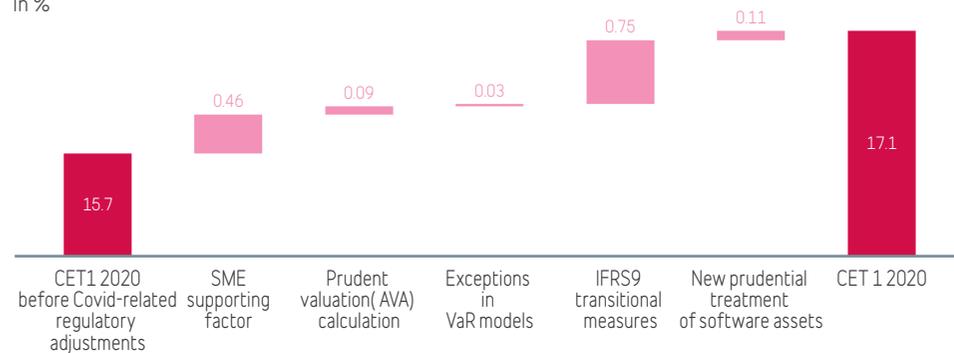
The severe economic shock caused by the Covid-19 pandemic and the exceptional containment measures have had a far-reaching impact on the economy. The extraordinary circumstances of the Covid-19 pandemic and the unprecedented magnitude of challenges triggered calls for immediate action to ensure that institutions were able to channel funds to businesses and households effectively and to mitigate the economic shock caused by the Covid-19 pandemic. As a result, the ECB took several measures to ensure that the financial system would be able to continue giving support to the economy. This was performed through an adaptation of the transitional measures for the impacts of IFRS 9 on expected credit losses and the possibility to apply some of the final elements of the Basel III framework early (CRR 2 / CRD 5).

For Belfius, the following Covid-19-related relaxations were applied, with impacts identified on the solvency ratios in the prudential consolidation perimeter:

- the accelerated application date for the revised supporting factor for SME loans;
- temporary relaxation rules for the Prudent Valuation (AVA) calculation;
- the exceptions for Covid-19-related overshooting in the market risk VaR models;
- the transitional measures for IFRS 9 provisions;
- the accelerated application date for a more favourable prudential treatment of some software assets.

#### Covid - related regulatory measures : +1.44 %

In %



### III.4. Capital adequacy

#### III.4.1. Belfius Bank

##### III.4.1.1. Solvency ratios for Belfius Bank on consolidated level

At the end of 2020, CET 1 capital ratio amounted to 17.11%, an increase of 126 bps compared with the end of 2019. Note that this transitional CET 1 ratio takes into account the transitional IFRS 9 measures and the other positive effects of the Covid-19-related regulatory adjustments, estimated at 144 bps.

The increase in CET 1 ratio is the result of positive effects from higher CET 1 capital (+214 bps) offset by the negative effects from the higher total risk exposure (-88 bps). We refer to the comments above for further information.

At the end of 2020, Tier 1 capital ratio amounted to 17.95%, an increase of 121 bps compared with the end of 2019.

The total capital ratio amounted to 20.37%, an increase of 117 bps compared with the end of 2019.

Note that without the application of the IFRS 9 transitional measures, the fully loaded CET 1-ratio would decrease by 75 bps, the Tier 1 capital ratio would decrease by 76 bps and the Total Capital ratio would decrease by 77 bps.

Further details are provided in the Risk report annex (Table IFRS9).

Applying the “Danish compromise” compared with the deduction method for capital instruments of Belfius Insurance (equity deducted from CET 1 capital and subordinated debt instruments deducted from Tier 2 capital) had the following impacts: using the deduction method would result in an increase of 31 bps of the transitional CET 1 ratio and a decrease of 32 bps on the transitional Total Capital ratio.

##### III.4.1.2. Leverage ratios on consolidated level

In December 2010, the Basel Committee on Banking Supervision (BCBS) published guidelines for calculating the leverage ratio as a non-risk based ratio, which primarily aims to restrict the size of the bank’s balance sheets and consequently the use of excessive leverage.



The leverage requirement became a binding requirement with CRR 2, published in the EU Official Journal on 7 June 2019 and will be applicable from June 2021. The CRR 2 integrates the leverage ratio in the Pillar I requirement and sets the level of minimum requirement at 3%, a surcharge for banks considered as G-SIB or O-SIB has also been introduced, the EBA has fixed this surcharge for G-SIB and has a mandate to analyse whether some O-SIB (like Belfius) should be given the same or similar additional buffer requirement.

The leverage ratio is defined as the Tier 1 capital (the numerator) divided by the exposure measure (the denominator), computed as balance sheet assets after certain restatements on derivatives, securities financing transactions, off-balance-sheet items and prudential adjustments (for items already deducted from the numerator).

In order to be consistent with the calculation of the regulatory Tier 1 capital (numerator), the calculation of the leverage exposure (denominator) is based on the prudential consolidation perimeter, where Belfius Insurance is accounted for using the equity method.

Furthermore, the application of transitional measures for IFRS 9 provisions from December 2020 and the Covid-19-related regulatory measure to temporarily exclude certain exposures to central banks from June 2020 have an impact on the denominator.

The risk of excessive leverage is managed through the Financial Plan process. The leverage ratio as defined in the CRR is further an integrated part of the Risk appetite framework for which internal limits and targets are set which is validated by the Board of Directors.

The risk of excessive leverage is included in the Belfius reporting and control processes and is monitored regularly. Any important deviation and/or prudential changes in the leverage ratio is reported to the appropriate committees for management actions.

At the end of 2020, the Belfius transitional leverage ratio stood at 6.85%, an increase of 91 bps compared with the end of 2019 and well above the minimum pillar 1 requirement of 3%, applicable from June 2021 onwards.

The increase is the result of positive effects (+76 bps) from the higher level of Tier 1 capital (see above) and positive effects (+15 bps) from the decreased total leverage exposure measure, mainly from higher volumes of loans to customers and an increase in securities financing transactions exposures due to increased off balance commitments, offset by the temporary Covid-19-related prudential adjustment allowing banks to partially exclude certain Central Bank exposures

Without the temporary partial exclusion of certain Central Bank exposures the transitional leverage ratio decreased by 96 bps.

Please note that the fully phased-in leverage ratio, excluding the transitional measures for IFRS 9 provisions, but including the temporary partial exclusion of certain Central Bank exposures, decreased by 25 bps

Further details are provided in the Risk report annex (Tables LRSum LRSpl LRCCom).

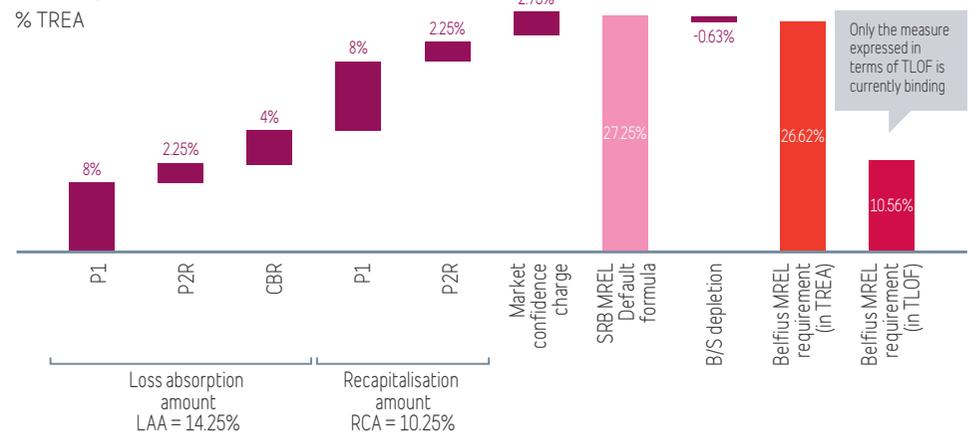


### III.4.1.3. Minimum requirement for own funds and eligible liabilities

On 17 April 2019, the National Bank of Belgium (NBB) notified Belfius Bank of the MREL requirement imposed by the Single Resolution Board (SRB), setting the consolidated MREL requirement for Belfius Group at 10.56% of Total Liabilities and Own Funds (TLOF), to be met at all times.

Based upon data as of 31 December 2020 and according to the current Banking Recovery and Resolution Directive (BRRD), Belfius is fully compliant with an eligible own funds and liabilities for MREL purpose standing at EUR 19.8 billion, in excess of the MREL requirements of EUR 16.1 billion.

#### SRB requirement





On 28 January 2021, the NBB notified Belfius that going forward it is to execute the SRB MREL instruction regarding the minimum requirement for equity and eligible liabilities at the consolidated level of Belfius Bank under BRRD2. For Belfius Bank, the MREL requirement on a consolidated basis is set at 22.87% of Total Risk Exposure Amounts (TREA) and 6.84% of Leverage Risk Exposures (LRE). Belfius Bank must meet the target no later than 1 January 2024 and must provide for a linear build-up of equity and eligible liabilities towards the requirement. The SRB has also determined an interim target of 22.37% of TREA and 6.84% of LRE, which must be met by 1 January 2022. The SRB MREL instruction also provides for a subordination requirement: Belfius Bank must meet at least 15.25% of TREA and 6.84% of LRE by means of subordinated MREL. Own funds used to meet the combined buffer requirement (CBR) set out in Directive 2013/36/EU (at 4% of TREA for Belfius currently) are not eligible to meet the requirements expressed in TREA. Belfius Bank must comply with this subordination requirement by 1 January 2024 at the latest, taking into account an intermediate target level of 15.25% TREA and 6.84% LRE that must be met by 1 January 2022.

With the annual review of MREL requirements by SRB, Belfius currently estimates that its MREL subordination requirement could be lowered from 2023 onwards, to 13.5% of TREA (or 17.5% of TREA including current CBR requirement), based on a forward-looking assessment of the formula applied by SRB.

It should be noted that Belfius is to be impacted by a change in MREL eligibility, from 1 January 2021 onwards, whereby “liabilities should be directly issued and should not be owned by an undertaking in which the institution has a participation of more than 20%”. As a consequence, the liabilities issued by Belfius Financing Company (Belfius’ Luxembourg-based issuance vehicle for CP and Retail Bonds) cease to be MREL-eligible and are to be excluded. Applying this exclusion pro forma as of the end of 2020, Belfius MREL would be EUR 2.2 bn lower (down from EUR 19.8 bn to EUR 17.6 bn).

Despite such an exclusion, Belfius already met its expected BRRD2 MREL requirements by the end of 2020. Indeed, expressed in TREA, Belfius MREL of EUR 17.6 billion amounted 29.67% (including a CBR of 4%), or 25.67%. This is to be compared with 22.87% of the 2024 final binding target. In the same way, Belfius MREL subordination of EUR 14.4 billion amounted to 24.28% (including a CBR of 4%), or 20.28% to be compared with EUR 15.25% of the binding target. Expressed in LRE, Belfius MREL subordination of 9.27% stood in excess of 6.84% MREL requirement.

## III.4.2. Belfius Insurance

### III.4.2.1. Prudential supervision

Belfius Insurance reports to its regulator, the NBB. Amongst others, a quarterly report concerning its solvency margin and liquidity is required, both at a consolidated and at a statutory level.

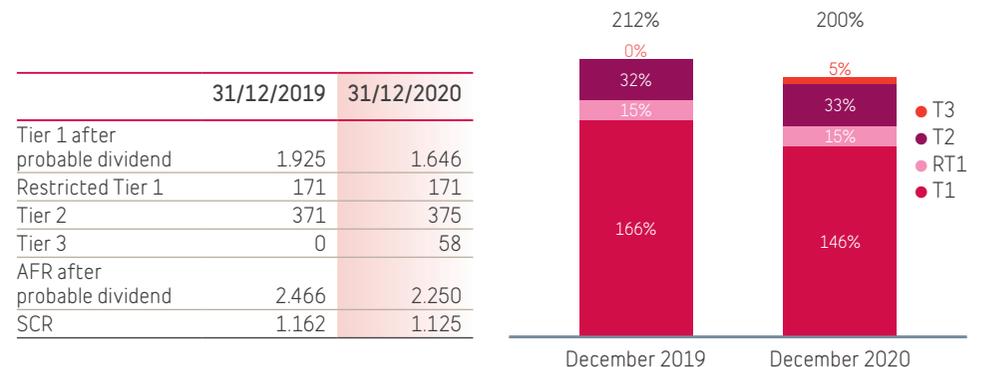
As part of prudential supervision over systemic insurers, highly detailed information is also provided to the NBB about the company’s strategy, its ALM policy and the sufficiency of its technical provisions.

### III.4.2.2. Regulatory own funds

The risks that Belfius Insurance faces are reflected in the “Solvency II requirements” which are applicable to all EU-Member States. The own funds of Belfius Insurance available to cover the requirements are determined according to the valuation and eligibility principles defined in the Solvency II regulation, Directive 2009/38/EU.

The regulatory own funds of Belfius Insurance amounted to EUR 2,390 million at the end of December 2020. These were composed 82% of the highest quality capital Tier 1. Tier 2 capital was EUR 375 million and consisted mainly of two subordinated loans granted by Belfius Bank, while the Tier 3 capital relates to a deferred tax asset of EUR 58 million

### Available Financial Resources and Solvency Capital requirement





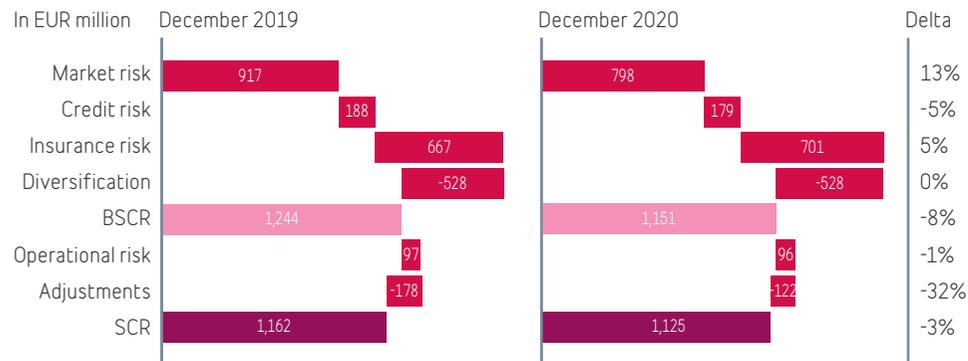
Compared with December 2019, the regulatory own funds of Belfius Insurance decreased by EUR 216 million. This development is due mainly to the provision of a probable dividend of EUR 140 million. The continuous decline of the interest rates led to an increasing Best Estimate of Technical Provisions and was not fully offset by the increasing market value of the investments. In addition, deferred tax assets were defined as a component of regulatory own funds.

### III.4.2.3. Solvency requirement

The Solvency II Capital Requirement (SCR) is calculated based on the consolidated asset and liability portfolio of Belfius Insurance, Corona and those investment entities that are fully consolidated for Solvency II purposes.

The SCR for Belfius Insurance is determined using the “Standard Formula” as defined in the Solvency II regulation, taking into account a volatility adjustment and making use of the transitional measure for equities. In its SCR, Belfius Insurance has to apply the restriction on the use of Loss Absorbing Capacity of Deferred Taxes as prescribed by the NBB.

#### Decomposition of Solvency Capital Requirement



Loss absorbing capacity of technical provisions and deferred taxes

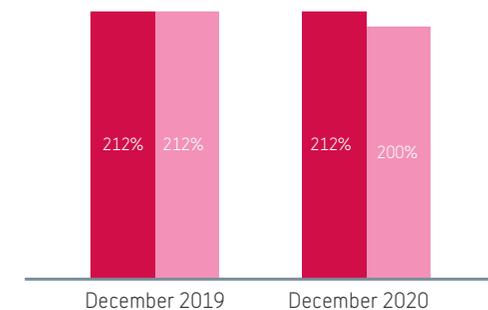
Belfius Insurance’s SCR amounted to EUR 1,125 million at the end of December 2020, a decrease of EUR 37 million compared with the end of 2019.

The decrease is the result of management actions particularly on the equities portfolio and ALM management and some refinements on models and assumptions including regulatory changes.

Market Risk is still the main contributor to the SCR due to the spread risk and equity risk, followed by underwriting risks. The SCR linked to the interest rate risk is limited thanks to Belfius Insurance’s ALM policy of strictly limiting the gap between the duration of assets and liabilities on the balance sheet of Belfius Insurance.

### III.4.2.4. Solvency ratios at Belfius Insurance

The Solvency II ratio (before dividend) of Belfius Insurance stood at 212% at the end of December 2020, similar to the ratio in December 2019 (without dividend). The decrease in regulatory own funds – without the probable dividend of EUR 140 million – was fully offset by a similar proportional decrease in SCR. Including the probable dividend, the Solvency II ratio was 200%.



However, given the current level of uncertainty on the depth, magnitude and duration of the impacts of Covid-19, the Board of Directors of Belfius Insurance proposed to the General Assembly to restrict the dividend over FY 2020 to EUR 35 million and to maintain the remaining profit to be allocated in retained earnings pending the further analysis of all impacts of the Covid-19 crisis. The dividend pay-out following the contractual profit allocation of EUR 4.6 million has been provided for.

Further to the minimum regulatory requirements of 100%, Belfius Insurance has, in current market circumstances and under current regulations, defined a minimum operational Solvency II ratio of 160% both on a solo and on a consolidated level.

In addition to the establishment of a complete risk framework, the Solvency II regulations also require a self-assessment in which, taking the business plan into account, the future capital buffers are estimated, and a number of sensitivity analyses are performed. In these analyses Belfius Insurance still has the appropriate capital margins required to absorb shocks, as stated in the Risk Appetite Framework approved by the Board of Directors.



A 50 bps fall in the level of interest (compared with the level at the end of 2020) would have an impact of -6 pp on the Solvency II ratio. A stock market shock of -30% on share prices would have an impact of -9 pp, while a drop in the real estate portfolio of 15% would decrease the solvency ratio by -9 pp. A 50 bps rise in the credit spreads across the whole bond and credit portfolio would result in a drop of -31 pp and the elimination of the Volatility Adjustment in the calculation of the Best Estimate of liabilities would result in an impact of -9 pp. The reduction of the Ultimate Forward rate (UFR) from the current level of 3.75% to a level of, for instance, 3% would decrease the solvency ratio by -10 pp.

### III.4.3. Internal capital adequacy

#### III.4.3.1. Risk appetite

Risk appetite is the level of risk that an institution is prepared to take given the expectations of the main stakeholders (shareholders, creditors, regulators, rating agencies, customers, employees...), in order to ensure the safeguard of a sound risk and financial profile in the context of the strategy 2020-2025. This risk appetite is defined by the Board of Directors, on proposals from the Management Board. The Risk Department prepares the Management Board's proposals and the Board of Directors' decisions, and also sets the rules and the framework for implementation of those rules.

Based on a holistic approach, risk appetite is a central reference point:

- for guiding strategy and planning;
- for framing performance in terms of growth and value creation;
- for facilitating day-to-day operating and commercial decisions.

The Bank's risk appetite consists of a series of quantitative elements (target Key Risk Indicators or KRI's) and qualitative elements (statements) that are designed to express the risk levels and types that are not acceptable, that are tolerated and targeted in order to achieve business strategy.

The quantitative framework is based on a mix of accounting ratios (gearing), regulatory ratios (solvency, liquidity), economic ratios (economic capital, earnings at risk) and internal KRIs. The different metrics cover a wide range of risks (credit risks, solvency, liquidity, market risks, concentration risks, non-financial risks, compliance risks, model risks,...).

Limits have been defined on each of these ratios with different zones, which lead to different governance and measures in case of breach. They are reviewed and updated each year by the competent bodies. The Risk and Finance departments are responsible for monitoring these ratios and, if there are discrepancies, for proposing measures to the Management Board to ensure the limits are met.

Next to the quantitative part, qualitative statements consisting of guiding rules aiming to define the risk appetite that cannot be expressed through quantitative ratios are imbedded in the RAF.

The Risk Appetite Framework (RAF) has been updated and approved by the Board of Directors in December 2020. The updated RAF includes a broader coverage with new or updated quantitative ratios for Financial risks (MREL), Non-Financial risks, Compliance and Model Risks.

#### III.4.3.2. Economic Capital

##### III.4.3.2.1. Definition

Economic capital is defined as the potential deviation of Belfius' economic value from its expected economic value at a given confidence interval and time horizon. The confidence threshold (99.94%) chosen for scenarios involving losses in value corresponds to the Bank's targeted senior unsecured debt rating at a horizon of one year (A rating for 2020).

The economic capital quantification process is organised in three phases: identifying the risks (risk inventory definition and cartography, reviewed on an annual basis, in collaboration with the various business lines), assessing (measuring) the risks (mainly on the basis of statistical methods and/or scenarios) and aggregating the risks based on an inter-risks correlation matrix.

Most risks are capitalised based on measuring the unexpected loss. However, if alternative management techniques (limits, other buffers than capital, governance) are considered more appropriate to cover them, some risks are not capitalised.

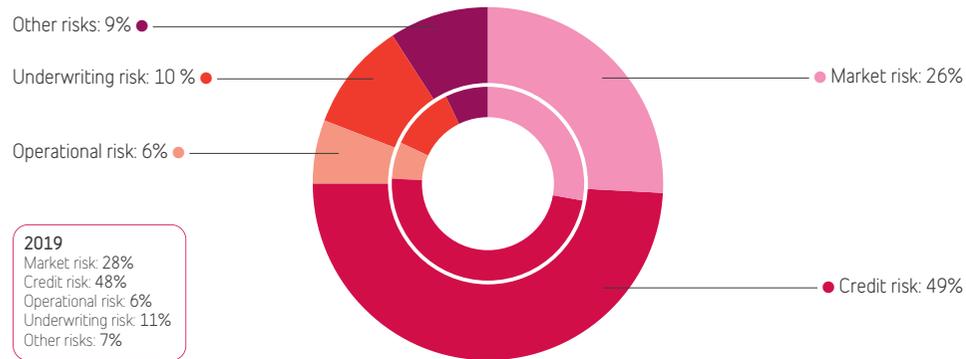
The economic capital is central in the context of Belfius' risk appetite and is also complementary to the Stress Tests framework for Internal Capital Adequacy Assessment Process (ICAAP) purposes.



### III.4.3.2.2. Economic Capital Adequacy

The Management Board, which also acts as the Risk Appetite Committee (RAC), is responsible for managing the capital level and allocation process and has authority in all matters relating to economic capital. The RAC analyses the various models involved in calculating the economic capital and monitors the (regulatory and economic) ratios, limits and triggers.

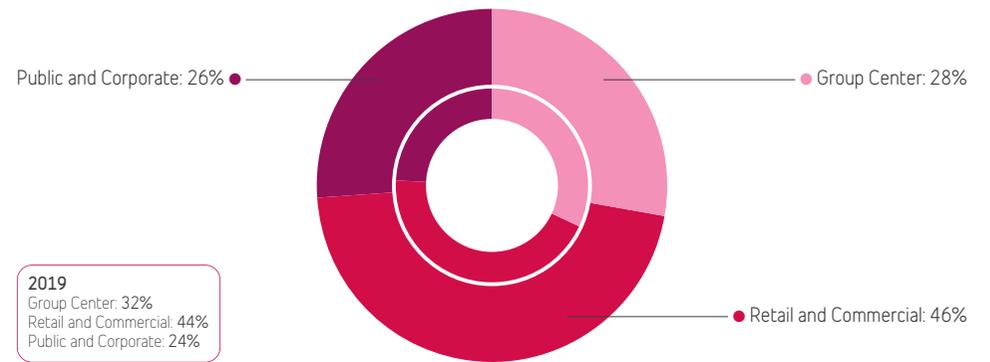
#### Breakdown of economic capital by type of risk (Outside 2020 - Inside 2019)



Belfius economic capital was EUR 5,579 million at the end of December 2020 (against EUR 5,486 million at the end of 2019).

Credit risk represented approximately 49% of the economic capital and was the main contributor; market risk (including interest rate risk, foreign-exchange rate risk, spread risk and equity risk) was 26%, underwriting risk 10%, operational risk 6% and other risks (prepayment, funding, etc.) 9%.

#### Breakdown of economic capital by business line (Outside 2020 - Inside 2019)



By business line, the economic capital was allocated as follows: Retail and Commercial and Public and Corporate represented 46% and 26% respectively of Belfius' economic capital; the balance was made up of 28% allocated to the Group Center (mainly for the Belfius' general balance sheet management in terms of interest and funding risks, including the bonds investment portfolios and for the portfolios of derivatives and run off credit guarantees).

### III.4.3.2.3. Stress Tests

Stress tests are part of the ICAAP and are designed to measure the Bank's sensitivity, in terms of losses, additional weighted risks, liquidity needs or equity capital requirements that could impact Belfius in scenarios featuring significant unexpected shocks on the financial markets and/or in the own financial situation of Belfius.

Belfius performed an internal stress testing programme with its financial Plan 2020-2025. The Bank developed a set of alternative and severe macroeconomic scenarios designed to anticipate different possible outcomes for the Covid-19 pandemic and to simulate how Belfius might be affected under these circumstances. These different stress tests measure the potential deviations from the "base case" Financial Plan and from the Risk Appetite targets set by the management in terms of solvency, liquidity and profitability. These stress tests were submitted to the Management Board as well as to the Board of Directors. Mitigating actions and recommendations were proposed for each of the stress tests.



#### III.4.3.2.4. Recovery plan

An update of Belfius Recovery Plan has been submitted to the ECB during the second half of 2020. According to regulator recommendations, Recovery plan stress scenarios were related to the Covid-19 pandemic. This plan provides a set of recovery measures that would be taken to restore the Bank's long-term viability in the event of a significant deterioration of the macro-economic environment.

#### III.4.3.2.5. Resolution

Resolution is defined as the restructuring of a bank within the Single Resolution Mechanism (SRM) issued by the Single Resolution Board (SRB) through the use of resolution tools. The objective of the SRB is therefore to ensure an orderly resolution of failing banks with minimum impact on the real economy and on public finances of the participating Member States and beyond.

Belfius, being considered as significant financial institution in Belgium, has to ensure that all necessary information will be provided to the SRB, responsible for preparing a resolution plan that would be available in case of a severe crisis leading to an hypothetical failure of the Bank.

Belfius resolution therefore consists of the application of identified resolution tool(s) to the Bank which best achieve resolution objectives.



# IV. Credit risk

2020 has been an unprecedented year associated with major uncertainties and multiple challenges with as main driver, the Covid-19 pandemic. In view of the nature of the crisis, and despite the widespread monetary and other public support measures, the increase in CoR has been an important driver of the P&L in 2020 (EUR 453 million). Ex-ante provisioning to absorb further default or expected rating downgrades in the coming years, make up a huge part of this CoR amount. Adjustments have been introduced to the IFRS 9 methodology to ensure sufficient forward-looking elements and to install a “through-the-cycle” IFRS 9 expected losses methodology to account for the sectorial and specific nature of the crisis and to avoid a cliff effect in the coming years. While Stage 1 and Stage 2 have presented the bulk of the CoR (EUR 331 million), Stage 3 remained relatively contained (EUR 122 million), although above the CoR 2019. Defaulted stock has increased, leading to an increase of the asset quality ratio to 2,02% (2019 : 1.96%).

Despite the strong deterioration of the economic environment, the quality of the loan production and the stock of credit exposures have remained globally stable in 2020.

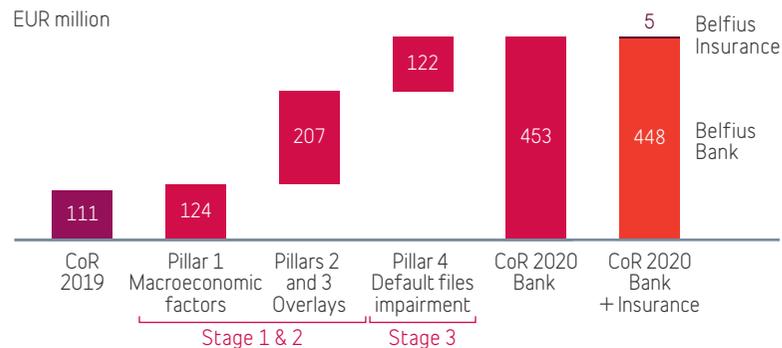
The credit risk chapters in the Risk Appetite Framework were reviewed in the light of the effects of the Covid-19 crisis.

In 2020, a fundamental redesign program of the IRBA models was started, with the first model reviews already delivered to the supervisors. This program will run further in 2021-2022.

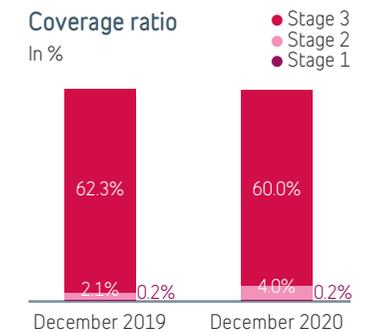
## DEFINITION

Credit risk is defined as, on the one hand, the possibility that a bank's borrower or counterparty will fail to meet its obligations (in the form of non-payment or non-performance) in accordance with the agreed terms, also called the payment default risk, and on the other hand, the possibility that the bank will not be able to recover its outstanding debt by means of the collateral that is linked to the debt, i.e. the risk of non-recovery.

## COR 2020 - P & L IMPACT



## ASSET QUALITY





## IV.1. Fundamentals of credit risk in 2020

The credit risk in the loan portfolio has been dominated in 2020 by the Covid-19 crisis and its significant economic impact. Due to lockdowns, social distancing, group and travel restrictions, businesses highly suffered from closure and lack of consumer confidence. Most sectors have known an important impact during the first lockdown but were able to recover without compensating the loss of revenues. Some sectors were/are still hit by a mandatory closure such as horeca, close contact professions, event and travel companies and would be severally hit without government intervention and financial concessions.

To mitigate the economic consequences of the Covid-19 pandemic, governance bodies installed different support measures for individuals, self-employed and businesses affected by the Covid-19 crisis.

Belfius responded to this unprecedented crisis by putting in place an end-to-end screening of the loan portfolio, consisting of:

- a bottom-up screening by the bankers to evaluate impact of and resilience to the crisis;
- an evaluation of the need to take risk mitigating actions or to apply a close monitoring;
- the granting of payment deferrals and state guaranteed loans;
- detection of vulnerable clients showing a significant increase of credit risk based on before mentioned criteria leading to classification into watchlist and/or forbearance and to higher and stressed ECL (expected credit losses);
- Covid-19 adjustment of the IFRS 9 Impairment methodology (see section IV.1.2.3.).

At the same time, Belfius strengthened its Credit Risk Framework in terms of:

- Governance: specific Covid-19 committees at regional and central levels with focus on screening, risk mitigating actions and reviews as well as a regular dedicated sessions of the Management Board to follow-up on the risk mitigating initiatives and impact on the Cost of Risk;
- Framework: a specific rating guidance has been developed to guide credit analysts to take into account on a level playing field the economic impact of Covid-19;
- Monitoring: development of a more detailed credit risk reporting and a bi-weekly dashboard, including on early warning signals integrating alternative data sourced from a transactional analysis of accounts.

Although regulatory credit risk exposures increased (see also Capital management chapter in this report), the full impact of the Covid-19 on the credit quality has not materialized so far in significant

downgrades impacting in a material way regulatory risk weights of our credit risk exposures. The impact on asset quality of Covid-19 is commented in section IV.1.5.

### IV.1.1. Measures in Covid-19 crisis to support the Belgian Society

Throughout the year, the economic shock caused by the Covid-19 pandemic and the exceptional and successive lockdown measures had a far-reaching impact on businesses and consumers. In particular, a material numbers of households have faced temporary or permanent unemployment and falling income, while enterprises have faced closures, disruptions in supply chains or productivity declines due to other sanitary measures and reduced demand, and some still are. Without support measures, all this could have resulted in significant (but mostly temporary) difficulties in repaying loan instalments or suppliers.

To help to mitigate these impacts, the Belgian federal government quickly installed an economic task force responsible for combating the economic consequences of the Covid-19 pandemic, which includes the Ministry of Finance, the NBB and Febelfin. The aim of the task force is to implement a program to support individuals, the self-employed and businesses affected by the Covid-19 crisis.

The program, that was put in place from March 2020, has two pillars:

#### Pillar 1: The Payment Holiday

This is applicable to loans to viable non-financial companies and self-employed people as well as to mortgage loans for individuals who are financially affected by the Covid-19 outbreak.

- For mortgage loans borrowers who suffered an income loss because of the Covid-19 crisis and who have limited financial resources, a moratorium was granted by the banks. Both the capital and the interest are deferred, so there is no repayment at all during the period of the moratorium for these borrowers. After this period, payments are restarted, including the interest due for the moratorium period. Only for "vulnerable" customers, i.e. customers who have a remaining Net Available Income<sup>(1)</sup> (less than EUR 1,700) there is no recovery of the interest due for the moratorium period.

(1) We use the following definitions for net monthly household income:

- For salaried workers: the monthly income in February 2020, including recurring incoming payments such as maintenance and rental income but not including child allowance payments and after the deduction of consumer loan and mortgage repayments for the primary residence.
- For self-employed: the monthly income before the coronavirus crisis (calculated as follows: income earned in 2019 divided by 12 months), including recurring income such as maintenance repayments and rental income but not including child allowance payments and after the deduction of consumer loan repayments, mortgage repayments for the primary residence and repayments for any business loans in your own name.



- A moratorium for non-financial companies and self-employed people is applicable for viable companies. During the moratorium period, companies must not make any repayments of principal amounts due. However, the interest payments remain due.
- In addition, a legal moratorium for consumer loans (i.e. a payment suspension) has been put in place from mid-May onwards and consists of a payment break for a maximum period of three months (postponement of resetting to zero for the credit lines) and renewable once the recovery of interest is due over the remaining term of the loan without NPV impact. In these cases, the request has to be initiated by the customer (no pro-activity from the banks) and the customer has to prove to have been financially affected by the Covid-19 crisis.

The deferral of payments for mortgages and non-financial companies has been in place since April 2020 and had initially been expected to last until 31 October 2020 for a maximum of six months. In a second phase, it was decided to extend the support measures until the end of 2020, but requiring a borrower request.

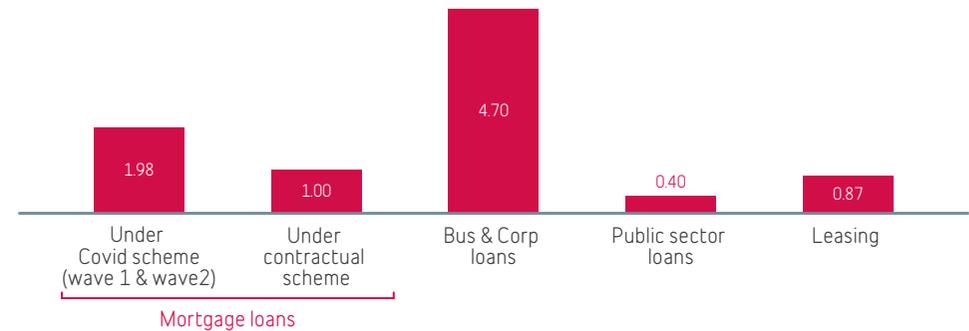
The EBA has clarified that only moratorium programs which fulfil the requirements of the General Payment Moratorium (for instance those under the Federal public moratorium) can benefit from flexible treatment. For instance, the EBA Guideline clarifies that the payment moratoria do not trigger classification as forbearance or distressed restructuring in case of legislative or non-legislative moratoria. However, the Guideline clearly highlights the need for adequate identification of situations where borrowers may face longer-term financial difficulties and requires to classify exposures in accordance with the existing regulations. To note that, in addition to these public moratoria, Belfius also executed some 'Belfius-specific' moratoria (which do not fall under the definition of General Payment Moratorium) to the customers of its leasing or factoring entities.

With the second partial lockdown starting at the end of October and running much longer than the first one, a second charter to extend the payment holiday scheme to 31 March 2021 was put in place for households as well as for non-financial companies and self-employed people.

Aside the public moratoria, Belfius granted also moratoria under contractual schemes

### Granted loans with payment deferrals during 2020

EUR bn



Recently an additional extension has been offered to non-financial companies and self-employed people until 30 June 2021. To offset the EBA requirement to limit the public payment holiday schemes to maximum 9 months, Belgian banks have combined the second charter with a third charter to continue to support self-employed people and financially sound companies who already enjoyed a public payment holiday for more than 9 months, without the banks benefiting of the flexible forbearance treatment.

More details on loans and advances subject to legislative and non-legislative moratoria as well as new loans originated under state guarantee mechanism are provided in the Risk report annex (Tables Template 1, Template 2 and Template 3).



### Pillar 2: The Guarantee Scheme

The (first) guarantee scheme consists of a total allowance of EUR 50 billion for all new loans and loan commitments up to 12 months maturity granted by banks to viable non-financial companies and self-employed people until 30 September 2020. Banks are entitled to a part of the overall amount of the state guarantee based on their market share. At the end of the guarantee scheme period the losses on the guaranteed loans incurred by each bank will be distributed as follows:

- first 3% to be covered by the Bank itself;
- between 3% and 5% to be equally shared by the Belgian state and the Bank;
- above 5%, 80% of the losses to be covered by the Belgian state.



In view of the need for longer maturities, the Government decided to introduce a (second) EUR 10 billion guarantee scheme for loans to SME (following the Belgian/European definition) with a minimum duration of >12 months and a maximum of 36 months, part of the former EUR 50 billion scheme. It was approved by the Belgian Parliament on 16 July 2020. In contrast to the first guarantee scheme, this second version is optional for the participating bank: banks can choose whether an eligible SME credit will be brought under the guarantee mechanism or not. This guarantee scheme covers 80% of all loan losses under this scheme, which also differs from the first scheme. This second guarantee scheme has been extended on 30 December 2020 and is valid until 30 June 2021 and allows maturities up to 60 months.

## Support by granted Covid-19 credits

**1,184** COVID 1.0 REQUESTS FOR AN AMOUNT OF  
EUR 468 MILLION

**331** COVID 2.0 REQUESTS FOR AN AMOUNT OF  
EUR 41 MILLION

A similar package of support measures has been taken by the insurance sector in March and April 2020:

- interest and capital repayments on mortgage loans contracted with insurance companies, as well as payment of premiums on mortgage protection insurance, are suspended until 31 March 2021, provided that insurance policyholders can prove that they are facing financial difficulties because of the Covid-19 crisis. This agreement is fully in line with that concluded by the government with the banks. In addition, a payment deferral until 31 March 2021 is possible for home insurance premiums linked to mortgage loans;
- concerning loans granted to corporates, the insurers also apply the conditions already set for the banking sector, namely a loan repayment delay until 31 March 2021;

- the insurance sector also committed to extend cover, with no further formalities, for pension, death, disability and hospitalisation under group insurance (contracted by employers) for all persons in temporary unemployment. The payment of premiums due by employers in this context is deferred until 31 March 2021. It is up to the employers to decide whether to use this possibility or not.

## IV. 1.2. Cost of Risk in 2020

### IV.1.2.1 IFRS 9 impairment methodology at Belfius

Reference is made to the Appendix IX.1.4. Risk Report 2019 for a full description of the Belfius process to compute IFRS 9 expected credit losses (ECL).

Please allow us to recall, the basic principles thereof:

- Belfius Bank, and its subsidiaries, recognise loss allowances for ECL on financial instruments at amortized cost or at fair value through OCI;
- ECL are measured through a loss allowance that depends on the financial instrument's status:
  - for performing exposures (i.e. instruments that have not incurred a significant increase in credit risk since origination), referred to as stage 1, a 12-month ECL is calculated;
  - for under-performing exposures (i.e. instruments that have incurred a significant increase in credit risk since origination), referred to as stage 2, Lifetime ECL are calculated;
  - non-performing exposures (i.e. exposures that become credit-impaired), are classified in stage 3 and the ECL reflect the remaining exposure after a best-estimate of future recoveries.
- ECL are probability-weighted estimates of credit losses. This is expressed as the present value of cash shortfalls i.e. the difference between the cash flows that are due to the entity in accordance with the contract and the cash flows that the entity expects to receive;
- ECL calculations use probability of default (PD) and loss given default (LGD) parameters. Point-in-time PD's are used that inter alia incorporate forward-looking macroeconomic information through the use of four different macro-economic scenarios. These scenarios are built upon internal information delivered by the Belfius Research Department, who uses external and internal information to generate a forecast "neutral" scenario of relevant economic variables along with a representative range of other possible forecast scenarios. The external information includes economic data and forecasts published by governmental bodies and monetary authorities.



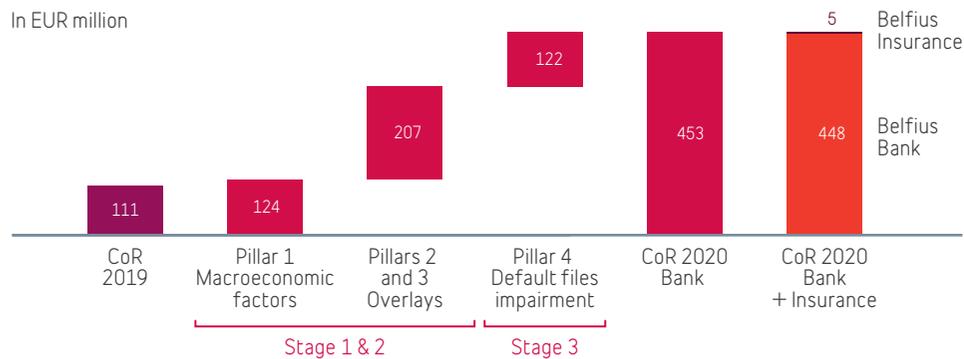
- Belfius assigns probabilities to the four forecast scenarios (neutral, optimistic, pessimistic and stress) and makes the link between:
  - macro-economic variables; and
  - credit risk and credit losses through identified and documented relationships between key drivers of credit risk and credit losses for each portfolio of financial instruments on the one hand and statistical analysis of historical data on the other hand.
- Given that ECL estimations are complex and to a certain extent judgmental, the afore-mentioned mechanical approach is completed by management judgment through “management call” layers. These layers can be positive or negative and aim to include any elements entering in the ECL calculation which have not been taken into account by the mechanical computation on an individual level or a (sub)portfolio level.

#### IV.1.2.2. Drivers of the cost of risk in 2020

In the Covid-19 perspective, the cost of risk is built according to a waterfall principle:

##### Cost of Risk 2020

In EUR million



- the provisions for stage 1 and 2 are calculated in a mechanical mode, based on a view on the macro-economic conditions (past and future) (pillar 1);
- if Belfius considers that certain risk pockets, defined in terms of sectors or groups of companies, are not sufficiently covered by the mechanical provisions, certain expert overlays are added (pillar 2);

- if, additionally, expert analysis pointing to counterparts with a potentially increased credit risk, that were not detected by the mechanical approach and not yet classified “as unlikely to pay”, the provisions constituted could be insufficient. For these cases, an individual management adjustment on the expected credit loss in stage 2 is added (pillar 3);
- for counterparts in a default status (stage 3), the normal impairment process is run and specific provisions are calculated and booked (Pillar 4). Provision levels are based on an individual assessment of exposure and collateral. A number of corporate loans, that were already showing increased risk profiles pre-crisis, have shifted to default in 2020, requiring additional specific impairments (stage 3). Some other loans resulted in release of impairments.

The Cost of Risk 2020 of EUR 453 million is composed of an increase of ECLs in stages 1 and 2 for a net amount of EUR 331 million and a provision for defaulted loans of EUR 122 million.

The net increase of EUR 331 million in stage 1 and 2 reflects the importance of the Covid-19 ECL overlays that were accounted for, in particular in the Business and Corporate segments. In order to cover for the increase of credit risk, linked to certain risk pockets in these segments, significant exposures were shifted from stage 1 to stage 2, inducing a net reduction of the ECL in stage 1 and an increase in stage 2 for which life time expected losses are calculated.

More details on the changes in the stock of expected credit losses are provided in the Risk report annex (Table CR2 A).



#### IV.1.2.3. Covid-19 adjustments to the impairment methodology: further insights

The current crisis is unprecedented with very unusual features such as its speed and scale, a widespread lockdown of activities, uncertainties about the timing and shape of recovery, the impact of the measures taken by the Federal State, the Regions, central banks and regulators, etc.

In this context, Belfius’ basic principles for ECL computations have remained largely unchanged, however some material adjustments to the afore-mentioned approach were required in order:

- to maintain adequate coverage ratios on estimated increased risk profiles; and
- to comply with updated regulations, for instance on forbearance and guidelines to avoid procyclicality.



Therefore, the following adjustments were made:

### Pillar 1: Macroeconomic factors: methodology

- Expected credit loss calculations are based on a long-term average (2009-2022) for all the relevant macroeconomic factors, with a backward and a forward looking part.
- To calculate ECL, Belfius still defines four probability weighted forward-looking scenarios each with their own macro-economic parameters to build optimistic, neutral, pessimistic and stress cases. Yet, the scenarios have been adapted to the current circumstances and more probability weight has been put on the pessimistic and stress scenarios.
- Counteractive dampening measures have been implemented by national and regulatory authorities. These have been included in the ECL calculations. They refer, inter alia:
  - to changes to avoid, to some extent, pro-cyclicality in ECL calculations by giving a greater weight to long-term normalized outlook evidenced by past experience when estimating long-term ECL (giving weight to through-the-cycle approach);
  - to account for moratoria and guarantee schemes: regulatory guidance was given with respect to the treatment of exposures covered by public and private moratoria related to Covid-19, both from a prudential (forbearance as unlikely-to-pay classification) and an accounting perspective (as an indication of significantly increased credit risk).

### Pillar 1: Macroeconomic factors used in 2020

- Belfius' neutral scenario includes an important recession for 2020, however, expectations have been revised to mitigate recession figures in the course of the year on the basis of macro-economic figures (Belgian GDP: -10,6% in Q2 vs -8% in Q4). This recession is expected to be followed by a partial rebound in 2021 and 2022 (Belgian GDP: +3.9% in 2021 and +3.3% in 2022) enabled by the vaccination campaign and assuming that no new major lockdown effect is to be expected;
- In terms of Unemployment, the neutral scenario implies an Unemployment increase from 5.4% in 2019 to 9.2% in 2020. An improvement to 7.4% in 2021 is forecasted. The 2020 Unemployment figure includes the exceptional temporary Unemployment observed that is expected to be, to a certain extent, converted into structural Unemployment;

### Neutral scenario

	GDP (% YoY)			CPI (% YoY)		Unemployment (%)	
	2020	2021	2022	2020	2021	2020	2021
Belgium	-8.0	3.9	3.3	0.2	1.3	9.2	7.4
Eurozone	-7.9	3.6	2.6	-	-	10.6	9.0
United States	-4.0	3.3	2.8	-	-	-	-

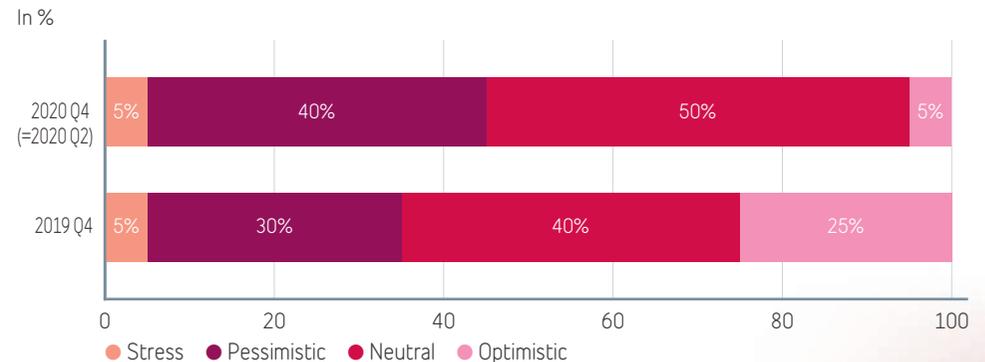
→ The neutral case is completed with an optimistic, a pessimistic and a stress scenario. The table (adjoining) illustrates the Belgian GDP Growth assumptions, as of 4Q 2020, under the four scenarios. Please note, that for the credit provisioning as of end 2019 other, pre-Covid 19 assumptions were used;

### 4 scenarios

GDP Belgium (% YoY)	As of end 2019		As of 4Q 2020	
	2020	2020	2021	2021
Optimistic	1.5	-7.3	9.0	
Neutral	1.1	-8.0	3.9	
Pessimistic	0.8	-10.3	3.1	
Stress	-0.5	-12.5	2.3	

→ A 50% weight has been assigned to the neutral scenario, while the weight of the more negative scenarios has been increased due the Covid-19 crisis, bringing the weight of these scenarios to 45%. The more optimistic scenario is given a 5% probability. The weights were modified in 2Q 2020 and kept unchanged since then.

### Scenario weights





## Sensitivity of the impairment stock stage 1 & 2 to changes in scenario weights

The following table provides an overview of the stage 1 & 2 impairments sensitivity to

- the weight of macroeconomic scenarios; and
- the most relevant macro economic factors being GDP and Unemployment assuming the current Covid-19 IFRS-9 method is maintained. Note that the sensitivity is not linear and cannot be simply extrapolated.

(In EUR million)	What if 85% optimistic <sup>(1)</sup>	Weighted average scenario 4Q20	What if 85% pessimistic <sup>(1)</sup>	What if 85% stress <sup>(1)</sup>
Impairment stock stage 1&2	846	964	1,008	1,113
% change vs WA scenario	-12%	0%	5%	15%
		Optimistic 5% Neutral 50% Pessimistic 40% Stress 5%		

(1) 5% on each of the 3 other scenarios.

## Pillar 2 and 3: overlays to cover for certain risk pockets

The Covid-19 adjusted mechanical calculations are completed with expert overlays. Due to the unusual situation and the sectoral impact of Covid-19, these overlays gained further scale and importance in the course of 2020. The layers are designed to result, overall, in best estimate total coverage of ECL in some specifically identified risk pockets (defined in terms of sectors, groups of companies or individual exposures) when the credit risk is estimated (potentially) insufficiently covered by the mechanical provisions.

### Risk pockets

<b>Vulnerable companies</b>	Companies with low ratings belonging to sectors identified as very much impacted by Covid-19 and flagged as having lower resilience
<b>Commercial real estate</b>	Sensitive market segments (e.g. retail, leisure, hospitality)
<b>Mortgages</b>	Loans at risk: to borrowers using moratorium and loans with indicators pointing out to potentially higher risk pockets (buy to let loans, loans to borrowers with low ratings)
<b>Individual names</b>	Expert analysis pointing to counterparts with a potentially increased credit risk, that were not detected by the mechanical approach and not yet classified "as unlikely to pay".

Concretely, one or more IFRS 9 parameters have been stressed when computing the ECL. For mortgages a stressed LGD value was applied, for Commercial Real Estate and vulnerable companies an add-on was applied on the mechanically calculated expected credit loss, reflecting the characteristic of the risk pocket.

This review fed the formal quarterly impairment process and resulted into shifts of individual files or risk pockets from stage 1 to 2 and to the application of the Expected Credit Loss levels that were deemed adequate to cover the increased credit risk.



## Governance

The governance process did not change fundamentally, with the Research team responsible for providing the macroeconomic parameters and scenarios, the computation engines (enhanced for increased flexibility and simulation power) and the governance of expert and impairment committees that were in place before the crisis. However, a higher frequency and in-depth reporting to the Management Board and Board of Directors was established to ensure proper guidance and decision-making process in view of the materiality of the Covid-impact and its unprecedented nature.

The current approach is deemed to reflect the expected credit losses in a best estimate way. Yet, the evolution of the pandemic and its economic impacts remain uncertain meaning that figures are subject to upwards or downwards adjustments in coming quarters.

It is to be recalled that stage 1 and 2 provisions constitute protection against expected credit losses on files that could enter into a default status. To what extent these stage 1 and 2 provisions will be transformed into stage 3 provisions, covering incurred credit losses on defaulted loans, remains subject to uncertainty. On the other hand, if there would be a significant improvement in macroeconomic environments and/or even more successful government support measures allowing that such currently anticipated transitions to default will not occur, part of the impairments could be reversed over time.

## IV.1.3. Evolution of the portfolio by segment

### IV.1.3.1. Retail (Mortgages and Consumer Credits)

Several factors have influenced the mortgage lending activity:

- termination of tax benefits on mortgage loans as of 1 January 2020, which has accelerated the production of loans at the end 2019 followed by a slowdown early 2020;
- supervisory expectations regarding the lending standards of mortgage loans which have been implemented by means of a strengthening of the underwriting criteria;
- the Covid-19 crisis, which has impacted the confidence of the customers, and which has made the acquisition of properties more difficult because of the lockdown.

Despite this complicated environment, the production volumes of mortgage loans remained relatively high leading to and FEAD at the end of 2020 of EUR 35,995 billion. The average PD is remaining stable at 0.50% over the years.

The integration into the Risk Appetite Framework of a target mortgage production and portfolio, the adjustment of the underwriting rules (with respect to LTVs, DSTIs) for specific risk pockets and a continuous monitoring with feedback loop to the underwriting criteria, have allowed Belfius to steer its mortgage production and portfolio to align with the NBB supervisory expectations.

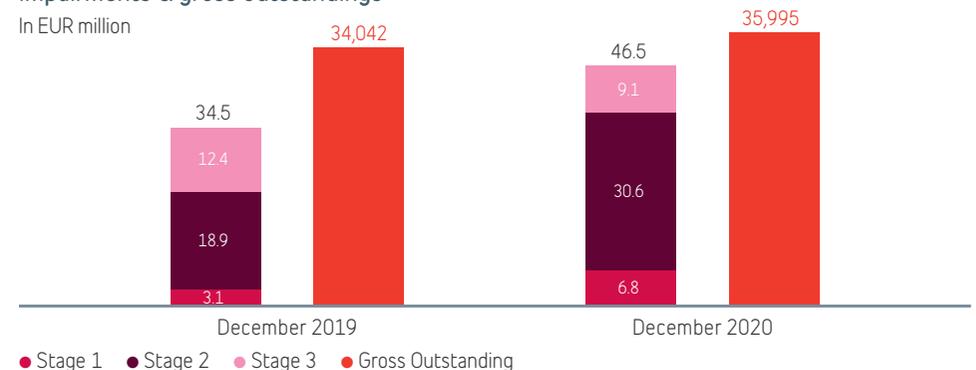
This resulted in a significant improvement of credit standards at origination, in particular the high LTV segment (>80% and 90%) for both buy-to-let loans and first time buyer loans. Since 2019, the part of the production with a LTV>90% decreased with 17%.

The asset quality ratios remained very low given that due to the Covid-19 moratoria and other support measures many clients were able to avoid payment difficulties.

Despite low inflow of NPL loans, and consequently low Stage 3 impairments, the Cost of Risk has been impacted by the Covid-19 crisis. This impact is fully related to the Stage 1 and 2 impairments, reflecting a strategy of anticipative provisioning in line with the macro-economic perspectives and to cover for potential negative evolutions in certain risk pockets (as higher LTV and/or a buy-to-let mortgage loan).

### Impairments & gross outstandings

In EUR million



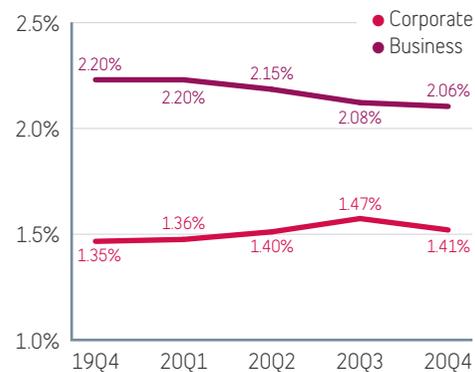
The production of consumer loans further slowed down/stabilised, a trend already observed in 2019 resulting in an FEAD at 2020 year-end of EUR 5,175 billion, 0.6% lower than in 2019. The PD remained stable (0.74%).



### IV.1.3.2. Business and Corporate clients incl. Covid-19 sensitive sectors

The Belgian economy heavily depends on international trade and most of its economic sectors are geared towards the export of products. Global trade weakened in 2020, while the disruption to trade flows and supply chains further amplified the negative effects, especially for the sectors delivering goods and services to sectors highly impacted by the sanitary crisis. The UK left the EU on 31 January 2020. An agreement on its new partnership with the EU, more specifically by the EU-UK Trade and Cooperation Agreement was agreed on 24 December 2020. As a result a number of uncertainties have been removed, but certain risks remain present: the treaty does not solve everything, lacks some safeguards and could hold some surprises.

#### Average PD of the portfolios Corporate & Business banking



Not rated and default excluded

Belfius' exposure to Business and Corporate (mostly large and medium sized corporates with a decision-making centre in Belgium as well as corporates offering services to the public sector) clients amounted end 2020 to EUR 50,456 billion.

The quality of the portfolios remains stable with a PD at 2.06% for Business Banking and at 1.41% for Corporate Banking. Belfius keeps taking the necessary measures to ensure that its growth strategy goes hand in hand with a good creditworthiness.

The credit risk in the loan portfolio has been dominated in 2020 by the Covid-19 crisis and its significant economic impact:

- a risk mitigation strategy for corporates, SME and self-employed was defined in the context of the Covid-19, based upon two complementary approaches: a bottom-up approach analysing individual clients identified as "at risk" and continuous credit risk monitoring. The bottom-up approach was executed by screening the portfolio with pluri-disciplinary teams of Front Office, Loans, Risk Management and Legal. This in-depth analysis of the loan portfolio was conducted in waves in order to prioritize on most Covid-19 impacted sectors and companies with the lowest estimated resilience. With 90% of the exposures screened at year end our analysis revealed that only a small fraction of Belfius' outstanding exposure is actually situated in these highly impacted sectors or have been subject to specific risk mitigating actions to temper the risk;

- Belfius has mapped the impact of the Covid-19 crisis specifically for the segment of Business and Corporate clients. The sectors actually suffering the most from the crisis are those which have been obliged to cease the major part of their activities due to a decision of the government, the second most affected sectors are those which are heavily impacted by social distancing measures. Business and market players active in these sectors have been severely hit financially, as it is extremely difficult for them to offset the lost turnover, and to return swiftly to the usual turnover once the economy rebounds;

#### Sector sensitivity

Sector sensitivity	% of total portfolio <sup>(1)</sup>
<b>CATEGORY 1</b> Sectors directly forced to stop the major part of their activities due to Government's decision (Such as hospitalities, arts, events and retail trade excluding food)	1.4%
<b>CATEGORY 2</b> Other sectors with activities heavily impacted by the social distancing measures (Such as travel, transport, airlines, automotive and wholesale trade)	4.0%
<b>CATEGORY 3</b> Other sectors delivering services for directly impacted sectors at levels 1 and 2 (Such as construction, shipping, warehousing, non-residential real estate and service companies)	6.8%
<b>CATEGORY 4</b> Sectors that will be suffering from the global economical impact of the crisis (Macro-economic effect with demand and production disruptions)	15.8%

(1) Total loans and debt instruments portfolio (FEAD) on Belfius Bank balance sheet amounts to EUR 180 billion (incl. GC) as per end December 2020.

- sector risks are monitored in a proactive way and specific measures have been defined with regard to a limited number of more vulnerable sectors:
  - Belfius exposure to the more Covid-19 sensitive sectors (categories 1 and 2) is limited to 5,4% of the total portfolio;
  - several assessments indicate that the commercial real estate sector has shown good resilience, also against the Covid-19 crisis, with the exception of certain pockets of risk as commercial real estate for Retail and Hotel/Leisure;
  - Belfius' exposure to these risk pockets is limited and overall, our acceptance policy, based on guidelines and best practices, has contributed to a sound risk level of the commercial real estate portfolio, which is correctly diversified in terms of underlying asset types, individual name concentration and geographical spread;



→ In addition to the existing risk monitoring and as part of the management of the Covid-19 impact, Belfius has put in place a robust risk mitigation strategy with specific committees, action plans and reporting & monitoring activities. The Risk department accelerated the improvement of the process of early warning indicators in order to keep permanently the risks in this market segment well under control.

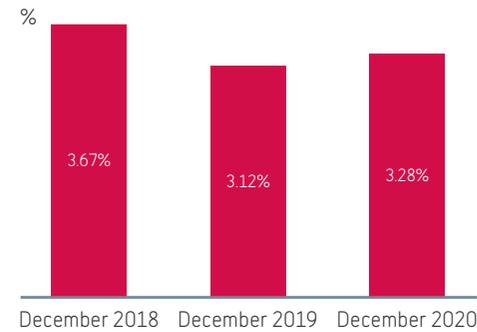
Within this global context, the number of bankruptcies decreased significantly (-33%) in 2020: many companies survive indeed the pandemic through robust support measures:

- they received financial assistance from the government;
- they retained access to credit thanks to agreements between the government & banks;
- they could temporarily suspend the repayment of their loans;
- while the moratorium on bankruptcies also played a not negligible role.

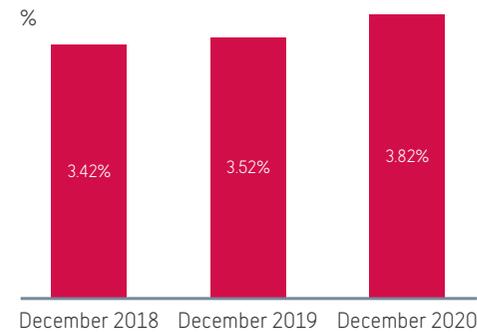
Nevertheless the Cost of Risk related to business and corporate loans exceeded in 2020 significantly the target level, not only driven by the strong increase of the Stage 1 and 2 impairment stock, caused by the deterioration of the macro economic factors and the creation of additional Covid-19 layers, but also by some important files that shifted to Stage 3.

### Asset quality ratio by segment

#### Business Loans

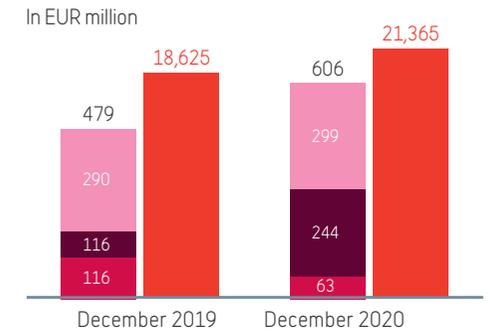


#### Corporate Loans

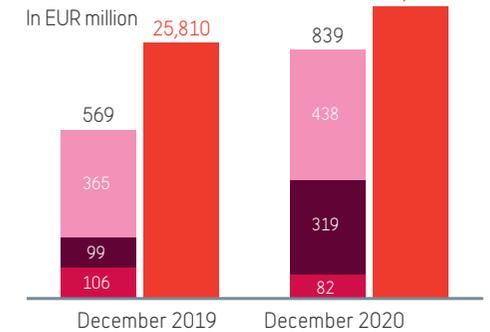


### Impairments and gross outstandings by segment

#### Business Loans (FEAD)



#### Corporate Loans (FEAD)



● Stage 1 ● Stage 2 ● Stage 3 ● Gross Outstanding



### IV.1.3.3. Public sector clients

Belfius' loan portfolio to the public and social sector amounted end 2020 to EUR 38,298 billion (FEAD) and maintained its low risk profile despite the Covid-19 pandemic:

- Belgian public finances headed for the year 2020 towards a historic deficit, while also the debt ratio jumped to record heights;
- the deterioration is of a comparable magnitude in all EU countries, so that the EU decided to mobilize for the first time the maximum budgetary flexibility by activating the 'general escape clause';
- independently of the Covid-19 impacts and the budgetary easing measures planned by the EU, the Belgian finances present an important deficit, which will require financial reconstruction measures in the medium term.

2020 has been a turbulent year for local authorities, who were right in the front line of the sanitary crisis:

- the health crisis will in general not make a material impact on the municipal finances, at least in the short term, although there are differences between regions;
- however, the issue of the pension cost related to their statutory staff and the higher pressure on Social Service will certainly be raised again later on this legislature, and it is just the question to what extent the ambitious and necessary local investment plans will be executed;
- a revision of the pluri-annual plan seems inevitable for some of the municipalities, but globally municipalities have strong tools to support economic recovery.

From a risk management point of view, the hospital sector is since a few years a focus of attention:

- the 2019 figures confirm once more the fragile financial situation of the hospitals, the extreme low margins remain a reality;
- hospitals are therefore hardly able to face financial setbacks, and certainly not a tsunami like the Covid-19 crisis;
- the (promised) government compensation will therefore be essential to absorb the losses;
- in the long term, a structural reform of their financing seems crucial; only in this way they will be able to provide the strong healthcare that is vital for a prosperous economy;
- 2020 can thus become a turning point for our health care system and for the way hospitals are organized.

The senior housing sector contains traditionally considerable additional risks to operators due to the age and average health profile of the occupiers:

- it is a fact that Covid-19 has severely hit older adults in Belgium;
- there is a clear concern that growing contagion in senior-care buildings could hurt operations and lead to occupancy declines;
- the viability of some smaller senior living operators might come under pressure, especially in regions where the sector already experienced headwinds related to oversupply and elevated cost pressure;
- the financial health and occupation rate of the affected senior homes are therefore closely monitored by Belfius.

### IV.1.3.4. Financial markets

The mission of Financial Markets, aligned with the mission of Belfius Bank, is to serve its clients and the Belgian economy with essential financial services. Next to this general objective, an innovative Financial Markets also contributes to the liquidity profile of the Bank through the management of Short-Term and Long-Term wholesale funding and through the management of the investment portfolios: both the ALM Liquidity and Yield portfolios (run-off management of the portfolio inherited from the past).

Despite the health crisis that spread rapidly during the year, credit risk in financial markets remained globally stable during 2020.

The most important credit risk events are as follows:

- Covid-19: Some sectors such as transportation, automotive, shopping centers and recreation, ... have been more impacted because of the length of the Covid-19 crisis. Nevertheless, Belfius' exposure towards these sectors remains limited and to date, the impact has been manageable and limited to a small number of internal rating downgrades;
- Brexit: A hard Brexit has been avoided through the agreement reached by the UK and the EU at the end of the year 2020. Thanks to this, the potential negative consequences are limited and remain manageable;
- Despite the headwinds that prevailed during the year 2020, the average rating of the investment portfolios and credit derivatives portfolio, managed within financial markets, remained stable at a level of A-;



- Risk concentration: Our main concentrations remain British inflation-linked corporate utility bonds and Italian sovereign bonds, which are of satisfactory credit quality and are closely monitored;
- De-risking: Market developments have enabled us to sell 30% of our exposure to Italian sovereign debt at the end of 2020 as well as to continue to reduce our exposure to the riskiest assets such as Tunisian sovereign debt or volatile assets such as old uncollateralized exposures.

Credit risks in relation to Financial Markets activities are monitored by the Credit Risk Limit Framework which is part of the Risk Appetite Framework. Counterparty and country limits are monitored by FM Risk Management in order to limit risk concentrations.

## IV.1.4. The risk management process concerning Forbearance, Watchlist, Default and Impairments

### IV.1.4.1. Forbearance

Forbearance measures imply the granting of concessions towards a debtor facing or about to face difficulties in meeting its financial commitments. These concessions may take the form of modifications to the loan contract or some refinancing.

They apply to all loans and debt securities that are on-balance sheet and also to some off-balance sheet commitments. They do not apply to debt securities held for trading exposures.

Specific criteria are established for each business segment. These provide a practical interpretation of the concepts of “financial difficulties” and “concession”. When granting a concession, the Bank is always led by a number of mainly business-related and economic factors. The fact that concessions are made is one of the Watchlist indicators at Belfius and lead to a transfer of the exposures from stage 1 to stage 2 under IFRS 9.

Due to the unprecedented situation, which customers and institutions face today with the Covid-19 pandemic and given that authorities have fully acknowledged that payment moratoria are effective tools to address short-term difficulties caused by the limited operations of many enterprises or by short-term unemployment for households, the EBA has provided flexibility and guidance to the banks with regard to forbearance reclassification.

According to the new EBA Guidelines on legislative and non-legislative moratoria<sup>(1)</sup>, institutions are allowed to grant payment holidays for a pre-defined set of obligors, for which there need not be an automatic regulatory reclassification as forbearance. However, the EBA clearly clarifies that banks are required to continue to correctly identify those situations where borrowers may face longer-term financial difficulties and classify exposures in accordance with the regulation. In addition, the EBA clarifies that the existence of any credit risk mitigation (including state guarantees due to Covid-19) should not exempt the banks from performing the assessment of the obligor’s unlikelihood to pay or affect the results of such an analysis.

Belfius reviewed its forbearance criteria established within this purpose. In line with the EBA guidance<sup>(1)</sup>, there is no automatic change in the forbearance classification for borrowers only due to new loan granted under the state guarantee scheme or EBA compliant requested moratoria. Clients which were granted legislative, non-legislative and other moratoria during the Covid-19 pandemic continued however to be assessed on an individual basis, taking into consideration the existing forbearance criteria and longer-term capacity to repay. In this context however, the most vulnerable clients associated with high PD’s and, with potentially longer-term use of moratoria are recognized as forborne.

At the end of 2020, an amount of EUR 1,031 million of loans at Belfius complied with the forbearance definition, of which EUR 79 million related to Belfius Insurance compared to EUR 818 million and EUR 61 million at the end of 2019. EUR 624 million or 60% of these forborne exposures are still performing. The most relevant contributors to the Forbearance are Corporate (EUR 376 million) and Business customers (EUR 383 million).

More details on forborne exposures are provided in the Risk report annex (Table CQ1).



### IV.1.4.2. Watchlist

The Watchlist Guideline defines internal and external (early warning) indicators to identify a significant increase of credit risk that may lead to an intensive follow-up and/or management of credit files. This allows the bank to closely monitor increasing credit risks and to take adequate credit mitigation measures in order to reduce credit risks pro-actively.

This is also reflected in the provisioning policy by applying a stage 2 for the majority of these exposures. On a quarterly basis, dedicated Risk Committees identify the files requiring a higher level of monitoring.

More details on the ageing of past-due exposures are provided in the Risk report annex (Table CQ3).



(1) EBA/GL/2020/02.



#### IV.1.4.3. Default

A transversal default definition is applied within the entire Belfius Group and on all market segments in line with the EBA Guideline<sup>(1)</sup>.

A default status is assigned to the debtors who satisfy either one or both of the following criteria:

- the debtor has material exposures which are more than 90 days past due;
- the debtor is assessed as unlikely to pay its credit obligations in full without realization of collateral, regardless the existence of any past due amount or the number of days past due.

Belfius Default guideline provides in-depth description of indicators used to categorize an exposure in default<sup>(2)</sup>. The Default Committee within the Risk department is competent to define the default status.

Based on regulatory evolutions, Belfius has implemented the EBA updated definition of default as of mid March 2020<sup>(1)</sup>. Its internal guidelines are updated accordingly. The aim of the EBA guideline is to harmonize the definition of default across the EU prudential framework.

Main impacts are the materiality threshold for obligations past due that are now composed of both an absolute and a relative threshold, and the introduction of a probation period of 3 months before reclassification to a non-defaulted status.

#### IV.1.5. Asset quality

At the end of 2020, the amount of impaired loans amounted to EUR 1,997 million, an increase of 7% compared to year-end 2019, mainly driven by a limited number of specific customers in default. During the same period, the gross outstanding loans to customers increased by 4.1% and amounted to EUR 98,639 million as the end of 2020. As a consequence, the asset quality ratio remained stable at 2.02% at the end of 2020. The coverage ratio slightly decreased to 60,0% at the end of 2020 compared to 62.3% at the end of 2019.



More details on the credit quality by exposure classes are provided in the Risk report annex (Table CR1).

(1) EBA/GL/2016/07.

(2) An economic loss related to the sale of credit obligations will be treated as an indication of default if the loss on the sale of credit obligations is related to the credit quality of the obligations themselves and material i.e. when the economic loss related with the sale of the credit obligation(s) amounts to minimum 5% of the total outstanding amount of the obligation(s) subject to the sale.

(3) EBA/GL/2016/11.

## IV.2. Credit risk exposure

### IV.2.1. Overview

The tables in the following chapter provide an overview of the overall credit risk. As prescribed in the EBA guideline<sup>(3)</sup>, different metrics are used referring either to accounting or to risk concepts.

The following metrics are used in this Risk report:

- gross carrying value: the exposure at default (EAD), before application of credit conversion factors (CCF);
- net carrying value: gross-carrying value less the exposure at default of credit risk adjustments;
- exposure value for counterparty credit risk: the exposure at default (EAD) after Credit Risk Mitigation Techniques;
- exposure amount: gross carrying value less the physical collateral.

In addition to these metrics, Belfius uses also the term of Full EAD or FEAD.

Full Exposure At Default (FEAD) is determined as follows:

- for balance sheet assets (except for derivatives): the gross carrying amounts (before credit risk adjustments);
- for derivatives: the fair value of derivatives after netting, increased with the potential future exposure calculated under the current exposure method (add-on);
- for Securities Financing Transactions: the carrying amount as well as the excess collateral provided for repurchase agreements;
- for off-balance sheet commitments: either the undrawn part of credit facilities or the maximum commitment of Belfius for guarantees granted to third parties.

FEAD for instance provides a consistent metric to present a combined view of the Bank and Insurance respective exposures to credit risk.

### IV.2.1.1. Contribution Belfius Bank – Belfius Insurance

#### Breakdown of credit risk by counterparty

(FEAD, in EUR million)	31/12/2019	31/12/2020	Of which	
			Bank	Insurer
Central governments	18,094	36,570	30,282	6,288
of which government bonds	9,967	9,703	3,629	6,074
of which EU Central Bank	6,673	25,418	25,418	0
Public sector entities	44,342	43,585	41,882	1,703
Corporate & Project Finance	38,864	42,958	41,659	1,299
Monoline insurers	4,718	4,600	4,600	0
ABS/MBS	749	427	392	35
Individuals, self-employed and SME's	52,220	54,554	50,393	4,160
Financial institutions	13,415	11,456	10,540	916
Other		0		0
<b>TOTAL</b>	<b>172,401</b>	<b>194,149</b>	<b>179,748</b>	<b>14,402</b>

The figures in the above table are after elimination of intra-group exposures and exclusion of equity positions and other assets not qualified as credit exposure, but with inclusion of credit exposure of trading activities and counterparty credit risk.

Exposures are allocated to the final counterparty, with the exception of ABS/MBS for which the exposure to the original counterparty is used.

As at 31 December 2020, the total credit risk exposure, within Belfius reached EUR 194.1 billion, an increase of EUR 21.7 billion or 12.6% compared to the end of 2019.

This increase is entirely attributable to the banking activity as the credit risk exposure at the level of Belfius Insurance remained stable at EUR 14.4 billion at the end of 2020.

→ The increase by EUR 18.5 billion observed on the segment central governments is mostly due to the additional liquidity reserve taken up by Belfius and deposited at the NBB regarding the adjusted TLTRO III scheme implemented by the ECB. Nearly half (49%) of the government bonds portfolio is invested in Belgian government bonds at the Group level. While at bank level the Belgian government bonds represents 45% of the total government bond portfolio, the relative proportion at Belfius Insurance stood at 51%.

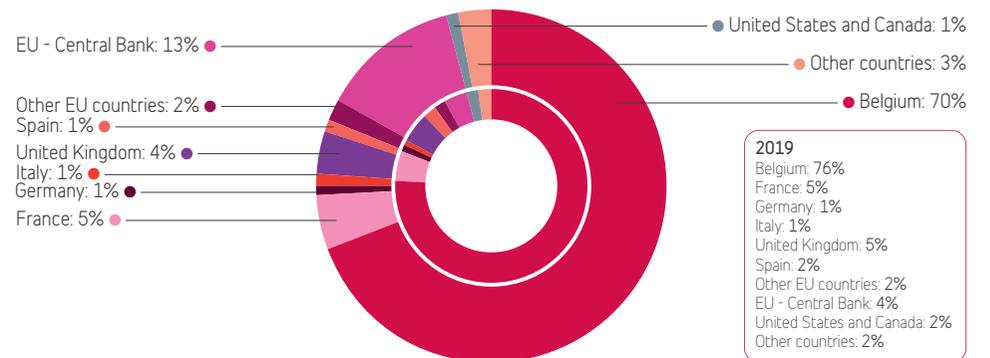
→ The credit risk exposure on individuals, self-employed and SMEs (28% of the total), Public Sector entities (22%) and corporates (22% of the total) constitute the three main categories. The exposure on the categories individuals, self-employed and SMEs and corporates increased by EUR 2.3 billion and EUR 4.1 billion respectively, reflecting Belfius' strategy to support the Belgian economy.

→ The credit risk exposure on public sector entities and institutions that receive guarantees of these public sector entities decreased with EUR 0.7 billion.

→ The credit risk exposure on financial institutions declined in 2020 by EUR 2.0 billion.

→ The credit risk on monoline insurers on bonds issued by issuers principally active in infrastructure and public utilities projects is predominantly an indirect risk arising from credit guarantees written by Belfius Bank and reinsured with monoline insurers. The exposure declined by EUR 0.1 billion over the period.

#### Breakdown of credit risk by geographical region (Outside 2020 – Inside 2019)



Belfius' positions are mainly concentrated in the European Union: 92% or EUR 166.1 billion at bank level and 89% or EUR 13.7 billion for Belfius Insurance. The total relative credit risk exposure on counterparties situated in Belgium is 70%, 5% in France, 4% in the United Kingdom, 1.4% in the United States and Canada, 0.9% in Spain and 0.9% in Italy.

→ The credit risk exposure to counterparties in the United Kingdom amounted to EUR 7.6 billion. About half of this credit risk exposure concerns bonds, of which close to two-third are inflation-linked, issued by utilities and infrastructure companies in the United Kingdom that operate in regulated sectors such as water, gas and electricity distribution. These bonds are of satisfac-

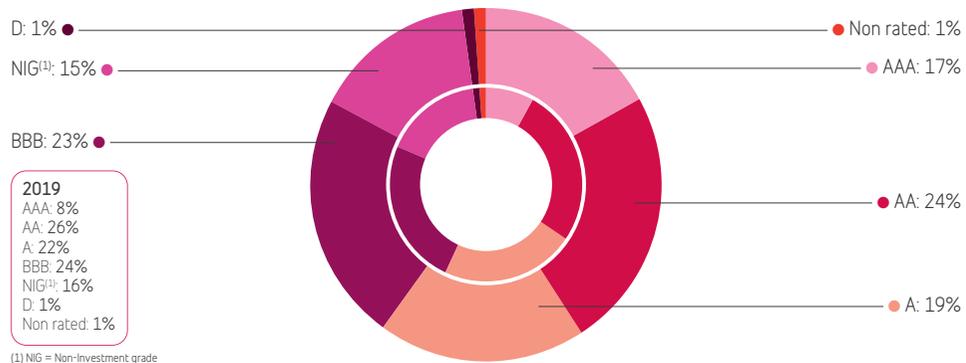


tory credit quality (100% investment grade), and moreover most of the outstanding bonds are covered with a credit protection issued by a credit insurer that is independent from the bond issuer. The remainder concerns the bond portfolio of Belfius Insurance, a short-term credit portfolio for treasury management of Belfius Bank and receivables on clearing houses. The credit risks on those portfolios are also of satisfactory credit quality.

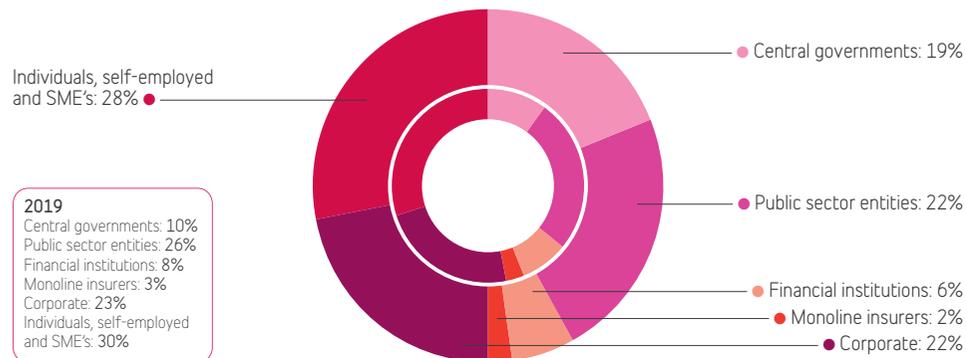
→ Exposures to UK declined by EUR 1.9 billion over the period as a consequence of business transfers from our counterparties in anticipation of Brexit.

At the end of December 2020, 82% of the total credit risk exposure had an internal credit rating investment grade (IG).

### Breakdown of credit risk by rating (Outside 2020 - Inside 2019)



### Breakdown of credit risk by counterpart (Outside 2020 - Inside 2019)



### IV.2.1.2. Overview credit risk under the prudential scope of consolidation

The differences between the accounting and regulatory scopes of reporting are described in the Risk report annex (Tables LI1 LI2 and LI3).



FEAD	Credit risk		Counterparty credit risk			Total
	On-balance-sheet amount	Off-balance-sheet amount	Securities Financing Transactions	Derivatives	Default fund Contribution	
(In EUR million)						
<b>IRB EXPOSURE CLASSES</b>						
Central governments and central banks	12,297	8,750	44	260		21,351
Institutions	18,379	3,231	2,348	2,675		26,633
Corporates	29,701	13,613	3,291	1,086		47,691
of which Corporates- SME	10,197	2,050	38	47		12,332
Retail	42,309	6,425	0	0		48,734
of which secured on RE SME	7,537	330				7,866
of which secured on RE non-SME	25,025	1,236				26,261
of which Qualifying Revolving		20				20
of which other retail SMEs	7,478	2,065		0		9,544
of which other retail non-SMEs	2,269	2,774				5,043
Equity	269					269
Securitisation	259					259
<b>TOTAL IRB APPROACH</b>	<b>103,214</b>	<b>32,019</b>	<b>5,683</b>	<b>4,022</b>	<b>0</b>	<b>144,938</b>
<b>STANDARDISED EXPOSURE CLASSES</b>						
Central governments or central banks	25,064	10		57		25,131
Regional government or local authorities	637	113		93		843
Institutions	816	239	1,034	358		2,447
Corporates	4,974	2,672	0	71		7,717
Retail	625	78				703
Secured by mortgages on real estate	281	22				302
Other <sup>(1)</sup>	9,396	212			92	9,700
<b>TOTAL STD APPROACH</b>	<b>41,793</b>	<b>3,346</b>	<b>1,035</b>	<b>579</b>	<b>92</b>	<b>46,844</b>
<b>TOTAL</b>	<b>145,007</b>	<b>35,365</b>	<b>6,718</b>	<b>4,600</b>	<b>92</b>	<b>191,782</b>

(1) includes exposure classes past due items, items belonging to regulatory high-risk categories, or other items and equity, including exposures under Danish Compromise,

→ At year-end 2020, 76% of the total credit risk exposures were calculated using the IRB approach. IRB exposures mainly consist of retail and corporate exposures.

→ As for the previous table, exposures are allocated to the final counterparty and expressed in gross carrying values.

→ Figures on counterparty credit risk do not take into consideration the financial collateral received.



Total and average exposures of the credit portfolio are further detailed in the Risk report annex (table CRB-B).



For further details on the credit quality of exposures by geography, economic sector or maturity, please refer respectively to the Risk report annex (tables CR1-C, CR1-B and CRB-E).

## IV.2.2. Internal rating-based approaches

### IV.2.2.1. Competent Authority's Acceptance of Approach

By letter sent on 21 December 2007 by the Banking, Finance and Insurance Commission (CBFA), the Belgian Regulator, Dexia SA was authorised to use the Advanced Internal Rating-Based Approach (AIRB Approach) for the calculation and the reporting of its capital requirements for credit risk starting from 1 January 2008. This acceptance was applicable to all entities and subsidiaries consolidated within the Dexia Group, which are established in a Member State of the European Union and are subject to the Capital Requirement Directive, and among them Belfius Bank (formerly Dexia Bank Belgium). The teams at the Bank have also been among the main contributors of this approval, and its risk management is in perfect continuity with the know-how developed so far.

### IV.2.2.2. Internal Rating Systems

In order to implement the consecutive EBA guidelines on the default definition, on PD, LGD and Credit Risk Mitigants and as a response to TRIM ("Targeted Review of Internal Models") findings, Belfius has set up in 2020 a comprehensive model transformation plan with respect to the pillar 1 models.

Rationalization and simplification are key principles that will guide this credit risk model portfolio transformation. The reduction of the number of models by reviewing the model scope in line with the Belfius Strategy, a simplification of the model structure of certain models, and the right balance between the A-IRBA approach and a less sophisticated approach will be analyzed. During the implementation of this program, a special attention will be given to:

- the data quality framework for modelling;
- the implementation of a comprehensive MOC (Margin of Conservatism) framework;
- the treatment of low default portfolios in the perspective of a limited number of observed defaults.

This transformation plan will be rolled out over about 3 years and will provide Belfius with a renewed set of models, fully compliant with the latest regulatory requirements, that will continue to be an effective cornerstone of the credit acceptance, loan lifecycle management, credit risk management processes and reporting.

At the end of 2020, the first new model related to mortgage LGD was already in a review process at ECB level.

The internal rating systems used by Belfius Bank are set up to evaluate the three Basel parameters: Probability of Default (PD), Loss Given Default (LGD) and Credit Conversion Factor (CCF). In the advanced method, a set of two models, one for PD and one for LGD, has been developed. Regarding the CCF parameter, Belfius makes a distinction between retail and Non-retail counterparties: an advanced model is applied for retail counterparties, while non-retail counterparties use the regulatory values.

The PD models estimate the one-year probability of default on a through-the-cycle basis. Each model has its own rating scale and each rating on the scale corresponds to a probability of default used for regulatory, reporting and use test purposes. The correspondence between rating and PD for each scale is set during the calibration process, as part of the model development, and is reviewed during the yearly back testing and adjusted when necessary. The number of ratings on each scale depends on the characteristics of the underlying portfolio (the number of counterparties, their homogeneity, whether it is a low default portfolio or not) and varies between 6 and 17 non-default classes. In addition, each scale has been attributed two default classes (named D1 and D2).

For non-retail, LGD models estimate the ultimate loss incurred in a downturn situation on a defaulting counterparty before taking the credit risk mitigants into account. The unsecured LGD depends on various factors such as the product type, the level of subordination for instance. LGD is an economic component accounting for direct and indirect costs related to the recovery process. The granularity of the estimate is a function of the quantity and quality of data available. For retail, LGD is mainly determined by product type and based on workout recoveries. Professional loans are segmented in 5 classes subject to collateral value.

CCF models estimate the portion of off-balance-sheet commitments that would be drawn should a counterparty go into default. The regulation authorises the use of CCF models only when CCF under the Foundation Approach is not equal to 100% (as it is for credit substitutes for instance). CCF granularity also depends on availability of data.



Internal estimates of Basel parameters are widely used within Belfius Bank. They are notably used in the decision-making process, credit risk management and monitoring, internal limit determination, and pricing, in addition to the calculation of the regulatory risk weighted exposure amounts.

The control mechanisms for Internal Rating Systems (IRS) are organised on two levels:

- Validation, that encompasses both Model Validation and Operational Control, is an independent Direction within the Risk department. It reports directly to the CRO and is not involved in any model development in order to guarantee its objectivity. Validation performs a global control on all the aspects of the production of results by the models, from a methodological but also an operational (implementation, usage) viewpoint. It intervenes prior to the first use of the models and afterwards performs a regular monitoring of their functioning;
- Internal Audit is responsible for auditing the general consistency and compliance with the regulation of the IRS. According to the CRD minimal requirement 131, Annex VII Part 4, Internal Audit has to include in its plan, at least once a year, a review of the IRS and its functioning, including credit scoring and estimation of PD, LGD, regulatory expected loss (EL) and CCF. Compliance with all the minimum requirements has also to be verified. Within Belfius Bank, this annual review has been delegated to the Validation Direction. Audit acts then as an additional level of control, given that the correct functioning of Validation is included in its Audit plan.

We refer to Appendix XI.2. for more details regarding Internal Rating Systems.

### IV.2.2.3. Back testing

The purpose of the back test is to assess the performance of the internal rating system ensuring an appropriate balance between capital and risk. As the formulas to calculate the Bank's capital are provided by the Basel Committee on Banking Supervision, the internal back test relating to Pillar 1 rating systems is based on the back test of the input parameters PD, LGD and CCF in the Basel credit risk portfolio model. Please note that even if the non-retail CCF parameters are not the result of a dedicated model, they are still subject to a monitoring in order to ensure the used values are suited.

The back test is the evaluation of the predictive power of the rating system and the assessment of its time evolution to detect any reduced performance in an early stage (as for instance the loss of rank ordering power of an input variable). Decreased performance of the rating system may

reduce the Bank's profitability, entail its use test and impact the risk assessments of the defined risk buckets. The performance is tracked by analysing the ability to discriminate between high and low risk and the stability of the data inputs into the rating system.

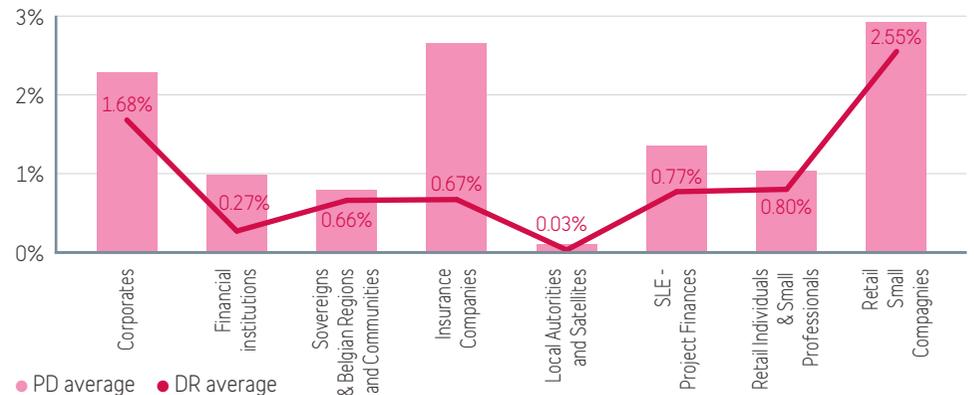
In general, the back-test procedure aims at assessing the discriminatory power of the model (ranking of the clients from "good" to "poor" grades), the calibration level (a rating system is well calibrated if the estimated PDs (or LGDs) deviate only marginally from the actual default rates) and the stability of the model's population/risk drivers.

The results of the back testing are assessed using statistical significance tests. The outcome of the significance tests drives required action plans (e.g. recalibration process, model structure re-development).

The additional part of the back-test procedure is related to the impact of judgemental aspects i.e. the importance of judgemental qualitative variables in the final rating and the effect of expert overruling.

The following table gives an overview of the Probability of Default (PD) and the Default Rates (DR) on the Bank's main portfolio under advanced method. It is based on an at least 5 years history of our advanced portfolios. As it can be expected, it shows greater PD values (predictions) than the default rates (observations).

### Backtesting of internal models





The following table shows an overview of the relation between IRB models as used above and the implicated asset classes:

	Corporates	Financial Institutions	Sovereigns & Belgian Regions and Communities	Insurance Companies	Local Authorities & Satellites	Retail Individuals & Small Professionals	Retail Small Compagnies
<b>ASSET CLASSES</b>							
Central governments and central banks			■				
Institutions		■			■		
Corporates	■			■	■		
Corporates - SME	■				■		
Retail - SME						■	■
Retail - non-SME						■	

For the relevant classes, the exposure weighted PD and number weighted PD by obligor type at year-ends 2019 and 2020 by PD range are further detailed in the Risk report annex (table CR9).

#### IV.2.2.4. Stress Testing

Pillar 1 stress tests are defined within Basel to deal with minimum capital requirements. They assess how the risk parameter levels may vary in the credit portfolio during periods of stress, in order to draw conclusions on individual asset classes and portfolios, as well as on the whole portfolio itself.

The focus of the stress testing Pillar 1 lies on a univariate analysis and the application of realistic and meaningful expert scenarios.

During the univariate analysis, the distribution of the model variables is investigated in order to detect if a significant part of the portfolio gets a value equal to the cap or floor. When this is the case, conclusions must be drawn in terms of the capability of the model to perform in such a scenario.

Expert scenarios can essentially be designed in two distinct ways:

- testing the robustness of the model by computing PD/LGD in an alternative (stressed) manner and comparing the results to the model outputs: the purpose is to challenge the model;
- stressing model results: this measures the impact on risk measures given the assumption that the model is correct.

These stress tests are performed on an annual basis on a group-wide basis.

### IV.2.3. Standardised approaches

#### IV.2.3.1. Introduction

Belfius Bank uses the Advanced Internal Rating-Based Approach (AIRB Approach) to calculate its capital requirements for credit risk. Nevertheless, it applies the Standardised Approach for some portfolios corresponding to cases specifically authorised by regulation such as:

- small business units;
- non-material portfolios;
- portfolios corresponding to activities in run-off or to be sold;
- portfolios for which it has adopted a phased roll-out of the AIRB Approach.

#### IV.2.3.2. Nominated External Credit Assessment Institutions (ECAI)

Belfius uses the regulatory defined risk buckets to assess the quality, and linked risk weight, for all exposures calculated according to the Standardised approach. It also uses external ratings from S&P's, Fitch and Moody's to define the risk bucket of exposures.

The EBA standard table is used for mapping these external ratings.

If two external ratings are available, the lower of the two is used. If there are three external ratings with different risk weights attached to them, the risk weight corresponding with the second-best rating is applied. If no rating is available, the risk weight provided by the Standardised approach is used.



## IV.3. Credit risk management and governance

Credit risk is defined as, on the one hand, the possibility that a bank's borrower or counterparty will fail to meet its obligations (in the form of non-payment or non-performance) in accordance with the agreed terms, also called the payment default risk, and on the other hand, the possibility that the bank will not be able to recover its outstanding debt by means of the collateral that is linked to the debt, i.e. the risk of non-recovery and the non-secured recoveries (not linked to a collateral or guarantee).

### IV.3.1. Governance and committees

Belfius' counterparty limit framework, which is part of its global Risk Appetite Framework (RAF), is the main instrument to limit risk concentrations:

- it serves by consequence as a reference point to determine the risk levels for which the Management Board and the Board of Directors are qualified; and
- affects as a result also the decision limits of all (other) credit committees.

Belfius has a hierarchically organized structure of credit committees and delegation rules:

- this implies that decisions are made by a higher decision level as the amount of the credit transaction increases and/or the rating quality of the counterparty declines;
- credit committees have in general equal numbers of Risk or Credit department and Business representatives, and are always chaired by a Risk or Credit department member;
- Belfius relies increasingly on an advanced and automated decision-taking process with behavioral or financial indicators - determined by Risk - as cornerstones;
- furthermore, credit (and risk) committees are to a significant extent regionalized, strengthening the principle of decision-by proximity.

Once Belfius has credit commitments on a counterparty, it is essential to monitor and control the risk evolution, in order to take corrective measures in case of quality deterioration and, when appropriate, to establish provisions for expected credit losses:

- to this end, Belfius has set up an early warning system based on behavioral and/or financial indicators;
- counterparties showing signs of weakness are closely followed by the Watchlist Committees, whose main task is to detect emerging risks as quickly as possible and to monitor them subsequently;
- in this context, Belfius strictly applies the directives of the EBA regarding Forbearance measures, i.e. all concessions towards debtors facing or about to face difficulties in meeting their financial commitments;
- a counterparty that seriously fails to meet its obligations towards the Bank receives a default status; the formal decision is the competence of Belfius' Default Committee, composed exclusively by members of the Risk department;
- the Impairment Committees decide on the adequate impairment levels for exposures in respectively Stage 1 (performing), Stage 2 (performing but significant credit deterioration since inception) and Stage 3 (default status).

Next to all afore-mentioned committees, Belfius also disposes of a set of:

- credit risk committees whose core mission is to provide an effective credit management oversight and steering regarding all business segments;
- Methodological committees whose main aim is to validate the internal rating systems and to ensure quality control.

We refer to II.2.3.3.3 for more information on the governance of credit committees.

The description of the internal rating process and the main control mechanism are described in the Appendix XI.2.2. and XI.2.3.

More details on the definition of default are provided in the Appendix XI.2.1.



## IV.3.2. Credit risk mitigation techniques

### IV.3.2.1. Description of the Main Types of Credit Risk Mitigants (CRM)

A Credit Risk Mitigant (CRM) is a technique used to protect or mitigate the credit risk associated with one or more risk exposures. Based on the regulation, CRMs can be classified into two main categories:

#### 1. Funded CRMs, encompassing:

- On balance-sheet netting;
- Netting agreements (covering repo-style transactions or OTC derivatives);
- Collaterals:
  - cash, debt securities, equities, gold, ...;
  - immovable property collateral,
  - receivables,
  - leasing,
  - other physical collateral (e.g. on floating charge).

#### 2. Unfunded CRMs, encompassing:

- Guarantees;
- Credit derivatives.

Immovable property collateral can be in the form of mortgages or mortgage mandates on physical assets such as homes, commercial property or vessels. In addition, loan agreements may contain a negative pledge clause prohibiting the customer from pledging assets to other lenders.

Guarantees can be given by private individuals, companies, national or regional governing bodies, municipalities, guarantee institutes and banks. As it is the case for the original obligor, the guarantor will be attributed a rating taking into account its debt-servicing capacity and financial wealth to intervene when the former goes into default. The rating of the guarantor is subject to an annual review in order to capture recent and forward-looking evolutions of his financial performance and his financial strength. Legal restrictions to use a guarantee as CRM are taken into account as well.

The main principle for valuing collateral is to determine and make use of the expected realisation value at the time of a possible future default when the Bank might have to realise the collateral. The valuation of collateral used in the credit origination and life-cycle:

- must be done in connection with all new credit applications;
- periodically during the credit life cycle in a risk-based and proportional manner (depending on the type of collateral, remaining level of credit exposure and evolution of the credit quality of the obligor); and
- are part of the basis for credit decisions and the credit review process.

Credit requests for residential or commercial real estate are considered based on the property's market value, external appraisals or internal value estimates as set out in Belfius' internal credit risk guidelines.

Financial collaterals are considered based on their market value with haircuts for market volatility, correlation with obligor and holding period. In order to reduce the risk, margin calls can be added to the loan or the pledge agreement. The use of financial collateral (except for cash in the case of derivatives transactions) is rather limited.

For Corporate and Specialized Lending credit files, in addition to the credit quality assessment and the credit risk mitigation techniques, moral commitments may be added e.g. in the form of financial covenants in order to monitor the evolution of the financial performance of the obligor and to take precautionary actions in case of non-respect. Examples of financial clauses are requirements for Net Debt/Ebitda (leverage) and minimum level of equity (solvency).

In the context of the government measures during the Covid-19 crisis to support the Belgian economy, a state guarantee mechanism has been put place in two phases.

The guarantee scheme is detailed further in section IV.1.1.



### IV.3.2.2. Policies and Processes

Within Belfius, managing the CRM involves the following tasks:

- analysis of the eligibility of all CRM under the Standardised and Advanced Approaches;
- collateral valuation in mark-to-market;
- description of all CRM characteristics in internal Risk Systems, such as:
  - mortgage: rank, amount and maturity;
  - financial collateral: valuation frequency and holding period;
  - guarantee/credit derivative: identification of the guarantor, analysis of the legally mandatory conditions, check whether the credit derivative covers restructuring clauses;
  - security portfolio: description of each security.

All relevant data concerning eligibility criteria, minimum requirements, specific characteristics and valuation are captured in various IT tools and detailed procedures are documented and implemented in the internal management process, both in line with the Basel II standards (Basel III for OTC and SFT).

More specifically, Belfius applies prudent collateral valuation rules integrating adequate haircut layers based on the relevant items influencing the value of the collateral for the Bank. Depending on the nature of the collateral, revaluation procedures based on automated information flows, on indexes or expert analysis are in place.

### IV.3.2.3. Regulatory Treatment

For derivatives and securities financing transactions netting agreements, Belfius recognises their impact (subject to eligibility conditions) by applying the netting effect of these agreements on the calculation of the Exposure at Default (EAD).

For guarantees and credit derivatives, Belfius recognises the impact by substituting the PD, LGD and risk weight formula of the guarantor to those of the borrower (i.e. the exposure is considered to be directly towards the guarantor) if the risk weight of the guarantor is lower than the risk weight of the borrower.

For financial and physical collateral, Belfius methodology relating to eligible CRM depends on the approach:

- IRB Approach:
  - for retail exposures, CRM are incorporated into the calculation of LGD based on internal loss data and calculated by the AIRB Approach models;
  - for non-retail exposures, an unsecured LGD is used, CRM (after regulatory haircuts) are taken into account directly through the EAD.
- Standardised Approach: eligible CRM (after regulatory haircuts) are directly taken into account in the EAD.

In the Risk report annex, following detailed specifications are provided:

- an overview of the credit mitigation techniques (Table CR3);
- for exposures under the standardised approach, details on the effect of credit risk mitigation techniques and the decomposition in risk weight bands (Tables CR4 and CR5);
- for exposures under the IRB approach, the same information for the significant portfolios (Table CR6);
- further details on the specialised lending activity under the slotting approach (Table CR10).





## IV.4. Counterparty credit risk

### IV.4.1. Management of the risk

A counterparty credit risk on derivatives exists in all Over-The-Counter (OTC) transactions such as interest rate swaps, foreign exchange swaps, inflation or commodity swaps, credit default swaps and securities financing transactions.

Counterparty credit risk is measured and monitored according to the general principles described in Belfius credit risk policies.

The exposure at default for derivative transactions is based on the mark-to-market value of the derivatives plus the application of an add-on, which is a regulatory percentage of the notional amount of the derivative (percentage depending of maturity and type of derivative).

To reduce the counterparty risk, Belfius OTC derivatives are in most cases concluded within the framework of a master agreement (taking into account the general rules and procedures set out in Belfius credit risk policies). Collateral exchanges for derivative contracts are regulated by the terms and rules stipulated in the Credit Support Annex (CSA).

The exposure at default for securities financing transactions is based on the cash or securities given, reduced by the collateral received (cash or securities) taking into account regulatory haircuts of the financial collateral comprehensive method. Also, Belfius applies netting when eligible agreements (GMRA or GMSLA) are in place.

All OTC transactions are monitored within the credit limits set up for each individual counterparty. Sub-limits may be put in place per type of product.

An adjustment, called Credit Value Adjustment (CVA) reflecting the market value of the counterparty credit risk, is calculated on all non-collateralised derivatives (concluded with a limited number of counterparties, such as local authorities, project SPVs, some corporates or monoline insurers), as well as on collateralised derivatives (although limited in credit risk amount due to the daily exchange of collateral). This adjustment is updated, monthly, based on the evolution of the value of the derivatives and the credit quality of the counterparty. Note also that, along the credit value adjustment, other types of adjustments are applied on derivatives (funding value adjustment, debit value adjustment).

### IV.4.2. Counterparty credit risk exposures

Exposures to counterparty credit risk, including exposures to central counterparties are detailed in the Risk Report annex (tables CCR1, CCR3, CCR4 and CCR8).



### IV.4.3. Counterparty credit risk mitigation

The impact of credit risk mitigation techniques is illustrated in the Risk report annex (tables CCR1, CCR5-A and CCR5-B).



The current net credit exposure at year-end 2020 was EUR 5,670 million.

Concentration limits are an essential part of the Risk Appetite Framework of Belfius and are monitored on a continuous basis. This also includes concentrations that might arise following credit risk mitigation techniques. As of Q4 2020 there are no concentration arising from credit mitigation which exceed the maximum limits of the Risk Appetite Framework.

### IV.4.4. Credit derivatives exposures

Exposures to credit derivatives transactions in the trading portfolio, are detailed in the Risk report annex (Table CCR6).



The portfolio contains:

- Single-name CDS: portfolio of back-to-back or open derivatives where protection is sold to banking counterparts and protection is bought from an A+ rated insurance counterpart. The sold derivatives are collateralized while the bought derivatives are not;
- Index CDS are used as mitigants of the CVA risk;
- Total return swaps: back-to-back portfolio of derivatives where protection is bought from an A rated banking counterpart and sold to an SPV. The bought derivatives are collateralized while the sold derivatives are not.

## IV.4.5. Credit valuation adjustment

The Credit Valuation Adjustment (CVA) is the price of the default risk for a derivative or portfolio of derivatives with a particular counterparty considering the effect of offsetting collateral. In other words, it is the difference between the risk-free portfolio value and the true portfolio value that takes into consideration the possibility of a counterparty's default.

As such, the CVA represents an estimate of the adjustment to fair value that a market participant would make to incorporate the credit risk of the counterparty due to any failure to perform on contractual agreements.

The capital charge for CVA risk is calculated according to the standardised approach.

The CVA RWA decreased with EUR 642 million to EUR 740 million due to active management of counterparty credit risk including additional CVA hedges, unwind of uncollateralised swaps with financial counterparts and an increased use of CCP clearing.



CVA capital charge is detailed further in the Risk report annex (Table CCR2).

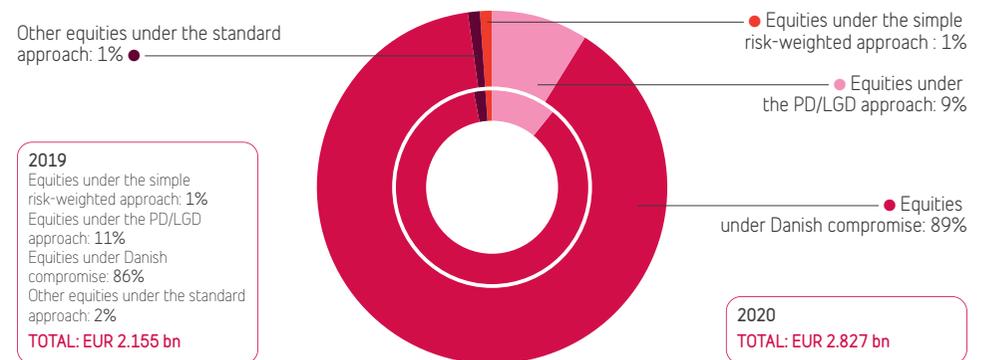
## IV.5. Focus on equity exposure

For the calculation of the capital requirement for equity exposure, Belfius Bank applies the PD/LGD method. If the PD/LGD method cannot be applied (e.g. no available ratings), the simple risk weight method is used.

Besides:

- at the beginning of 2014, the NBB granted the Danish Compromise option (financial conglomerate) to Belfius allowing a new prudential treatment for Belfius Insurance participation and subordinated debts (370% risk weight);
- items classified as significant investments according to Article 48 of Regulation 575/2013 are weighted at 250%.

### Equity method by exposure (Outside 2020 - Inside 2019)



Further details are provided in the Risk report annex (Tables CR10\_B, INS1 and CR5).

For information on Belfius Insurance equity exposure, we refer to the chapters Risk Management of the Annual Report 2020 of Belfius Insurance, Risk Management and the Belfius' Management report (see dedicated section on insurance risks).



## IV.6. Securitisation risk

Depending on the role played by Belfius Bank regarding securitisation transactions, the objectives can vary from bringing differentiation in the long-term funding mix, reduction of the economic capital requirement or improvement of the risk-return ratio.

Belfius Bank currently has two types of transaction. It has retained asset-backed securities which can for instance be used as collateral for secured funding agreements. In other transactions, the senior tranches were placed with external investors to raise long-term funding.

### IV.6.1. Objectives and roles of Belfius Bank

As Originator: Belfius Bank carries out securitisation transactions related to various asset classes: mainly residential mortgage loans, public finance loans and loans to SMEs. These transactions are in general carried out with a view to optimising the liquidity and funding profile.

The securitisation activity as originator is described in the Section VI.2.

As Servicer: In transactions where Belfius Bank is the originator, Belfius Bank in general continues to service the assets being securitised.

As Arranger of Securitisation Transactions for Customers: Belfius Bank acts as arranger or advisor on securitisation transactions for customers. In these instances, Belfius Bank will structure or advise on the securitisation transaction (or part of a transaction) and could take up other roles such as hedging counterparty, account bank or liquidity provider at arm's length market rates. In general, Belfius Bank receives fees for structuring or advising on transactions.

Another Role: depending on the specific details of a transaction, Belfius Bank may undertake various roles in securitisation transactions ranging from account bank to hedging provider or liquidity facility provider. Belfius Bank may also act as calculation agent, paying agent or corporate services provider.

Belfius Bank does not act as a sponsor for ABCP, third party assets or multi-seller programmes, and it does not provide liquidity facilities to such programmes.

### IV.6.2. Securitisation activity as investor

At the end of 2020, the Belfius Bank's investment portfolio was EUR 358 million, compared to EUR 486 million at the end of 2019.

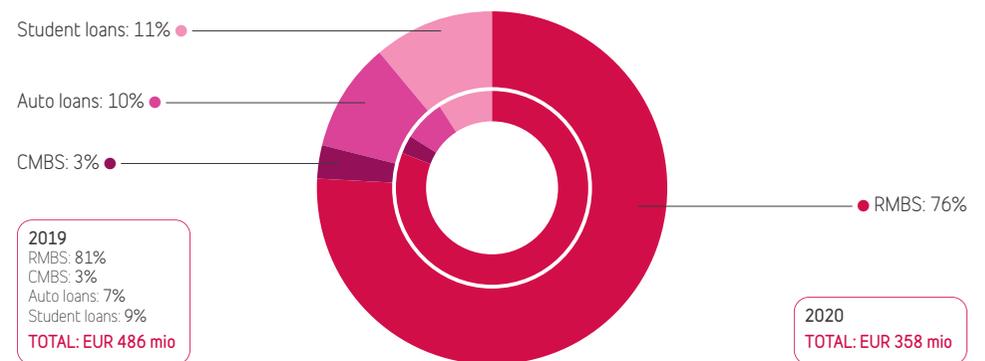
The decrease is the result of the amortisation of the existing portfolio (EUR -128 million).

The portfolio is only composed of senior granular ABS transactions and EUR 110 Million of this exposure are STS securitisations.

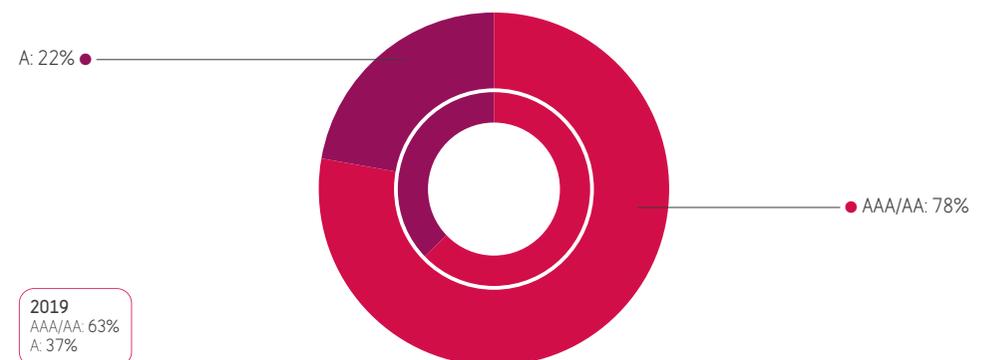
Further details on underlying assets and capital requirements are provided in the Risk report annex (Tables SEC1 and SEC3).



#### Activity as investor - by underlying (Outside 2020 - Inside 2019)



#### Activity as investor - by rating (Outside 2020 - Inside 2019)





# V. Market risk

## V.1. Overview

### V.1.1. Market Risk Definition

Overall, market risk can be understood as the potential adverse change in the value of a portfolio of financial instruments due to movements in market price levels, to changes of the instrument's liquidity, to changes in volatility levels for market prices or changes in the correlations between the levels of market prices.

Management of market risk within Belfius encompasses all Financial Markets activities of the Bank and focusses on interest rate risk, credit spread risk, foreign-exchange risk, equity risk (or price risk), inflation risk and commodity price risk.

In the Risk report we make the distinction between the Structural & ALM risk on the one hand and Trading Market Risk on the other hand.

Market risk of Belfius Insurance is separately managed by its ALCo's. Belfius Insurance's ALCo makes strategic decisions affecting the balance sheets of the insurance companies and their financial profitability taking into consideration the risk appetite pre-defined by the Belfius Bank and Insurance group (i.e. directional ALM position in interest rate risks, equity and real estate risks, volatility and correlation risks).

### V.1.2. Risk types

The sources of market risk are changes in the levels of:

- interest rates;
- credit spreads;
- inflation;
- foreign-exchange rates;
- equity prices;
- commodity prices;

and their related risk factors like volatility or correlation for example.

Interest rate risk may be understood as the variation of the value of assets or liabilities of the Bank following changes in interest rates quoted on the markets. It is most pronounced in debt instruments, derivatives that have debt instruments as their underlying reference asset and other derivatives whose values are linked to market interest rates.

Credit spread risk is linked to the credit spread curve that can change for a counterparty even if the credit quality (rating) remains the same. This impacts the XVAs and mainly the Credit Value Adjustment (CVA).

Foreign-exchange risk is the potential risk that movements in exchange rates may adversely affect the value of a financial instrument or portfolio. Despite exchange rates being a distinct market risk factor, the valuation of foreign-exchange instruments generally requires knowledge of the behaviour of both spot exchange rates and interest rates.

Equity price risk is the potential risk for adverse changes in the value of an institution's equity-related holdings. Price risks associated with equities are often classified into two categories: general (or non-diversifiable) equity risk and specific (or diversifiable) equity risk.



## V.2. Structural & ALM risk

The low interest rate environment has continued to put pressure on the Net Interest Income of Belfius.

Nevertheless, the negative impact of the continuously increasing volumes of (floored) Non Maturing Deposits has been more than compensated by continuously growing outstanding volumes in loans at higher margins as well as the ALM strategy to protect Belfius' NII against low interest rates for an extended period of time.

### DEFINITION

The structural & ALM risk exposure at Belfius results from the imbalance between its assets and liabilities in terms of volumes, durations and interest rate sensitivity.

In respect to the interest rate risk, Belfius Bank pursues a prudent risk management of its interest rate positions in the banking book within a well-defined internal and regulatory limit framework, with a clear focus on generating stable earnings and preserving the economic value of the balance sheet - macro-hedging approach - thoughtfully considering natural hedges available in the bank balance sheet.

The **long-term sensitivity of the ALM perimeter** was EUR -35 million per 10 bps at 31 December 2020 (compared to EUR -50 million per 10 bps at 31 December 2019), excluding interest positions of Belfius Insurance and of the pension funds of Belfius Bank.

A **50 bps increase of interest rates** has an **estimated positive impact on net interest income (before tax) of EUR +31 million of the next book year and an estimated cumulative effect of EUR +168 million over a three year period**, whereas a 35 bps decrease would lead to an estimated impact of EUR -20 million of the next book year and an estimated cumulative effect of EUR -143 million over a three year period.



For further information on Structural & ALM Risk, we refer to the section on market risk in chapter Risk management of Belfius Management report.

## V.2.1. IRRBB Risk Management

In recent years, the interest rates have continuously decreased while the amount of non-maturing deposits are ceaselessly increasing (+EUR 7.2 billion over 2020). These trends are being reinforced by the Covid-19 crisis. This low rate environment puts pressure on the pricing of commercial loans on the one hand and keeps compressing margins in bank's deposit and sight accounts on the liability side of our balance sheet, on the other hand. Consequently, Belfius is actively managing its interest rate risk to maintain a solid level of profitability keeping its core banking business activities running and to continue to strengthen the Belgian real economy. In this respect, Belfius Bank continues to pursue a prudent risk management of its interest rate positions in the banking book thanks to its well defined internal and regulatory limit framework.

Even though Belfius has demonstrated an excellent resilience in terms of profitability despite the current difficult economic and market environments, an important focus is still given to challenge the current Interest Rate Risk framework and fine tune our general Interest Rate Risk strategy. The complexity of this continuous assessment relies on the management of key models and assumptions around Interest rate Risk mainly relying on two main indicators complemented by several scenarios' analyses. Firstly, the Earning-at-Risk indicator (EaR) is used to assess proactively the impact on the Net Interest Income induced by potential changes of interest rates over time. Secondly, the economic value of equity (EVE) indicator which calculates the long-term effect of interest rate changes on the economic value of Belfius Bank (Net Present Value of Assets minus Net Present Value of Liabilities) under certain conditions is used.

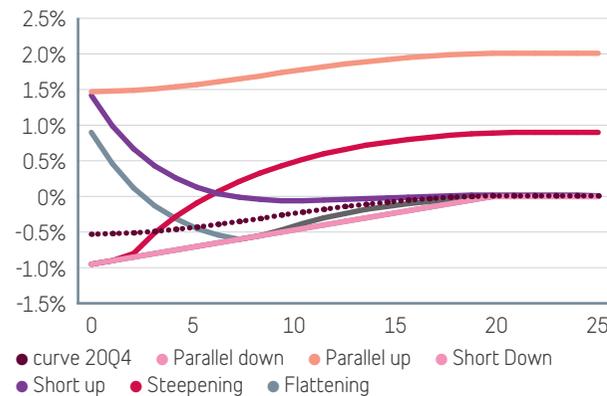
Considering the low rate environment and increasing uncertainties driven mainly by the Covid-19 outburst, Risk management drew a specific attention in 2020 to challenge all material components of the ALM IRRBB framework. A deep review of the models and assumptions used in the management of the non-maturing deposits, such as sight and saving accounts, took place targeting among other topics the expected duration at granular level, rate-fixing periods, the prepayment model and the tariff function evolution. By means of replicating independently the work performed by the ALM team in this field, challenging the assumptions by applying different scenario's (e.g. Monte-Carlo simulations) or performing some reverse stress-testing exercises, the ALM Risk Team has confirmed the detailed proposals of the Finance department.

Based on its independent analyses, risk has shown that Belfius general strategy in the fields of diversification, cross-selling and interest rate risk management is key to maintain our profitability level. Nevertheless, ALM Risk strongly recommended to keep focusing on alternative protection to change of rates like keeping expanding our Negative Interest Rate Policy and continuing the reinforcement of our Risk-Based pricing process. Also, a risk dashboard has been created in 2020 to monitor and proactively detect signals alerting on an increased probability to see potential rise of interest rates or other behavioural trends (e.g. prepayment wave). Finally, it was also recommended to regularly assess our framework in light of recent and new available information related to the Covid-19 crisis to tackle as soon as possible its related level of uncertainties.

### Value impact

(mio EUR)	31/12/2020
Parallel down	53
Parallel up	-1,468
Short Down	92
Short up	-115
Steepening	-408
Flattening	-21

### Scenarios





## V.3. Market Risk – Trading Market Risk

The Covid-19 crisis was in the (first) heat of the crisis particularly hard on financial markets, resulting in very high volatility of equity prices, counterparty credit spreads (that enter our P&L via XVA) and lower rates. Even during the initial shock of the crisis the following actions were taken to reduce P&L volatility and de-risk legacy positions:

- More active management of both the XVA and credit derivatives positions.
- De-risking of Legacy swap positions with a strong focus on non collateralised derivatives.
- De-risking of Legacy trading positions for which Belfius has a NBB derogation.
- De-risking of the bond portfolio: a strong reduction in Italian sovereign exposure was realized due to the sale of Italian Government bonds at the of Q4.

The Brexit uncertainty combined with the Covid-19 crisis also resulted in quite some volatility in the UK real rates which impacts directly the Risk weighted exposure (not profit & loss) via Belfius' ex-legacy UK inflation bonds.

### DEFINITION

Overall, market risk can be understood as the potential adverse change in the value of a portfolio of financial instruments due to movements in market price levels, to changes of the instrument's liquidity, to changes in volatility levels for market prices or changes in the correlations between the levels of market prices.

### ITRAXX 5Y/10Y EVOLUTION OVER 2020



### EVOLUTION OF UK REAL RATE EVOLUTION OVER 2020





Financial Markets activities encompass client-oriented activities and hedge activities at Belfius Bank. No Financial Markets activities are undertaken at Belfius Insurance. For their needs in Financial Markets products, they turn to Belfius Bank or other banks.

### V.3.1. Fundamentals of market risk in 2020

The Covid-19 crisis was in the (first) heat of the crisis particularly hard for our counterparty credit spreads (translated into Fair Value through P&L via XVA). Quick action at the start of the crisis resulted in maximum closing of open positions and buying proxy-hedge credit protection through iTraxx / OLO. This reduced the credit spread sensitivity drastically but did not result right away in a stabilization of the P&L also due to the extreme market shocks that resulted in model issues on illiquid positions, which were resolved after the initial shock.

In the second half of the year, many of the losses were recuperated due to credit spreads returning to pre-crisis levels. This pattern was also observed on typical mean-reverting parameters that are difficult to hedge like the CDS-bond basis and funding curve used for FVA calculation.

The other remaining risk sensitivities, although well within limits at the beginning of the crisis, created losses mostly due to the worldwide drop in equity, equity volatility rise and deformation of interest rate curves. Also, for these risks, maximum reduction of open sensitivities was executed in the first week of the crisis and permanent monitoring between Risk and FO was put in place.

After the initial shock of the crisis the following actions were taken to reduce P&L volatility, de-risk legacy positions and improve RWA levels:

- more active management of both the XVA and credit derivatives positions;
- de-risking of Legacy swap positions with a strong focus on non-collateralised derivatives;
- de-risking of Legacy trading positions for which Belfius has an NBB derogation;
- de-risking of the bond portfolio: a strong reduction in Italian sovereign exposure was realized due to the sale of Italian Government bonds at the of Q4.

The Brexit uncertainty combined with the Covid-19 crisis also resulted in quite some volatility in the UK real rates. Belfius is well hedged in terms of profit & loss fluctuations but remains due to his ex-legacy UK Water Inflation bonds very sensitive to RWA volatility linked to shifts in the UK real rate.

Another driver of fair value through P&L volatility within the Financial Markets perimeter is related to the Belfius funding cost which is based on wholesale funding and is translated in XVA mostly for non-collateralised deals and CCP cleared derivatives.

With regards to the regulatory Internal Model and the back-testing, seen the volatility of the financial markets, 2020 was characterized by 5 negative back-testing exceptions. However, due to ECB intervention, firstly by not counting temporarily certain exceptions and secondly by receiving authorization to definitively remove 3 Covid-19-related exceptions, there was only limited impact on capital requirements for market risk. Belfius also received approval to reduce the multiplier for HVaR from 4 to 3.75 (structural measure).

A better recurrent reporting of the Financial Market activities up to the Board of Directors as well as an improved Risk Appetite Framework (RAF) were realised in 2020. Apart from the refined Market Earnings at Risk indicator, the VaR has now been included in the RAF.

### V.3.2. Market risk governance

With the purpose of effectively managing the market risks Belfius Bank is facing, FM Risk Management has identified the following cornerstones as key pillars for the risk management of its Financial Market (FM) activities:

- an efficient organisation fostering an accurate identification, analysis and reporting of the different risks Belfius Bank is bearing, as well as a continued training of people in order to remain up to date with the latest evolutions in theories, regulatory issues, metrics or market changes;
- a robust limit framework with differentiated limits by activity or risk factor that is to be respected by all parties involved in market activities. On top of the VaR limits or P&L triggers, several other metrics have been identified as key controlling tools in the risk management process:
  - limits on notional amounts;
  - limits on maturities;
  - limits on type of products;
  - limits on sensitivities (known as “Greeks”: delta, etc.);
  - back testing;
  - stress tests;
- finally, this framework is regularly submitted for revision to the FM Committee in order to be commensurate to the risk appetite defined by the Board of Directors of Belfius Bank.



## Committees

The Financial Markets Committee (FMC) is the main committee for Financial Markets Management. Its main objective is to provide effective risk management oversight and steering of the Financial Markets activities. This includes reviewing business, risk and P&L reports, and providing an appropriate risk management and governance framework aligned with the RAF and business objectives set forward by the Management Board. As a consequence, the FMC is responsible for determining market risk limits consistently with the Market Risk Appetite.

The Risk Policy Committee validates all major changes in risk governance. For the sub-committees, we refer to II.2.3.3.2.

## V.3.3. Market risk measures

### Evolution of global VaR in 2020

In EUR million



The Value-at-Risk (VaR) concept is used as the principal metric for proper management of the market risk Belfius Bank is facing. The VaR measures the maximum loss in Net Present Value (NPV) the Bank might be facing in normal and/or historical market conditions over a period of 10 days with a confidence interval of 99%. The following risks are monitored at Belfius using a VaR computation:

- the interest rate, inflation and foreign exchange (forex) rate risk: this category of risk is monitored via a historical VaR based on an internal model approved by the National Bank of Belgium. The historical simulation approach consists of managing the portfolio through a time series of historical asset yields. These revaluations generate a distribution of portfolio values (yield histogram) on the basis of which a VaR (% percentile) may be calculated. The main advantages of this type of VaR are its simplicity and the fact that it does not assume

a normal but a historical distribution of asset yields (distributions may be non-normal and the behaviour of the observations may be non-linear);

- the general and specific equity risks are measured on the basis of a historical VaR with full valuation based on 300 scenarios;
- the spread risk is measured via a historical approach, applying 300 observed variations on the sensitivities.

To reduce the Earnings-at-Risk of financial markets, the overall FM VaR limit was reduced in the June FMC, by eliminating parts that were no longer or only partly used.

## V.3.4. Market risk exposure

The overall average VaR of Financial Markets activities increased to EUR 14.7 million in 2020 vs EUR 12.9 million in 2019.

### Value-at-risk by activity

VaR <sup>(1)</sup> (99% 10 days) (In EUR million)	31/12/2019				31/12/2020			
	IR <sup>(2)</sup> & FX <sup>(3)</sup>	Equity	Spread	Other risks <sup>(4)</sup>	IR <sup>(2)</sup> & FX <sup>(3)</sup>	Equity	Spread	Other risks <sup>(4)</sup>
By activity								
Average	6.8	4.8	0.7	0.7	7.3	5.8	1.2	0.4
EOY	6.0	4.4	0.3	0.4	8.7	6.2	0.5	0.4
Maximum	11.6	7.6	2.2	1.5	12.3	8.4	3.6	0.4
Minimum	3.5	3.7	0.2	0.4	4.5	2.6	0.2	0.3
Global								
Average	12.9				14.7			
EOY	11.2				15.8			
Maximum	18.4				21.5			
Minimum	9.1				9.4			
Limit	26.5				24.3			

(1) The Value at Risk (VaR): is a measure of the potential change in market value with a probability of 99% and over a periode of 10 days.

(2) IR: interest rate risk and inflation risk.

(3) FX: forex risk.

(4) CO<sub>2</sub> risk.

The VAR decreased first part of 2020 but increased sharply during the first heat of the Covid-19 crisis in March and continued to fluctuate. During the third quarter, the VAR decreased due to closing positions and market value evolutions. There was a slight increase during the final quarter.



## V.3.5. Stress testing

Although the VaR is a very useful risk management tool for controlling day-to-day loss-risk exposures, it does not fully withstand the test of abnormal market movements, and it does not always give a total accurate picture of market exposure. Stress tests reveal sometimes better such information by gauging Belfius' vulnerability of the market position to exceptional events and hence by providing additional information about market risks alongside the information embedded in the VaR. These risks include those associated with extreme price movements and those associated with scenarios not reflected in recent history or implied by the parameters used to compute the VaR. Consequently, Belfius Bank uses stress tests in addition to the VaR approach.

The stress test framework has been reviewed (update of the scenarios) and the scope has been enlarged to include stress tests on Fair Value Hedge positions, XVA and Credit Derivatives.

Three types of scenarios are considered: calibrated scenarios (shocks on each risk factor, calibrated as quantiles of their historical distribution), specific scenarios (specific shocks on some risk factors) and historical scenarios (scenarios based on previous crises).

The results of these stress tests are monthly reported in the FM Risk Monitoring Report and Quarterly to the FMRR.

## V.3.6. Regulatory internal model and back testing

### Evolution HVaR and SVaR (internal model) in 2020

In EUR million



Belfius Bank uses its internal VaR model for the regulatory capital requirement calculation on foreign exchange risk and general interest rate risk within the trading scope.

Beside the VaR described above, Belfius Bank calculates a Stressed VaR (SVaR). The SVaR is computed on a weekly basis using 250 historical daily evolutions of parameters from the period May 2008-June 2009.

The regulatory capital is calculated by using both the VaR and the SVaR. In 2020, the Internal Model VaR amounted to EUR 10.1 million on average versus EUR 13 million for the SVaR.

The other market risks are treated under the Basel Standardized approach.

Further details are provided in the Risk report annex (Tables MR1, MR2-A, MR3 and OV1). 

The aim of back testing is to test the accuracy and the mathematical soundness of the internal market risk measurement methodologies by comparing the calculated market risk figures with the volatility of the actual results. Back testing is a prerequisite for Belfius Bank since we use internal models to calculate the regulatory capital requirement for market risks.

The result of the back test is the number of actual market losses greater than their corresponding VaR figures (i.e. "the number of exceptions"). According to this number, the regulators will also decide on the multiplier to be applied for determining the regulatory capital requirement for market risks.

Currently, two types of back testing are processed at Belfius Bank:

- Hypothetical back testing compares the hypothetical results of the portfolio's end-of-day value and, assuming unchanged positions, its value at the end of the subsequent day. This result is therefore without any provisions adjustments and other non-involved risk factors. The holding period is one day. During 2020, there were 5 negatives exceptions to the hypothetical back testing. This results from the worldwide financial crisis following the Covid-crisis in March. Therefore, the ECB decided to not take into account the exceedings procured during this crisis. As a result, only 2 negative exceedings are officially taken into account for the calculations of the RWA during 2020.
- Real back testing compares the portfolio's end-of-day value and its actual value at the end of the subsequent day excluding fees, commissions, and net interest income. In 2020, there were 4 exceptions to the real back testing, but only 1 is taken into account due to exclusion of the ECB.

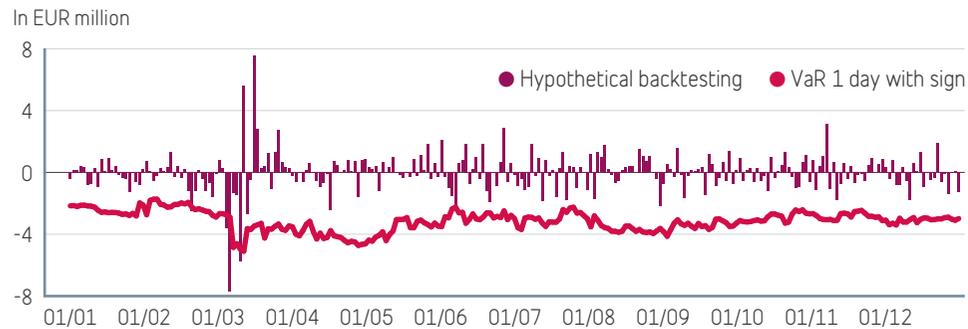


The back-testing processes provide therefore a view of the number of (hypothetical and real) exceptions. The maximum between these two numbers is taken into account to adjust the VaR & SVaR multiplier used for calculating the Bank's risk capital requirements for market risk under the internal model approved by the regulator. After ECB revision of the Internal Model quality, the multiplier factor for the HVAR dropped from 4 to 3.75 end December.

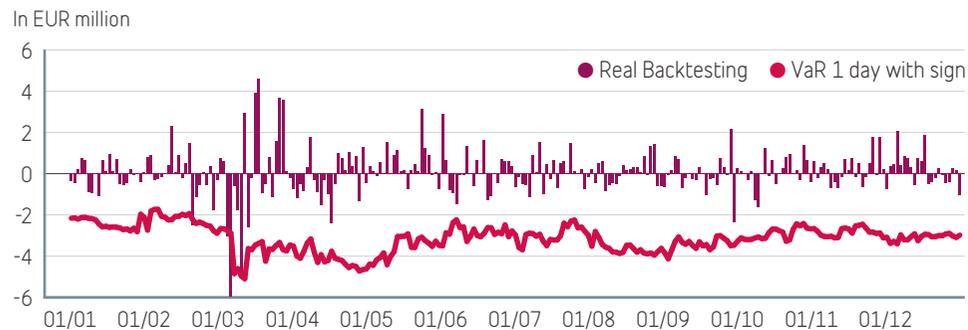
At the end of 2020, the RWA for market risk under the internal model approach was EUR 1,055 million.

The following charts show real and hypothetical back testing in 2020 for interest rate and foreign exchange perimeters:

### Hypothetical Back Testing



### Real Back Testing



## V.3.7. Validation

Validation is responsible for the independent overall assessment of the market risk and valuation models. The process set up to endorse the validation of models deployed within Belfius Bank is multi-layered, ensuring compliance with regulatory requirements. Validation controls the models from a methodological but also an operational (implementation, usage) viewpoint. It intervenes prior to the first use of a new model or of any significant change of an existing model. It also reviews periodically the performance of the models. Validation works are summarised in reports indicating the controls that were performed, their findings, proposed corrective actions and a validation status.

The decisions regarding the Market models are taken by the FMFV Committee, composed of the CRO, the CFO, the Board Member in charge of Financial Markets and their direct reports in charge of Market activities:

- green light to put new models or model updates in production;
- endorsement of the corrective action plans recommended by Validation.

Once a year the Management Board and the Risk and Audit Committees are informed of the status of the Market Models (evolutions, points of attention, outlook).

## V.3.8. Systems and controls

On a daily basis, FM Risk Management follows up, analyses and reports the risks and results of the FM desks. On a monthly basis, the FM Committee (FMC) meets to discuss the risks and results, the market limits, procedures, guidelines and policies and approves or amends new valuation methodologies.

All market activities are backed by specific guidelines describing the objectives, the authorised products, sensitivity, VaR and/or outstanding limits. The systems and controls that are established within Belfius are described in various procedures to ensure a complete and formal framework that is established to support all market risk responsibilities.



# VI. Liquidity risk

During 2020, Belfius further strengthened its liquidity position:

- The commercial activities delivered a funding surplus as the increase of deposits has been higher than the increase of the outstanding of commercial loans.
- Belfius increased its participation to the TLTRO and reached a total amount of TLTRO III funding of EUR 14.3 billion.
- Belfius issued EUR 0.5 billion Covered Bonds, EUR 0.5 billion Preferred Senior Bonds and EUR 0.5 billion Non-Preferred Senior Bonds. On top of the liquidity benefit, the Preferred and Non-Preferred Senior Bonds will enable Belfius to further contribute to the MREL requirements.

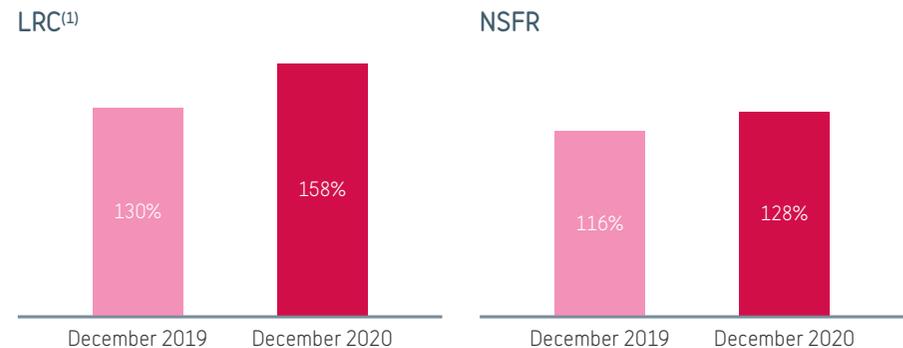
## DEFINITION

The liquidity risk at Belfius Bank is mainly stemming from:

- the variability of the amounts of commercial funding collected from Retail and Private customers, small, medium-sized and large companies, public and similar customers and the way these funds are allocated to customers through all type of loans;
- the volatility of the collateral that is to be deposited at counterparties as part of the CSA framework for derivatives and repo transactions (so called cash & securities collateral);
- the value of the liquid reserves by virtue of which Belfius Bank can collect funding on the repo market and/or from the ECB;
- the capacity to obtain interbank and institutional funding.

## LCR & NSFR

Strong liquidity stance, even further boosted by Covid-19 crisis



(1) Calculation based on 12 months average



Belfius Bank manages its liquidity with a view to comply with internal and regulatory liquidity ratios. In addition, limits are defined for the balance sheet amount that can be funded over the short term and on the interbank market. These limits are integrated in the Risk Appetite Framework (RAF) approved by the Board of Directors and reported on a quarterly basis. Available liquidity reserves also play a key role regarding liquidity: at any time, Belfius Bank ensures it has sufficient quality assets to cover any temporary liquidity shortfalls, both in normal markets and under stress scenarios. Belfius Bank defined specific guidelines for the management of LCR eligible bonds and non LCR eligible bonds, both approved by the Management Board.

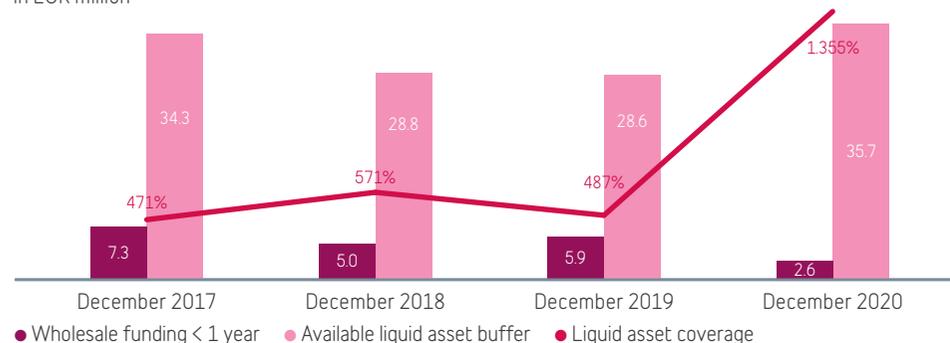
Given its solid liquidity position, Belfius' funding plan is more than ever driven by MREL requirements rather than by an expected liquidity shortfall.

Given the T-LTRO III drawing of EUR 14.3 billion, less short-term Wholesale funding has been attracted than previous years.

For the liquidity risk in general, we refer to the section Liquidity risk in the chapter Risk management of Belfius' Management report. We provide some additional focuses here below.

### Exceptional refinancing need coverage

In EUR million



## VI.1. Covered bond activity

Belfius Bank has set up 2 programmes for the continuous offer of Belgian pandbrievens (Belgische pandbrievens/lettres de gage belges) in accordance with the legal framework for Belgian covered bonds, i.e. a Mortgage Pandbrievens and a Public Pandbrievens programme.

The main asset class of the special estate of the Mortgage Pandbrievens programme consists of residential mortgage loans that were originated by Belfius Bank. The main asset class of the special estate of the Public Pandbrievens programme consists of public sector loans that were originated by Belfius Bank.

Over the course of 2020, Belfius Bank issued a nominal amount of EUR 2.5 billion of Mortgage Pandbrievens and no Public Pandbrievens have been issued.

The main characteristics of those 2 programmes are provided in Appendix XI.3.2. and XI.3.3.



## VI.2. Securitisation activity as originator

The steering of the set-up for securitisation transactions is performed by the FIG & Structured Finance department with the support of the dedicated organisation/project management departments. As such, both prior to and after the closing of a transaction, transversal task forces are set up including all relevant departments, such as accounting, asset and liability management, credit risk, market risk, back-office, transaction processing, etc.

Post-closing, the transaction follow-up concerns the efficiency and effectiveness of the servicing, the appropriate monitoring of the transaction from a credit, market and liquidity risk perspective as well as the reliability of the reporting being produced.

All outstanding transactions were carried out with a view of obtaining long-term funding or establishing a liquidity buffer.

No assets have been originated with the intention to securitise. The underlying assets have been originated in the regular course of lending business to retail, public and corporate customers of Belfius Bank. Hence no assets on the balance sheet awaiting securitisation can be identified as such. Only performing assets are included in the securitisation transactions. No profit or losses are realised upon sale of the assets to the SPV.

Engaged ECAs include Moody's, Fitch Ratings, Standard & Poor's and DBRS.

The table shows the securitisation activity (Belfius Bank as originator): amount of exposure securitised, and gains and losses on sales during the period, the amount of underlying assets (amount of defaulted assets disclosed separately) originated by Belfius Bank by nature of securitisation and type of underlying assets.

Belfius Bank has not yet securitised any revolving exposures or liquidity facilities which are shared between investors and Belfius Bank as originator. The main changes impacting 2020 compared to 2019 relate to the amortisation in the underlying portfolios of assets securitised and the exercise of the early redemption call of Penates-5.

31/12/2020 (In EUR million)	Residential mortgage loans	Public sector loans	Corporate & SME exposures	Total
<b>TRADITIONAL SECURITISATIONS</b>				
Underlying assets	3,222	745	843	4,809
Defaulted assets <sup>(1)</sup>	4	0	14	18
of which exposures securitised in 2020 <sup>(2)</sup>	0	0	0	0
Gains and losses on sales in 2020	0	0	0	0
<b>SYNTHETIC SECURITISATIONS</b>				
Underlying assets				
Defaulted assets <sup>(1)</sup>				
of which exposures securitised in 2020 <sup>(2)</sup>				
<b>RELATED SPVS</b>	Penates Funding (Penates-5 Penates-6)	Dexia Secured Funding Belgium (DSFB-2)	Mercurius Funding (Mercurius-1)	

31/12/2019 (In EUR million)	Residential mortgage loans	Public sector loans	Corporate & SME exposures	Total
<b>TRADITIONAL SECURITISATIONS</b>				
Underlying assets	4,685	809	1,071	6,565
Defaulted assets <sup>(1)</sup>	4	0	16	20
of which exposures securitised in 2019 <sup>(2)</sup>	0	0	0	0
Gains and losses on sales in 2019	0	0	0	0
<b>SYNTHETIC SECURITISATIONS</b>				
Underlying assets				
Defaulted assets <sup>(1)</sup>				
of which exposures securitised in 2019 <sup>(2)</sup>				
<b>RELATED SPVS</b>	Penates Funding (Penates-5 Penates-6)	Dexia Secured Funding Belgium (DSFB-2)	Mercurius Funding (Mercurius-1)	

(1) Amount of defaulted assets (as of the date of default) using the definitions used in the securitisation transaction.

(2) Gross amount of exposure (as of year end based on reference obligations).

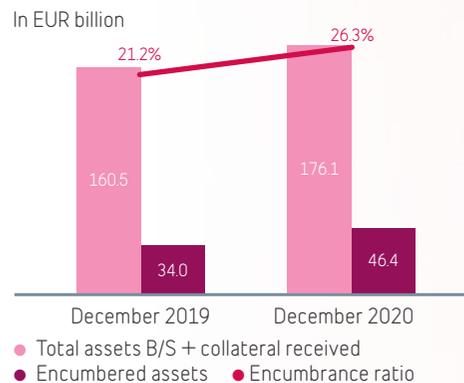


## VI.3. Encumbered assets

The regulatory consolidation scope used for the purpose of the disclosures on asset encumbrance is the same as the scope retained for the application of the liquidity requirements on a consolidated basis as defined in Part II, Chapter 2 of Regulation (EU) No. 575/2013.

Following the EBA instructions, the unused part of pledged assets (i.e. the part above the minimum amount required by the counterparty) should not be considered as encumbered. It is the case, for instance, for the collateral pledged to the ECB.

According to the EBA guideline based on the median values of the encumbrance reportings of the last four quarters, the encumbered assets at Belfius Bank amounted to EUR 46.4 billion end 2020. This represents an increase with EUR 11.5 billion compared to end 2019 (following median values calculation). The Asset Encumbrance Ratio based on the median values results in 26.3% end of 2020. This is in breach with our internal RAF, but given this is mainly due to the TLTRO funding, this breach is accepted.



The encumbered assets are located within Belfius Bank, which is the only banking entity of the group generating encumbrance. The main sources of encumbrance are linked to the TLTRO (EUR 16.4 billion) and the collateral pledged (gross of collateral received) for the derivatives exposures for EUR 14.0 billion (stable compared to end 2019), under the form of cash or securities. A significant part of collateral is financed through collateral received from other counterparties with whom the Bank concluded derivatives in the opposite direction.

Other main sources of encumbrance for funding purposes are loans in cover pools underlying covered bonds issues (EUR 9.7 billion median).

Seen there is no currency representing more than 5% of total Belfius liabilities, all encumbrance figures are computed in EUR only.



Further details are provided in the Risk report annex (Tables AE).

## VI.4. Liquidity risk at Belfius Insurance

For the liquidity risk at Belfius Insurance, we refer to the dedicated section in the Belfius' Management report, chapter Risk management.





# VII. Non-financial risk

Non-Financial Risk Management is growing in importance given evolutions of risks and threats combined with the challenges of the ambitious Belfius Group 2020-2025 strategy.

The reinforcement of the 1<sup>st</sup> line of defence as risk manager and the development of an adequate internal control environment are key factors in the VUCA (Volatile, Uncertain, Complex, Ambiguous) world. The NFR framework has been extended to new areas such as outsourcing risks/ 3<sup>rd</sup> party risks and IT project risk. Traditional operational risks are under control (lower number of incidents and potential net impacts) and continuous efforts are made to keep up to date to the digitalization challenges regarding information security, data related risks and well organized external (phishing) fraud attempts by criminal organizations. The Covid-19 pandemic has taken a lot of attention and efforts. People’s safety and staff motivation as well as business continuity are the priorities while overall resilience is crucial to assure a high service quality level for our clients.

## DEFINITION

The term Non-Financial Risks (NFR) is to be understood as a broad umbrella covering all risks except “financial risks”. They are not only complex and cross-dependent but also not unbounded due to regularly emerging risks.

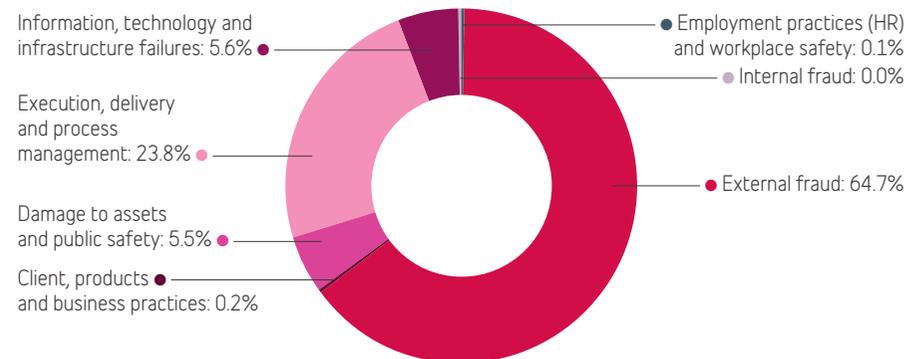
## AVERAGE ANNUAL POTENTIAL NET LOSSES FROM OPERATIONAL INCIDENTS (2018-2020)

EUR  
**2.19** million

5% of events represent  
95% of impact

## OPERATIONAL INCIDENTS

Breakdown of total losses by standard category of incidents over the past three years at Belfius Bank





## VII.1. Fundamentals of Non-Financial Risk in 2020

Non-Financial Risk (NFR) Management is growing in importance given evolutions of risks and threats (VUCA world) combined with an ambitious business strategy. Some examples of this evolving environment are: an increase of IT security concerns everywhere in the world; swift changes in public opinion and regulatory scrutiny about AML and fiscal fraud requiring strong management practices; statistics on external frauds in Belgian banks showing a strong increase in number and amount - the modus operandi also evolving (increased phishing), and so on.

The management of non-financial / operational risks has been integral part of the Belfius' risk management for years and Belfius' operational losses remained relatively low in 2020.

The 2020 main NFR realisations are summarised hereafter:

- successful management and coordination of the Covid-19 crisis with health protection and business continuity as main priorities;
- update of the Risk Appetite Framework with a focus on actionable KRIs and new KRIs related to resource risk, project risk and outsourcing & third-party risk;
- set up of a risk framework for transversal/corporate projects for Belfius Bank;
- additional efforts regarding awareness and ownership of Privacy and GDPR topics at business departments;
- structural integration of the GDPR workflow in the NPAP process, working out advises for strategic files;
- consolidation of the NFR management framework through a clear overview on NFR roles and responsibilities and laying down the foundation for a sound conglomerate NFR management framework.
- strengthening of the outsourcing risk management by developing a risk scoring model, by extending the initial scope to other material arrangements and by paying special attention to GDPR compliance towards 3rd parties;
- major steps for improving the NFR tooling;
- successful execution of all NFR processes despite the crisis situation and management.

Since March, Belgium has been severely affected by the coronavirus (Covid-19), which has led to national confinements and the massive and long-term use of teleworking. Moreover, Belfius has committed itself to providing financial support to individuals and companies for getting through the crisis.

All these measures have led to adapted working methods and processes, but also to a changed environment in which Belfius operates and to which Belfius reacts in line with the following key objectives:

- protecting the health of its collaborators and clients;
- guaranteeing the continuity of its activities and services to the clients;
- communicating constantly and in a timely manner; and
- assuming the responsibilities to be meaningful and inspiring for Belgian society.

During the Covid-19 situation, Belfius gave evidence of operational resilience and successful crisis management thanks to a pro-active approach based on risk analyses and scenarios.

Belfius strictly applied all governments' directives in order to protect the health of its collaborators and clients, inter alia, by distributing shifty protection means and by enabling social distancing in all premises. On its own initiatives and beyond the official directives, additional measures were also taken, such as quarantine for collaborators that went skiing in Italy or Austria in March 2020, global instructions about internal meetings, trainings, business trips or external visitors, the split of almost all staff into two teams (A/B) which could come alternatively on a bi-weekly basis, the installation of thermal cameras at the entrance of the main building, the compulsory wearing of a mouth mask, the limitation of the building capacity to maximal 30%, the implementation of approval and reservation processes for those coming on site, and so on.

Further, telework became the absolute standard work organization in 2020. Belfius had proactively and largely in advance increased the telework capacity and provided those who had no experience with teleworking (e.g. collaborators of branches) the necessary equipment. As a result, more than 95% of all collaborators worked exclusively from home during these periods of confinement.

In order to guarantee the continuity of the operations, critical activities were closely monitored in order to identify and resolve potential (staff) issues well in advance. As telework was the new organizational standard, a specific business continuity plan was also developed and tested in July in the case of a major failure of telework so that staff members performing critical activities at home are able to return to the buildings and to restart their activities within 2 hours whilst avoiding any unnecessary contamination risk.



The Covid-19 crisis also increased certain exposures such as information security, outsourcing and fraud risk. Close monitoring was performed and additional mitigation measures were taken where necessary to reduce the related risks. For example, awareness campaigns were launched to cope with increasing fraud attempts, due to changing customer behaviour and new very intensive fraud schemes with focus on customers. Next, major outsourcing arrangements were scrutinized with focus on business continuity, financial stability and logistics in order to identify potential disruptions in time. Finally, the impact of this long-term crisis on the organization was also assessed: only 7% of the key internal controls were impacted and adjustments were made so that the control environment was appropriately adapted to the new situation.

## VII.2. Non-financial risk - operational risk

### VII.2.1. Non-Financial Risk Management Framework

In 2019, the operational risk management framework has been extended to “Non-Financial Risk”. The term Non-Financial Risk (NFR) must be understood as a broad umbrella covering all risks except “financial risks” (such as market, ALM, liquidity, credit and insurance risks). NFR covers among others operational risks (including fraud, HR, IT, IT security, business continuity, outsourcing, data-related risks, privacy ...) as well as reputational, compliance, legal risks, ...

The NFR management framework determines the principles that ensure an effective management of the non-financial risks. The principles are further elaborated in specific Policies/Guidelines adapted to the business activities. These general principles are compliant with the applicable legal and regulatory requirements.

The framework is based on four axes:

- a risk mapping and taxonomy in order to ensure consistency within the organization, including a regular review in order to identify emerging risks;
- clear roles and responsibilities, as well as a well-defined way of working together for all the risks based on the 3 LoD model (decentralized responsibility);
- a strong governance/committee structure involving the appropriate level of management; and
- transversal risk processes and related policies, such as: self-assessment of risks and internal controls, incident monitoring, risk reporting, risk appetite definition and follow-up, business continuity and crisis management.

### VII.2.2. Risk Appetite

The formal definition of a Risk Appetite Framework (RAF) is the key reference for the group risk management practice and it covers both financial and non-financial risks.

The RAF for NFR contains quantitative elements (target values or ratios) and qualitative elements (statements) and is articulated around three concepts on which limits are defined:

- “Risks” – What are the risks? How to appreciate the risk level (past and forward looking)?
- “Risk management capacity” – What is the capacity to manage the risks?
- “Loss tolerance” – What are the potential P&L and future RWA impacts we tolerate?

### VII.2.3. Transversal risk processes

#### VII.2.3.1. Incident management

The systematic collection and control of data on operational incidents is one of the main requirements of the Basel Committee regarding operational risk management.

The reporting mechanisms ensure that the responsible parties are notified quickly when incidents occur.

Major incidents are also reported to the CRO/Management Board, and these reports always include an action plan for avoidance, mitigation or limitation of risk in the future. The major operational incidents are investigated thoroughly and are subject to specific action plans and appropriate follow-ups under the responsibility of the concerned line management.

For the period 2018-2020, Belfius Bank’s average annual potential net losses stemming from operational incidents amounted to EUR 2.19 million. Note that one-off costs to manage the Covid-19 situation and operational savings made in the Covid-19 context are not included.

The main areas of operational losses were essentially due to incidents associated with external fraud and incidents in relation to execution, delivery and process management. Other categories remain limited in amount but not necessarily in number of events.

The most important part of the financial impact resulting from operational incidents comes from the Bank’s retail business.

#### VII.2.3.2. Self-Assessment of Risks and Internal Controls (SARIC)

Another important task of risk management is the analysis of the overall main potential risks and related key controls, performed within Belfius Group’s main entities. This is achieved through a



bottom-up self-assessment of Risks and Internal Controls in all departments and subsidiaries, using the COSO methodology. These exercises may result in the development of additional action plans to further reduce potential risk and they provide an excellent overview of the main risk areas in the various businesses. These self-assessments are conducted annually and use the same methodology both for the Risk Control Self-Assessment (RCSA) and for the yearly reports submitted to the respective Boards of Directors regarding the assessment of internal control. Belfius Bank submits the Senior Management Report on the Assessment of the Internal Control also to its regulator.

### VII.2.3.3. New Product Approval Process (NPAP)

The process of developing or changing a function (product, service, activity, process or system) involves a sound (ex-ante) risk assessment, so called the New Product Approval Process. It is purposed at ensuring that all risks related to any new or changed function are assessed by relevant experts and addressed accordingly and is overseen by a dedicated steering committee.

### VII.2.3.4. Managing insurance policies

The possible financial impact of Belfius' operational risks are also mitigated by taking out insurance policies, principally covering professional liability, fraud, theft, interruption of business and for cyber risk. This is standard practice in the financial services' industry.

### VII.2.3.5. Business continuity

Belfius is committed to its clients, counterparties and regulators to put in place, maintain and test viable alternative arrangements that, following an incident, allow the continuation or the resumption of critical business activities at the agreed operational level and entirely compliant with the Belgian Regulation and beyond.

The supporting process, the business continuity and crisis management, is in a uniform way applied at all Belfius entities and relies on a.o. threat analysis, business impact analysis, reallocation strategies (dual office, remote work, etc.), effective management reporting, business continuity plans as well as exercise and maintenance programs. In that way, Belfius can proof its resilience also to the current Covid-19 situation.

## VII.2.4. Focus on key non-financial risks/domains

### VII.2.4.1. Information Security

For Belfius, the purpose of information security is to protect Belfius' information that has a value for the organization: i.e. the information generated by the business, the information belonging/ to our clients, and also the information, derived from freely accessible or publicly available data, which

has acquired a value as a result of the treatment carried out by or on behalf of Belfius. The threats against data and information are: their loss of integrity; their loss of confidentiality; and their unplanned unavailability. The mission of information security is to guard against these threats.

Belfius also considers that the objective regarding information security extends to managing the risks linked to the consequences of these threats if they have materialized in terms of customers' confidence, finance, reputation, peer confidence (regulators, financial markets) and confidence of our business partners. An information security strategy derived from these principles has been approved and is applicable to all actions pertaining to information security.

In order to guarantee the information security within Belfius, the Information Security Steering (ISS) Committee, managed by the Chief Information Security Officer (CISO) and chaired by the Chief Risk Officer, ensures a well governed and coordinated information security strategy whereby an adequate system of "prevention", "detection", "protection" and "reaction" is put in place, in line with regulatory requirements towards information security.

The steering of Belfius information security is relying on tangible figures and quantitative statements, not on perception or qualitative-only findings. Deviations from our risk appetite are challenged by risk towards the business lines within the ISS framework. Moreover, large security projects are grouped together in a security roadmap which typically spans the course of two years. Of course, the ever-evolving security threat landscape requires organizations to be resilient and anticipate existing and future threats.

A risk management framework has been successfully implemented in 2020 for supporting the Core Banking Renewal (CBR) that is a major digital and transversal transformation project for the group leading to a change of paradigm for IT. Its governance relies on a CBR Controlling Board, for managing the risks of this project, chaired by the CRO and managed by the CISO.

### VII.2.4.2. Data privacy

#### Respect for privacy and customer satisfaction

The respect for privacy and the protection of personal data is a key commitment at Belfius, which is translated into a sound internal governance and principles to be followed in the respect of GDPR. Belfius is also very committed to avoid personal data breaches and to manage any incident as quickly as possible.

Belfius published in May 2020 an updated privacy charter - the initial GDPR-version dates from May 2018 - on its website and informed its customers about this update. Towards the staff, an HR-privacy charter is published.



All activities treating personal data are obviously centrally documented by the business lines in a privacy register. GDPR conformity, including a risk assessment for the rights and freedom of the persons whose personal data are treated, is integrated into every process to offer (existing, adapted and new) products, innovative digital tools, services and information sharing to its clients. A network of privacy correspondents, active in each department, has been set up. They work closely with the DPO to continuously raise awareness, control and monitor processes and activities being in line with GDPR. Staff members must also follow on a regular basis GDPR-courses.

In order to continuously guarantee data privacy within Belfius, a dedicated steering related to GDPR regularly meets and a Data Privacy Officer (DPO) is part of the 2<sup>nd</sup> line of defence. The Belfius Management and several committees are on a recurrent basis informed about GDPR conformity in Belfius.

Data subject rights can be executed by data subjects via multiple channels, including the Belfius online applications and mobile apps. More than 98% of the data subject rights are asked via the Belfius online app and receive an answer in the same app within 1 business day.

#### **VII.2.4.3. Fraud risk**

Belfius applies a zero-tolerance policy for all forms of fraud (internal, external and mixed fraud schemes), is monitoring the threats continuously and is managing the risk based on a global anti-fraud policy defined and steered by senior management.

The roles and responsibilities have been clearly defined which implies in a concrete manner that business and support lines are the first risk managers. The CRO and NFR team including the Anti-Fraud Officer as expert have a clear 2<sup>nd</sup> LoD role.

In a context of evolving digital channels and faster payments processing, internal controls are continuously screened to prevent fraud and this, to protect the interests of Belfius and its employees, customers, suppliers and other stakeholders.

#### **VII.2.4.4. Outsourcing risk**

Belfius is aware that outsourcing & third-party risk are addressed adequately and fully assumes its responsibilities in that regard, including but not limited to overseeing and managing the concerned arrangements and the risks involved.

The Outsourcing risk & material arrangements Policy is compliant with “Final Report on EBA Draft Guidelines on Outsourcing Arrangements”. In particular, the policy provides the appointment of the outsourcing function and the set-up of the Outsourcing Management (steering) Committee

(“OMC”), whose mission consists in ensuring a well governed and coordinated outsourcing in line with Belfius strategy, risk appetite and regulatory requirements. Monitoring and control of the significant providers, in particular to whom personal data is transferred, will be sharpened as of 2021 within the 3 lines of defense.

#### **VII.2.4.5. Employment Practices (HR) & Workplace Safety, Damage to Assets & Public Safety**

Concerning physical security & workplace safety, Belfius has a very low appetite for risk. Belfius strives to provide a secure environment for its staff, clients, visitors and assets by ensuring its physical security measures & procedures meet high standards. To reach this goal a Security Steering Committee with all stakeholders monitors systematically the overall situation by means of a dashboard. It also acts as a forum to reflect and to dialogue on actual incidents, and on action plans to reduce the risk to acceptable levels.

## **VII.3. Business, strategic & execution risk**

### **VII.3.1. Business risk**

#### **Definition**

Business risk reflects the unexpected decrease of profitability from the expected (or budgeted) one resulting from deviations from Financial Plan, changes in competitive environment, lack of responsiveness to changes in the business environment (macroeconomic, regulations, client behaviour, competitive landscape, socio-demographic, climate, ...) or adverse/improper implementation of business decisions.

#### **Organisation and management of the Risk**

The business risk is at the heart of the daily management of the Bank. Indeed, management control as an independent department is responsible for the consolidation of data necessary to calculate income, expenses and profitability, as well as related reporting. Additionally, with regards to the Financial Plan, sensitivity analyses and stress-testing are executed.

#### **Capitalisation**

Business risk is not capitalized through Economic Capital but treated through Earnings at Risk and Stress Testing frameworks.



## VII.3.2. Strategic risk

### Definition

Strategic risk is defined as the current or prospective loss of value arising from adverse business decisions or the lack of responsiveness to changes in the business environment. Strategic risks often focus on the risk opportunity, “there is no return without risk.”

### Organisation and management of the Risk

The steering of future profitability as well as the strategic vision and strategic risks are operated through the various business line committees, by the Management Board and ultimately by the Board of Directors: the latter defines strategic decisions to achieve the levels of expected profitability as announced to the market and ensure the survival of the Group and its business lines.

### Capitalisation

Strategic risk is not covered by capital but is handled and managed through an appropriate governance process at Belfius.

## VII.3.3. Execution risk

### Definition

Execution Risk corresponds to the risk of not being able to fully execute the decided strategy or the improper implementation of decisions. Examples of execution risk are insufficient resources (HR, IT, ...), failing new product introductions or rolling out complex new systems, etc.

### Capitalisation

Execution risk is not covered by capital but is handled and monitored through an appropriate reporting and follow-up at Belfius.

## VII.4. Reputation risk

### Definition

Reputation risk is defined as the potential decrease in the value of Belfius arising from adverse perception of the image of the financial institution on the part of customers, counterparties, shareholders, investors, regulators and other stakeholders.

## Organisation and management of the Risk

Reputation risk (mainly image and branding) is steered by the Brand, Experience and Communication Department in direct line with the CEO and the Chair of the BoD.

The CRO is an active partner in this specific risk management field, on the one hand, in her role as responsible for the Risk Department and, on the other hand, as general risk owner of Non-Financial Risks and of the crisis management process.

The existence of the reputation risk policy, the integration of the reputation risk in the RAF, and in general the Risk Charter, Risk Culture, Risk Roadmap, Ethical codes and codes of conduct cover reputation risk and are proof that all team members are handling reputation risk as it is an overall and common responsibility.

The reputation strategy aims to implement sound, prudent and effective risk management and is based on three pillars:

- prevention: transparency regarding the reputation risk governance, combined with well-defined processes, guidelines and procedures, mainly to identify sources of reputation risk;
- detection: an early warning reporting ensures a proactive detection of factors affecting reputation risk and stimulates the alertness and speed of response both having a significant impact on the level of reputational damage;
- mitigation: tactical and operational mitigation actions are top-down driven with adapted short decision & communication lines assuring a clear and univocal response to incidents or crises. The emphasis is amongst others on effective response to press, interaction on social media, sound complaint management and crisis communication.

These key internal control actors have set up appropriate risk management frameworks and policies to prevent, detect and monitor potential reputation impacts on the risks of which they are primarily in charge.

They each assess risks relating to their areas of expertise on a regular basis, in order to identify areas that might not yet be sufficiently covered and accordingly define corrective actions. This exercise is performed on a consolidated basis within the Bank using harmonised methodologies and tools.

Meetings between the different departments are organised on a regular basis in order to share information and to ensure a consistent and exhaustive risk management approach within the Bank.



## Risk Appetite

Belfius wants to be perceived as a sound and trustworthy partner by its relevant stakeholders (mainly customers, potential customers, investors and regulators) by proving Belfius is taking up its deep rooted commitment to achieve client satisfaction and to focus on a long term profit strategy with low risk profile.

Belfius wants to affirm, promote and protect its excellent reputation. Reputation is built over years but is vulnerable and possibly destroyed in an instant.

Reputation risk is a top strategic business risk and a key business challenge. Reputation risk management is key to Belfius since our business model is based on trust. Avoiding all threats that can possibly undermine the trust of our stakeholders is very important.

## Capitalisation

The risk is not capitalised and is managed through strong corporate governance and compliance rules within Belfius as described above.

# VII.5. Compliance risk

## Definition

Compliance risk is associated to any financial institution's failure to comply with laws, regulations, rules, internal policies or prescribed best practices that can result in financial sanctions or loss of reputation.

## Organisation and management of the Risk

Compliance is organised around a central Compliance department based on 3 pillars: Business Advisors (advisory function), the Compliance Risk Control team (control function) and the anti-money laundering unit (AML). These three teams are supported by a specific unit which frames projects at an IT and organisational levels.

The central Compliance department may also call on the services of a large network of Compliance Correspondents within the Bank's divisions, as well as on a network of Compliance Managers within the branch network. This network plays an important role, particularly in the introduction of Compliance policy and procedures as well as in the training and awareness programs in that regard.

A Compliance Officer recognised by the FSMA and NBB is at the head of the Compliance organisation. The Compliance Officer reports directly to the Chief Risk Officer and to the Audit Committee and, if necessary, may directly approach the Chairman of the Board of Directors, the external auditor and the Regulator.

As provided by the regulations, the department also has an Anti-Money Laundering Compliance Officer.

The Anti-Money Laundering Compliance Officer (AML CO) is head of the anti-money laundering team, which combats money laundering practices. Belfius does all it can not to be involved in laundering money from illegal activities, the organisation of tax fraud, financing terrorism or circumventing international embargos. To underline this commitment, the AML CO has established preventive measures and broadened controls. Proper knowledge of the customer and their identification, verification of the origin of financial flows on accounts and detection of dubious transactions are all vital elements in the prevention of such practices.

The Compliance Officer of Belfius Bank ensures that a coherent and effective Compliance policy is applied within all the subsidiary companies of Belfius Group. Belfius Bank traces out the group policy and defines the Compliance methodology to be used. Each regulated subsidiary company disposes of a Compliance Officer who is responsible for the application of the adapted policy within his/her company. These Compliance officers report functionally to the Compliance Officer of Belfius Bank.

## Capitalisation

This risk is not covered by capital. The reasons behind the absence of quantification of Compliance risk are primarily driven by the absence of data and/or history to support robust quantification. In that context, capital is not the adequate answer to cover Compliance risk. We therefore consider more relevant to monitor this risk through procedures and processes and to set aside 'ad hoc' provisions for this type of specific events which are most of the time characterized by long term procedures.



## VII.6. Legal risk

### Definition

Belfius' legal risk results from the following risks:

- Risks relating to the regulatory framework:
  - non-compliance with the regulatory framework: the risk of not applying, in whole or in part, applicable laws or regulations;
  - incorrect application of the regulatory framework: the risk of incorrectly applying a law or regulation, which could be challenged by a third party;
  - non-optimal use of the regulatory framework: the risk of not providing the appropriate or optimal legal support, or of not benefiting from an advantage resulting from the regulatory framework, due to a lack of sufficient knowledge of that framework;
  - breach of the general duty of care: the risk of a behaviour, fact or decision adopted in violation of the general duty of care, which may involve Belfius' non-contractual civil liability.
- Risks relating to the contractual framework:
  - inadequate drafting of contracts: the risk of not protecting Belfius' interests in its contracts with any third party (contracts with terms that are either inadequate, unfair or unenforceable);
  - ignorance of the contractual framework: the risk of not taking into account all of the commitments Belfius has made with or towards any third party (failure to keep track of and meet or enforce its contractual obligations or right).

The materialization of the legal risk may entail the following consequences for Belfius:

- a financial impact;
- a reputational impact;
- litigation, liability (civil or criminal) of Belfius or an employee, sanctions (administrative or criminal) imposed on Belfius or an employee, or measures imposed on Belfius by a supervisory authority; and/or
- an impact on customer satisfaction.

## Organisation and management of the Risk

In order to control legal risks, a Legal & Tax Risk Framework (also known as Legal Risk Policy - including a Risk Assessment Matrix) has been set-up and approved by Belfius' Management Board. This Legal & Tax Risk Framework is being implemented and a risk measurement & management process is applied.

This process involves successively:

- a risk assessment, in terms of impact and probability of occurrence;
- a risk taxonomy & risk appetite; and
- the implementation of risk management measures.

A Legal & Tax report, including a dashboard of the identified major Legal & Tax Risk is submitted to the Risk and Audit Committees on a half-yearly basis.

### Capitalisation

This risk is not covered by capital. The reasons behind the absence of quantification of Legal risk are primarily driven by the absence of data and/or history to support robust quantification. In that context, capital is not the adequate answer to cover Legal risk. We therefore consider more relevant to monitor this risk through procedures and processes and to set aside "ad hoc" provisions for this type of specific events which are most of the time characterized by long term procedures.

## VII.7. External risk

### Definition

External Risk relates to the risks that arise from events outside the company and are beyond its influence or control. These risks can offer negative and/or positive benefits. Organizations cannot influence the likelihood of these risk events, but can reduce the cost of an impact. Sources of these risks include natural and political disasters and major macroeconomic shifts

### Capitalisation

External risk is not covered by capital but is handled and monitored through appropriate processes at Belfius.



# VIII. ESG Risk Management

## VIII.1. Why ESG risks matter

Belfius aims to create long-term value for the Belgian society in a credible manner by taking responsibility for its actions and engagements. Sustainable entrepreneurship mainly creates opportunities, such as the development of new sustainable products. Nevertheless, the climate-related, environmental and social implications can entail risks. An extensive Environmental, Social and Governance (ESG) risk management embedded into the daily business of the Bank and insurance company, is important to ensure a sustainable and resilient business model. Through proper management of ESG risks Belfius also contributes to safeguard Belgian society from transition, physical and society-related risks.

The Covid-19 crisis highlighted the urgency to incorporate ESG in Belfius' risk management, while at the same time giving Belfius the opportunity to accelerate its strategy in order to be meaningful and inspiring by rebuilding our world with a "green recovery".

Belfius has started to develop an ESG risk framework in 2020.

## VIII.2. What our strategy and goals are

Belfius wants to be a leading actor in the transition towards a sustainable society. Therefore, we need to contribute to achieve net-zero emissions and limit global warming in line with the Paris Agreements.

Belfius wants to build its own resilience in a world where major disruptions caused by rising temperatures, new climate-related policies and emerging technologies are likely to affect most economic sectors and industries both in the short and long term and thus also to impact Belfius (since these changes might for instance entail lower profitability and creditworthiness of our customers and substantial losses in asset values).

Belfius wants to be exemplary and therefore aims to comply with regulatory requirements. At the European level, this concerns inter alia: the EU Action Plan and the European Green Deal, the EU Taxonomy for sustainable activities. Besides, we strive to meet ECB's expectations on the ECB guideline on climate-related and environmental risks with an ESG risk action plan.

Belfius wants to set ambitious goals and targets. We need to fulfill our ten commitments (we refer to the CSR chapter of the annual report) within our Belfius Sustainability Strategy and monitor the ESG risks involved. Another important commitment made to map out and expand our sustainability efforts, is the signature of the United Nations Environment Programme Finance Initiative (UNEP FI) on 27 April 2020, together with the Principles for Responsible Banking (PRB), the Principles for Sustainable Insurance (PSI) and the Principles for Responsible Investment (PRI). Belfius will take the appropriate risk mitigation and adaptation actions so as to minimize the occurrence and the impact of potential climate-related risks, after which we can set ambitious targets towards 2030 by using the methodology of Science Based Targets initiative (SBTi) to comply with the objectives of the Paris Agreement on climate change, the Sustainable Development Goals and our own goals and ambitions. Furthermore, we also committed to the ten principles of the UN Global Compact by joining this voluntary initiative on 27 May 2020.



Belfius wants to stay on top of evolutions and to make sure being ready to meet additional requirements. This is only possible by continuous looking forward, by following all evolutions and by anticipating, e.g. on EBA discussion papers, on EIOPA discussion papers. We interact with different stakeholders, such as NBB, EIOPA, Febelfin, Assuralia etc., to stay abreast of the latest evolutions and thus expand the quality of our ESG risk management. Furthermore, we are following up on the evolutions of the Network for Greening the Financial System (NGFS).

### Belfius' 10 ESG commitments to society

- Be a leading actor in the transition to a sustainable Belgian economy & society
- Our CO<sub>2</sub> neutrality is the new normal
- Guide our customers towards positive impact investments
- Leverage our balance sheet to contribute to a more sustainable society
- Reshape Belgian mobility with substantial positive impact on the environment
- Future-proof infrastructure is our absolute priority
- Put privacy and data security of our customers first
- Foster fairness and equal opportunity
- Be an exemplary employer for diversity and sustainable careers
- Sustainable example for risk & financial solidity and stability

### Engagement signed by Belfius



## VIII.3. Governance & culture: How we have organized ourselves in order to reach those goals

Sustainability and ESG risks drive a lot of types of risks: credit risk, market risk, liquidity risk, operational risk etc. Though, ESG risk is a transversal risk and it cannot be tackled alone, so a holistic approach is crucial. Therefore, ESG risk management is monitored at the conglomerate level and all Belfius' subsidiaries are involved with close cooperation, without losing sight of each one's specificities.

In 2020 a dedicated ESG Committee was set up at the level of the Board of Directors to closely monitor the evolution of Belfius Sustainability Strategy. On the level of the Management Board, the CEO is responsible for all ESG topics since 2020. Our management body always has due consideration with ESG and sustainability aspects when deciding on our overall strategy and, although not formalized yet, this aspect is also on the mind of credit committees.

There are ESG roles and responsibilities allocated, also beyond the Risk department, within the whole organization and conglomerate. There is a follow-up by the ESG Steering Committee on a monthly basis and various transversal workgroups per ESG topic and specific competence centres are set up to achieve our Sustainability Strategy. Additional financial and human resources have been made available to create this ESG organization and governance.

### VIII.3.1 A first step taken: Adapting our Risk Appetite Framework (RAF)

Certain qualitative ESG targets were already integrated into the RAF in 2020, such as CO<sub>2</sub> neutrality of Belfius, sustainable funds by 2025, signature of different principles etc. In 2021 - after rolling out our roadmap and implementing our action plan - some quantitative indicators and limits will be defined for the RAF and as from 2022 this will be followed up.



## VIII.3.2 Roadmaps and action plans: What we have done and plan to do in order to reach those goals

### Direct risks

Belfius is aware of the direct ESG risks, with the associated adverse impact on business continuity, and has therefore already performed several internal assessments. A screening of our physical risks, such as our buildings and operations, has been done. Since 2020, Belfius is CO<sub>2</sub> neutral (including Belfius main building, paper, water, energy, fleet etc.). This guarantees that Belfius is actively calculating and reducing its local and global climate impact. Belfius offsets its remaining emissions by financing global climate projects. Furthermore, a critical review of our data centers has identified potential risks and necessary actions are being taken, with for instance the use of the cloud technology and the cloud project.

### Indirect risks

To determine how we will address climate-related risks to which we are exposed through our lending and investment portfolios, we decided to set up a detailed ESG risk roadmap and action plan, consisting of several short term and long-term key steps.

#### Step 1: Identify, assess and measure ESG risks

Belfius started with a thorough ESG Risk identification and measurement. In order to guarantee sufficient expertise and quality, we will rely on specialized external parties, such as data providers. We are setting up an ESG data strategy to define a data collection and storage process.

A first high-level screening of the portfolio based on the NACE code – based on the EU Taxonomy – highlights that Belfius has a relative “sound” balance sheet, based on available information. In the context of detailed analysis, Belfius has chosen to focus first on the real estate portfolios. We are convinced that this will have a major positive impact and that several important climate risks will be managed in this way. We have started measuring the energy efficiency label of our mortgage portfolios in April 2020. We will further deep dive in all our portfolios and are expanding the screening to other climate-related, environmental and social aspects. The necessary developments are currently being made to adapt our systems and to create additional databases. A next step will be the development of a Real Estate Repository (RER), where this energy efficiency data can be integrated together with other climate information on real estate.

A progressive and accurate screening of the balance sheet for our lending and investment portfolios is our first main focus. Based on the ESG risk sensitivity of the economic sectors, we obtain an even more detailed picture of the ESG risk sensitivity of our balance sheet. In determining the ESG sensitive sectors, we rely, among other things, on the EU taxonomy for sustainable activities, our own Transition Acceleration Policy (TAP) and dialogue with a number of important external stakeholders, including NGOs. A task force within Belfius has been set up with various stakeholders and experts to work on this topic.

Belfius will first focus on climate-related risks, in this way we concentrate on the most priority topic and follow general trends. Belfius will focus on both transition risks and physical risks.

In the context of a Transition risk materiality assessment, Belfius Bank already performed a first screening and classification of its lending and investment portfolios (based on sector and NACE codes). After this, a Transition Acceleration Policy (TAP) was drafted. Committing to a better society without compromising the wellbeing of future generations requires making clear-cut decisions about what we want to do and what we choose not to do. This policy entails restrictions on eight sensitive sectors and business areas, because we as a bank insurer assess, based on thorough analysis, the activities in those sectors and business areas that are not in line with our ESG policy. These sectors are considered the most urgent to be dealt with: tobacco, gambling, weapons, energy, mining, palm oil and soy, agricultural commodities and controversial governments. Since 2020, the criteria of the TAP have been implemented in the various internal processes: the Credit Risk Acceptance guidelines, the Money Market guidelines, the decision-making processes of Belfius Lease, the validation processes of Belfius Auto Lease and the insurance policies of Belfius Insurance.

In addition to the evolution of the criteria and sectors of the TAP, Belfius will also engage in dialogue at client level, as these activities are evolving. Via the sector limits, we manage our exposure to different ESG risks. Though, when doing so, Belfius also wants to encourage and support businesses in their shift towards more sustainable activities, not only applicable to the eight sensitive sectors, but in general to all our clients. Through a partnership with CO2Logic, we want to help our clients with the transition to a low-carbon economy. Belfius started a lot of initiatives and developed new products to promote sustainability, such as Portfolio 21, thematic funds with themes as cancer, climate and diversity.

With regard to Physical risks, an assessment of risks embedded in Belfius Insurance portfolio (life and non-life insurances) was performed by the Actuarial Function. This assessment included recommendations, some of which have already been implemented. It was reminded that Reinsurance is a major mitigation method (among others, for climate related risks) already implemented for long years at Belfius Insurance. Further work will be done as part of an ESG risk identification.



### Step 2: Quantify the potential financial impact of ESG risks

Preparatory work has been done to carry out a first climate stress test in 2021-2022. On the basis of scientific research, it has been investigated which stress test is possible for Belfius with a specific portfolio and with the available internal data. Moreover, thorough scenario analysis is needed to quantify the possible financial consequences of ESG risks.

As the concerns for climate risks are increasing, managing physical climate risks linked to meteorological events is part of the usual practices of Belfius Insurance. To measure these risks, potential or past events are modelled and applied on our insurance portfolio. Conclusions are then used to adapt our reinsurance contracts on yearly basis. Nevertheless, Belfius concerns for climate risks are increasing as this risk type is emerging under the form of physical and/or transition risk. In this context, two studies have been performed by the Actuarial Function regarding the long term impacts of the climate changes on the physical risks in the insurance portfolios. They include qualitative and quantitative elements: impacts on the Non-Life insurance and impacts on the Life insurance. Several recommendations are included in these studies, some of which have already been implemented (e.g.: pricing increase related to the rise of climate related claims). Concerning the Belfius Insurance side, the definition of "Climate Stress Scenario" is currently in discussion. The goal is to measure potential impacts of such a stress scenario on the 5Y Business Plan of the company.

### Step 3: Manage, monitor and mitigate ESG risks

Furthermore, setting up ESG risk scoring and modelling is a next step. Our goal is to individually score each counterparty and take this into account in our decision processes, like credit granting, pricing etc. to minimize our negative impact and to maximize the positive transition towards a sustainable, fair and transparent society.

Another action to manage our ESG risks, is the enlargement and adaptation of our ESG Risk policies and guidelines, such as credit granting policy, outsourcing policy, procurement policy etc. As already indicated, the Transition Acceleration Policy (TAP) in 2020 has been written and validated at group level and is therefore valid for all Belfius Group entities. Belfius Insurance has written an Engagement Policy in 2020, see: [Engagement policy](#).

### Step 4: Disclose and report ESG risks

Belfius wants to be transparent and accountable. So, a final step to take within our ESG risk action plan is to disclose our initiatives and achievements. Regarding the Sustainable Finance Disclosure Regulation (SFDR), we are, first of all, writing general information on entity level about our investment policy and the investment products we market. Secondly, we are making the necessary preparations to publish the details on product level of the sustainability of each investment product we sell. There will follow more disclosures on entity level about principle adverse impact (PAI) and com-

plementary periodic disclosures on product level.

We even go a step further and we are working on additional voluntary climate disclosures. For instance, we take into account the Task Force on Climate-related Financial Disclosures (TCFD) recommendations with the core elements – which are crucial for climate risk management – Governance, Strategy, Risk management, Metrics and targets. As recommended, an outside in approach will be applied. To achieve high-quality disclosures, we consider the seven principles of the TCFD for effective disclosure.





# IX. Other financial risks

## IX.1. Settlement risk

### Definition

Settlement risk is defined as the risk that the credit institution will deliver the sold asset or cash to the counterparty and will not receive the purchased asset or cash as expected.

This risk is not to be confused with the operational risk classified under “Execution, delivery and process management risk”. The settlement risk only refers to the situation where the delivery process fails because of a solvency issue.

### Organisation and management of the Risk

The most general way to reduce the settlement risk is to proceed through an intermediary performing Delivery Versus Payment (DVP). For Forex in particular, there is one main agent: Continuous Linked Settlement (CLS). With DVP one can say that the risk becomes negligible. Belfius intends to generalise the recourse to DVP.

Historically, there has been no instance of loss related to this risk at Belfius and very few external-ly. In fact, losses would only occur if Belfius simultaneously faces a mismatch in the delivery against settlement process and the default of the counterparty bearing the resulting temporary exposure. Of course both events can be strongly correlated: a bank close to bankruptcy is much more likely to fail in its settlement duties.

### Capitalisation

Settlement risk capital is currently not computed via a statistical model but rather results from the occurrence of a single settlement problem (a presumably very rare event). It therefore consists of a fixed amount set a priori based on a judgemental assessment.

## IX.2. Funding risk

### Definition

Funding risk is the risk that the refinancing cost for Belfius increases.

### Organisation and management of the Risk

For more details regarding the Organisation and Management of funding risk, please refer to Risk Management Governance - II.4.2.3.3. .Risk organisation.- Strategic Risk Management.

### Capitalisation

Funding risk capital is not computed via a statistical model. Its calculation is based on a scenario analysis, with a severe liquidity Stress Test considering a combined systemic and severe lack of confidence of the market about Belfius solvency during a global liquidity crisis and affecting its income statement.

This liquidity stress scenario will generate a funding risk which can be defined as the sum of P&L impacts resulting from, on the one hand, the cost linked to the replacement of the existing funding that left the balance sheet by funding obtained through pledging the assets from liquidity buffer at ECB and, on the other hand, the capital losses due to sales of non-ECB-eligible bonds to close the potential liquidity gap.

In line with economic capital standards, the loss incurred over one year is measured and the confidence interval of the considered scenario (a presumably very rare event) is assumed to be 99.94%.

Note that the various outflow scenarios included within the liquidity stress test materialise the outflow risk which is considered to be integrated within the funding risk calculation.



## IX.3. Behavioural risk

### Definition

Behavioural risk is defined as the potential change of exposure to interest rate and funding risks due to the uncertain behaviour of customers.

On the liability side, it includes the uncertain amortization of non-maturing liabilities, such as deposits, and the uncertain rate of termination of insurance contracts (also referred to as “lapse” risk within Solvency 2). On the asset side, it includes uncertain mortgages prepayment schedules.

The uncertain amortisation of non-maturing liabilities, such as certain types of deposits, forms the outflow risk and is integrated within the funding risk approach. For example, customers may decide to reduce their savings or their sight accounts impacting the Bank’s interest rate position.

### Organisation and management of the Risk

Behavioural risk is managed through sensitivity and convexity measures reported to the members of the Belfius ALM Committee. In addition, this risk is included in the Belfius Economic Capital reporting.

### Capitalisation

Behavioural risk is capitalised through a prepayment risk capital approach which consists of a statistical model.

## IX.4. Pension plan risk

### Definition

Pension risk is the risk stemming from commitments on employee pensions plans (e.g. pension and post-employment employee benefits).

These commitments and the related assets are externalized to an insurance company or an OFP (pension fund). Belfius Bank pays premiums to the insurance company or pays contributions to the OFP. The contributions in the OFP are invested in assets (equity and bonds). Belfius Bank remains the ultimate responsible for the commitments.

The risk for a pension plan is that the net present value of its liabilities (commitments to employees) is higher than the net present value of its assets (investments in the OFP or the value of the commitments of the insurance company).

As a result, pension risk is a set of risks. The most important are market risk (interest rate risk, equity risk, inflation risk), credit risk and behavioural risk (turnover, mortality).

### Organisation and management of the Risk

The OFP grants an investment mandate to the pension fund asset manager. This investment mandate establishes clear investment objectives for the pension fund consistent with the characteristics and the risk appetite of the pension fund.

The approach for achieving these objectives takes into account the need for proper risk management, diversification needs, liquidity requirements and asset allocation limitations.

The ALCo evaluates the risks in the OFP and insured pension plans and decides if further mitigation is required.

### Capitalisation

Pension plan risk is capitalised. The risk capital is based on the different risk factors.



## IX.5. Model risk

### Definition

Model risk is defined as the potential risk assessment errors resulting from inadequate methodology and models, and/or data uncertainty or from the inappropriate use of models.

The major issues that should be addressed by model risk are the following:

- risk of poor model development/backtesting;
- risk of incorrect model calibration or rank ordering power;
- wrong data use and/or data problems;
- inadequate model usage;
- risk of population and/or performance non-stationarity.

### Organisation and management of the Risk

In addition to the Economic Capital assessment that is carried out for model risk, the risk of each issue described above is mitigated by a process-oriented handling of model risk.

Without being exhaustive, the following practices are considered for containing model risk:

- allocating experienced professionals to the development of risk models;
- providing a systematic “four eyes approach” via the independent model validation;
- monitoring and capitalising model risk within the Belfius Economic Capital framework.

### Capitalisation

For each risk type and each economic capital calculation methodology, the potential increase (not decrease) of economic capital resulting from model risk is assessed using a unified scorecard approach. It includes the result of quantitative and qualitative assessments of the models and is also linked to the outstanding validation recommendations. This judgement results in an “uncertainty coefficient” depending on the perceived comfort “with which the model has been developed and implemented and is being fed and used”.

## IX.6. Conglomerate risks

### Definition

A distinction is made between:

- “Group consolidated risk” which is the risk inherent to a “group” i.e. a company owning and consolidating other companies, whatever the sector the company and its affiliates belong to; and
- “Conglomerate risk” which the risk arising from a group of companies - a financial conglomerate - composed of credit institutions, insurance undertakings and investment firms.

Conglomerate risk comes on top of “group consolidated risk” as the financial conglomerate will be submitted to “group consolidated risk” and to “conglomerate risk” as the conglomerate manages financial companies regulated under at least two different prudential frameworks (Banks and Insurance).

Conglomerate Risk is defined as the risk arising from a group of companies - a financial conglomerate - composed of credit institutions, insurance undertakings and investment firms.

A distinction is made between financial risks on the one hand, and non-financial risks on the other hand. The following conglomerate risks are defined at Belfius:

### Financial Risk

- Regulatory inconsistency: regulatory inconsistency could lead to ‘double gearing’, where the same capital, issued by the conglomerate, is being counted twice, to satisfy both banking and insurance capital requirements. Another result of inconsistency is ‘excessive leveraging’, which can occur when debt is issued by the conglomerate and the proceeds are given as equity to the regulated subsidiary. Because of regulatory inconsistency a financial conglomerate could shift activities from one of its banks to one of its insurance firms, or vice versa, if the respective capital requirements are lower.
- Intragroup insurance contracts are contracts between the insurance. These will not be effective at conglomerate level (e.g. property risk).



## Non-Financial Risk

- Contagion/reputation: financial difficulties in one subsidiary in one sector could have contagion and/or reputation effects on another subsidiary in a different sector, especially when using the same brand name. In that case, the conglomerate may be more vulnerable than its stand-alone subsidiaries.
- Moral hazard – subsidiaries: subsidiaries themselves may assume help from the holding company in cases of financial stress and behave riskier in a financial conglomerate than as a stand-alone institution.
- Moral hazard – conglomerate level: at conglomerate level may exist the moral hazard risk associated with the 'too big to fail' position.
- Size & complexity: it becomes more difficult to manage and understand the operation of a firm as the organization grows. Both these issues are not unique to financial conglomerates but arise because financial conglomerates tend, in most case, to be larger than pure sectorial players.
- Governance and conflict of interest: as financial conglomerates run activities in different sectors (Bank, Insurance, Investment services ...) they may be more exposed to conflict of interest. These may arise from subsidiaries vs mother company, from promoting banking products vs insurance or investment products, confidentiality conflicts, etc.
- Concentration between sectors linked to outsourcing ( same service providers, back office services, ...), continuity (BCP, DRP, workplace safety, employment,...), business practices (products, new business, CSR, ...), strategic risk, legal, tax and compliance risks and IT risk.

## Organisation and management of the Risk

With regards to conglomerate risks, Belfius has put in place several mitigating actions. We refer to some of them (not exhaustively) here below.

- The Belfius Capital Group committee in charge of monitoring of adequacy of capital management at conglomerate and sector level.
- Stress Tests are designed and run at Group level but also at bank and insurance levels.
- ECAP and EaR are computed at group level giving an exhaustive view of the capital needed to cover all major risks.
- FICOD test give a view of the regulatory capital needed to cover risks in each part of the conglomerate.
- A cartography of intragroup insurance contracts has been set up and monitoring takes place on a regular basis.

- There are reinsurance rules above specific thresholds.
- There is a common communication and reputation follow up at Group level.
- There exist a capital and dividend policy at Group level with consistency at entity level.
- At Group level, several joint committees are in place at the highest level: Joint RC/RUC Committee, Joint AC Committee, Joint Management Committee (Group Management Board), potential conflicts between Bank and Insurance BoD are dealt at the level of the Group Mediation Committee
- ...

## Capitalisation

The conglomerate risks are not covered by capital seen the multitude of mitigating actions in place.





# X. Belfius Insurance's risks

For more information regarding the Belfius Insurance risks, we refer to the chapters Risk Management of the Annual Report 2020 of Belfius Insurance, Risk Management and the Belfius' Management report (see dedicated section on insurance risks)



# XI. Appendices

## XI.1. Information exempted from disclosure

### Information not disclosed due to non-materiality, proprietary or confidential nature

<b>ARTICLE 447 (B,C ,D,E)</b> Exposures in equities not included in the trading book	We consider that Belfius investment in its insurance subsidiary is detailed in several sections of this report. The remaining exposures are considered non-material as illustrated in section IV.5.
<b>ARTICLE 449</b> Exposure to securitisation position	We consider Belfius risk-weighted (external) securitisation position to be non-material and therefore only limited information based on the securitisation templates recommended by the Basel Committee. We also disclose the information required by article 449 CRR only when relevant either for our activity as investor or as originator.

## XI.2. Risk methodology

### XI.2.1. Description of the internal rating process

#### General Organisation of the Internal Rating Process

The internal rating process is organised in three Stages: the model development, the maintenance and the control of the internal rating.

The model manager is responsible for the entire process of developing and maintaining a model, whereas the control of the internal rating is dispatched through several control functions within the Bank (validation, audit, quality control, ...).

#### Development of the Models

The model management process is coordinated by the Model Management team within Belfius Bank. Model managers perform the model management activities enhancing both consistency and efficiency.

The various steps are:

- defining the scope of the counterparties concerned;
- identifying and gathering the most relevant available data (financial data, data on defaults of the segment concerned, institutional framework);
- building a database if needed;
- defining a broad list of financial ratios and qualitative criteria;
- testing these ratios (repetitive processes between statisticians and analysts);
- building the score function. A score function is the mathematical function that allows determination of the counterparty (or exposure) PD, LGD or CCF on the basis of its characteristics. Score function is established by the modelling team on the basis of statistical analysis and modelling techniques;

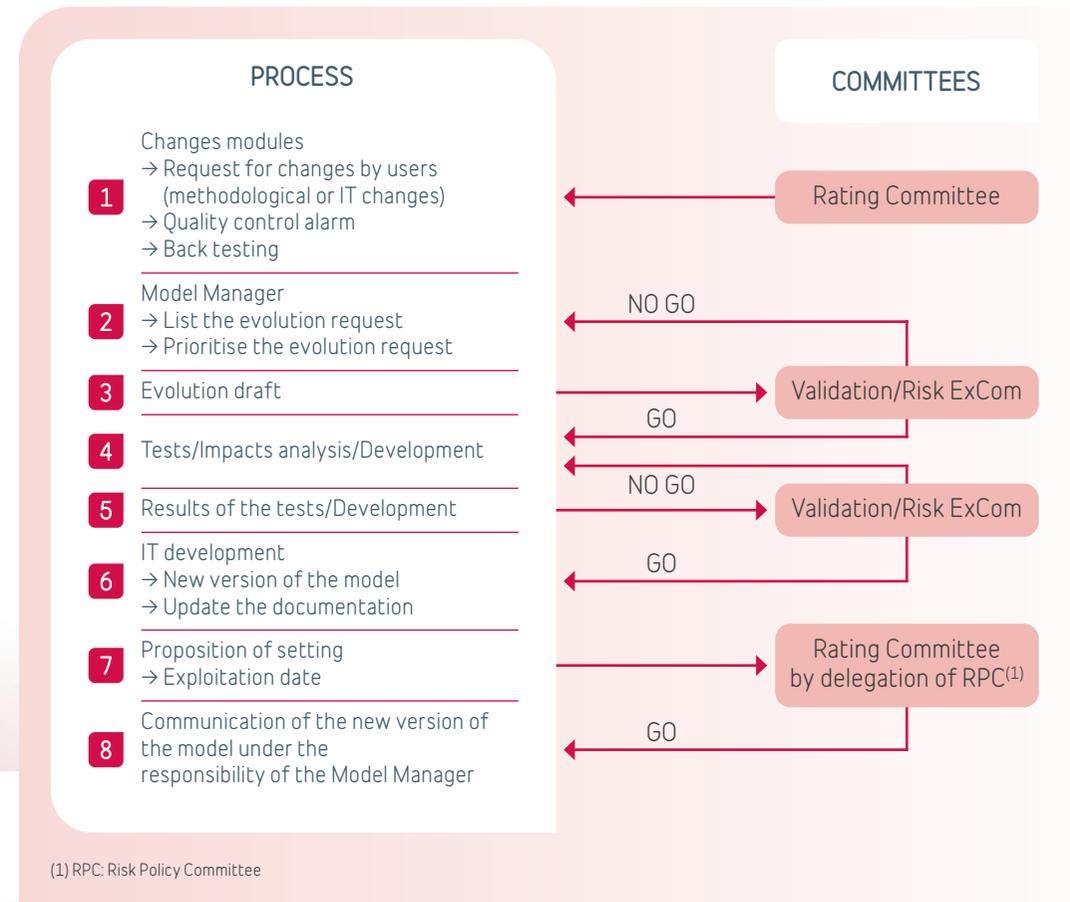


- testing the score function;
- developing IT tools;
- validating and implementing the model;
- adjusting risk policies to take internal risk systems into account;
- documentation (user guide, documentation for the regulator, notes concerning the building of the model). Nevertheless, some steps in the development process detailed above (such as building the score function, testing the function, etc.) are not applied for some specific models:
  - models based on an expert approach (such as the model used for Regions and Communities) do not include a score function. They are based on internal experience and qualitative knowledge and not on statistical data (which may not be available due to very low number of defaults for instance);
  - models based on a derivation approach are derived from an existing model;
  - models based on an assimilation approach are not stricto sensu models due to the fact that counterparties treated by assimilation simply inherit the rating of their “master” counterparty.
- assimilations and derivations are applied when it is neither financially intuitive nor statistically relevant to develop, adapt or use an existing model. Such cases occur typically for low default portfolios with a low number of observations, limited data availability (both for design and for model use) and for portfolios where strong relations exist between the “master” counterparty and the “assimilated” or “derived” counterparty. These relations can be legally bound or based upon long-term past experience and practice.

### Maintenance of the Models

As mentioned above, the model manager is responsible for the entire process linked to the model developed, including the maintenance of the model.

The model maintenance process is detailed in the diagram hereafter.





## Internal Rating Process by Broad Exposure Class

Type of Exposure included in Each Exposure Class

Belfius has developed a wide range of models to estimate PD, LGD and CCF of the following types of counterparties:

### Sovereigns

#### Sovereigns

The scope of the model encompasses sovereign counterparties, defined as central governments, central banks and embassies (which are an offshoot of the central government), and all debtors of which liabilities are guaranteed irrevocably and unconditionally by central governments or central banks.

#### Assimilations to Sovereigns

The in-depth analysis of some public sector counterparties (such as some public institutions, like the National Social Security Office or Buildings Agency) shows that they share the same credit risk as the “master” counterparties to whom they are assimilated (usually local authorities or sovereigns). They are consequently assimilated to these “master” counterparties and benefit from the same PD and LGD as their “master” counterparties.

### Retail

#### Retail – Individuals (Ripar)

These models encompass retail customers (individuals). Individuals are defined as retail counterparties without a self-employed activity or a liberal profession and are not linked to the activity of a legal entity.

#### Retail – Small Professionals (Ribus)

These models encompass small professional retail customers defined as individuals with a self-employed activity or a liberal profession (i.e. doctors, lawyers, etc.) or small companies generating a turnover lower than a certain threshold. A split is made between individuals with self-employed activity or liberal profession and small companies.

#### Retail – Small Companies (RSC)

The models encompass small companies which are defined as companies generating a turnover higher than a certain threshold, but that are still considered as retail counterparties on the basis of distinctive criteria (i.e. not considered as mid-corporate or corporate counterparties).

## Project Finance (Specialised Lending)

This model encompasses the project financing activity of Belfius on all segments of activity in which Belfius intervenes (which are actually mainly Energy and Infrastructure). The specialised lending portfolio is a subgroup of the corporate portfolio which has the following characteristics: the economic objective is to finance or acquire an asset; the flows generated by this asset are the sole or practically the sole source of repayment; this financing represents a significant debt in respect of the liabilities of the borrower; the main distinguishing criterion of risk essentially being the variability in flows generated by the financed asset, much more than the borrower’s ability to repay.

## Insurance Companies (including Monoliners)

Insurance companies are legal entities having insurance activities as their usual profession. The insurance activity consists of covering the potential damage from an uncertain event against the receipt of premiums from policyholders. The received premiums are invested and used as a source of profit by the insurance company. When an event covered by the insurance contract occurs, the policyholder sends a claim to the insurance company, and the claim is paid using the pool of premiums from all policyholders.

## Financial Institutions

### Banks

The scope of the model encompasses worldwide bank counterparties, defined as legal entities which have banking activities as their usual profession. Banking activities consist of the receipt of funds from the public, credit operations and putting these funds at the customers’ disposal, or managing means of payment. Bank status is gained by the delivery of a banking license given by the supervisory authority.

### Corporates

Two models have been designed for corporate counterparties: corporate and mid-corporate models.

#### Corporates

The scope of the model encompasses worldwide corporate counterparties. Belfius Bank defines a corporate as a private or a publicly-quoted company with total annual sales higher than EUR 50 million or belonging to a group with total annual sales higher than EUR 50 million which is not a bank, a financial institution, an insurer or a satellite.



### Mid-Corporates

This model encompasses mid-corporates from Belgium. Belfius Bank defines a mid-corporate as a private company with a total turnover lower than EUR 50 million and belonging to a group with a consolidated total turnover lower than EUR 50 million and with total assets higher than EUR 5 million. This company is not a bank, a financial institution, an insurer or a satellite.

NB: for Belgian and Luxembourg companies the frontier is set at a EUR 250 million turnover.

### Public Sector Entities

Public sector entities represent a large proportion of the Belfius Bank portfolio. Some differences between counterparties have been noticed within this portfolio, and this explains the number of models.

### Local Authorities

This model encompasses Belgian local authorities, namely municipalities and provinces.

Belfius defines local authorities as sub-sovereign governmental elected bodies empowered by the legislation with specific responsibilities in providing public services and with certain resources and a capacity to decide their own practical organisation in terms of administrative procedures, personnel, buildings, equipment, etc.

### Belgian Regions and Communities

An expert methodology has been developed to rate the five Belgian regions and communities which are the French Community, German Community, Flemish Community (including Flemish Region), Walloon Region and Brussels Capital Region.

### Assimilations to Public Sector Entities

The in-depth analysis of some public sector counterparties (such as church companies, municipalities' Social Service Departments, intermunicipal police zones) shows that they share the same credit risk as the "master" counterparties to which they are assimilated (usually local authorities or sovereigns). They are consequently assimilated to these "master" counterparties and benefit from the same PD and LGD as their "master" counterparties.

### Other Satellites

The model encompasses Belgian non-public satellites.

Satellites are entities:

- for whom main activity - i.e. the one generating a very large proportion of their income - is a Public Authority's commitment which has been delegated to the concerned entity; and
- for whom most of the "shareholders" - i.e. those who have the power of final decisions within the entity - are not-for-profit entities; and
- for whom these two main characteristics are not likely to be changed within a year.

Among all the "satellites", the "Public Satellites" are those:

- whose strategic decisions (including financial) are made (or approved) by the Public Authority; and
- whose business cannot be closed down:
  - in particular the entity cannot be declared bankrupt;
  - or if so, either a public authority gets Assets and Liabilities back, or an equivalent entity does.

The "satellites" which do not correspond to this definition are the "other satellites" and are (Belgian perimeter) or will be covered by a specific Internal Rating System.

### Equity and Securitisation Transactions

No internal models have been developed specifically for equity or securitisation transactions which follow a different regulatory approach. Securitisation risk weighting is based on external and not internal ratings (see IV.6.) equities do not require the development of specific models (see IV.5.).

### Default Definition Used in the Models

The "default" notion is uniform, covering all business segments with some minor exceptions due to special characteristics.

The notion of default has been harmonised from the beginning of the Basel II project with the impairment notion used in IFRS. All loans in default and only those flagged as in default give rise to an impairment test (that can or cannot eventually lead to an impairment).



The notion of default is not automatically related to the notion of potential loss (for instance, a loan may present unpaid terms but may be totally collateralised and consequently present a nil expected loss) or to the notion of denunciation (which is decided upon on the basis of the interest the Bank may have to do so).

### Main Principles Used for Estimating the PD

Types of Counterparties	Through the Cycle Models	Default Definition	Time Series Used	Internal/ External Data
Sovereigns	Models are forward looking and through the cycle. They are designated to be optimally discriminative over the long term. The through the cycle aspect of the rating is also addressed in a conservative calibration of the PD.	Default at first day	> 10 years	External
Banks		Default at first day	> 10 years	External
Insurance companies		More than 90 days past due or unlikely to pay criteria	> 10 years	External
Corporates		More than 90 days past due or unlikely to pay	> 10 years	Internal + External
Local Public Sector		More than 90 days past due or unlikely to pay	> 10 years	Internal + External
Specialised Lending		More than 90 days past due or unlikely to pay	6 years	Internal
Mid-corporates		More than 90 days past due or unlikely to pay	6 years	Internal + External
Other Satellites		More than 90 days past due or unlikely to pay	5 years	Internal
Public Satellites		More than 90 days past due or unlikely to pay	5 years	Internal
Retail		More than 90 days past due or unlikely to pay	2 years	Internal
Equity	Specific approach: PD/LGD Approach.	N/A	N/A	N/A
Securitisation	Specific approach: Rating-Based Approach.	Default if related ABS is classified as impairment 1 (loss probability > 50%) or impairment 2 (loss probability = 100%).	N/A	N/A

In order to harmonize risk identification and hence reduce unwanted RWA difference between institutions, EBA has released a new default definition with new thresholds. This material change has been implemented this year accordingly to ECB expectations. The models recalibrations will be done in 2021, in line with ECB's 2 step approach process.

### Main Principles Used for Estimating the LGD

Types of Counterparties	Through the Cycle Models	Time Series Used	Internal/ External Data
Sovereigns	Expert score function on the basis of Fitch country loss risk methodology and internal expert knowledge to discriminate between high and low loss risk.	> 10 years	Internal + External
Banks	Statistical model derived from LGD corporate model and integrating additional risk factors adapted to banking counterparties (country of residence, business profile, etc).	> 10 years	Internal + External
Insurance Companies Corporates	Statistical model based on external rating agencies loss data. The LGD depends on counterparty rating, exposure seniority level, geographic region and macro-economic factors.	> 10 years	Internal + External
Local Public Sector	Statistical model based on the internal existing default cases observed which were related to French municipalities. Final LGD are segmented on the basis of the number of inhabitants and on an economic parameter.	> 10 years	Internal
Specialised Lending	This model belongs to the 'Workout LGD' type: the LGD computation was developed according to the workout of the bank during a 10-year period concerning internal Project Finance default facilities. Cash flows are estimated on the basis of the observed historical recovery process, and LGD is computed by means of discounted cash flows.	10 years	Internal
Mid-Corporates	The LGD model is a white box model with explanatory variables: number of workout years. The LGD is calculated as the multiplication of the LGD unsecured (LGD when the loans are not collateralised) and of the haircut factor taking into account the collateralisation of the loan.	7 years	Internal
Other Satellites Public Satellites	On the basis of internal observation and expert judgement.	5 years	Internal
Retail	LGD determined by product type based on workout recoveries flows. Huge number of counterparts, individual valorization of collateral impossible. Professional loans are segmented in 5 classes based on value of collateral.	7 years	
Equity	Specific approach: PD/LGD Approach.	N/A	N/A
Securitisation	Specific approach: Rating-Based Approach.	N/A	N/A



## XI.2.2. Control mechanisms for rating systems

Belfius is organized to meet the requirements expressed by the Basel regulation regarding the control of the internal rating systems. The controls cover the whole chain of production of the regulatory parameters under all its aspects, e.g. (non-exhaustively):

- the data input
  - are they correctly loaded and up-to-date?
  - are the counterparties addressed to the right model?
- the models
  - do they meet regulatory requirements?
  - are they meaningful?
  - are they sufficiently discriminating?
  - are they stable and robust?
  - are they correctly implemented?
  - are they sufficiently conservative?
- the work of the analysts
  - do they use the models correctly?
  - are the final ratings sufficiently motivated?
  - are the rating procedures respected?
  - are they auditable?
  - are the (re)ratings performed in a timely manner?
- the usage of the model and its outcomes
  - are the parameters used in credit and risk management decisions?
  - are they correctly stored in the systems?
  - do all the users master correctly the model?

and during the whole life cycle of each IRS:

- before its first use or any update
  - in-depth control of methodological and operational issues
- on an annual basis while being used
  - back testing aimed at checking whether the IRS continues to perform well
  - audit of the whole production process
- on a quarterly basis for the work of the analysts
  - endorsement of the rating overrides above a tolerance threshold
  - control of the respect of the rating procedures.

## Responsibilities and Decision Process

The controls are performed by the Validation department<sup>(1)</sup>. Validation also confirms the degree of significance of the model changes, in order to determine the decision process to follow with the ECB (approval required, ex-ante or ex-post notification).

Audit acts as an additional level of control, included in its audit plan<sup>(2)</sup>.

- the market models are reviewed globally (on 3 years basis);
- regarding the credit models, Audit decided to conduct each year a dedicated mission by credit activity segment/type (Retail, Corporate, Public) that aims at assessing the origination and the servicing of the credit activity line including the related models;
- audit also decided to conduct on yearly basis a high level assessment on credit and market models in order to provide the Oversight bodies with reasonable assurance with regards to the evolution of the models, the material changes, the validation process (respect of planning, the evolution of the major recommendation raised by the Validation department).

The decisions regarding the IRS are taken by two Committees.

## The Risk Executive Committee

Composed of the CRO and of his direct reports, it takes the decisions regarding the models:

- green light to submit models or model updates for approval to the ECB (or to put them in production if prior ECB approval is not required);
- endorsement of the validation reports on the recurrent model follow-ups (annual back testing and operational audit);
- endorsement of the corrective action plans recommended by Validation.

The Risk ExCom decisions are further presented to the Risk Policy Committee.

(1) Annual back tests are performed by the Credit Modelling team and validated by Model Validation.

(2) According to the CRD minimal requirement 131, Annex VII Part 4, "Internal Audit has to include in its plan, at least once a year, a review of the IRS and its functioning, including credit scoring and estimation of PD, LGD, EL and CCF. Also compliance with all the minimal requirements has to be verified". At Belfius Bank, this annual verification has been delegated to the Validation and Quality Control department.



## The Rating Committee

The key role of the Rating Committee is to monitor the appropriate use of internal rating systems within the Bank as a whole and to ensure that these IRS are effective. For these reasons, the Rating Committee:

- validates overrides, above tolerance threshold, proposed by analysts<sup>(1)</sup>;
- monitors the homogeneous application within the Bank of the rating and derogation principles;
- validates operational establishment of the models once they are validated by the Risk ExCom.

## Validation

Validation is a direction within the Risk department. It reports directly to the CRO and is not involved in any model development in order to guarantee its independence. Its main missions are:

- to guarantee the reliability of the model outcomes used within Belfius and to verify their compliance with the regulation;
- to highlight their possible weaknesses and to communicate them to all stakeholders (from analysts to top management).

It focuses primarily on regulatory models (Pillar 1 and 2), ALM and market models (post-trade valuations, market risk management) but it can also intervene on other topics.

Validation controls all the aspects of the production of results by the models, from a methodological but also an operational (implementation, usage) viewpoint. It intervenes prior to the first use of the models and afterwards regularly reviews their functioning.

Validation works are summarised in reports indicating the controls that were performed, their findings, proposed corrective actions and, when required, a validation status.

(1) Dedicated "Overrides Committees" are regularly organized for that purpose.

## XI.2.3. Business integration of internal estimates

Internal estimates of Basel parameters are used within Belfius Bank, at present covering a large number of applications in addition to the calculation of the regulatory risk-weighted exposure amounts. They are notably used in the following fields:

- decision-making process;
- credit risk management and monitoring;
- internal limit determination;
- provisioning methodology;
- capital allocation;
- pricing.

### Decision-Making Process

Basel parameters are key elements considered by the Credit Committee in assessing the opportunity to accept or reject a transaction. Credit guidelines have been updated in order to integrate Basel parameters while assessing credit proposals.

### Credit Risk Management and Monitoring

Basel parameters are actively used in periodic credit Risk reporting and also for the individual follow-up of distressed transactions and counterparties within Watch List Committees.

Belfius Bank integrates the Basel parameters to define new internal reporting on the basis of a unique and common reporting credit risk data warehouse and uniform concepts. The counterparty internal ratings, the LGD, the level of EL and the regulatory weighted risks are the key Basel parameters used within the new internal reporting and the credit risk portfolio review.

A central database registers internal ratings and keeps them available for all relevant needs.

### Internal Limit Determination

Basel parameters have been integrated for fine-tuning the Belfius Bank credit limit system and determining delegation levels for credit acceptance.

### Provisioning Methodology

The implementation of Basel parameters has made it possible to develop more synergies between accounting and prudential issues (IFRS/Basel), while relying on the processes, data and tools of the Basel project.



The Basel notion of default and the accounting notion of impairment have converged in relation to Stage 3 impairments.

As a consequence, only defaulted assets identified as such in the Basel compliant risk management systems are identified as impaired assets for both accounting and risk management purposes. However, some exceptions to this general principle exist in relation to some specific Asset Class such as Asset-Backed Securities (ABS). For these types of products, the notion of default cannot be applied due to their characteristics; hence the sole notion of impairment prevails.

### Capital Allocation

Belfius performs its internal capital allocation to its businesses as part of the budget process which will include an “optimisation” phase, based on strategic, competitive and risk-reward considerations of the Business Lines on the one hand and the liquidity, funding and balance-sheet profile of Belfius on the other hand. Completion of the budget process including capital allocation is a preliminary requirement of the Capital Adequacy process.

More specifically, a financial plan including capital allocation and analysis of the evolution of both the results of activity lines and capital supply is performed by the Belfius Finance division. This financial plan is challenged from a risk and capital point of view jointly by Risk/Finance teams and surveyed by the dedicated RAC Committee.

The RAROC pricing tool enables control by all business units of their Normative Regulatory Equity (NRE) capital consumption on a transaction by transaction basis through RoNRE (Return on Normative Regulatory Equity) calculation. Based on this information, business units are able to assess the impact of a particular transaction on their budgeted capital consumption.

### Pricing

To support the credit decision process, a RAROC (Risk Adjusted Return on Capital) based on Economic Capital and a RoNRE (Return on Normative Regulatory Equity) based on Normative Regulatory Equity are calculated, to measure the expected profitability of the credit transaction and/or even the full credit relationship with the customer. Not only the expected income in the form of interest margins is taken into account, however also, inter alia, the operational costs and losses which might be statistically expected on loans are also considered. As a consequence, the Basel parameters are therefore integrated in the pricing.

## XI.2.4. IFRS 9 impairment methodology

We refer to the Risk Report of 2019.

## XI.3. Additional disclosures on the liability side

### XI.3.1. Belfius Bank originations

Belfius currently has three traditional securitisation vehicles: Dexia Secured Funding Belgium, Penates Funding and Mercurius Funding. The total assets of these companies amount to EUR 4,809 million at 31 December 2020 compared to EUR 6,565 million at 31 December 2019.

According to the definition of control under IFRS 10, Dexia Secured Funding Belgium, Penates Funding and Mercurius Funding are included in the consolidated financial statements. Belfius has:

- full power over its securitisation vehicles;
- exposure to their variable returns; and
- the ability to use its power to affect the amount of the returns.

Dexia Secured Funding Belgium (DSFB) is a Belgian securitisation vehicle (société d'investissement en créances (SIC) under Belgian Law) with currently six compartments, one of which with activity, namely DSFB-2.

DSFB-2 (using the second ring-fenced compartment of DSFB) is a securitisation transaction of loans granted to Belgian entities (public and other). All the loans are 100% guaranteed by one of the three Belgian regions. This EUR 1,621 million transaction was launched on 28 April 2008. One tranche of floating rate notes, rated at closing AA/Aa1/AA+ by respectively S&P, Moody's and Fitch, was issued. Belfius Bank has guaranteed the full and timely payment of principal and interest on the notes. As at 31 December 2020, EUR 745 million were still outstanding. The notes had a rating of A-sf/Aa3/A-sf at 31 December 2020. The DSFB-2 Notes are held by Belfius Bank and its subsidiary Belfius Ireland.

Penates Funding is a Belgian securitisation vehicle with currently ten compartments, one of which with activity, namely Penates-6.

On 15 May 2017, Belfius closed a EUR 6,030 million RMBS securitisation transaction. The SPV, Penates Funding acting through its compartment Penates-6, securitised Belgian residential mortgage loans originated by Belfius Bank and issued EUR 2,490 million Class A1 Mortgage-Backed Floating Rate Notes due 2051 (DBRS AAAsf/Moody's Aaa(sf)); EUR 2,490 million Class A2



Mortgage-Backed Floating Rate Notes due 2051 (DBRS AAAsf/Moody's Aaa(sf)); EUR 1,020 million Class B Mortgage-Backed Floating Rate Notes due 2051 (unrated); EUR 30 million Class C Floating Rate Notes due 2051 (unrated).

At 31 December 2019, these ratings were unchanged from their initial rating. The Class A1 Notes were redeemed in full over the course of 2020. The outstanding amount of the Class A2 Notes stood at EUR 2,202 million, while the outstanding amounts of the other classes of notes were still at their initial amount. Hence there was EUR 3,252 million outstanding under Penates-6 at 31 December 2020. The notes are held by Belfius Bank and its subsidiary Belfius Insurance Invest. The Penates-6 senior notes can be used as collateral in agreements with the European Central Bank or other counterparties.

Mercurius Funding is a Belgian securitisation vehicle with currently six compartments. It was established in 2012. One compartment, Mercurius-1, had outstanding notes at the end of 2020.

On 7 May 2012, Belfius Bank closed a EUR 4,124 million SME (Small & Medium Enterprises) CLO securitisation transaction. The SPV, Mercurius Funding acting through its compartment Mercurius-1, securitised Belgian SME loans originated by Belfius and issued two classes of notes: EUR 3,200 million Class A SME Loan-Backed Fixed Rate Notes due 2035; EUR 924 million Class B SME Loan-Backed Fixed Rate Notes due 2037.

On 12 May 2014, the Mercurius-1 issued new notes: EUR 3,200 million Class A SME Loan-Backed Fixed Rate Notes due 2035 (Fitch A+(sf)/Moody's A1(sf)/DBRS A(high) (sf)); EUR 924 million Class B SME Loan-Backed Fixed Rate Notes due 2037 (not rated). The proceeds were used to purchase an additional portfolio of SME loans and to redeem the old notes.

On 25 June 2018, the Mercurius-1 transaction was restructured. The main modifications were on the Interest Rates, the Reserve Fund and the Principal Priority of Payments. The rating of Fitch was also discontinued.

At the end of 2020, the ratings on the Class A Notes were AA(sf) at DBRS and Aaa(sf) at Moody's. The outstanding balance of the Class A Notes and the Class B Notes decreased to respectively EUR 458 million and EUR 424 million at 31 December 2020.

The Mercurius notes are held by Belfius Bank and its subsidiary Belfius Ireland. The notes can be used as collateral in agreements with the European Central Bank or other counterparties.

## XI.3.2. Belfius mortgage pandbrieven programme

### Belfius Mortgage Pandbrieven Programme

Total Amount Outstanding (in EUR)	7,292,000,000
Current Weighted Average Fixed Coupon	0.866%
Weighted Average Remaining Average Life	6.80

#### Characteristics of Cover Assets as at 31 December 2020

##### a/ Residential Mortgage Loans

Outstanding balance of residential mortgage loans	8,708,646,952
Number of borrowers	109,350
Number of loans	189,653
Average outstanding balance per borrower	79,640
Average outstanding balance per loan	45,919
Weighted average original loan to initial value	77.26%
Weighted average current loan to current value	47.04%
Weighted average seasoning (in months)	66.02
Weighted average remaining maturity (in years, at 0% CPR)	12.20
Weighted average initial maturity (in years, at 0% CPR)	17.79
Remaining average life (in years, at 0% CPR)	6.51
Remaining average life (in years, at 2% CPR)	5.96
Remaining average life (in years, at 5% CPR)	5.18
Remaining average life (in years, at 10% CPR)	4.17
Remaining average life to interest reset (in years, at 0% CPR)	5.80
Percentage of fixed-rate loans	85.09%
Percentage of resettable-rate loans	14.91%
Weighted average interest rate	2.243%
Weighted average interest rate fixed rate loans	2.433%
Weighted average interest rate resettable-rate loans	1.123%

##### b/ Registered Cash

Registered cash proceeds under the residential mortgage loans	360,349,086
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##### c/ Public Sector Exposure (Liquid Bond Positions)

Mark-to-Market Value	81,191,320
Accounting Value	76,893,177



## XI.3.3. Belfius public pandbrieven programme

### Belfius Public Pandbrieven Programme

Total Amount Outstanding (in EUR)	2,461,000,000
Current Weighted Average Fixed Coupon	0.476%
Weighted Average Remaining Average Life	4.67

#### Characteristics of Cover Assets as at 31 December 2020

##### a/ Residential Mortgage Loans

Outstanding Balance of Public Sector Assets	3,270,462,284
Number of borrowers	863
Number of loans	28,896
Average Outstanding Balance per borrower	3,789,643
Average Outstanding Balance per loan	113,180
Weighted average seasoning (in months)	100.92
Weighted average remaining maturity (in years, at 0% CPR)	12.67
Weighted average initial maturity (in years, at 0% CPR)	21.12
Remaining average life (in years, at 0% CPR)	6.92
Remaining average life (in years, at 1% CPR)	6.62
Remaining average life (in years, at 3% CPR)	5.96
Remaining average life (in years, at 5% CPR)	5.39
Remaining average life to interest reset (in years, at 0% CPR)	6.34
Percentage of Fixed Rate Loans	89.42%
Percentage of Resetable Rate Loans	10.58%
Weighted average interest rate	2.772%
Weighted average interest rate Fixed Rate Loans	2.932%
Weighted average interest rate Resetable Rate Loans	1.424%

##### b/ Registered Cash

Registered cash proceeds under the Public Sector Exposures	53,942,376
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##### c/ Public Sector Exposure (Liquid Bond Positions)

Mark-to-Market Value	16,058,154
Accounting Value	14,941,344



## XI.4. Glossary

### **ABS** *Asset-Backed Securities*

Securities issued by a vehicle created for the purpose of buying assets from a bank, a company or a state, like trade receivables or inventories, and to provide the seller with cash and the buyer with a financial product that is characterised by a certain risk profile and a rate of return.

### **AIRB** *Advanced Internal Rating-Based Approach*

Institutions using the AIRB approach are allowed to determine borrowers' probabilities of default and to rely on own estimates of loss given default and exposure at default on an exposure-based on an internal model approved by the supervisor. These risk measures are converted into risk weights and regulatory capital requirements by means of risk weight formulas specified by the Basel Committee.

### **ALM** *Asset and Liability Management*

Managing of the net risk position between assets and liabilities, particularly with respect to imbalances generated by the evolutions of interest rates, currencies and inflation, but also maturity mismatch, liquidity mismatch, market risk and credit risk.

### **BRRD** *Bank Recovery and Resolution Directive*

The Bank Recovery and Resolution Directive (BRRD) provides the authorities with comprehensive and effective arrangements to deal with failing banks at national level and with cooperation arrangements to tackle cross-border banking failures. The directive requires banks to prepare recovery plans to overcome financial distress. It also grants national authorities powers to ensure an orderly resolution of failing banks with minimal costs for taxpayers. The directive includes rules to set up a national resolution fund that must be established by each EU country.

### **CBFA** *Commission bancaire, financière et des assurances*

The Belgian Banking, Finance and Insurance Commission is the former Belgian Financial Institutions regulator, since April 2011 succeeded by the FSMA.

### **CCF** *Credit Conversion Factor*

The ratio of the currently undrawn amount of a commitment that will be drawn and outstanding at default to the currently undrawn amount of the commitment. The extent of the commitment will be determined by the advised limit, unless the unadvised limit is higher.

### **CDS** *Credit Default Swap*

Swap contract in which the buyer of the CDS makes a series of payments to the seller and, in exchange, receives a pay-off if a credit instrument (typically a bond or loan) undergoes a defined "Credit Event", often described as a default (fails to pay).

### **CRD** *Capital Requirements Directive*

The Capital Requirements Directive (CRD) for the financial services industry introduces a supervisory framework in the EU which reflects the Basel II and Basel III rules on capital measurement and capital standards.

### **CRM** *Credit Risk Mitigant*

Range of techniques whereby a bank can, partially, protect itself against counterparty default (for example by taking guarantees or collateral, or buying a hedging instrument).

### **CRR** *Capital Requirements Regulation*

The CRD is the legal framework for the supervision of credit institutions, investment firms and their parent companies in all Member States of the European Union and the EEA. The CRR came into force on 27 June 2013, while the supervised entities within its scope are subject to it as of 1 January 2014.

The CRR-Regulation is directly applicable to anyone in the European Union and is not transposed into national law. Much of the CRR is derived from the Basel III standards issued by the Basel Committee on Banking Supervision (BCBS). It includes most of the technical provisions governing the prudential supervision of institutions.

### **CSA** *Credit Support Annex*

A credit support annex provides credit protection by setting forth the rules governing the mutual posting of collateral.

### **CVA** *Credit value adjustment*

Market CVA is the difference between the risk-free portfolio value and the true value portfolio value that takes into consideration the possibility of a counterparty's default. In addition to default risk capital requirements for counterparty credit risk, Basel III introduced an additional capital charge to cover the risk of mark-to-market losses.

### **DR** *Default Rate*

The rate of borrowers who fail to remain current on their loans.

**DVP** *Delivery Versus Payment*

A settlement practice stipulating that cash payment must be made prior to or simultaneously with the delivery of the security.

**EAD** *Exposure At Default*

Estimate of the amount outstanding (drawn amounts plus likely future drawdowns of yet undrawn lines) in case the borrower defaults.

**EAD** *post CRM*

Refers to the amount relevant for the capital requirements calculation having applied CRM techniques; including financial collateral

**EBA** *European Banking Authority*

The European Banking Authority (EBA) is an independent EU Authority which works to ensure effective and consistent prudential regulation and supervision across the European banking sector. Its overall objectives are to maintain financial stability in the EU and to safeguard the integrity, efficiency and orderly functioning of the banking sector.

The main task of the EBA is to contribute to the creation of the European Single Rulebook in banking whose objective is to provide a single set of harmonised prudential rules for financial institutions throughout the EU. The Authority also plays an important role in promoting convergence of supervisory practices and is mandated to assess risks and vulnerabilities in the EU banking sector.

**ECAI** *External Credit Assessment Institutions*

Under the Basel II agreement of the Basel Committee on Banking Supervision, banking regulators can allow banks to use credit ratings from certain approved Credit Rating Agencies when calculating the risk weight of an exposure. Competent authorities will recognise an ECAI as eligible only if they are satisfied that its assessment methodology complies with the requirements of objectivity, independence, ongoing review and transparency, and that the resulting credit assessments meet the requirements of credibility and transparency.

**ECB** *European Central Bank*

The ECB is the central bank for Europe's single currency, the euro. The ECB's main task is to maintain the euro's purchasing power and thus price stability in the euro area. The euro area comprises the 19 European Union countries that have introduced the euro since 1999.

**EL** *Expected Loss*

The amount expected to be lost on an exposure from a potential default of a counterparty or dilution over a one-year period.

**EOPIA** *European Insurance & Occupational Pensions Authority*

European Union financial regulatory institution aiming at promoting a sound regulatory framework and consistent supervisory practices in order to protect the rights of policyholders, pension scheme members and beneficiaries and contribute to the public confidence in the European Union's insurance and occupational pensions sectors.

**FEAD** *Full Exposure At Default*

FEAD is the total exposure at default (EAD), including the total amount of a free credit line and other off-balance-sheet transactions (with the exception of derivatives), before application of credit conversion factors (CCF). EAD is hence seen in this report as an estimation of the maximum extent to which a bank may be exposed to a counterparty in the event of, and at the time of, that counterparty's default.

**FRTB** *Fundamental Review of the Trading Book*

FRTB is the commonly used denomination of the revised market risk framework. The final version was published by the Basel Committee of Banking Supervision (BCBS) on 14 January 2016. According to BCBS, national supervisors are expected to issue final regulations by January 2019, with banks required to report under the new standards by year-end 2023.

**FSMA** *Financial Services and Markets Authority*

The FSMA is the successor to the former Banking, Financial and Insurance Commission (CBFA), which on 1 April 2011 changed its name as a consequence of the changes in its mandate, in particular its exclusive competence for the supervision of rules of conduct. The FSMA is responsible for supervising the financial markets and listed companies, authorising and supervising certain categories of financial institutions, overseeing compliance by financial intermediaries with codes of conduct and supervising the marketing of investment products to the general public, as well as for the "social supervision" of supplementary pensions. The Belgian government has also tasked the FSMA with contributing to the financial education of savers and investors.

**G-SIB** *Globally Systemically Important Banks*

G-SIBs are defined as institutions whose failure would have a significant impact on the financial system or the real economy. The Financial Stability Board in consultation with the Basel Committee on Banking Supervision and national authorities reviews each year the list of G-SIBs based on a common methodology that takes into consideration a.o. the size, complexity and interconnectedness of those institutions. G-SIBs are subject to higher capital buffer requirements, Total Loss-Absorbing Capacity (TLAC) requirements and higher supervisory expectations in terms of risk management and governance, risk data aggregation capabilities and resolvability.

**HVaR** *Historical VaR*

HVaR corresponds to the VaR measurement based on the historical market conditions for the Bank, putting them in order from worst to best. It then assumes that history will repeat itself, from a risk perspective.

**ICAAP** *Internal Capital Adequacy Assessment Process*

The ICAAP file describes how a bank monitors and assesses the adequacy of its minimum capital level regarding the risk it is taking. The file is accompanied by a series of appendices that describe in details the various Ecap models and stress tests methodologies, the complete Risk Appetite policy, Ecap and stress tests policies, Risk Cartography (RICAP) procedure and the Recovery and Resolution Plan (RRP).

**ISDA** *International Swap and Derivative Association*

Trade organisation of participants in the market for over-the-counter derivatives. Its headquarters are in New York, and it has created a standardised contract (the ISDA Master Agreement) to enter into derivatives transactions.

**LCR** *Liquidity Coverage Ratio*

The Liquidity Coverage Ratio forces financial institutions to maintain a sufficient stock of quality liquid assets to withstand a crisis that puts their cash flows under pressure. The assets to hold must be equal to or higher than their net cash outflow over a 30-day period under stress (having at least 100% coverage). The parameters of the stress scenario are defined under Basel III.

**LGD** *Loss Given Default*

The ratio of the loss on an exposure due to the default of a counterparty to the amount outstanding at default.

**LTV** *Loan To Value*

Ratio between the amount borrowed and the appraised value of a property, used in mortgage underwriting to assess the lending risk.

**LRE** *Leverage Ratio Exposure measurement*

The IFRS balance sheet after netting of derivatives & cash collateral and including the off balance sheet commitments. The leverage ratio is the % of LRE which is covered by the Tier 1 capital.

**MBS** *Mortgage-Backed Securities*

Asset-backed securities or debt obligations representing a claim on the cash flows from mortgage loans.

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**MDA** *Maximum Distributable Amount*

The MDA is an amount calculated by the banks in line with article 141 of the CRR. In case banks fall under the MDA, dividend payment, AT1 coupon and variable remuneration will be restricted.

**NBB** *National Bank of Belgium*

The National Bank of Belgium is the current Belgian Financial Institutions regulator. The NBB is in charge of prudential supervision of the less significant institutions and of the insurance sector. However, some tasks are performed in close cooperation with ECB under the Single Supervision Mechanism.

**NBB LAC DT** *Circular NBB Loss Absorbing Capacity of Deferred Taxes Circular*

In Solvency II, the computation of the regulatory capital requirement is based on the loss of economic own funds in case an adverse event would happen. In such an event, the amount of expected taxes to be paid would also be reduced. The LAC DT mechanism enables insurers to reduce the capital requirement by the expected tax decrease. Netting amount

Is the reduction in exposure due to the use of legally enforceable netting agreements, including the effect on potential future exposure in accordance with Article 298 of the CRR.

**NSFR** *Net Stable Funding Ratio*

NSFR is defined as the amount of available stable funding relative to the amount of required stable funding. This ratio should be equal to at least 100% on an on-going basis. "Available stable funding" is defined as the portion of capital and liabilities expected to be reliable over the time horizon considered by the NSFR, which extends to one year. The amount of such stable funding required of a specific institution is a function of the liquidity characteristics and residual maturities of the various assets held by that institution as well as those of its off-balance-sheet (OBS) exposures.

**ORSA** *Own Risk and Solvency Assessment*

ORSA is an internal process undertaken by an insurer or insurance group to assess the adequacy of its risk management and current and prospective solvency positions under normal and severe stress scenarios.



### **O-SII** *Other Systematically Important Institutions*

O-SII is the term used in the EU legislation to designate domestically important banks. National authorities (NBB for Belgium) reviews each year the list of O-SIIs in accordance with the methodology specified by the EBA. Belgian O-SIIs are subject to a capital surcharge.

### **OTC** *Over-The-Counter*

Over-the-counter (OTC) or off-exchange trading is carried out directly between two parties, negotiating bilaterally and privately without any supervision of an exchange.

### **PD** *Probability of Default*

The probability of default of a counterparty over a one-year period.

### **PFE** *Potential future exposure*

Potential future exposure (PFE) is the product of the notional amounts or underlying values as applicable by specific percentages set out in Article 274 of the CRR (Gross Add-on).

### **RAROC** *Risk Adjusted Return On Capital*

Risk-based profitability measurement framework for analysing risk-adjusted financial performance and providing a consistent view of profitability across businesses.

### **RC** *Replacement cost*

The Replacement cost (RC) is the current exposure value, meaning the larger of zero and the fair value of a transaction or portfolio of transactions within a netting set with a counterparty that would be lost upon the default of the counterparty, assuming no recovery on the value of those transactions in insolvency or liquidation.

### **RMBS** *Residential Mortgage-Backed Securities*

RMBS are securities for which the primary source of payments is a mortgage loan or a pool of mortgage loans secured mostly on residential real property. Investors receive payments of interest and principal that are derived from payments received on the underlying mortgage loans.

### **REA** *Risk Exposure Amount* & **RWA** *Risk-weighted assets*

Risk exposure amount (REA) is the total risk exposure calculated as the sum of risk-weighted exposures for credit risk, market risk, counterparty risk and operational risk. The term Risk Weighted Assets (RWA) is still commonly used and refers to the same as well as Total Risk Exposure amount which is the term used by the SRB when referring to MREL.

**SARIC/RCSA** *Self-Assessment of Risks and Internal Controls/Risks and Controls Self-Assessment Process* through which the likelihood and potential impact of operational risks and the effectiveness of controls used to circumnavigate them are assessed and examined.

### **SFT** *Securities Financing Transactions*

SFTs are transactions where securities are used to borrow cash (or other higher investment-grade securities), or vice versa – this includes repurchase transactions, securities lending and sell/buy-back transactions.

### **SPV** *Special Purpose Vehicle*

Separate legal entity created specially to handle a venture on behalf of a company. In many cases, the SPV belongs from a legal standpoint to banks or to investors rather than to the company. The IASB has however stipulated that the company should consolidate the SPV if it enjoys the majority of the benefits or if it incurs the residual risks arising from the SPV even if it does not own a single share of the SPV.

### **SRB** *Single Resolution Board*

The SRB has been operational as an independent EU Agency since 1 January 2015. The SRM started its work on developing resolution plans for banks from January 2015 and became fully operational, with a complete set of resolution powers, on 1 January 2016. The SRB is the resolution authority for banks which are considered significant or in relation to which the ECB has decided to exercise directly all of the relevant supervisory powers, and other cross-border groups, where both the parent and at least one subsidiary bank are established in two different participating Member States of the Banking Union.

### **SREP** *Supervisory Review and Evaluation Process*

The key purpose of SREP is to ensure that institutions have adequate arrangements, strategies, processes and mechanisms as well as capital and liquidity to ensure a sound management and coverage of their risks, to which they are or might be exposed, including those revealed by stress testing and risks the institution may pose to the financial system.

### **SRM** *Single Resolution Mechanism*

The Single Resolution Mechanism entered into force on 19 August 2014 and is directly responsible for the resolution of the entities and groups directly supervised by the European Central Bank as well as other cross-border groups.



### **SSM** *Single Supervision Mechanism*

The SSM operates as a system of common bank supervision in the EU that involves national supervisors and the European Central Bank. From 4 November 2014, banks deemed “significant” are supervised directly by the ECB. Smaller banks, called less significant, continue to be directly monitored by their national authorities, though the ECB has the authority to take over direct supervision of any bank.

### **SVaR** *Stressed VaR*

SVaR corresponds to the VaR measurement based on the worse historical market conditions (stressed period) for the bank.

### **TLOF** *Total Liabilities & Own Funds*

The IFRS balance sheet after netting of derivatives & cash collateral. The amount is used to

- compute the MREL requirement in Bank Recovery & Resolution Directive 1
- compute the MREL subordination requirement in Bank Recovery & Resolution Directive 2 and
- determine the level from which a bank may have access to the Single Resolution Fund.

### **TLTRO(-III)** *Targeted Longer Term Refinancing Operations*

One of the ECB’s unconventional monetary policy instruments. They provide long-term loans to banks and thereby encourage them to increase their lending activity for the benefit of businesses and consumers in the euro area.

### **TRIM** *Targeted Review of Internal Models*

Large scale project conducted by the ECB over 2016-2020 aiming at reducing inconsistencies and unwarranted variability when banks use internal models to calculate the risk weighted assets.

### **UCITS** *Undertakings for Collective Investment in Transferable Securities*

Set of European Union directives that aim to allow collective investment schemes to operate freely throughout the EU on the basis of a single authorisation from one member state. In practice many EU member nations have imposed additional regulatory requirements that have impeded free operation with the effect of protecting local asset managers.

### **VaR** *Value at Risk*

VaR represents an investor’s maximum potential loss on the value of an asset or a portfolio of financial assets and liabilities, based on the investment timeframe and a confidence interval. This potential loss is calculated on the basis of historical data or deduced from normal statistical laws.

