BAWAG GROUP AG
QUALITATIVE DISCLOSURE REPORT ACCORDING TO REGULATION (EU) NO. 575/2013 (“CRR”)

2021

CONTENTS

QUALITATIVE DISCLOSURE

Qualitative disclosure

LIST OF TABLES

LIST OF ABBREVIATIONS

ALM	Asset Liability Management
AML	Anti Money Laundering
AS	Application Scoring
BCBS	Basel Committee on Banking Supervision
BP	Basis Point
BPV	Basis Point Value
BS	Behavioral Scoring
BWG	Bankwesengesetz (Austrian Banking Act)
CAC	Credit Approval Committee
CCF	Credit Conversion Factor
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CHAID	Chi-square Automatic Interaction Detectors
CHF	Swiss Franc
CLO	Collateralized Loan Obligation
CMM	Capital Management Meeting
CRD	Capital Requirements Directive
CRO	Chief Risk Officer
CRR	Capital Requirement Regulation
CSA	Credit Support Annex
CET1	Common Equity Tier 1
EAD	Exposure at Default
EBA	European Banking Authority
ECB	European Central Bank
ECL	Expected Credit Loss
EDP	Electronic data processing
EEA	European Economic Area
ERM	Enterprise Risk Meeting
ESG	Environmental, Social and Governance
EUR	Euro
EV	Economic value
EVE	Economic value of equity
FACE	Free Available Cash Equivalent
FMA	Financial Market Authority
FTP	Funds Transfer Pricing
FVPL	Fair Value through Profit or Loss
FVOCI	Fair Value through Other Comprehensive Income
FX	Foreign Exchange
GBP	British Pound
GDP	Gross Domestic Product
HQLA	High-Quality Liquid Assets
IAS	International Accounting Standards
ICS	Internal Control System
ICT	Information and Communications Technology
ICAAP	Internal Capital Adequacy Assessment Process
ID	Identity Document
IFRS	International Financial Reporting Standards
IKS	Internal Control System
ILAAP	Internal Liquidity Adequacy Assessment Process
IRB	Internal Ratings Based Approach

ISDA	International Swap and Derivatives Association
ISTC	ICAAP & Stress Test Committee
KRI	Key Risk Indicator
KSHK	Kreditsicherheitenkatalog (Credit Collateral Catalogue)
KSV	Kreditschutzverband
KYC	Know your Customer
LAS	Liquidity Adequacy Statement
LCR	Liquidity Coverage Requirement
LGD	Loss Given Default
LTIP	Long Term Incentive Program
LTV	Loan-to-Value
NFR&ESGC	Non-Financial Risk & Environment Social Governance Committee
NII	Net Interest Income
NPL	Non-performing loans
PD	Probability of Default
PIP	Product Implementation Process
P&L	Profit and Loss
PSC	Portfolio Steering Committee
PVBP	Present Value of Basis Point
RAP	Risk Adjusted Pricing
RBC	Risk Bearing Capacity
RCC	Risk and Credit Committee
RCSA	Risk Control Self-Assessment
RM	Risk Modelling
RMBS	Residential Mortgage Backed Securities
ROC	Receiver Operating Characteristic
RWA	Risk Weighted Assets
SA-CCR	Standardized Approach for Counterparty Credit Risk
S-ALCO	Strategic Asset and Liability Committee
SEQ	Sicherheitenerlösquotient (Collateral Return Rate)
SICR	Significant Increase in Credit Risk
SME	Small and Medium Enterprises
S&P	Standard & Poor’s
SSPE	Securitisation Special Purpose Entity
TM	Treasury & Markets
TMA	Asset Liability Management
TPU	Temporary Partial Use
UGB	Unternehmensgesetzbuch (Austrian Commercial Code)
USD	US-Dollar
VaR	Value-at-Risk
WAL	Weighted Average Life
WAM	Weighted Average Maturity
WGG	Austrian Non-profit Housing Act

DISCLOSURE INDEX

Review of risk management systems according to Article 435 (1) point (e) CRR	Consolidated Annual Report IFRS 2021
Figures and information according to Article 435 (1) point (f) CRR	Consolidated Annual Report IFRS 2021
Information according to Article 41 FMA circular letter on accounting issues in connection with derivatives for controlling interest rates	BAWAG P.S.K. Annual Financial Report according to Section 124 Stock Exchange Act 2018
Details on accounting and valuation methods according to Article 447 point (a) CRR	Consolidated Annual Report IFRS 2021

GENERAL PRINCIPLES

According to Article 13 of Regulation (EU) No 575/2013 (hereinafter abbreviated to "CRR"), this Disclosure Report is published on the BAWAG Group AG level. BAWAG Group AG is a financial holding company in the form of a corporation. Its main business purpose is the management of the company's assets (BAWAG P.S.K. with its subsidiaries). From a risk perspective, the main Bank-wide steering processes are performed by its subsidiary, BAWAG P.S.K. AG. These processes are disclosed in this report.

SCOPE OF CONSOLIDATION AND CONSOLIDATION METHODS

Article 436 points (a), (b) sublit (i-iv) CRR

Owing to diverging regulations in the International Financial Reporting Standards ("IFRS") and the CRR, there are two different sets of consolidation guidelines, one for accounting and one for regulatory purposes which also lead to two different scopes of consolidation. The following paragraphs present the scopes of consolidation and explain changes that occurred in 2021.

Consolidation for accounting purposes

In accordance with IFRS 10, the scope of consolidation includes BAWAG Group AG and all material subsidiaries owned directly and indirectly.

The Group's share in the total assets and profit or loss of the subsidiary are the criteria for materiality.

The consolidated financial statements as of 31 December 2021 contained 60 fully consolidated companies and two companies that are accounted for using the equity method. The book value of associated equity interests including banks not consolidated at equity amounted to € 0 million as of 31 December 2021.

Controlled companies with a book value of € 23 million were not consolidated because of their negligible effect on the assets, financial and earnings position of the Group. The proportionate total assets (higher than € 30 million) and profit or loss (higher than € 3 million) of the subsidiary are the criteria for inclusion. Subsidiaries with a negligible effect on the assets, financial and earnings position of the Group are not included in the consolidation.

- In the first quarter 2021, the LSREF3 Tiger entities (five real estate companies located in Luxembourg each of which them holds an investment property in the United Kingdom) and their two holding companies were deconsolidated.
- In the second quarter 2021, E2E Kreditmanagement GmbH as the transferring company was merged with E2E Service Center Holding GmbH as the absorbing company. Due to the merger, E2E Kreditmanagement GmbH was eliminated from the scope of consolidation. E2E Service Center Holding GmbH was then renamed to E2E Services GmbH.
- Also in the second quarter 2021, ROMAX Immobilien GmbH was deconsolidated due to immateriality.
- In the third quarter 2021, RF 12 BAWAG Leasing Gesellschaft m.b.H. was deconsolidated due to immateriality.
- In the fourth quarter 2021, BAWAG P.S.K. Datendienst GmbH as the transferring company was merged with BAWAG Services GmbH as the absorbing company. Due to the merger, BAWAG P.S.K. Datendienst GmbH was eliminated from the scope of consolidation.
- Also in the fourth quarter 2021, SWBI Stuttgart 2 GmbH, SWBI Stuttgart 3 GmbH, SWBI Mainz 1 GmbH, SWBI Darmstadt 1 GmbH and SWBI München 1 GmbH were deconsolidated due to immateriality. SWBI München 1 GmbH as the transferring company was then merged with SWBI Stuttgart 2 GmbH as the absorbing company.

Furthermore SWBI Darmstadt 1 GmbH as the transferring company was merged with SWBI Mainz 1 GmbH as the absorbing company.

- Furthermore, DEPFA BANK plc and its subsidiary DEPFA ACS BANK DAC were acquired and consolidated for the first time in the fourth quarter 2021.
- In addition, Feldspar 2016-1 Mortgage Holding Limited and Feldspar 2016-1 PLC were deconsolidated due to immateriality in the fourth quarter 2021.
- Finally, Garrison Earlsfort Investments 2 DAC and its subsidiaries Dromalane Mill Limited, Fairgreen Shopping Centre (Carlow) Limited and GEI Newry Ltd were consolidated for the first time in the fourth quarter 2021 due to control according to IFRS 10.

Consolidation for regulatory purposes

The scope of consolidation in accordance with the CRR includes BAWAG Group AG as the highest financial holding company, and all material subsidiaries owned directly and indirectly.

Consolidation for regulatory purposes is carried out in accordance with Article 18 and 19 CRR, with the financial statements of the individual companies and the consolidated financial statements being prepared in accordance with the principles of the IFRS (International Financial Reporting Standards).

The criteria used to determine the scope of consolidation are total assets and off-balance sheet items. The scope of consolidation for regulatory purposes is different from the scope of consolidation for accounting purposes.

As of 31 December 2021, the scope of consolidation for regulatory purposes included 46 fully consolidated companies, 2 companies that were proportionally consolidated and 8 companies that were accounted for using the equity method.

The following table shows an overview of the companies that are treated differently in the scopes of consolidation for accounting and for regulatory purposes:

Table 1: Divergent consolidation basis

	IFRS	CRR
	IFRS	CRR
BAWAG Leasing & fleet s.r.o. Prague	FVPL	F
BAWAG Leasing s.r.o. Bratislava	FVPL	F
Bonnie RE UK 1 B.V.	F	E
Fides Leasing GmbH	FVOCI	P
Gara RPK Grundstücksverwaltungsgesellschaft m.b.H.	FVPL	F
HFE alpha Handels-GmbH	FVOCI	P
Kommunalleasing GmbH	FVOCI	F
Promontoria Holding 136 B.V.	F	E
PT Immobilienleasing GmbH	FVOCI	F
Dromalane Mill Limited	F	E
Fairgreen Shopping Centre (Carlow) Limited	F	E
GEI Newry Ltd.	F	E
SWBI Stuttgart 1 GmbH	F	E

F .... Fully consolidated
P .... Proportionally Consolidated
E .... Equity consolidated
FVOCI .. Equity Instruments at Fair Value Through Other Comprehensive Income
FVPL .... Equity Instruments at Fair Value Through Profit or Loss

Significant subsidiaries in terms of Article 43 CRR were not deducted from CET1, as they did not exceed the defined threshold of Article 48 CRR. For significant positions in instruments of supplementary capital, there is an obligation for deduction exists (Article 66 CRR).

According to Article 36 (1) point (h) institutions shall deduct the applicable amount of direct, indirect and synthetic holdings by the institution of CET 1 instruments of financial sector entities where the institution does not have a significant investment in those entities.

Non-significant subsidiaries in terms of Article 46 CRR were deducted from CET 1 in the amount of € 23.5 million and from Additional Tier 1 in the amount of € 1.7 million, as they did exceed the defined threshold of Article 46 CRR.[1]

As all subsidiaries subject to banking regulation laws are included in the scope of consolidation or all relevant book values are deducted from own funds in the event that the threshold is exceeded, there is no shortfall in own funds in terms of CRR, Part 8, Title II, Article 436 point (d).

IMPEDIMENTS TO THE TRANSFER OF OWN FUNDS

Article 436 point (f) CRR

There are currently no restrictions or other significant impediments to the transfer of own funds or regulatory equity within BAWAG Group.

[1] referring to column "(a) Amounts as in published financial statements" of the template "Composition of regulatory own funds (EU CC1)" in the quantitative disclosure report according to regulation (EU) NO. 575/2013 ("CRR")

TOTAL SHORTFALL IN OWN FUNDS OF ALL SUBSIDIARIES NOT INCLUDED IN THE SCOPE OF CONSOLIDATION

Article 436 point (g) CRR

No shortfalls in own funds are known among subsidiaries that are not consolidated but deducted from own funds.

USAGE OF ARTICLES 7 AND 9 CRR

Article 436 point (h) CRR

There are no issues for the usage of Articles 7 and 9 CRR in BAWAG Group.

RISK MANAGEMENT

GROUP-WIDE RISK MANAGEMENT

Article 435 (1) point (b) CRR
Article 435 (2) point (a) – (e) CRR
Article 435 (1) point (e) – (f) CRR

Risk management decisions are taken at various places within BAWAG Group on daily basis. The systematic orientation of risk decisions at the company's targets requires the development of a common fundamental understanding concerning the risk-related issues, the specification of strategic and operational objectives in the individual business units as well as a comprehensive process of continuous risk management covering all risk areas.

The guidelines regarding the risk management are laid down in framework of risk management documents. The Governance Policy documents the group-wide governance arrangements with particular focus on the risk governance (i.e. risk principles, risk culture and the risk organization). The Risk Strategy (derived from the specifications defined in the business strategy) considers the risk appetite statement, details about the ICAAP-Framework (economic and normative perspective) including the capital allocation structure), concentration risk features reflecting how the Group manages concentration risk and the risk catalogue including the respective risk definitions. The management of the individual risk types is part of specific risk guidelines.

The Management Board determines the business strategy for the Group and the individual business segments as part of its risk management responsibilities and defines target values for the key ratios. The Management Board then derives from this business strategy the Risk Strategy and sets the risk appetite for the current planning period. Finally, the Management Board takes fundamental decisions with respect to the processes to be applied to identify, measure, control and monitor risks.

The Chief Risk Officer (CRO) is a member of the Management Board and assumes responsibility as the risk manager for the entire Group. All risk management divisions report to the CRO. The CRO regularly informs the Management Board about the current risk situation. As required by the supervisory authority, this organizational structure separates the front-office and back-office units, particularly risk management, at all levels of BAWAG Group including the Management Board level.

In addition, the Management Board is informed within the Enterprise Risk Management (ERM) Committee about all risks within the Group on a monthly basis. With regard to the ERM Committee the provided Group Risk Report builds the information basis in which various key risk indicators are reported, analyzed and their development commented. Furthermore, any significant change in the risk situation must be immediately reported to the full Management Board. The external stakeholders are informed about the risk situation on a semi-annual basis (in the form of the annual report and half year report). The reports and presentations are published on BAWAG Group's website.

BAWAG Group has implemented a clear risk strategy, which is fully aligned with the Group's overall business strategy. The Management Board defines and approves the overall risk appetite and risk strategy on an annual basis. By defining the risk strategy, the overall risk appetite serves as a constraint and represents the Group's intention to use a defined extent of the available internal capital for risks, taking into consideration regulatory and economic capital availability, the liquidity position and the profitability expectations. The risk strategy breaks the overall risk appetite down into more detailed business appetite metrics and limits.

The Risk Strategy is defined by the Risk Controlling division and states the Risk Appetite and defines the ICAAP capital allocation based on the results of the Risk Self-Assessment. All the components of the ICAAP economic perspective are forecasted for the year, based on the capital planning; i.e. all the limit indications provided in the Risk Self-Assessment are already assessed in order to be consistent with the respective Risk Appetite targets and limits and are considered for the capital allocation.

The Risk Appetite Statement provides a compact overview about the targets and limits set in term of Capital and, Liquidity metrics for the year 2021.

Table 2: Risk Appetite Statement

	YE 2021	Target[1)]	Limit[1)]
CET1 ratio [2)]	14.97%	> 12.25%	> 9.14%
Tier 1 ratio [2)]	17.33%	n.d.	> 11.01%
Total Capital ratio [2)]	20.42%	n.d.	> 13.51%
ICAAP limits utilization [3)] (PSF level 1 to level 4)	42%	< 90%	< 95%
LCR	239%	> 120%	> 110%
NSFR	139%	n.d.	> 110%
FACE	6,050	n.d.	> € 1.5bn
Leverage ratio	6.07%	n.d.	> 3%
NPL ratio	1.4%	< 3%	< 3.5%

1) Target and limit were approved within the 2021 risk strategy and were valid for 2021 as a whole.
2) Excluding Pillar 2 Guidance buffer of 1% according to SREP.
3) In the context of ICAAP utilization, the defined 90% is not to be understood as a target, but as a warning level.

Other important figures and information according to Article 435 (1) point (f) CRR can be found in the annual report.

The Risk Strategy and the Governance Policy are updated on an annual basis, approved by the full Management Board, approved by the Risk and Credit Committee and recommended for approval to the Supervisory Board, and in a final step, approved by the Supervisory Board. The Group Risk Report is presented to and discussed within the Risk and Credit Committee on a quarterly basis.

Proactive risk management is a major target of BAWAG Group and is among the core tasks of the risk organization. Efforts must be made to ensure that BAWAG Group takes on risks that are not excessively high (but rather reasonable and measurable). At the same time, the business model must also definitely be supported along with the planned business growth defined in it. Basically, BAWAG Group follows a low-risk strategy, which means that risks are managed conservatively.

With regard to data management (especially risk data management), BAWAG Group pursues strategic objectives that are fully compliant with the regulatory requirements of BCBS239 as the effectivity and efficiency of Risk Management is dependent on appropriate, correct, complete and consistent data that is available on a timely basis. Therefore, BAWAG Group emphasizes the importance of strong data (quality) management and the continuous aim for improvement in this regard.

Moreover, all rating and scoring systems are subject to an annual validation process in which the adequacy and the performance of the systems are monitored. If further measures are required, appropriate analyses will be initiated and, if necessary, adjustments will be implemented and communicated to the Management Board.

Due to the variety of monitoring processes, ongoing reporting activities and the immediate introduction of countermeasures in the case of significant deviations from the target risk profile defined in the Risk Strategy, it is ensured that the risk management processes and systems are appropriate.

Risk management organization as of 31.12.2021

The Chief Risk Officer (CRO) is responsible for the Risk Control function and for monitoring the risk management framework across the entire Group.

BAWAG Group applies a Group-wide Fit and Proper Policy. It sets forth the procedure for selecting members of the management body and for reviewing actual knowledge, skills and experience. In addition, the aspects of the personal reliability, internationality and age structure of the members are to be taken into account.

The following risk divisions report directly to the Chief Risk Officer and, in the case of the Group Data Warehouse division, to both, the Chief Risk Officer and the Chief Financial Officer:

- Group Data Warehouse
- Validation
- Risk Controlling
- Risk Modelling
- Commercial Risk Management
- Retail Risk Management

The Group follows an integrated risk management approach which consistently and coherently covers all risk throughout the Group with full alignment of the risk management units of subsidiaries.

The Group Data Warehouse division is responsible for the overall operation, maintenance and further development of the Data Warehouse and perform the business support for all Data Warehouse related topics for the Group. The focus is on the data content itself and the reporting/usage of the data.

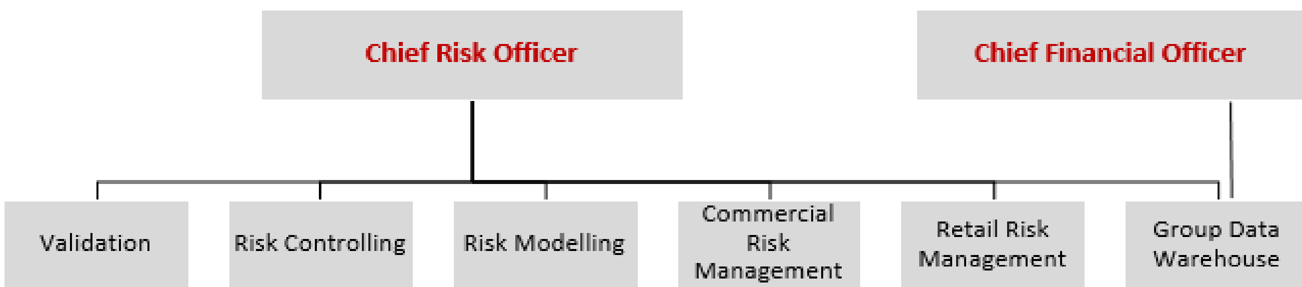
The Validation division is responsible for the model validation of the Group's internal risk models. It is an independent unit to ensure the adequate quality of the risk models and their performance. Regular validation is performed on at least an annual basis, and pre-implementation validation reports are prepared in the event of material model changes. As part of the second line of defense, Validation takes on responsibility for data governance and the validation function. The head of Validation also acts as Data Governance Manager and reports in this function directly to the full Management Board. In addition, the Validation division is responsible for the operational risk management including the internal control system, the product introduction process, outsourcing management and business continuity management. Furthermore, the Validation division is responsible for the coordination of the implementation and monitoring of ESG (environmental, social and governance) risks in all risk divisions and also oversees the risk due diligence and integration function, which covers the steering of M&A and integration-related projects for the risk function.

The Risk Controlling division is responsible for the monitoring and reporting of credit risk and as well the development of the ICAAP and stress testing framework. The main tasks include the ICAAP (normative and economic perspective) calculation for credit risk, the credit risk stress testing (internal and regulatory), credit risk reporting and the calculation of the Stage 1–3 provisions. Risk Controlling is also responsible for the annual review of the Risk Strategy, Governance Policy and Risk Appetite.

Risk Modelling is responsible for developing, implementing and maintaining risk models, techniques, risk management practices, analysis and reporting for market, liquidity and credit risk. The aim is to accurately measure all types of respective risks using a comprehensive set of quantitative analytics and risk metrics, including economic, regulatory and accounting considerations. Furthermore, the division's tasks include the valuation of financial instruments and ensuring the integrity of data and market parameters used in this context.

Operative credit risk for non-retail lending is managed within the Group by Commercial Risk Management. In daily business, credit risk is managed in cooperation between relationship and risk management based on the dual control principle and assigned authorities. Commercial Risk Management is also responsible for the non-retail sub- and non-performing portfolio, which is primarily managed by the Corporate Restructuring and Workout department.

The Retail Risk Management function is responsible for managing the entire credit risk life cycle (including real estate appraisals, fraud management and collections) for Retail & SME customers.



The above risk management divisions are directly subordinated to the Chief Risk Officer (CRO) and in case of the Group Data Warehouse division, to both, the Chief Risk Officer and the Chief Financial Officer, and periodically referred to the following committees at the Management Board level:

The **Enterprise Risk Meeting (ERM)** is a monthly risk meeting of all members of the Management Board and is chaired by the CEO. It takes fundamental risk decisions, such as:

- approving the Risk Strategy and determining the risk appetite, and, if needed, giving recommendations to the Supervisory Board on changes and modifications
- approving and (if required) amending the capital allocation in the ICAAP framework of the Bank
- delegating competence for credit risk limit setting to the Portfolio Steering Committee (PSC) at the profit sub-segment level (level 3) and for specific countries and industries within each sub-segment (level 4)
- approving capital reallocation in level 3 and level 4 above € 40 million upon explicit recommendation by the PSC
- delegating competence for market risk limits for the Group to the S-ALCO
- reviewing and approving underwriting guidelines for all business units
- reviewing significant findings resulting from regulatory examination and initiating action for remedy

- discussing the monthly Group Risk Report
- discussing the monthly Capital Report
- reviewing and approving the use of rating models, scorecards and cut-offs as well as the development of or changes to risk parameters
- reviewing and approving results or rating and scoring model validation and the resulting actions
- reviewing and approving or recommending (according to regulatory requirements) credit policies

Furthermore, the ERM has the following competences and authorities regarding stress testing whenever required, at least semiannually:

- Check of requirements concerning stress testing
- Identification of risk factors
- Definition and review of stress test scenarios
- Interpretation of results of stress tests
- Definition of risk measures

Credit Approval Committee (CAC): Approves loan applications within the authorities defined in the Competence and Power Regulation.

Strategic Asset and Liability Management Committee (S-ALCO): This committee is the key decision-making body on all topics related to market and liquidity risk. The S-ALCO allocates the respective risk limits and serves as the escalation body for exceeding individual limits or regulatory requirements. Furthermore, all relevant Market- and Liquidity Risk reports as well as ALM and Treasury reports are presented to the board via this committee.

Non-Financial Risk & ESG Committee (NFR&ESGC): This committee is chaired by the CRO and is responsible for all non-financial risks and topics related to environmental, social and governance with Management Board relevance. Among others (the following list is not exhaustive), this committee deals with Bank-wide NFR Risk Assessment (as part of the Group Risk Strategy), significant outcomes of sub risk self-assessments including monitoring of utilization of operational risk sub limits, process optimizations and discontinued processes which could imply reputational risk (as well as an increase in customer complaints) as well as changes in regulatory requirements (report to Regulatory Office, Legal or designated project leaders). Additionally, anti-money laundering/counter terrorist financings (AML/CTF), ethics, conduct and compliance themes are dealt with along with the regular Securities Compliance and AML/CTF reports. Further, regular reports in the NFR&ESGC include the Operational Risk Report, Outsourcing Report, Business Continuity Management Report, Information Security Report, Complaints Management Report, Regular update of ESG topics, BWG Compliance Report, Securities Compliance, etc.

The **Data Quality Governance Board (DQGB)** is responsible for decisions of measures concerning Data Quality Management, Strategy and Governance. It is a decision-making body (e.g. prioritization or ownership) and escalation level for the Data Subject Area Committee (DSAC) on the division level. Moreover, the DQGB assigns responsibility regarding DQ measures, error corrections, ownership of findings, task distribution, etc. and approves significant changes regarding DQ-relevant topics. Among others (the following list is not exhaustive), this committee is responsible for the following topics:

- Decision of measures concerning Data Quality Management, Strategy and Governance
- Decision making (e.g., prioritization or ownership) and escalation level for the DSAC
- Assignment of responsibilities with regard to DQ measures, error corrections, ownership of findings, task distribution, etc.
- Strategic decisions regarding the following topics:
    - DQM organization, governance and strategy
    - Data deliveries from subsidiaries and reporting data flows
    - Risk data aggregation and data lineage capabilities

  - Data ownership, data access management
  - Reconciliation, data architecture, data dictionary

The **Model Governance Committee (MGC)** is responsible for the steering and monitoring of all risk models according to the model inventory including the overall design of the model governance framework. Furthermore, the MGC deals with the (pre-) approval and monitoring of the modelling and validation planning as well as the IRB roll-out plan. Moreover, model-related findings (both internal and external) are regularly presented to the Model Governance Committee. It also acts as the internal supervision body for ongoing IMIs and, together with the ERM, it approves (pre-) application packages.

Various committees are established at the Supervisory Board level. The most essential one from a risk perspective is the **Risk and Credit Committee (RCC)**, which also deals with the Group Risk Report. Four meetings were held in 2021.

Under the current valid version of the Rules of Procedure for the Supervisory Board of BAWAG Group AG dated 1 October 2021, the RCC has the following responsibilities:

- approves the granting of loans and lines of credit as well as other forms of financing (including but not limited to credit derivatives and receivables represented by securities) to individual borrowers or groups of associated customers within the meaning of Article 392 CRR (exposures that equal 10% or more of the Bank's own funds)
- reports annually to the Supervisory Board on large exposures and investments
- decides on transactions with the Bank's affiliated parties within the meaning of Article 28 BWG
- approves material credit policies and advises the Management Board regarding general questions of credit and risk policy
- advises the Supervisory Board on the current and future risk appetite and Risk Strategy and monitors the implementation
- regularly monitors the effectiveness and efficiency of the risk management system and compliance with legal and regulatory requirements.
- reviews whether prices of offered services and products fully take into account the business model and the risk strategy
- reviews whether incentives provided by the Bank´s remuneration system take into consideration risk, capital, liquidity and the likelihood and timing of earnings

In 2021, the **ESG Committee (ESGC**) was established. This committee deals with the review of the Group-wide ESG strategy and ESG targets and the monitoring of their implementation and reviews regular updates on ESG-related topics. Furthermore, the committee advises the Supervisory Board regarding the current and future risk appetite and risk strategy relating to ESG risks. It also monitors the effectiveness and the efficiency of the management of ESG risks (including risk control, risk policies and management reporting on ESG risks) as well as the compliance with legal and regulatory requirements with regard to ESG topics. The ESG Committee held one meeting in 2021.

Quarterly ESG Committee on the Supervisory Board level established to ensure comprehensive management of upcoming ESG requirements and targets focusing on all dimensions (environmental, social and governance)

Since ESG risks span across all risk management pillars, we pursue a multidimensional steering approach within our risk management framework. Our "safe and secure" risk profile is a core strategic pillar and commitment towards our internal and external stakeholders, especially in relation to ESG risks. BAWAG Group has established a wide-ranging and forward-looking risk management framework, taking into account ESG risks as an integral component.

The interaction of ESG risks and other material risk types is evaluated as part of the overarching risk materiality assessment. Within BAWAG Group's portfolio steering framework, both high ESG-risk sectors and countries are limited accordingly maintaining a very low exposure to high-risk ESG industries and de minimis oil & gas exposure. In particular, the management of restricted and prohibited sectors as part of the underwriting process is essential in this regard. As part of our robust governance framework, ESG risk management is embedded in our key policies and processes, ensuring an appropriate consideration of ESG risks within outsourcing management, product introductions and so on. Numerous awareness initiatives such as townhall events, newsletters and many more ensure that the strategy for managing ESG risks is recognized and practiced across the organization.

In 2021, HR-related ESG targets were incorporated into BAWAG Group's operating plans: In terms of diversity, the Nomination and Remuneration Committee has established a female gender quota of 33% for both the Supervisory Board as well as the Senior Leadership Team (including the Management Board) by 2025. Attracting and retaining the right mix of employees is challenging. Great progress has been made with the defined initiatives in recent years. One key aspect has been to encourage women to participate in personnel development programs.

BAWAG Group encourages women to take on leadership roles, in particular after maternity leaves. The strategy for reaching this goal was further developed and defined together with the BAWAG Group Women's Initiative and Human Resources. The focus is on promoting female employees within the Women's Promotion Program, internal and external mentoring programs for female leaders and experts, gender-specific workshops for all female employees and appointing females as Supervisory Board and Management Board members of subsidiaries. The BAWAG Group Women's Initiative Framework consists mainly of the following initiatives:

- Women's Initiative

  The BAWAG Women's Initiative is a network of female experts and female managers from all areas of the Bank supported by the Management Board of BAWAG Group. The goal of the initiative is to promote equality for women in BAWAG Group in the form of achieving career goals in management or expert positions, monetary equality and the compatibility of family and career.

- Women's Advancement Plan

  The Women's Advancement Plan, which has been in force since 2012, serves as a binding framework for promoting equality and ensuring equal opportunities for women and men in the company. The plan is based on four principles and concrete measures:

  - Raising awareness
  - Equal career opportunities
  - Financial equality
  - Promoting a better work-life balance for employees

- Women's Mentoring Program

  The Women's Mentoring Program is aimed at female employees with longer management experience who would like to benefit from external top managers from the business world as mentees and broaden their horizons as well as at all female colleagues who would like to develop themselves further, have already gained initial leadership experience or would like to move in this direction.

  The goal of the Women's Mentoring Program is to give female employees the opportunity to deal intensively with the topic of women and careers, to have an in-depth personal exchange with their mentors and to build a network within the Bank. In this program, top executives from BAWAG Group make themselves available to the female mentors to share their experience in joint discussions and to provide advice to the mentees.

During the mentoring year, the mentees are offered professional and personal development content in workshops, networking events and extensive further training as part of the BAWAG Group Business Academy. Participants have the opportunity to talk to internal experts on the topics of finance, risk and retail, as well as to exchange ideas with members of BAWAG Group's Management Board in a very personal setting during business talks. The 7th BAWAG Group Women's Mentoring Program was successfully completed in Q3 2021.

Since 2013, BAWAG has been committed to the compatibility of work and family as part of a structured auditing process and received certification as a family-friendly company, which is valid for three years. Since then, BAWAG has completed the auditing process on an ongoing basis and has been recertified with the work and family audit certificate several times.

- Number of directorships held

  Disclosure of the number of management and supervisory functions held by BAWAG P.S.K. Management and Supervisory Board members pursuant to EBA/GL/2016/11 and Article 435 (2a) CRR as of 31 December 2021:

Table 3: Functions held by Management Board and Supervisory Board members

Name	Function at BAWAG P.S.K.	Number of Management Board functions	Number of Supervisory Board functions
Egbert Fleischer	Chairperson of Supervisory Board	0	3
Frederick Haddad	Member of Supervisory Board	7	3
Kim Fennebresque	Member of Supervisory Board	0	5
Adam Rosmarin	Member of Supervisory Board	1	2
Tamara Kapeller	Member of Supervisory Board	0	4
Gerit Schneider	Member of Supervisory Board	1	2
Anas Abuzaakouk	Management Board, CEO	2	0
David O´Leary	Member of Management Board	2	1
Andrew Wise	Member of Management Board	2	2
Enver Sirucic	Member of Management Board	3	2
Sat Shah	Member of Management Board	2	2
Guido Jestädt	Member of Management Board	2	4

INTERNAL CAPITAL ADEQUACY ASSESSMENT PROCESS (ICAAP) AND GROUP-WIDE STRESS TEST

Article 435 (1) point (a) CRR
Article 438 point (a) CRR
Article 439 point (a) CRR

The Internal Capital Adequacy Assessment Process (ICAAP) is part of the regulations known as Pillar II. The ICAAP-related processes and methods established at BAWAG Group ensure that the existing internal capital is adequate to cover the relevant risks that may arise.

According to the ICAAP Guides issued in November 2018 by the European Central Bank, BAWAG Group has implemented both the normative and economic perspectives for the Group steering.

The Risk Self-Assessment, which is conducted on an annual basis, provides an overview of BAWAG Group's risk situation using quantitative and qualitative evaluation methods, i.e. all potential risks arising in connection with the implementation of the business strategy are evaluated with respect to their relevance, materiality and their impact on BAWAG Group. Material and non-material risks are considered under the economic perspective, while the normative perspective encompasses Pillar I risks (credit risk, market risk, operational risk) and all other material risks.[2].

BAWAG Group's economic perspective compares the quantified risks, in the form of so-called economic risk covering both expected and unexpected losses, with the internal capacity. The economic perspective is calculated on a monthly basis. The calculation and its components are discussed and reported monthly to the full Management Board in the ERM.

The following risk categories represent the relevant risk type within BAWAG Group that are quantified and compared with the available internal capital:

- **Credit risks**: Credit risk is quantified by applying the single risk factor model from Merton which is also underlies the core of the IRB formula, eliminating the additional regulatory parameters, and is populated with economic, not regulatory, point-in-time (pit) risk parameters, under the assumption of a given macroeconomic scenario. Furthermore, credit risk covers:

    - credit risk concentrations in connection with loans to major customers/to groups of affiliated customers
    - losses resulting mainly from granting loans in currencies different from those in which debtors receive regular income to reimburse their debts (FX-lending credit risk)
    - the risk of the reduction in value of receivables due to the deterioration in the debtor´s credit quality without a default having occurred yet (Migration Risk)
    - ESG risk stemming from credit risk[3]

- **Market risks**: The quantification of interest rate risk in the banking book and credit spread risk are based on value-at-risk models. Other market risks, such as funds risk or foreign currency risk in the banking book, are quantified with similar value-at-risk valuation models. These value-at risk models are based on a historical full valuation approach and generalized hyperbolic distribution. In addition, market risk also covers ESG risk stemming from market risk. [4]

- **Liquidity risk**: Structural liquidity risk quantification is based on current liquidity gaps applying assumed potential deteriorations of own funding costs. Quantification methods based on historical worst-case analyses are used for market liquidity risk in the banking book and FX basis spread risk.

- **Operational risk:** This category covers operational risk (including compliance risk) quantified using Standardized Measurement Approach, as described in the Basel VI regulation. Furthermore, operational risk also covers ESG risk stemming from operational risk. [5]

- **Other risks** For the following risk types, economic capital has been quantified: participation risk, reputation risk, real estate risk, business risk and pension risk. For the other risks, a simplified VaR model has been implemented taking into

[2] Furthermore, some non-material risk types are automatically taken into account in the normative perspective via P&L in terms of expected loss alone.

[2] The consideration of ESG risk stemming from credit risk is applicable from 2022.

[3] The consideration of ESG risk stemming from market risk is applicable from 2022.

account an average loss occurring in a one-year time horizon and the relative (compared to the average) variability in terms of how much the one-year loss tends to fluctuate over time by applying a confidence level of 99.9%.[6]

The individual relevant risk types are subsequently aggregated to form the total risk of the Group, considering interrisk correlation effects, and are set into relation to the internal capital. The aim of BAWAG Group´s ICAAP steering is to ensure an adequate coverage of all risks at any time. This aim is supported via a specifically allocated capital buffer subject to allocation at the Management Board's discretion.

The scope of the economic perspective is intended to ensure that all economic risks of the Group are sufficiently covered by the Group's internal capital. All positions that are able to cover losses without transferring the cost to the Group's creditor, i.e. that are risk-bearing, are considered to be part of the internal capital. This mainly constitutes the positions contained in common equity, with a few deductions and add-ons on top.

A confidence level of 99.9% is applied for the calculations. The confidence level indicates the probability that potential losses do not exceed the quantified risk.

The normative perspective is also fully integrated into the strategic risk management, capital management and planning processes of BAWAG Group.

In connection with the normative perspective, Pillar I risks and material risks are quantified, projected and subsequently considered in the respective capital (RWA) and P&L views[7]. The following risk types are considered and quantified:

- **Credit risk**: The quantification of credit risk is based on the regulatory approach (Pillar I view) and is considered under the capital view (RWA). Credit risk losses are also accounted in the P&L view in the form of expected credit losses.

- **Market risk**: BAWAG Group has identified interest rate risk in the banking book (materialized as EVE and NII risk) and credit spread risk as the material market risks. Equity risk is also considered to be a material risk[8], even though it is present to a much lesser extent than the previously mentioned risks. Other market risk types include funds risk as well as FX risk in the banking book. There is no proprietary trading and therefore no trading book. If applicable, all mentioned risks are also considered in the P&L, gains and losses and other comprehensive income. In addition, market risk also covers ESG risk stemming from market risk.

- **Operational risk**: The quantification of operational risk is based on the regulatory approach (Pillar I view) and is considered under the capital view (RWA). Operational risk losses are also accounted for in the P&L view.

The methodology and results of both ICAAP perspectives are discussed in the regular ICAAP & Stress Test Committee (ISTC) on a quarterly basis and reported to the ERM. The ERM oversees the assessment of the results and defines any corrective action for the risk appetite or business strategy, where necessary.

The link between the ICAAP perspectives and capital management is formally defined within the internal risk and capital governance.

The capital ratios defined within the capital planning process and monitored on a monthly basis by the Capital Management Meeting are used as a benchmark for the normative perspective. The capital contingency plan is drawn up to account for extreme stress scenarios. As part of the normative perspective and stress test exercises, senior management reviews

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[4] The consideration of ESG risk stemming from operational risk is applicable from 2022.

[7] Furthermore, some non-material risk types are automatically taken into account in the normative perspective via P&L in terms of expected loss alone.

[8] Equity Risk has been identified as material in the RSA process for the year 2022.

whether the stressed capital ratios remain above the recovery levels. In the event of breaches of the recovery levels, measures must be taken to improve the capital position sufficiently in order to keep the capital ratios above the recovery levels even under a stressed scenario.

Stress Test Framework

BAWAG Group performs stress tests on a regular basis in order to assess potential effects on the Group's financial situation stemming from unusual yet plausible specific events and changes in variables such as the impact of a severe economic downturn on the Group's risk profile and financial position. Within BAWAG Group, stress testing is considered an important management tool and an essential part of the internal risk management.

Governance procedure has been defined and established for the performance of stress tests and the key decision-making body is the ICAAP & Stress Test Committee. The Portfolio Analysis and Stress Test group in the Risk Controlling division is in charge of the coordination and guidance of each stress test exercise.

Stress Test program

A comprehensive program for the management of stress testing within BAWAG Group has been defined as an integral part of the stress test framework. The program includes several stress test exercises applying a series of techniques that are performed on a regular basis as well as on demand. Regular stress tests exercises include the following:

- scenario stress test (ICAAP), performed on a quarterly basis
- reverse stress testing, performed once a year
- sensitivity analyses, performed on demand or at least once a year
- ad-hoc-analyses, performed on demand (e.g. specific COVID-19 scenario impacts).

ICAAP Stress Test

The ICAAP stress test is a macroeconomic stress test with general assumptions of a dynamic balance sheet and without possible mitigation measures during the projection period. BAWAG Group's stress test exercise is based on macro-economic scenarios (baseline, adverse and including idiosyncratic shocks) covering a three-year horizon starting from the reference date of the stress test exercise.

Macroeconomic scenario effects are transmitted to the portfolio via regression models (e.g.: IFRS 9 models) as well as stress factors based on expert judgment (for unavailable historical data or for models with low explanatory power). Outcomes of the ICAAP stress test are expressed in terms of effects on capital ratios through both P&L and RWA.

Reverse Stress Test

The Reverse Stress Test is designed to identify a set of scenarios leading to a breach of warning or recovery thresholds of the CET1 ratio. The ICAAP Stress Test framework is utilized as the basis for the identification of such scenarios along with targeted sensitivity analyses.

ICAAP & Stress Test Committee

The ICAAP & Stress Test Committee (ISTC) provides the central coordination of the ICAAP and stress testing processes at the Group level. The main objective is to ensure effective oversight and control over the operative proceedings of all ICAAP and stress test analyses and to recommend strategic decisions.

Meetings are held whenever required, but at least quarterly and the scope of activity includes:

- ICAAP normative and economic perspectives analyses and monitoring;
- all cross-divisional stress test or similar economic analyses.

For the analyses in scope, the ISTC is in charge of the following items:

- Approval of the process guidelines for each stress test or economic analysis
- Approval of the process guidelines for ICAAP normative and economic perspectives analysis
- Discussion and approval of the results of stress test exercises and ICAAP perspectives
- Definition of the recommended action / mitigation plan for ERM approval based on the ICAAP and stress test results

Macroeconomic Scenario Committee (MSC)
The main objective of the Macroeconomic Scenario Committee (MSC) is to identify appropriate scenarios for each stress test exercise and the ICAAP perspectives.

The scope of activity includes:

- Identification and alignment of the baseline macroeconomic scenario
- Identification and design of the adverse macroeconomic scenarios, either from an external source or tailored-made for the Group or for a specific institution
- Identification and design of the idiosyncratic shocks (e.g. vulnerable big exposures, shock on house price index, retail overlays, etc.)
- Approval of the identified scenarios and related assumptions

Portfolio Steering Framework

Credit Risk Limits in the economic perspective are determined for all segments as part of the Risk Strategy. BAWAG Group follows a detailed Portfolio Steering framework concept based on hierarchical capital allocation.

For the main risk categories, namely Credit Risk, Market Risk, Liquidity Risk, Operational Risk and Other Risks the capital allocation is fixed. The risk quantification for the “other risks” is revalidated at least annually in conjunction with the strategic capital allocation process and further updated on a needs basis.

The following four levels of capital allocation are considered:

- Level 1: Capital allocation to risk categories and the MB capital buffers
- Level 2: Capital allocation to business segments (credit risk) and sub-categories (market and liquidity risk)
- Level 3: Capital allocation to business sub-segments (only for credit risk)
- Level 4: Capital allocation to countries for the total portfolio and to industries for the segment Corporates, Real Estate & Public (only for credit risk).

In 2022 new limits will be allocated on level 2 for the migration risk (for credit risk) and ESG risk (for all risk types).

Portfolio Steering Committee

This committee provides the central coordination of the credit portfolio steering processes at the Group level. The main objective is to ensure effective oversight and control over the credit risk capital allocation and capital utilization levels and to inform strategic decisions on such topics or, alternatively, to define recommendations for the ERM at the Management Board level. Meetings of the PSC are held on a quarterly basis and the duties of the PSC are as follows:

- Monitoring of Credit Risk capital allocation and capital utilization at all levels
- Approval of the standard Portfolio Steering Framework Report
- Assessment of the portfolio dynamics and the current utilization of the assigned limits
- Assessment of the needs and opportunities for re-allocation of capital within the capital allocation hierarchy
- Tactical capital allocation, within the restrictions defined by the Portfolio Steering Framework embedded in the ICAAP and Stress Test Policy
- Assessment of the impact of relevant prospective credit decisions requiring capital re-allocation
- Assessment of the status of risk concentrations in the Bank's portfolio, across all relevant risk categories
- Monitoring of the single-name concentrations for credit risk, including the Large Capital Consumers
- Prioritization and assessment of the enhancements to the Portfolio Steering Framework to be sought over time
- Definition and evaluation of in-depth analyses regarding specific discussion topics related to the core responsibilities of the Committee.
- Definition of the recommended action / mitigation plan for ERM approval, where necessary.

CAPITAL ALLOCATION AND LIMITATION AT TOTAL BANK LEVEL

Article 438 point (a) CRR
Article 439 point (a) CRR

The process for limitation and capital allocation runs parallel to planning and budgeting at least once a year, and if required, more often. Within the defined process, the established premises such as confidence level and capital buffer (risk appetite) are reviewed and updated. Steering portfolios are defined for credit risk and are geared towards the customer segments or organizational responsibilities as well as countries and industries. The bank subsidiaries are included in the control portfolios. In addition, Migration Risk and ESG Risk stemming from credit risk[9] are covered within the credit risk category. Specific sub-limits are defined for operational, market and liquidity risks, and a respective capital buffer is assigned for risks within the risk category "other risks."

The capital allocation/limitation according to Article 39a of the Austrian Banking Act is defined under the following premises and information:

- The Management Board sets forth the strategy for the next five years in the annual medium-term plan
- Confidence level, holding period, capital buffer, steering units
- Planning and budgeting process and any changes in risk value/balance sheet items taking an adequate liquidity position into account
- Existing limit setting systems (e.g. in connection with market risks)
- Limitation for the steering units according to the quantification methods defined for the individual risk categories.

The capital allocation, as a major component of the Group-wide risk management and limitation of the risk categories, is approved by the full Management Board, approved by the Risk and Credit Committee and recommended for approval to the Supervisory Board, and in a final step, approved by the Supervisory Board.

[9] The consideration of ESG Risk stemming from credit risk is applicable from 2022.

CREDIT RISK

OBJECTIVES AND PRINCIPLES OF CREDIT RISK MANAGEMENT

Article 435 (1) points (a) – (e) CRR
Article 439 point (a) CRR

Strategies and processes

Corporate customers

Strategies and processes presented in this section on corporate customers are also largely applied to sovereigns, the financing of government authorities, and institutions. Loans are processed and decided upon according to extensive work instructions. The decision-making powers are set forth in order of competency order.

Credit is granted on the basis of the following considerations:

- All individual customers and customers in a customer group or a corporate group are rated at least annually.
- The analysis of creditworthiness is based on current business documents (the national accounts for sovereigns) including planning calculations of the company and other information to ensure a meaningful analysis for the rating and the decision.
- The assessment of a customer's creditworthiness and credit bearing capacity is based on ratings that must systematically cover all information made available by the relationship manager. The final rating confirmation is handled by the responsible organizational risk division. The loan decision is taken solely according to the Competence and Power Regulation.
- BAWAG Group strives to collect suitable collaterals to minimize the credit risk which is assessed by using a standardized valuation based on the Group collateral catalogue. In the event of any net exposure, correspondingly higher collateral must be provided if the rating shows any signs of worsening.
- Finance for complex business models (e.g. leveraged finance) or in new countries or regions is based on a thorough analysis and description of the associated (credit) risks.
- The (credit) risk units must be involved with appropriate expert opinions, as set forth in the product implementation process. New business segments must also be compatible with the general treatment of credit risk in terms of classification and basic rules in order to ensure consistency.
- Any decision that could change the risk position in a customer relationship requires approval from the competent authorized person. Each application requires a positive front-office recommendation (from the customer advisor) before being submitted to the risk-unit.
- If key ratios are defined in a credit relationship as auxiliary conditions (known as covenants), they must be stated in the credit application and approved. Compliance with the key ratios at the contractually fixed dates must be checked by the responsible risk unit.

Retail and Small Business customers

Risk from new business is managed by using clear and conservative underwriting guidelines. Decisions at the point of sale are mostly made on the basis of automated scoring systems that issue recommendations, or the decision is made downstream in the risk division. Special attention is paid to processing compliance and assuring data quality. A central monitoring process ensures on-going quality assurance.

Credit risk in retail business is measured monthly focusing on the following elements:

- Portfolio trends in terms of overdue/late payments (e.g. vintage and flow rate analyses)
- Portfolio trends in terms of risk class distribution and risk concentration
- Portfolio trends in terms of credit affordability and collateralization
- Portfolio trends with regard to defaulted loan facilities

- Portfolio trends in terms of incurred risk costs and losses
- Scorecard performance (approval rates and manual decision)
- Performance monitoring of fraud detection
- Portfolio distribution trends by products and channels
- Collection and workout performance

The findings of the analysis are reported periodically to the ERM.

Independently of this process, risk-relevant data from standardized assessments between business managers and risk management are discussed and documented in monthly committee meetings. This process ensures a regular and standard flow of information while also making it possible to respond directly to changes in risk parameters and market conditions.

In the collection process additional measures support the dunning process to be more efficient on working with overdrafts and loans in delay.

Structure and organization of relevant risk management functions

Credit risk is an integral part of many business activities and is controlled in the Commercial Risk Management and Retail Risk Management units. In daily business, credit risk is controlled by each business area in coordination with the respective credit risk division on the basis of the authority granted and applying the dual control principle. The authority is based on the CRO´s respective delegation and approval.

The regulations governing the authority granted, can be found in the "Competence and Power Regulation".

Risk measurement systems (approved approaches)

Article 452 point (a) CRR

With the decision of the FMA dated 23 April 2013, BAWAG Group received approval in accordance with part 3 title II chapter 3 section 1 CRR to calculate the basis of assessment for credit risk as per Article 107 (1) CRR applying the internal ratings based (IRB) approach pursuant to part 3 title II chapter 3 CRR starting on 1 April 2013. The approval extends to the institutions of the BAWAG Group described below and the indicated exposure classes. For individual exposure classes, credit institutions and business units indicated below, the basis of assessment for credit risk will be determined using the Standardized Approach to credit risk pursuant to Article 148 and Article 150 CRR (permanent or temporary partial use) with approval from the ECB as per part 3 title II chapter 2 CRR. BAWAG Group uniformly applies the IRB approach and jointly satisfies Article 144 and Article 145 CRR for the institutions of BAWAG Group.

Portfolios in the IRB approach

Approval to use the IRB approach applies to the following credit institutions in the Bank Group:

- BAWAG P.S.K. AG

For the exposure class ‘exposures to corporates’ (Article 147 (2) point c CRR), the approaches specified by the supervisory authority are used in the scope of the IRB Approach for the risk parameter LGD and conversion factors. The risk weights pursuant to Article 147 (2) point c CRR apply for exposures from Specialized Lending.

In the exposure class "retail exposures" (Article 147 (2) point d CRR), the parameter PD as well as LGD and conversion factors are based on the Group's own estimates.

Exposures in the exposure class "participations" (Article 147 (2) point e CRR), are calculated based on the simple risk weight approach pursuant to Article 155 (2) CRR and using grandfathering in accordance with Article 495 (1) CRR.

Portfolios in the temporary standardized approach

These portfolios are currently in the temporary standardized approach:

- exposures to institutions pursuant to Article 147 (4) point d CRR
- retail exposures within start:bausparkasse AT
- retail exposures within the German portfolio of BAWAG P.S.K. AG and start:bausparkasse DE
- retail exposures within BFL Leasing GmbH and Morgenstern Miet + Leasing GmbH

Portfolios in the standardized approach

Permission was/will be obtained from the FMA/ECB pursuant to Article 150 CRR to permanently apply the standardized approach to credit risk to calculate the basis of assessment for credit risk for the following exposure categories and immaterial lines of business:

- exposures to central governments and central group's pursuant to Article 150 (1) point a CRR
- exposures to institutions pursuant to Article 150 (1) point b CRR
- exposures belonging to the classes of exposures to the Austrian federal government, provincial governments and public-sector entities pursuant to Article 150 (1) point d CRR
- guarantees and counter-guarantees of central governments pursuant to Article 150 (1) point j CRR
- exposures to local and regional governments and public-sector entities as well as legally recognized churches and religious communities falling into the exposure class "Institutions" pursuant to Article 150 (1) point a CRR
- exposures within the Bank Group pursuant to Article 150 (1) point e CRR
- within the exposures to corporates, the immaterial business units insurance companies, political parties, leasing companies and other financial companies pursuant to Article 150 (1) point c CRR
- participations whose credit obligations qualify for 0% risk weight under the Standardized Approach to Risk Weight in accordance with the provisions of Article 150 (1) point g CRR
- in accordance with Article 150 (1) point c CRR, for the exposures of the following subordinate institutions pursuant to Article 30 (1) BWG:

- BAWAG P.S.K. Wohnbaubank AG
- easyleasing GmbH and BAWAG Leasing Holding GmbH and its leasing subsidiaries
- start:bausparkasse AG, if not provided for in the temporary standardized approach
- real estate companies of BAWAG Group if they provide ancillary services as subordinate institutions of the Bank Group
- other smaller financial institutions and providers of ancillary services

Furthermore, the regulatory capital requirements for the International Retail Mortgage Portfolio are calculated by using the standardized approach.

Reporting systems

The full Management Board is informed monthly about all risks in the ERM based on the comprehensive, monthly Group Risk Report. In addition, the full Management Board is informed immediately in the event of any material change in the risk situation.

Risk hedging and mitigation[1)]

Article 435 (1) point (d) CRR

Collateral is recognized and assessed in accordance with the Credit Collateral Catalogue (Kreditsicherheitenkatalog; KSHK), which reflects the principles of the CRR, other relevant legal regulations and internal procedural rules. Together with the collateral checklist, the Credit Collateral Catalogue serves as the basis for cataloguing collateral according to internal risk criteria. The Credit Collateral Catalogue also determines the amount to be set for the market value and lending value (internal value "Belehnwert") and whether or not the collateral may be applied to reduce risk under the current regulatory requirements. If new collateral is not yet defined in the Credit Collateral Catalogue, the organizational unit Strategic Risk must check whether this new collateral is eligible for recognition and select the method for the valuation of the market value and the limits for the lending value in coordination with the affected areas and submit these items to the ERM for approval.

Monitoring is conducted regularly, and the currently valid lending value estimates are reconciled with the historical realization proceeds and checked.

The lending value ("Belehnwert") is the value at which the collateral is internally estimated in terms of reducing exposure. The lending value incorporates values empirically obtained from salability, duration of realization or discounts based on risks specific to the rating or country. In the case of real estate with prior liens, these liens are also considered in calculating the lending value. The lending value is set for daily credit business and is generally far below the current market value. The lending values in general and the discount rates per risk category in particular are subject to periodic review.

The market value is the value of the collateral usually attainable from selling the asset in a fair business transaction. The market value is determined using a valuation process that takes into account future marketability and is geared towards standardized valuation processes (e.g. for real estate: income approach, cost approach, sales comparison approach, etc.). Speculative aspects are not considered in the calculation of the market value.

1) Refer also to 'credit risk mitigation techniques in the internal rating based approach'.

COUNTERPARTY DEFAULT RISK ARISING FROM DERIVATIVES, REPURCHASE TRANSACTIONS, SECURITIES AND COMMODITIES LENDING TRANSACTIONS, MARGIN LENDING TRANSACTIONS AND LONG SETTLEMENT TRANSACTIONS

Strategies, processes and management

Article 435 (1) point (a) CRR

The counterparty default risk is treated as part of the credit risk. Details on strategies and procedures of the management of credit risks are presented in the section “Objectives and principles of credit risk management.”

Structure and organization of relevant risk management functions and risk reporting systems

Article 435 (1) point (c) CRR

Counterparty default risk is a version of credit risk designating the potential risk of default in treasury transactions, especially derivative transactions. It quantifies the risk of loss that would materialize if the credit rating of a counterparty of BAWAG Group worsened during the term of a transaction – all the way to the worst-case scenario of a default.

The credit risk divisions assess actual counterparties based on front-office requests. A limit system is employed to monitor this risk category and sets separate limits for the three asset classes of derivatives, money market and securities (product limit system). Risk Modelling (RM) is responsible for monitoring compliance with the set limits. The extent to which the limit is used is calculated methodically following the approach “positive market value plus add-on” utilizing credit risk mitigation techniques (refer to section “Credit risk mitigation”).

This monitoring of limit use is done in real time and in the form of daily reports. The RM division reports to the front office on a daily basis and to the back office whenever limits are exceeded. The front office and back office then order countermeasures to be taken, subject to an escalation process coordinated by RM.

All relevant provisions for counterparty risk and the associated processes are described in detail in the risk management manual for treasury markets, which is updated annually and approved by the full Management Board. The rules are supplemented by various process instructions for Treasury & Markets (TM) and credit risk manuals for the credit segments.

Risk hedging and mitigation

Article 435 (1) point (d) CRR
Article 439 point (b) CRR

BAWAG Group can demand the furnishing of collateral or take other steps to mitigate risk based on bilateral agreements (repurchase agreements, lending transactions, ISDA netting agreements, credit support annexes, etc.). From the standpoint of BAWAG Group, credit risk only exists in cases in which the net market value is positive (replacement risk). As this risk depends largely on fluctuations in market risk parameters (exchange rates, interest rate movements, stock prices, etc.), regular recalculation of this risk is indispensable as is the appropriate adjustment of the collateral.

The types of collateral generally allowed include cash in several (major) currencies found in a set list (usually EUR, USD, GBP and CHF) and securities from issuers with very good ratings (government bonds of select European countries and the United States).

If securities are provided as collateral, a haircut based on the remaining term is additionally applied. The collateral amounts are adjusted to the current risk situation (market valuation of the counterparty’s transactions), or the intrinsic value of the collateral is checked at contractually agreed times (exchange rate fluctuations are taken into account for collateral denominated in foreign currencies and the market value of securities). The customary intervals for valuation in the market are daily, weekly or monthly. For the majority of contracts, a daily valuation is provided.

The possibility of realizing the deposited collateral in the event of the partner's bankruptcy and its further use (e.g. re-hypothecation or passing along of the collateral as security for another contracting party) is ensured by the legal opinions drawn up on behalf of the ISDA for the given jurisdiction of the individual contracting parties.

For derivative business, currently only cash collateral denominated in EUR and USD – as well as in CHF and GBP in the case of a clearer – is allowed. This type of security therefore does not result in any reserves being formed nor is hedging required for the financial collateral taken in, as (with the exception of USD, CHF and GBP) its value does not change due to price changes.

Correlation risks

Article 439 point (c) CRR

According to the Basel Committee, there are two types of correlation risk, general and specific. A general correlation risk exists if there is a high correlation between the counterparty's probability of default and risk factors in the general market risk. A specific correlation risk exists if there is a high correlation between the counterparty's probability of default and the replacement value of current transactions being conducted with that counterparty due to the nature of these transactions.

Possible correlation risk is taken into account in connection with deliberations on the collateral portfolio. Any specific correlation risk is countered by combining the granting of limits to a counterparty or obligor group of counterparties and the setting of internal limits (exposure determination). For derivative business, only financial collateral in the form of cash deposits is generally allowed. This practice is also intended to help avoid specific correlation risks. In determining the limit and limit structure during the rating check, BAWAG Group considers the counterparty's rating and a possible worsening of this rating. These factors are not part of the determination of exposure.

In the case of counterparties with whom a relatively large volume of derivative business is conducted, collateral agreements are also signed. They stipulate that positive market values are regularly compensated solely in the form of cash deposits.

With respect to repos and securities finance, additional risks are largely eliminated in the corresponding agreements (repo annex, tri-party agreement) by setting restrictive criteria on acceptable types of securities, issuers, rating classes and haircuts. In repos trade, margin calls are periodically executed to compensate for the market value.

Settlement and delivery risk is composed of the pre-settlement/fulfillment risk and the replacement risk. Pre-settlement/fulfillment risk results from the unilateral provision of an input by BAWAG Group under a mutual transaction. It exists until the complete fulfillment of the counter-performance. Replacement risk occurs if the full settlement of a transaction is not carried out immediately upon its conclusion. If the counterparty defaults prior to full performance, the Group has to find a replacement in the market based on the conditions prevailing at that time. Due to changes in market value in the meantime, BAWAG Group may incur losses from the necessary replacement. From an economic point of view, replacement risk is identical to the counterparty risk. In contrast to counterparty risk, however, it does not occur for forward transactions, for which a future settlement was explicitly agreed. It exists in the framework of step-by-step transactions where, due to standard market practices, a period of several days may separate the conclusion of the contract and settlement.

Rating downgrade and its impact on collateral

Article 439 point (d) CRR

Contractual clauses on dependencies between the collateral provided and the rating assigned exist only in a few isolated cases in connection with risk mitigation agreements from derivative transactions. In some of these agreements, this provision affects what are known as the “independent amount,” the “threshold amount” and the “minimum transfer amount”.

Based on existing agreements and as matters stand today, a rating downgrade of the Bank would not have any material effect on the additional amount to be provided.

Measures for exposure value

Article 439 point (f) CRR

Treasury business is focused on asset and liability management. Derivative financial transactions are conducted in the form of interest rate and currency swaps, forward exchange dealing, interest rate and foreign exchange options. BAWAG Group was not engaged in securities lending, commodity lending or in any margin lending transactions or long settlement transactions as of 31 December 2021.

The fair value is applied in the valuation of derivatives and repos. It is determined from publicly quoted prices. If there is no quoted price available, the fair value is determined using accepted valuation methods. The fair value represents the potential replacement cost.

BAWAG Group has opted to use the Standardized Approach for Counterparty Credit Risk as defined in Article 274-280f CRR. The counterparty risk thus consists of the replacement cost (Article 275 CRR) plus the potential future exposure (Article 278 CRR) multiplied by the alpha factor of 1.4. A positive market value from the standpoint of BAWAG Group is an economic exposure in relation to the counterparty that would be lost in part or altogether in the event of default. The market value thus also represents the additional cost that would be necessary to place a comparable transaction In calculating the internal exposure (limit add-on), BAWAG Group is guided by the procedure stipulated for determining capital adequacy.

Estimation of the scaling factor

Article 439 point (i) CRR

Own estimates for determining the scaling factor are not in use.

CREDIT RISK MITIGATION

Policies and processes for netting

Article 453 point (a) CRR

BAWAG Group has made use of off-balance-sheet netting since 31 December 2008. Netting pertains exclusively to derivative instruments with counterparties that have signed a corresponding master agreement entitling BAWAG Group to undertake netting. In the case of additional agreements covering open receivables by collateral (Credit Support Annex), BAWAG Group intends to include the highest possible volume of derivatives as defined by the CSA agreement. Furthermore, attention is paid to ensuring low correlation between the probabilities of default of the debtor and the security.

Netting is applied to the entire derivative business. The pertinent netting agreements are legally valid and legally enforceable in all relevant jurisdictions in the event that the counterparty becomes insolvent or goes bankrupt. All netting cases are regulated by an adequate standardized process. Data are maintained and calculated via an electronic data processing (EDP) supported system.

Types of collateral and collateral valuation and management

Article 453 points (b) – (c) CRR

The following guidelines must be followed for collateral valuation and management:

- BAWAG Group has the right to accept or reject collateral or to assign to collateral the value deemed necessary and reasonable in order to protect the Group´s interests.
- The Credit Collateral Catalogue and the collateral policies of the affiliated companies define what combinations of goods (characteristics of the economic good/asset) and collateral (to which BAWAG Group has title) are deemed basically acceptable and what value (market value, nominal value, etc.) to apply. It also indicates what discounts from the calculated value apply and under what circumstances this collateral can be applied to reduce capital requirements. This document is revised as necessary but at least once a year.
- The accompanying documents stipulate the process steps required to evaluate, take in and put into effect the collateral and to manage and realize it.
- All collateral must have a market value that is easy to determine or an internally calculated value, and BAWAG Group must be in a position to represent its interests in the collateral.
- Collateral must meet the general legal requirements, in particular the minimum recognition requirements and the policies defined by the ERM.

The compliance of the collateral with the legal criteria and the policies is determined during the credit application process in the front office and reviewed by the risk departments.

Generally, the value of collateral is checked during annual prolongation or the annual risk check or as warranted (e.g., increase, default).

The table below provides a summary of the key types of collateral, their estimated values, and the frequency of valuation:

Table 4: Types of collateral and collateral valuation and management

Type of collateral	Estimated values	Frequency of valuation
Financial collateral	Market value according to current GEOS price data, for example (with volatility adjustments taken into account)	Automatic daily valuation except for deposits at other banks
Residential real estate	Market value	The centralized Residential Real Estate Appraisal team determines the value of all residential properties in Austria on the basis of a standard methodology and valuation tool. Valuation of real estate properties in other countries is also done by independent experts according to international standards. The periodic review and updating of property values is automated based on the real estate price index published by the Association of Real Estate and Asset Trustees of the Austrian Federal Economic Chamber (Fachverband der Immobilien- und Vermögenstreuhänder der Wirtschaftskammer Österreich) for Austrian residential properties, on the Halifax House Price Index for residential properties in Great Britain and by MAC (MeilleursAgents.com) for French residential properties. The values of the properties in the Netherlands are periodically updated based on the CBS index (Centraal Bureau voor de Statistiek) and the real estate properties situated in Germany are periodically checked with the help of the market volatility concept ("Marktschwankungskonzept").
Commercial real estate	Market value	The value of commercial real estate is assessed by an independent expert at the current market value, at the maximum. Once a year, the risk units additionally check whether any material changes have occurred. A new valuation is ordered where warranted. A new valuation is conducted by the Real Estate Appraisal department at least every three years for loans > € 3 million and at least every five years for loans < € 3 million
Other physical collateral	Market value (no use for regulatory purposes)	At least once a year
Pledging or assignment of life insurance policies	Repurchase value (only conventional and funds-oriented life insurance policies where the surrender value cannot be reduced are used for regulatory purposes)	Automatic updating of repurchase value (through the insurance platform). For all other insurance companies when data is not transmitted via the platform: The customer must be obligated to submit the insurance confirmation annually.
Guarantees	Guaranteed amount (nominal value) less possible currency risks (volatility adjustment)	Monthly reconciliation of liability amount with the balance – depending on scope of liability
Co-obligations	Outstanding balance unless a restriction applies (no estimate for regulatory purposes)	Ongoing

Guarantors/counterparties for credit derivatives

Article 453 point (d) CRR

The main types of guarantor eligible for regulatory credit risk mitigation are domestic and foreign banks, the federal government, state governments, local governments and sovereigns. With respect to the eligibility of the guarantees, there are internal minimum requirements defined in the Commercial Underwriting Guidelines. These guidelines explain under which conditions the customers are allowed to have limits granted for derivative transactions and guarantees. For instance, the rules say that derivative limits may only be granted to banks with a very good credit rating (the equivalent of a minimum rating of A-[1)]). Any exceptions must be well-founded, separately requested and explicitly approved.

The small volume of hedging transactions that existed on the reporting date in the form of credit derivatives was concluded exclusively with major international banks with AA or A ratings.

Collateral risk concentrations

Article 453 point (e) CRR

A concentration risk exists if a significant percentage of collateral items Group-wide (at the portfolio level) are concentrated in a small number of collateral categories, instruments, sectors or special protection providers (e.g. collateral providers). Certain reporting and monitoring activities are conducted at the consolidated level for all types of physical collateral and guarantees for credit risk as well as market risk.

In order to cope with the potential concentration of the Credit Risk Mitigation techniques, a large collateral providers list is provided within the Portfolio Steering Framework Report on a monthly basis. The list contains guarantors with a collateral market value over € 50 million and shows the internal rating, net exposure towards BAWAG Group and specific comments for each guarantor explaining the usage of the guarantee. The list is presented to the Portfolio Steering Committee on a monthly basis and is discussed with regard to guarantee effectiveness and potential countermeasures during the quarterly meeting..

VALUE ADJUSTMENTS AND RESERVES

Definition of “past due,” “forborne loans and forbearance measures,” “impaired,” “general credit risk adjustments” and “specific credit risk adjustments

Article 442 point (a) and (b) CRR
Article 442 point (i) (i) CRR

Definition of “past due”

According to the CRR, days past due begin once an obligor has breached an advised limit, has been notified of a limit smaller than current outstandings or has drawn credit without authorization and the underlying amount is material. Days past due for credit cards commence on the earliest maturity date. In addition, a receivable is deemed past due if the counterparty has failed to make their contractually agreed payments.

Definition of “Forborne loans and forbearance measures”

Measures of forbearance can be extended if borrowers face financial difficulties and are considered to be unable to meet contractual obligations. BAWAG Group has sound and transparent processes in place to define the conditions under which concessions, in the form of the modification of terms and conditions, may be granted. Depending on the customer segment, possible measures include the temporary postponement or reduction of interest or principal payments, the restructuring of credit facilities or other forbearance measures. In exceptional cases, a permanent reduction of interest rates may be granted.

1) Rating given by the rating agency Standard & Poor’s.

Measures of forbearance or refinancing are instruments to ultimately reduce the existing risk and avoid default with respect to debt claims, if it is expected that a default can thereby be forestalled. However, forbearance measures are by no means used to avoid or postpone the recognition of an unavoidable impairment or disguise the level of credit risk resulting from forborne assets.

By implementing forbearance measures appropriate in terms of time and scope, BAWAG Group supports clients in maintaining financial stability. If the supporting measures are not successful, exposures will be recognized as non-performing and impaired according to regulatory and accounting standards. For clients or a group of clients where a default is identified, a provision is booked in accordance with internal guidelines.

For reporting as well as internal risk management purposes, BAWAG Group implemented processes and methods according to regulatory standards in order to identify exposures for which forbearance measures have been extended. These are classified as forborne.

Definition of "impaired"

A key feature of ECL estimation under IFRS 9 is the stage allocation of assets. If a financial asset shows a significant increase in credit risk (SICR) or is recognized as credit-impaired, the ECL estimate of the asset is the lifetime expected credit loss (stage 2 or stage 3), and the 12-month expected credit loss otherwise (stage 1).

Stage 1: 12-month ECLs

The 12-month calculation applies to all financial instruments at initial recognition (with a few exceptions, e.g. for purchased or originated financial assets that are credit-impaired on initial recognition "POCI") and those which do not show a significant increase in credit risk since initial recognition (in the case of POCI, only the cumulative changes in lifetime expected losses since initial recognition are recognized).

Stages 2 and 3: Lifetime ECLs

When a financial instrument has been in stage 1, but a significant increase of credit risk since the initial recognition is observed, the instrument is transferred to stage 2. If the instrument's credit risk increases further to the point that it is credit-impaired, the instrument is then transferred to stage 3. The measurement of the risk provisions for stage 2 and stage 3 are lifetime expected credit loss, estimated by lifetime risk parameters.

The Group examines the stage allocation of assets at each reporting date. The transfer criteria from stage 1 to stage 2 are in three pillars:

- quantitative criteria
- qualitative criteria
- backstop criterion

The quantitative criteria examine the worsening of lifetime PDs since the initial recognition, while the qualitative criteria gather additional information about the assets to assess the SICR. As an additional backstop criterion, payment in arrears is considered in the Group. If one of the criteria is satisfied, a financial instrument is transferred from stage 1 to stage 2. Hence, if none of the transfer criteria is active, the asset is kept in or reassigned to stage 1.

The quantitative criteria examine the financial asset's credit risk profile based on two aspects:

- the relative PD change
- the absolute PD change

If both indicators surpass the pre-determined thresholds and indicate a significant increase in credit risk, then the asset is transferred to stage 2.

The qualitative criteria

Qualitative staging criteria factors selected by the Group are:

- Entry in watch list (non-retail customers)
- Entry in warning list (retail customers)
- Forbearance flag: If one of these factors is flagged as active, a financial asset is transferred to stage 2.

Backstop criterion

As a backstop criterion, the Group employs payment in arrears for more than 30 days. All financial instruments that are more than 30 days past due would be transferred to stage 2, if not yet in stage 3. In cases where no staging factor is active, the exposure is automatically reassigned to stage 1.

Stage 3: Lifetime ECLs

At each reporting date, the Group assesses whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or group of financial assets is impaired, and impairment losses are incurred if:

- there is objective evidence of impairment as a result of a loss event that occurred after the initial recognition of the asset and up to the reporting date ("a loss event").
- the loss event had an impact on the estimated future cash flows of the financial asset or the group of financial assets; and
- a reliable estimate of the loss amount can be made.

Information regarding the level of provisions and the respective changes can be found in the quantitative section of the Disclosure Report and in the annual report.

RATING SYSTEMS AND RATING PROCESSES

External ratings systems

Article 444 points (a) – (d) CRR

The weighted exposure amounts are calculated for regulatory purposes for a part of the loan portfolio (banks, subsidiaries in TPU) using the standardized credit risk approach according to Part 3 Title II Chapter 2 of the CRR. It is generally geared solely towards ratings from Moody's.

The distinction between issuer rating and issue rating as described in Article 139 CRR is taken into account when external ratings are used. Issuer ratings are used in particular only if no issue rating is available and the conditions in Article 139 CRR are satisfied.

The commission implementing regulation (EU) 2016/1799 is consulted with regard to the mapping of external ratings to the individual credit quality steps. The following table shows the relationship of the application of the ratings of ECAI for specific exposure classes.

Table 5: Mapping of external ratings to the individual Credit Quality Steps

Exposure classes according to Article 112 CRR	Moody's	S&P	Fitch
Central Governments or Central Banks	X		
Regional Governments or local authorities	X		
Public Sector entities	X		
Multilateral Development Banks	X		
International Organizations	X		
Institutions	X		
Corporates	X		
Retail exposures			
Secured by mortgages on immovable property			
In Default	X		
Associated with particularly high risk			
Covered Bonds	X		
Securitization positions	X	X	X
Exposures to Institutions and corporates with a short-term credit assessment			
Units or shares in Collective Investment undertakings	X		
Equity			
Other items			

The assignment of Ratings is based on a daily data feed of the ECAI Moody's which is processed in the IT systems of the Bank. This data is joined with the client or, respectively, security master data automatically in order to ensure an up-to-date and – in terms of the calculation of own funds requirements – complete set of input data.

Relationship between internal and external ratings

Ratings from Moody's are employed to calculate the minimum capital requirements for regulatory purposes that are applied in accordance with permanent or temporary partial use. For securitizations, the ratings from Moody's, Standard & Poor's and Fitch are incorporated in the calculation of risk-weighted exposures.

The results of the internal rating procedures are depicted using a master scale. The following table shows the relationship between the internal rating notches and the external ratings.

Table 6: Rating notches and classes for all segments

	External rating agencies		
Rating notch	Moody's	S&P	Fitch
1,1	Aaa[1]	AAA[1]	AAA[1]
1,2	Aaa[1] , Aa1	AAA[1], AA+	AAA[1], AA+
1,3	Aa2	AA	AA
2,1	Aa3	AA-	AA-
2,2	A1	A+	A+
2,3			
3,1	A2	A	A
3,2			
3,3	A3	A-	A-
4,1	Baa1	BBB+	BBB+
4,2	Baa2	BBB	BBB
4,3	Baa3	BBB-	BBB-
5,1	Ba1	BB+	BB+
5,2	Ba2	BB	BB
5,3	Ba3	BB-	BB-
5,4	B1	B+	B+
6,1	B2	B	B
6,2	B3		
6,3	Caa1	B-	B-
6,4	Caa2		
7	Caa3	CCC+, CCC, CCC-, CC, C	CCC, CC, C
8,1 – 8,8	Ca, C	R, SD, D	RD, D

1) Aaa and AAA correspond to class 1,1 for sovereigns and to class 1,2 for all other segments.

The internal rating processes for the exposure classes also take into account external ratings under certain conditions (e.g. information that is more current or more comprehensive).

Control mechanism for rating systems

Article 452 point (c) and (d) CRR

During the life cycle of the rating system, different independent units within BAWAG Group are involved, based on the three lines of defense principle: The first line of defense is the CRCU (credit risk control unit according to Article 190 CRR) which is part of RM. The second line of defense is the Validation team (VA) according to Article 185 CRR and the third line of defense is Internal Audit with the function as outlined in Article 191 CRR. Each of the units report directly to the CRO without any further dependencies.

The CRCU is in charge of the initial model development as well as the review of estimates for the rating systems that take place either yearly, semi-annually or quarterly, driven by the materiality of the rating system. Based on the outcome of the review of estimates, different actions are taken, e.g. recalibration or new estimation of the risk parameters. The result of each review of estimates is presented to the Model Governance Committee and has to be approved accordingly.

The Validation unit is in charge of the initial model validation as well as the yearly validation for all rating systems comprising the following activities:

Table 7: Description of the validation methods

Validation method	Description
Method 1	Verification of the documentation for the rating and scoring systems
Method 2	Verification of the quality of the database being used for validation
Method 3	Verification of the correct use of the rating and scoring systems as part of a use test
Method 4.1	Distribution analysis to identify clusters of customers in individual risk classes
Method 4.2	Comparison of internal ratings with external ratings (benchmarking)
Method 4.3	Identification of clustering of high exposures in individual risk classes
Method 4.4	Verification by the risk manager of the frequency of overrulings/overrides in the automatically generated rating classes
Method 4.5	Verification of clusters of defaults in individual rating or scoring systems
Method 5.1	Testing of rating and scoring systems as regards calibration by comparing the mean forecast PD and the mean observed default rate
Method 5.2	Testing of individual risk classes as regards calibration by comparing the mean forecast PD and the mean observed default rate using binomial distribution tests
Method 6	Testing of the discriminatory power of the rating and scoring systems using ROC and Gini coefficient
Method 7.1	Stability analyses of discriminatory power over time
Method 7.2	Analyses of migration matrices

The results achieved using the described methods are presented in a traffic signal system. If results of statistical significance and major deviations from established values exist, subsequent analyses are initiated and may result in corresponding adjustments.

Besides the internal quality assurance in the course of the model development and the validation, Internal Audit conducts assessments in the event of material model changes.

Reporting related to credit risk models

Article 452 point (e)

The reporting for the credit risk models follows the three lines of defense as well: The CRCU has the yearly, semi-annual or quarterly monitoring reports (review of estimates) which are presented to the Model Governance Committee. These are the main topics of this reporting:

- Representativity of the application portfolio
- Model performance (e.g. discriminatory power)

- Calibration (realized versus estimated risk parameters)

- The Validation unit as the second line of defense provides the yearly validation report for all credit risk models. Among others, the following categories are prepared regularly as part of standardized monitoring reports:

- Distribution of the customers and exposures across the Basel segments according to CRR, an internal subdivision of the exposure classes
- Distribution of the risk classes across the Basel segments according to CRR
- Risk classes based on overruling
- Discriminatory power of the rating and scoring system
- Analyses regarding calibration

If defined limits are exceeded or fallen short of, the causes are analyzed in detail and countermeasures are initiated as needed.

Internal Audit reports on an ad-hoc basis, e.g. for material model changes and tracks the regulatory findings, but has no regular reports regarding the credit risk models.

Internal rating systems

Article 452 point (f)

Probability of default
The probability of default (PD) is the estimated probability that a borrower will default within the next 12 months. The occurrence of one of the events listed below is deemed as a default event throughout the Group. The definition of default corresponds to the regulatory reference definition ("90 days past due" and "unlikely to pay") as set forth in Article 178 CRR. The new definition of default based on EBA/GL/2016/07 including the lower materiality thresholds of Regulation (EU) 2018/1845 was introduced on 1 July 2020.

Table 8: Description of the reference definitions for default

Reference definition for default	Description
90 days past due	More than 1% of the Group-wide on-balance exposure is more than 90 days past due..
Unlikely to pay (UTP)	Restructuring (e.g. non-accrued status, distressed restructuring etc.)
	Specific credit risk adjustments (e.g. manual loan loss provisions, write-offs etc.)
	Soft and hard UTP triggers (e.g. license withdrawn, repayment gap etc.)
	Legal proceedings (filing for bankruptcy, bankruptcies etc.)

At present, BAWAG Group mainly uses statistical PD estimation models. The models are chosen such that they provide a high discriminatory power, business interpretability and stability over time. The base for estimation is mostly internal data collected within the Group data warehouse, which is regularly checked for representativeness with respect to the application sample, particularly at the stage of model development and calibration. Representativeness analysis enables the definition of the calibration segments and the calibration sample length, as well as early identification of deficiencies specified within EBA/GL/2017/16 and changes in risk appetite and lending standards. The models are then calibrated towards the long run average default rates as per EBA/GL/2017/16, using mostly internal data and employing the maximum available default history. Finally, margins of conservatism covering uncertainty from the identified deficiencies and estimation errors are applied. A recalibration of the models is performed annually and performance of the models is carefully monitored on a regular basis. The estimation and calibration process are executed considering EBA/GL/2017/16. Regulatory floors are reflected in the sense of the PD of the best risk class a customer can obtain. The PD estimation is validated annually using qualitative and quantitative methods. The qualitative methods focus on data quality, utilization and on the quality of the documentation for the estimation process. Discriminatory power is measured in the quantitative area. Furthermore, a binomial test is used for calibration and to check the discrepancy between the forecast PD and the rate of default actually observed. The stability of the estimation models is also observed over extended periods of time.

Table 9: Overview of rating and scoring systems

	Rating system	Model type	BAWAG P.S.K.	Others[1)]
	Corporate Standard	log. regression	x	x
	Cash Based Accounting	Expert model	x	x
	Commercial Real Estate	log. regression	x	x
Corporates	Specialised Lending	Cash Flow Model	x	x
	Private Individual	log. regression	x	x
Retail	SME	log. regression	x	x

1) Other institutions.

Corporate Standard

This area of application pertains to companies that use accrual accounting and that cannot be assigned a special rating procedure because of their business purpose (e.g. real estate companies). These companies must also have a group exposure under Basel II equal to or greater than € 1 million or consolidated operating revenue equal to or greater than € 50 million. The customer's risk class is calculated from a combination of a financial rating from a statistically based balance sheet rating and an assessment of qualitative characteristics (e.g. management, organization, market/sector, general factors and account management). The risk analyst can overrule[1)] or override[2)] a confirmed customer rating if needed. The major reasons for this step are downgrades based on an outdated balance sheet, or warning signals (e.g. outstanding taxes, warning list entries) and consideration of a group influence, ratings of a rating sponsor (e.g. support from dominant shareholders, personal partner with unlimited liability) or, under certain restricting circumstances, consideration of external ratings. In 2017, the Corporate Standard model was redeveloped with the regulatory approval being granted in April 2019.

The performance of the model is assessed on a regular basis, and differences between the observed and actual default rates reveal no underestimation of the observed default rates.

Cash Based Accounting

This expert model covers Austrian counterparties with cash-based accounting in the exposure class "corporates." This model received the initial approval in 2013. The performance of the model is assessed on a regular basis, and differences between the observed and actual default rates reveal no underestimation of the observed default rates.

Commercial Real Estate

This area of application covers companies with accrual accounting that can be designated as real estate agents/investors based on their business activities. The rating system is generally structured like the Corporate Standard Austria process. It combines hard-fact and soft-fact ratings, which can be altered by overruling/override. The model was redeveloped and reviewed by the regulator in 2017. An approval from the ECB was received in 2018. The performance of the model is

1) Overruling refers to a deviation of the confirmed rating from the automatically calculated rating in predefined cases with defined effects, i.e. according to defined rules (e.g. outdated annual financial statements of the customer, various warning signals, and group influence).
2) An override refers to a variable deviation from the automatic rating outcome based on a subjective assessment with a review made by a risk analyst and with a corresponding decision by an authorized employee.

assessed on a regular basis, and differences between the observed and actual default rates reveal no underestimation of the observed default rates. The regulatory floor for the minimum PD is 0.03%.

Specialized Lending

According to the CRR, specialized lending refers to exposures created in relation to companies specially set up to finance or operate real properties that comply with the criteria set down in Article 147 (8) point (a) to (c). For specialized lending, BAWAG Group applies the regulatory slotting approach. The first model, which used qualitative criteria to assign a slot, was replaced by a cash flow tool in 2017. Based on cash flow predictions for the whole maturity, a probability of default is calculated for different risk drivers (e.g. interest rate risk, rental risk, sales risk). Additionally, the expected loss rate is determined for the project. The expected loss is calculated based on probability of default and loss rate, which is mapped to a slot according to Article 158 (6) CRR.

Private Individuals

Private individuals are defined as natural persons whose income does not derive primarily from self-employment. The main exposure categories in the retail customer segment are private loans, overdrafts on salary accounts and credit card products. The rating model takes into account customer characteristics (e.g. age, occupation), application and product characteristics (e.g. amount of credit extended) and external data on any incidences of payment problems. Loans can be approved only for customers up to certain risk class or score thresholds. Beyond the determination of risk class, scoring gives a recommendation on what decision to make (accept/green; reject for now/yellow; reject/red) based on the regulations specifying the essential criteria in the credit extension guidelines (total credit exposure, affordability, security, etc.). These recommendations are binding for the authorized employees in sales. Only authorized staff in the risk centers can overrule the categories “reject for now” and “reject.” Another application scoring procedure can be carried out during the term of any product where warranted, particularly if essential new information has come up that indicates a (positive or negative) change in the customer’s current risk class. Differences between the observed and actual default rates is driven by the fact that predicted PD is based on the historical information. Recurring calibrations or model adjustments are aimed at rectifying the gap. The minimum attainable default probability that a customer can be assigned is the regulatory floor of 0.03%.

Small and Medium-sized Enterprises

The Retail category includes all enterprises with operating revenues of less than € 50 million and an exposure (for the entire customer group) of less than € 1 million in BAWAG Group. If these enterprises cannot be assigned to a special rating based on business purposes (see “Rating systems and processes at companies and institutions”), the scoring procedure for small and medium-sized enterprises is applied. In the Retail/Small Business segment, further sub-segments geared towards the type of accounting (cash-based, lump-sum and accrual accounting) and the operating revenues are formed to take into account the different information bases and the procedural requirements. The exposures consist mainly of overdrafts in payment accounts as well as operating loans and medium- and longer-term investment loans. Differences between the observed and actual default rates is driven by the fact that predicted PD is based on the historical information. Recurring calibrations or model adjustments are aimed at rectifying the gap. The minimum attainable default probability that a customer can be assigned is the regulatory floor of 0.03%

Loss given default

Loss given default (LGD) is defined as economic loss as a percentage of the outstanding exposure at default (EAD). The economic loss comprises the outstanding EAD less recoveries from the realization of collateral and other non-collateral proceeds.

Internal Bank estimates are only carried out for the retail portfolio (Private Individuals and Small Business). The LGD estimate is based on a two-step process. First, the collateral return rate (SEQ) is determined per collateral pool. Then the outstanding exposure less collateral return (EAD*) is determined. For the non-collateralized portion of the exposure, a non-collateralized LGD is estimated using a CHAID-class decision-tree process applying criteria with a high degree of discriminatory power. In a final step, the two components SEQ and non-collateralized LGD are then merged to arrive at the final estimated LGD. The generated values of the individual pools are calibrated at a conservative level using an upward surcharge based on the standard deviation and the number of data sets and taking into account any downturn effects that may be observed. All data available since 2008 were used for model development as long as the data were of sufficient quality and were sufficiently representative. The exposure-weighted average LGD for all retail exposures secured by residential or commercial property is scaled such that it is not below 10% or 15%, respectively. Differences between the observed and actual loss rates is driven by the fact that the LGD is based on the long-term historical information. Recurring calibrations or model adjustments are aimed at rectifying the gap.

The annual validation of the estimated LGD comprises analyses of the deviation between observed values and estimated values, plausibility checks and descriptive statistics and tests for the individual LGD pools.

Credit conversion factor

The credit conversion factor (CCF) is the expected utilization in per cent of a line of credit existing but not yet drawn at the time of estimation until such time as a default event occurs. In other words, the CCF is used for estimating exposure at default (EAD).

Internal Bank estimates are only carried out for the retail portfolio (Private Individuals and Small Business). The CCF estimate is based on a CHAID-class decision-tree process using criteria with a high degree of discriminatory power. The generated values of the individual pools are calibrated at a conservative level using an upward surcharge based on the standard deviation and the number of data sets and taking into account any downturn effects that may be observed. All data available since 2008 were used for model development as long as the data were of sufficient quality and were sufficiently representative. Differences between the observed and actual credit conversion factors are driven by the fact that the credit conversion factor is based on the long-term historical information. Recurring calibrations or model adjustments are aimed at rectifying the gap.

The annual validation of the estimated CCF comprises analyses of the deviation between observed values and estimated values, plausibility checks and descriptive statistics and tests for the individual CCF pools

MARKET RISK

OBJECTIVES AND PRINCIPLES OF THE MANAGEMENT OF MARKET RISK

Article 435 (1) points (a - d) CRR
Article 449 point (m) CRR

Strategies and processes

BAWAG Group has a clearly defined market risk appetite framework. The Group's market risk strategy has a focus on balance sheet hedging and mitigating earnings (volatility of Net Interest Income (NII)), Gains & Losses and Other Comprehensive Income) and economic risks arising from market risk factors. Consequently, the bank has decided to discontinue all trading book activities. This risk appetite is reflected in the bank's limit framework, which ensures the management of the respective risk categories within narrow limits.

The quantification and monitoring of market risks comprise interest rate risk, volatility risk, credit spread risk, funds risk and foreign currency exchange risk. The measurement and monitoring of risk positions is provided by applying sensitivity analyses as well as the analysis of the associated loss potential derived from periodic stress tests. The steering of risks is achieved through setting limits for the individual types of risk, which are approved by the Management Board.

The objectives of the limit system are defined as follows:

- To create a risk-oriented limit system that consistently and methodically covers all positions in the trading and banking book that are sensitive to market risk and all risk factors using standard risk ratios.
- To ensure the controllability of market risk using clear-cut, non-ambiguous risk ratios and to set limits for these ratios in a proactive limit system.
- To integrate risk measurement, limit setting and the monitoring of limit utilization systematically for all positions in the trading and banking book sensitive to market risk at the individual and aggregate level in order to improve the basis for making decisions on risk policy and risk diversification.
- To integrate the market risk limits into budget planning and to take account of calculated risk-bearing capacity and, thereafter, of risk appetite in the scope of the overall ICAAP framework.

Structure and organization of relevant risk management functions

The Risk Controlling (RX) division reports directly to the CRO. The division is responsible for the steering, measurement and controlling of liquidity and market risk of BAWAG Group. The most important responsibilities concern the monitoring of market risk, in particular interest rate risk, volatility risk, credit spread risk and foreign currency exchange risk. This is achieved through the limitation of the individual types of risk, and in this regard it is RX's responsibility to set such limits as approved by the Management Board within the ICAAP.

Additionally, the counterparty credit risk monitoring of treasury positions is located within the area of market risk.

The relevant committee with regard to market risk is the Strategic Asset Liability Committee (S-ALCO). Topics in the context of total risk including ICAAP are handled within the ERM.

Market Risk limit framework

Market risks are limited at least at two levels at a minimum, and where regulatory limits apply, at three levels:

- by ICAAP limits within the context of overall Bank risk management (e.g. VaR)
- operational limits for the management of the specific risk category (e.g. Present Value of Basis Point (PVBP) limits, Greeks limits, volume limits, etc. including limits by accounting method and time bands).
- regulatory limits (e.g. the Outlier Ratio of 20% for interest rate risk)

To limit the interest rate risk, a maximum available basis point value (BPV) is defined for individual credit institutions that are relevant to the interest rate risk and in the scope of consolidation in accordance with IFRS. The basis point value is also sub-divided into maturity ranges and limited at this level. Positions affecting the profit and loss account and equity are also subjected to separate limits. Volume limits per currency are applied to reduce the foreign currency risk of the customer bank. In general, BAWAG Group follows the strategy of minimizing or avoiding foreign currency risk in the banking book.

In addition, a limit framework has been set up to capture the impact of interest rate changes on the Bank's future earnings capacity and the resultant implications for internal capital buffer levels. The (cumulative) net interest income risk limit handles the impact on the future earnings capacity/planned NII in a stress scenario over the three-year planning horizon.

In addition to and as part of the ICAAP, both historical VaR and various stress tests are reported for the economic and normative ICAAP perspective, respectively.

Reporting systems

The market risk reporting comprises internal and external risk reporting. Limit compliance is checked daily for FX risk and interest rate risk BPV and reported to the Management Board. Compliance with the basis point value limits (enterprise and maturity range limits as well as limits relevant to OCI and P&L for interest rate risk and credit spread risk) is monitored monthly at the institution and Group level.

Furthermore, stress tests, reverse stress tests and scenario analyses are conducted. Intended future measures are included in all reports as needed. A net-interest-income simulation (NII simulation) with associated stress tests is performed monthly.

All relevant key figures along with the stress tests are reported to the S-ALCO or as part of the Group Risk Report to the ERM. A VaR is calculated monthly at the Group level.

External reporting comprises the reporting to the Joint Supervisory Team.

Risk hedging and mitigation

Market risks are steered within the applicable limit framework.

To manage market risks within the economic and earnings perspective, the TM division develops hedging and positioning strategies.

To steer the volatility of gains and losses and other comprehensive income, BAWAG Group applies hedge accounting pursuant to IAS 39. The following hedge accounting methods are currently used:

- Micro fair value hedge: hedging against the risk of interest rate changes for fixed-interest instruments held as assets and liabilities.
- Portfolio fair value hedge ("EU carve-out"): application to sub-portfolios of sight deposits.
- Cash flow hedge accounting: hedging of FX risks of future spread income and cross-currency basis risks.
- Net investment hedge accounting: hedging FX risk arising from participations in foreign currency.

Interest rate derivatives that are not assigned to a hedge accounting relationship are recognized at their fair values.

For AGAAP accounting, BAWAG Group uses a macro-hedge as specified in the FMA circular letter on accounting issues in connection with derivatives for managing interest rate risk. The management of interest rate risk covers all interest-bearing positions related to derivatives business in the banking book. Non-interest-bearing positions (equity capital, participations, etc.) are excluded from the macro-hedge.

INTERNAL MODELS FOR LIMITATION OF MARKET RISK

Article 455 point (a) (i - iv) CRR

BAWAG Group does not make use of an internal model to calculate its own funds requirements for market risk.

INTEREST RATE RISK FROM POSITIONS NOT HELD IN THE TRADING BOOK[1)]

Article 435 (1) point (a - d) CRR
Article 448 point (a) CRR

Measurement of interest rate risk

The methods currently used for the banking book include sensitivity analysis, stress tests and value-at-risk as well as volume limits for open positions.

The interest rate risk in the banking book is measured at least monthly. An analysis of interest rate risk is conducted for subsidiary banks and other financial institutions that are relevant in terms of interest rate risk.

There are two complementary methods of measuring the potential impact of IRRBB:

- Present value perspective (changes in economic value - EV, or economic value of equity - EVE when measuring the change in value relative to equity): Account is taken of risks resulting from changes in the market value of transactions accompanied by shifts in interest rate curves. Changed interest rate curves are simulated for the main currencies in the monthly stress tests.

  In addition to and as part of the ICAAP, the VaR is also reported for the economic steering circle.

- Income perspective: Risks that may cause an unexpected decline in the interest margin (interest margin risk, impact of possible interest rate scenarios).

Present Value perspective

EVE: The change in EVE (ΔEVE) represents a risk measure, which is the present value change in EVE, i.e. in the net present value of the balance sheet excluding equity under a particular interest rate stress scenario.

The PVBP is the difference between the Net Present Value (NPV) based on the yield curve shifted by 1bp and the NPV based on the current yield curve. The NPV is calculated based on a discounted cash flow full valuation method. The NPV is obtained either by discounting the expected cash flows of the contract (Marked to Model) or using a given Market Value observation of the contract (Marked to Market).

1) Please note that the text was amended on September 28, 2021 to consider additional information in accordance with regulatory requirements.

The following table depicts BAWAG Group's interest rate risk sensitivities as of 31 December 2021 on the basis of the PVBP concept:

Table 10: Interest rate sensitivities

31.12.2021 in € thousand	<1Y	1Y–3Y	3Y–5Y	5Y–7Y	7Y–10Y	>10Y	Total
EUR	(173)	(27)	(89)	(56)	517	(198)	(26)
USD	23	(29)	(23)	(9)	24	(8)	(22)
CHF	(3)	4	(2)	1	(5)	0	(4)
GBP	15	14	0	(1)	0	7	36
Other currencies	(4)	(5)	0	0	0	0	(10)
Total	(141)	(43)	(114)	(66)	535	(198)	(27)

For the VaR (Value at Risk) within ICAAP the Group applies a historical simulation combined with a general hyperbolic distribution. Based on the market data history, monthly loss scenarios are defined. The time intervals are not overlapping to ensure independent scenarios. To prevent the underestimation of heavy tails, special cases (including the most general one) of a flexible family of distributions – the generalized hyperbolic (ghyp) distributions – is calibrated to the defined loss scenarios. A one-year VaR is determined for each and finally, a robust mean is calculated to minimize the model risk. The ghyp family includes several well-known distributions (normal distribution, Student's *t*-distribution, normal inverse gauss distribution).

Income perspective

Net interest income risk is quantified through the simulation of future interest income and expense under various scenarios. The analysis incorporates all of the Group's NII-relevant assets, liabilities, and off-balance instruments. On-balance-sheet contracts with maturities scheduled within the simulation period are replaced upon runoff with planned new business volumes and margins, thereby reflecting the general ALM policy of the Bank.

The market rate scenarios applied cover parallel and non-parallel upward and downward shifts of relevant yield curves, thereby incorporating limits to the degree to which rates are allowed to drop below zero.

Furthermore, loan prepayment rates (which govern the early redemption of a certain portion of the loans under a given market rate scenario) are also modelled along with alternate new volume, rate and margin scenarios.

Hedging strategies, for example the hedging of FX credit spread risk and non-maturity deposits, are generally assumed to be continued through the end of the simulation horizon.

Variation in earnings and economic value

Based on the internal interest rate risk measurement model, BAWAG Group measures the fluctuations in both EVE and NII driven by the interest rate movements.

Economic value of equity is a cash flow calculation that subtracts the present value of the expected cash flows on liabilities from the present value of all expected assets (including derivatives).

For BAWAG Group, the following EVE calculation assumptions apply:

• Positions included: The calculation of EVE includes all cash flows from all interest rate-sensitive assets, liabilities and off-balance-sheet items in the banking book. Other non-interest-bearing positions are recognized at their book values. Equity is not included.

• Cash flows: The method used is a DCF (discounted cash flow) method. Both principal and interest rate cash flows are rolled out according to the contractual specifics and, if applicable, these cash flows are adjusted by customer behavior assumptions, mainly prepayment assumptions. Deals with undefined maturity profiles are modelled according to the respective models, which reflects both the repricing behavior as well as the liquidity aspects (for ALM models, please see below).

• Time horizon: EVE measures reflect changes in value relative to equity over the remaining life of the balance sheet, i.e. until all positions have run off.

• Balance sheet assumption: ΔEVE is computed with the assumption of a run-off balance sheet, where existing banking book positions amortize and are not replaced by any new business.

The following table shows BAWAG Group's variation in EVE in the event of a +/-200bp parallel rate shock as well as six upward and downward rate shocks (in line with Articles 113 and 114 of EBA/GL/2018/02 Guidelines on the management of interest rate risk arising from non-trading book activities), broken down by currency.

The change in EVE sensitivity compared to the previous year is driven by an overall more neutral interest rate risk position on gradually rising interest rates (see also PVBP sensitivity), with EVE impacts more pronounced for significant rate shifts, following the interest rate risk strategy defined and executed by the S-ALCO during 2021.

Table 11: Instantaneous change of the economic value of equity

31.12.2021 in € million	+200bp	(200bp)	Parallel Shock Up	Parallel Shock Down	Steepener Shock	Flattener Shock	Short Rates Shock Up	Short Rates Shock Down
Total	(141.8)	92.3	(144.5)	93.4	(55.6)	46.7	36.4	38.3
EUR	(178.0)	25.4	(179.5)	25.4	(70.3)	29.0	9.4	7.9
USD	24.7	66.9	24.7	66.9	13.8	13.4	21.2	32.0
GBP	7.7	2.5	9.6	2.2	(0.1)	4.3	5.6	(2.0)
CHF	4.2	(3.8)	1.3	(3.8)	0.4	0.2	0.7	(0.9)
OFX	(0.4)	1.2	(0.7)	2.6	0.5	(0.2)	(0.5)	1.2

Net Interest Income (NII) is a common earnings-based measure calculated as the difference between revenues generated by interest-bearing assets and the cost of servicing interest-bearing liabilities. It focuses on changes in future profitability. ΔNII, the change in NII, is the projected change in NII over a particular time horizon resulting from a sudden or gradual interest rate movement. To the extent that future earnings will impact future equity levels, ΔNII and ΔEVE are aligned, although estimated EVE changes also include adjustments to net income which would occur beyond the (three-year) horizon applied to earnings measures.

For BAWAG Group, the following NII calculation assumptions apply:

• Positions included: NII includes all cash flows from all assets, liabilities and off-balance-sheet items in the Group, including all non-interest-bearing positions, which are assigned an interest rate of 0%. Cash flow balancing is conducted using predefined pricing assumptions.

• Cash flows: Similarly to EVE, NII calculations also employ prepayment assumptions for relevant portfolios. As is the case for NMDs (but not for replication assumptions), the so-called client rates are utilized. The client rates reflect the elasticities of average customer rates to the various key tenors of the yield curves, thereby taking the timing of customer rate reactions into consideration (with time lags of up to 12 months after a given market rate movement).

• Margins: Cash flows include commercial margins and other spread components.

• Time horizon: BAWAG Group generally simulates NII over a three-year horizon, which is consistent with the planning process. Thus, NII risk can be viewed as the short- to medium-term vulnerability of the Bank's NII to IRR.

• Balance sheet assumption: BAWAG Group uses a constant balance sheet approach, under which matured existing business is replaced by new business production.

The following table shows BAWAG Group's variation in EVE in the event of a +/-200bp parallel rate shock (in line with Article 113 of EBA/GL/2018/02 Guidelines on the management of interest rate risk arising from non-trading book activities), broken down by currency.

Compared to the end of last year, the NII risk increased mainly due to strong retail deposit growth (non-maturity deposits, or NMD), which are expected to show lower repricing sensitivity of client rates versus changes in interest rates, particularly in an environment characterized by rising rates.

Table 12: Change in the forecasted net interest income within 12 months

31.12.2021 in € million	+200 bp	(200) bp
Total	206.3	(32.6)
EUR	199.6	(51.9)
USD	8.3	21.1
GBP	1.2	(2.8)
CHF	(0.4)	0.2
Other FX	(2.5)	0.8

Assumptions regarding Non-Maturity Positions

For positions without a defined interest rate (non-maturity positions), BAWAG Group applies replication assumptions based on mathematical models. These models, in turn, are based on a holistic view of interest rate and liquidity risk and consist of the following components:

- Future oriented interest rate scenarios derived based on a forward-looking 2-Factor Hull-White Model.
- Client rate prediction based on historical data. Client rates are expressed as functions of market interest rates – the model applies return-based regression models. The functions are then used to estimate client rates for each interest rate scenario.

- Volume prediction: Volume trends are developed according to plan figures; seasonal fluctuations are captured by time series models.
- Optimization: The model defines the optimal replication portfolio satisfying a set of liquidity, regulatory and internally defined constraints.

The duration of the replication model is constrained in accordance with EBA guidelines for each product group. Furthermore, the Bank has defined a set of different model constraints in order to reflect different types of risk appetite (conservative, moderate, liberal) and mitigate inherent model risks.

Retail non-maturity deposits (NMDs) of BAWAG Group are generally classified into transactional and non-transactional portfolios or further sub-portfolios depending on the product characteristics. The transactional accounts have a duration ranging from 2.98 to 3.14 years, depending on the product's characteristics, due to stable long-term core deposits. The duration of non-transactional accounts, predominantly savings products, is 2.5 years.

Commercial NMDs of BAWAG Group have a duration ranging from 1.08 to 1.56 years.

The interest rate replication model is reviewed and validated once a year. Back-testing and the adjustment of replication assumptions are carried out prior to the planning process.

Assessment of call rights and prepayment behavior

The measurement of interest rate risk also considers embedded call rights and customer prepayment behavior. To determine the value of such embedded options, two different approaches are applied:

- Rational right holders: For professional market participants (e.g. large corporate customers) who are able and willing to take action if prevailing market conditions are in their favor, rational behavior is assumed. For such clients, call and termination rights are valued using the method of replication with swaptions.
- Behavior-based assessment: For clients who do not fulfill the assumption of a rational acting right holder (e.g. retail and SME customers), prepayments are modelled on the basis of historically observed behavior of homogeneous customer groups.

Two types of prepayment models are currently used: on the one hand, portfolio prepayment models which assign a single prepayment rate for an entire loan portfolio. This approach is applied to loan portfolios with a low interest-rate-risk profile (e.g. portfolios with low volume or low duration). A simple average of past observed prepayment rates (expressed in CPR [conditional prepayment rate]) is used as an estimate of future prepayment rates. On the other hand, more sophisticated loan prepayment models are used which assign a prepayment rate to each loan individually based on certain loan characteristics (e.g. loan age, remaining time to maturity, difference between mortgage rate and current refinancing rate, etc.).

The CPR of retail loans ranges between 2.5% p.a. and 35% p.a. depending on the market and characteristics of the product. Commercial loans prepay with a CPR ranging between 0.9% p.a. and 35% p.a.

In addition to prepayment models relevant for the assets, a model was developed for savings deposits to derive the early termination rate (ETR) from the ten-year data history. The ETR amounts to 2.5% p.a.

Scenario analysis

A static and a dynamic analysis are currently carried out for BAWAG Group (internal risk report).

Interest rate gaps, key rate durations, average interest rates and changes in market values for various scenarios are calculated for each defined portfolio as part of the static analysis. The various scenarios and risk parameters below are analyzed to determine their impact on the economic value of the position:

- Parallel shifts in the interest rate curves (+/-25 bp, +/-50 bp, +/-110 bp, +/-145 bp, +/-200 bp, +/-300 bp)
- Non-parallel shifts (flattening, steepening, humping scenarios using different slope and shift pace).
- Worst-case scenario (derived from historical time series)
- Regulatory scenarios based on EBA/GL/2018/02 Guidelines on the management of interest rate risk arising from non-trading book activities
- Forward-looking scenarios based on macroeconomic expectations
- Other scenarios as required.

In the dynamic simulation of interest income, different scenarios are investigated along with their impact on net interest income (parallel and non-parallel shifts of the yield curve).

Interest rate risk mitigation strategies

BAWAG Group uses hedge accounting pursuant to IAS 39. The following fair value hedge accounting methods are currently used to mitigate market risks:

Micro fair value hedge: Hedging of financial assets or financial liabilities against changes in their fair value. The decision on instruments is to be assigned to micro hedge accounting is made in the context of the overall interest rate risk position.

Portfolio fair value hedge (“EU carve-out”): BAWAG Group has identified sight deposits in euros as a portfolio that is to be protected against interest rate risks. These deposits are divided into time buckets in accordance with the expected repayment and interest rate adjustment dates. BAWAG Group determines an amount of liabilities from the identified portfolio that corresponds to the amount to be hedged as the underlying for the portfolio fair value hedge using a bottom layer approach. At the end of 2021, approximately 29% (2020: 28%) of the total volume of sight deposits was allocated to a portfolio fair value hedge.

In addition, contractually agreed interest rate caps and/or floors embedded in financial assets (e.g. loan receivables or securities) or liabilities (e.g. savings deposits) are designated to portfolio fair value hedge accounting in order to mitigate changes in the fair value of these instruments resulting from changes in interest rates. The decision on the amount to be designated to portfolio fair value hedge accounting is determined using a bottom layer approach and made in the context of the overall interest rate risk position and limit framework.

Interest risk reporting systems

The full Management Board is informed monthly about all risks in the S-ALCO based on the comprehensive Market Risk Report and in the ERM (part of the Group Risk Report). In addition, the full Management Board is informed immediately in the event of any material changes in the risk situation.

OPERATIONAL RISK

The definition of operational risk refers to “the risk of losses due to inadequacy or failure of internal processes, people and systems or due to external events”. This definition includes all its subtypes e.g. legal risk, compliance risk, outsourcing risk, conduct risk and ICT risk as well as ESG risk.

STRATEGIES, PROCESSES AND MANAGEMENT

Article 435 (1) point (a) CRR

A clear organizational structure and authorization levels form the basis of operational risk governance. Operational risks are managed by established Group-wide processes for loss data collection via OpRisk Monitor (ORM), yearly risk assessment processes for all divisions and subsidiaries, uniform materiality and risk assessment of outsourcing activities, a sound product implementation process (PIP) including an ESG statement, and monthly key risk indicators.

Upon exceedance of defined thresholds – e.g. red KRI, high risks identified – mandatory measures for risk mitigation are agreed and monitored. In addition, BAWAG Group works continuously to bolster its defenses against cyberattacks. The selected security approach is based on regulatory requirements and the security policy set.

A consistent guideline and a risk-adequate internal control system (including automated controls embedded in the IT infrastructure) as well as a security control set including a variety of organizational and technological measures are in place to manage and mitigate BAWAG Group’s operational risk. Aligned teams in the first and second line of defense ensure the implementation and effectiveness of these measures.

STRUCTURE AND ORGANIZATION OF OPERATIONAL RISK MANAGEMENT

Article 435 (1) point (b) CRR

- Within the OpRisk Management Policy, the Management Board determines principles for the management of operational risks that are applicable throughout the Group. These activities are coordinated centrally by the unit Data Governance, OpRisk & ESG in order to ensure a common approach. The management of operational risks is handled locally in the individual business segments in the respective Group units by the division heads or managing directors and their operational risk agents. All employees are responsible for identifying operational risks and proceeding in accordance with the appropriate regulation. The guidelines for operational risks management are defined in the OpRisk Management Policy, the IKS Policy, the Outsourcing Policy, the Product Implementation Process Policy and in the respective internal manuals and technical documentation.

RISK MEASUREMENT SYSTEMS

Article 435 (1) point (c) CRR

The following risk measurement systems are in use:

Loss data collection

Events, losses, profits, recoveries and near-losses resulting from operational risks in the business segments and areas are collected continuously as part of an institutionalized loss reporting system to provide a database for the management of operational risks (decentralized capturing in an intranet application).

The losses resulting from operational risk are collected in a centrally administrated web-based database within clearly defined regulations and processes. The collected data are analyzed to identify patterns/clusters and faulty processes.

Definitions:

- Operational risk events are incidents occurring during a business process with unexpected effects owing to inadequacy and failure of internal processes, people or systems or owing to external events or circumstances. An operational risk event can, but does not have to, lead to an economic or financial effect.
- Losses from operational risks result from operational risk events with a negative financial impact. The analysis of these losses provides important evidence that can be used to identify the operational risks and to take steps to avoid future losses. Depending on the nature and timing of the events, they may reflect the existing or historical environment of the checks.
- Profit from operational risks has a positive financial impact. Even if profit results from an operational risk event, the event itself is an indication of a process weakness that could result in a loss the next time it occurs. Therefore, these events provide valuable clues to risk management.
- Recoveries refer to the reduction of a loss (e.g. insurance). Operational risk recoveries are divided into insurance recoveries and other recoveries.

  Insurance
  Insurance policies are an important way of reducing loss. Even if the act of taking out an insurance policy cannot prevent a possible operational risk event, it can at least reduce the financial effect caused by such an event.

  Other recoveries
  Other recoveries are payments by third parties that reduce the loss for the company. Examples are damage claim payments, penalty payments, recourse payments and refunds.

- Losses that had a high probability of occurrence ("near-losses") are risk events that ultimately did not result in a financial impact. Near-losses refer to mistakes, system failures or process accidents that could have a negative financial effect but have no impact thanks to favorable circumstances. The identification of near-losses can open up possibilities for improving system structures and processes and reducing the extent of loss that occurs. A near-loss is an event signaling that a system or process weakness can result in losses if not remedied.

Risk Control Self-Assessment (RCSA)

Annual RCSA per business unit (division/subsidiary)

Using the RCSA framework, all organizational units and subsidiaries identify and assess their material processes, operational risks, the risk of disregarding regulatory requirements and the effectiveness of their control measures on a yearly basis via a uniform framework. This includes the assessment of individual control measures, the estimation of probabilities and the extent of losses arising from individual risks. A link to the Business Continuity Plan and Business Impact Analysis is also established within the RCSA. In addition, the responsible divisions and subsidiaries define worst-case estimations and identify the respective risks related to climate change and renewable energy transactions, as well as related to demographic change or other social issues.

Each year, individual key topics are examined and assessed based on internal and external necessity.

If the risk potential exceeds a defined limit, the implementation of appropriate measures is mandatory. Their implementation is subject to continuous subsequent monitoring. An intranet application enables all divisions to make decentralized enquiries about the agreed actions and to process and report the completion of these actions in a decentralized way.

Ad-hoc Risk Assessment

The identification and assessment of potential risks and measures in the case of ad hoc issues is realized through clearly defined processes, especially for outsourcings and the implementation of new products and new systems.

Outsourcing Assessment

An Outsourcing RCSA must be conducted for significant outsourcing -projects. The aim is to identify and assess any operational risks associated with outsourcing projects and must be performed before an agreement is signed so the risk assessment findings can be incorporated into the contract.

Outsourcing specifications are defined in the outsourcing policy. Along with operational risk, the policy covers the assessment of other risks such as strategic risks, regulatory risks and risks from collaborating with business partners.

Key Risk Indicators

Key Risk Indicators (KRIs) show risks in the banking processes and indicate signal change in the risk profile in a timely manner in order to identify and forecast negative trends or a changed risk profile in company workflows and divisions/subsidiaries in a timely manner.

Based on the results from the annual RCSAs, the main operational risks are identified and used as the basis for the elaboration or annual review of the definition and threshold values of the KRIs. Each KRI is valued using a traffic light system (red/yellow/green) and reported to the divisions and subsidiaries on a monthly basis. If the thresholds are exceeded, increased observation (yellow) or a mandatory measure for risk reduction (red) must be specified. The measures and their implementation are constantly monitored and are reported periodically.

Operational risk assessment of new business segments or products

New business segments or products have to be introduced using a product implementation process in which all defined divisions submit their vote and any possible conditions in an end-to-end analysis of the process. ICS is included within the process steps and in the automated workflow.

Latitude of Judgment and Uncertainty of Estimates – City of Linz

Uncertainties in estimations also apply to the claim of BAWAG Group against the City of Linz. On 12 February 2007, the City of Linz and BAWAG Group concluded a swap agreement. This transaction was intended by the City of Linz to optimize a CHF bond (please note that the party to the transaction and consequently the lawsuit is BAWAG P.S.K. AG, a subsidiary of BAWAG Group AG).

Because of the development of the Swiss franc exchange rate starting in the autumn of 2009, the City of Linz was obligated to make increased contractual payments to BAWAG Group. On 13 October 2011, the Linz City Council decided that it would make no more payments in connection with the swap agreement. Consequently, BAWAG Group exercised its right to close out the transaction.

The City of Linz filed a lawsuit against BAWAG Group at the Commercial Court of Vienna (court of first instance) at the beginning of November 2011 seeking payment of CHF 30.6 million (equaling € 24.2 million at the exchange rate at that time), which corresponds to the net cash payments made by the City of Linz while performing the swap agreement. BAWAG Group filed a (counter) suit against the City of Linz for the performance of its contractual rights arising from the same transaction in the amount of € 417.7 million, which mainly reflects close-out costs BAWAG Group incurred. The court combined the two suits. The first hearings were held in the spring of 2013 and a court-commissioned expert opinion as well as a supplementary opinion thereto were submitted in August 2016 and December 2017. On 8 April 2019, the City of Linz filed a motion for an interim judgment (*Zwischenurteil*) with respect to their CHF 30.6 million claim to determine whether the swap agreement is valid. The court responded to this motion with a separation of the previously combined two proceedings and suspended BAWAG Group's (counter) claim pending the outcome of the interim judgment. On 7 January 2020, the court of first instance issued an interim judgment in which it held that the swap agreement is void. The Court of Appeal confirmed the interim judgment of the court of first instance on 31 March 2021 and permitted a regular appeal (*ordentliche Revision*) to the Supreme Court. BAWAG Group filed its appeal to the Supreme Court on 4 May 2021 and the decision of the Supreme Court is still pending.

The interim judgment relates to the validity of the swap agreement only and is not a decision on the mutual payment claims of BAWAG Group and the City of Linz. Therefore, notwithstanding the final decision on the validity of the swap agreement by the Supreme Court, the mutual payment claims will ultimately be decided by the court of first instance and potentially the Court of Appeal and the Supreme Court once again. BAWAG Group therefore believes that its strong legal position remains unchanged and is well prepared for the forthcoming court proceedings. It is difficult to predict how much longer the lawsuit is going to continue. However, based on experience it is assumed that the further legal proceedings until a final judgment is enforceable will take several years.

Future court decisions on the validity of the swap agreement may impact the recognition of the receivable asserted thereunder. In the event that the swap agreement is deemed void by the Supreme Court, BAWAG Group would have to derecognize the receivable against the City of Linz. A potential consequential damage claim resulting therefrom would only be recognized after a final judgment has determined the amount awarded to BAWAG Group. In addition, even if the courts ultimately were to hold that the swap agreement is valid, BAWAG Group may still not be awarded, in full or in part, the payment sought, in which case it may also be required to further write down its receivable.

BAWAG Group has valued the transaction until termination according to the general principles (see Note 1 Accounting policies in the Annual Report) and has adequately accounted for the risks associated with the claim arising from the swap agreement. In particular, management had to estimate the risks that are associated with the transaction, such as non-payment, legal, process and other operational risks and had to make judgments as part of the continuous valuation process; this resulted in a respective valuation adjustment.

After the termination of the transaction, the swap was derecognized, and a receivable was recognized under receivables from customers (classified under At amortized cost – receivables from customers). In 2011, when derecognizing the swap, a credit value adjustment of € 164 million (equals around 40% of € 417.7 million) was set off against the gross receivable, thus a new receivable was recognized in the amount of approximately € 254 million.

Stress tests

Operational risk is included in the stress testing activities. For the semi-annual stress test, the operational risk stress parameters are defined as expert estimation based on macroeconomic stress scenarios. The impacts are calculated on the historical loss data. An operational stress test scenario was developed for the reverse stress test activities but has a very limited probability of occurrence.

Risk reporting systems

Reports are produced periodically on material operational risks and on the actions needed to prevent similar future risks. These documents enable the Management Board and the division heads to manage operational risks and minimize possible losses arising from those risks.

- The ERM receives a summary of the P&L impact of the KRIs and the regulatory own funds requirements, as well as the ICAAP limit including the utilization as part of the Group Risk Report.
- The divisions and the subsidiaries receive periodic summaries of the losses, RCSA results, KRIs and open measures.
- The results from the annual RCSAs and ad hoc risk assessments are reported in separate reports to the respective division heads, to the responsible board member, the CRO and Internal Audit.
- The results from the Outsourcing Assessments are reported periodically in the NFR&ESGC.
- Relevant PIPs are reported periodically in the NFR&ESGC.
- An overview of all pending measures for reducing operational risk (as set forth in the RCSA and the PIP) is reported via the NFR&ESGC to the responsible board member on a quarterly basis.

RISK HEDGING AND MITIGATION

Article 435 (1) point (d) CRR
BAWAG Group has laid the basis for operational risk mitigation with its segmented organizational structure, clear rules on competencies and responsibilities, and work instructions. In addition, consistent guidelines on corporate authorization levels help to achieve the goal of a controlled risk situation, as well as the implemented ICS, which (adequately) captures the risk. The ICS does so, for example, by means of the dual control principle, separation of functions, access checks, limited authorizations, computer-assisted plausibility checks and system tests. In addition, centrally regulated insurance management helps to hedge the risks.

OWN FUND REQUIREMENTS

Article 446 points (a) – (c) CRR

The regulatory own fund requirements for operational risks are calculated using the standardized approach pursuant to the Article 317 CRR. The advanced measurement approach pursuant to the Article 321 CRR is currently not applied.

Therefore, it is not subject to disclosure obligations in accordance with the Article 454 CRR.

LIQUIDITY RISK

Article 435 (1) points (a) – (d) CRR

STRATEGIES, PROCESSES AND MANAGEMENT

The ALM team in the TM division and the S-ALCO (Strategic Asset Liability Committee) handle liquidity management throughout the Group. RM independently measures and monitors liquidity risks. The principles and goals below serve as the point of departure for liquidity management:

Principles of liquidity control

- Liquidity management is a central core competence.
- Together with capital, liquidity represents the most important scarce resource of the Bank and must therefore be controlled.
- Liquidity has a price that fluctuates with supply and demand.
- Primary responsibility for liquidity management is allocated to the TM division, which is part of the CFO organization. Within TM, the TMA department is tasked with the main responsibility for liquidity management including acting as the central function with control to monetize the liquidity buffer.
- ALM does not pursue its own profitability goals in the process.
- BAWAG Group follows a centralized approach to liquidity management. This includes that the size and quality of the liquidity buffers, liquidity risk-relevant KPIs, the funding strategy and the execution of refinancing measures as well as the disposition of excess liquidity is determined by BAWAG Group and aligned with its subsidiaries. Subsidiaries are generally expected to refinance their funding needs or to deposit their excess liquidity with BAWAG P.S.K. in accordance with their governance and legal or regulatory constraints (e.g. legal lending limits, LCR inflow caps etc.).
- RM is responsible for liquidity risk measurement, quantification, monitoring and controlling, and providing independent risk oversight.
- Control activities are geared primarily towards liquidity cover, secondly towards liquidity structure and thirdly towards liquidity costs.
- From an organizational standpoint, ALM manages liquidity independently of the business areas, but the effects of liquidity actions are analyzed and taken into account at the level of the business areas.
- Income, accounting and RWA effects are considered in the process, as are the ramifications for collateral, regulatory key ratios, maturity structure and the franchise value.
- Liquidity control is performed indirectly with internal clearing prices for customer business and indirectly with needs-based transaction pricing for large-volume wholesale funding.
- The price of liquidity is determined centrally using defined methods. ALM serves as the counterparty for all business areas with respect to obtaining and extending liquidity.
- Liquidity control takes account of possible negative effects from risks to BAWAG Group's reputation.

Goals

The central goals of liquidity control are as follows:

- Ensure sufficient liquidity even in a stress case
- Meet short- and medium-term liquidity needs and ensure long-term funding based on planning and forecast calculations for each currency
- Develop and maintain the strategic refinancing structure
- Maintain sources of financing on the capital market and in customer business even in periods with a minimal need for obtaining refunding
- Reduce the concentration risk as regards the maturities profile and through diversification of funding sources and counterparties

- Optimize the maturity structure and funding costs
- Maintain a sufficiently large liquidity buffer at the lowest possible costs
- Comply with all internal and external key ratios and regulatory limits for liquidity
- Invest excess liquidity based on planning and forecast calculations
- Adjust liquidity prices in the short term to optimally control liquidity
- Take into account strategic elements for the procurement of funds such as the franchise value for customer deposits and customer relationships

Liquidity Risk Statement

BAWAG Group has established a Group-wide Internal Liquidity Adequacy Assessment Process (ILAAP) framework which defines the Group's liquidity risk management processes, steering mechanisms, funding strategies and liquidity risk limits to adhere to the overall risk appetite. The overall risk appetite defined by the Management Board serves as the boundary condition for the risk strategy. The limits set for liquidity risk within the ILAAP are strategic specifications for the steering and limitation of the Group's overall risk position and express the Group's risk appetite. Compliance with these limits ensures an adequate liquidity position.

Within the overall business and risk strategy, the management of BAWAG Group has outlined the focus on maintaining a conservative, low-risk balance sheet with an explicit commitment to a strong capital position, low levels of leverage, a strong liquidity position with a conservative funding profile and a deposit-based funding strategy.

Retail and corporate savings products have been the core part of the Group's funding strategy over the years and will continue to be the dominant source of funding for the balance sheet. This strategy is confirmed by a growing share of stable customer deposits contributing more than 60% of total balance sheet funding, with retail deposits representing the most important pillar.

The stable deposit base is supplemented with a diversified strategy of wholesale funding. The funding instruments comprise both unsecured bonds as well as bonds secured by mortgages (covered bonds and RMBS) and public sector collateral.

In addition to the stable deposit base, in the course of 2021 the Bank successfully placed € 1,500 million in mortgage covered bonds (March: € 500 million; May: € 500 million; September: € 500 million – Green Covered Bond), which again proved BAWAG Group's good capital market access and the positive perception among investors. The maintenance of a robust liquidity and funding position is considered to be a core element of the successful implementation of the overall business strategy.

BAWAG Group has implemented a liquidity risk limit framework covering the relevant time horizons from short to long term as well as comprehensive stress testing procedures to measure potential liquidity risks and to ensure liquidity adequacy even in adverse scenarios. These stress analyses are based either on empirically available data, hypothetical but plausible stress scenarios, or forward-looking information derived from business forecasts. The liquidity stress testing is designed to identify and address the key vulnerabilities of the Group towards contingent liquidity risks and to determine the size of its liquidity buffer and counterbalancing capacity needs beyond the regulatory minimum standards.

BAWAG Group maintains a significant liquidity buffer to cover unexpected liquidity outflows in a stress scenario. The holding of the liquidity buffer therefore represents a preventive measure to reduce liquidity risk. Furthermore, the Group has contingency funding plans in place which define what constitutes a liquidity contingency, the monitoring procedures in place to identify the occurrence of a liquidity contingency event, changes in the governance resulting from the declaration of a liquidity contingency as well as the measures available to rectify a liquidity crisis. BAWAG Group has a set of predefined measures that can be taken in the event of a liquidity contingency to improve the liquidity situation of the Group.

On the basis of its ILAAP, the Group conducts an ongoing self-assessment of its liquidity risk profile, risk measurement and management framework, and liquidity adequacy. The outcome of this process is documented annually in the Group's liquidity adequacy statement (LAS) signed by the Management Board of BAWAG Group. On the basis of the ILAAP, the Management Board is convinced that the current risk management framework allows for the comprehensive identification, quantification, measurement and steering of all relevant liquidity risks and considers the liquidity and funding position of BAWAG Group to be solid and fully adequate as of 31 December 2021.

STRUCTURE AND ORGANIZATION OF RELEVANT RISK MANAGEMENT FUNCTIONS

Organizational structure

The full Management Board determines the business strategy of the Group and the individual business areas and defines target values for the central key ratios. The board is therefore responsible for the liquidity strategy and defines the level of risk tolerance for the planning period.

The CFO, as a member of the Management Board, performs the function of liquidity manager for the Group as a whole. The TM division reports to the CFO and incorporates the liquidity management. The CFO monitors the activity of the organizational units and regularly informs the full Management Board about the liquidity situation. TM bears the central specialized responsibilities for liquidity management. A central Collateral Management for BAWAG Group is integrated in Asset Liability Management (ALM).

Controlling is responsible for operational accounting of the liquidity costs and premiums in the profit center calculations and for the methods used in the FTP system. The liquidity cost system derives prices from current market rates. The fine tuning is performed by ALM to balance short-term gaps.

RM, a division reporting to the CRO, measures the current liquidity risk, prepares limit proposals for the S-ALCO and monitors compliance with the defined limits and liquidity buffers.

TM is responsible for the operational execution of money market and capital market transactions.

Liquidity management is subdivided into four task areas: operational, tactical and strategic liquidity management and liquidity buffer management. With regard to liquidity risk categories, a distinction is made between dispositive, structural and market liquidity risks.

The reporting of the current and projected liquidity position as well as the funding potential is performed by the TM division. One of the most important key ratios is FACE (Free Available Cash Equivalent), which is internally defined at BAWAG Group. The liquidity buffer is divided into a short-term and medium-term portion that can be liquidated. The reporting of the liquidity risk is done by RM.

RISK MEASUREMENT SYSTEMS

The liquidity risk is calculated by rolling out the cash flows from existing transactions. These cash flows are calculated from business data drawn from the central data warehouse. Based on the transaction data for customer business (loans, deposits, securities, etc.), the cash flows from the repayment of principal are rolled out at the individual transaction level within the market risk management system OneSumX and are reported in aggregated form according to defined criteria (e.g. product type, customer category, and behavior with respect to the repayment of principal). Positions with undefined maturities (current accounts and customer deposits) are assigned to the time bands based on the modelled liquidity replication assumptions reflecting the historical retention period and volume fluctuations.

The total of asset and liability cash flows determines the gap in the static balance of cash flows, i.e. new business is not assumed. The stressed funding cost resulting from closing the funding gaps is quantified as well. Special attention is payed to the structural risk in FX funding, which is articulated in FX basis spread risk. To measure this risk, the PVBP concept (similar to the interest rate risk) has been implemented. Furthermore, stress tests are then conducted in BAWAG Group's balance sheet by making certain assumptions regarding volume changes in certain stress situations. These stress tests are based on the existing balance sheet structure and assume that transactions drawing to an end will be replaced under the same conditions (terms, volumes but with different circumstances). With this constant balance sheet, the volume assumptions for individual products are then weighted with the relevant stress factors (outflow assumptions).

The stress scenarios are distinguished as follows:

- Intraday stress
- Idiosyncratic stress
- Systemic stress
- Mixed stress scenario
- Reverse stress test
- Forward looking adverse scenarios (ICAAP/ILAAP)

The stress tests also take account of the liquidity buffer and the counterbalancing capacity, i.e. unencumbered liquidity reserve. It is assumed that these buffers can be converted into genuine liquidity in a short time either in a sale, in repurchase agreements or through refinancing from the central bank.

The time-to-wall is measured in these stress tests. The stipulated risk limits must be adhered to in the stress tests taking into account the liquidity buffer and the counterbalancing capacity; otherwise, TM must suggest or initiate countermeasures. The stress test results determine the size of the liquidity buffer and the counterbalancing capacity.

RISK REPORTING SYSTEMS

The liquidity status is presented and reported in standardized, regular reports. These reports are divided into the following categories:

- Operational liquidity status
- Tactical liquidity status
- Structural liquidity status

The reports on the operational liquidity status basically provide a concrete forecast of liquidity for the next several days so that the operational liquidity management can immediately indicate a need for liquidity or a surplus of liquidity. This status is then adjusted by conducting short-term interbank transactions or by compensating account balances.

The reports on the tactical liquidity status are used to estimate business developments on the assets or liabilities side of the balance sheet and to present them to the S-ALCO on a monthly basis. These reports depict developments in economic and regulatory liquidity statically and dynamically, pointing out potential gaps. The corresponding limits and compliance with them are measured in these reports for economic and regulatory liquidity. TM is responsible for closing unplanned tactical gaps (in a time horizon of 15 months) by taking preemptive actions.

On the one hand the reports on the structural liquidity status are produced under a dynamic perspective as part of the overall Bank planning. In the process, TM coordinates the planning of overall funding, which comprises theoretical scenarios, business shifts and planned assumptions for new business. The funding plan has a time horizon of five years. On the other hand, the structural liquidity risk is also measured monthly under a static perspective and quantified with stress assumptions.

RISK HEDGING AND MITIGATION

Risks are hedged and mitigated by means of ongoing checks of the current and forecast liquidity status from an economic, regulatory and also strictly cash standpoint. Plans are constantly adjusted based on current developments in the business areas and the market and on a re-evaluation of the liquidity buffer and the counterbalancing capacity.

A liquidity emergency plan for the actual stress case was drawn up and is periodically updated.

The purpose of the liquidity risk strategy is not only to hedge and mitigate risks. It is also used for rendering risks measurable, for raising awareness of risks and for actively controlling risks (in terms of a conscious decision to take a liquidity risk). In this same context, BAWAG Group continuously tests market liquidity for individual balance sheet items and constantly assesses the ability of the market to absorb products on the liability side (and the potential refinancing costs associated with them). It also prepares forecasts of the volume of collateral material for securitized refinancing (and reconciles it with the business plan).

LIQUIDITY COVERAGE RATIO

The Commission Delegated Regulation 2015/61 with regard to liquidity coverage requirement for credit institutions (Delegated Act) came into force as of 1 October 2015. The Delegated Act supplements and amends the rules for the calculation and reporting of the liquidity coverage requirement (LCR) of the CRR. At the consolidated level, BAWAG Group is subject to the LCR requirement and to the LCR disclosure requirement. LCR requires banks to hold high-quality liquid assets (HQLA) to cover net cash outflows over the period of 30 calendar days and is calculated under the assumption of severe liquidity stress

Hiqh Quality Liquid Assets (HQLA)

Assets are considered to be HQLA if they can be easily and immediately converted into cash at little or no loss of value. The LCR defines HQLA in three asset categories: Level 1, Level 2A and Level 2B, and applies haircuts and limits to certain asset categories.

BAWAG Group’s HQLA consists primarily of central bank and government assets assuring maximum reliability in times of stress. All securities that are included into BAWAG Group’s HQLA needs to meet internal requirements that secures low levels of concentration with respect to issuers and their origin.

Net Cash Outflows

Net cash outflows are defined as the total expected cash outflows minus total expected cash inflows in the specified stress scenario for the subsequent 30 calendar days. Total expected cash outflows and inflows are based on the contractual maturity of assets, liabilities and off-balance-sheet commitments. Where contractual maturity is not applicable, the LCR sets forth maturity assumptions by multiplying the outstanding balances of these categories by the rates at which they are expected to flow under the scenario. Inflows are subject to an aggregate cap of 75% of total expected cash outflows.

The structure of the LCR outflows reflects the Group's conservative funding structure, with retail deposits being the most important source of the liquidity and with very low counterparty concentrations among all funding items.

Outflows related to derivative exposures and other collateral requirements reflect contractual derivative settlements as well as contingent derivative outflows (largest net cumulative collateral outflow or inflow in a 30-calendar day period over the last two years).

BAWAG Group has no individual currency concentrations above the regulatory thresholds. For this reason, the LCR metrics are only reported in euros.

As of 31.12.2021, the average LCR value for the last 12 months amounts to 235% with an HQLA portfolio of € 11,032 million and € 4,707 million in net outflows.

The increase in the above figures in comparison to the figures disclosed for 31.12.2020 is primarily due to the following:

In the course of 2021, BAWAG Group further solidified its liquidity position by increasing its stable core funding bases, primarily deposits from retail customers, despite the ongoing COVID-19 crisis.

In March 2021, BAWAG Group also increased its participation in the ECB's TLTRO III program by an amount of € 580 million.

In addition to the increase in its stable deposit base, during the year, the group successfully placed €1,500 million of mortgage covered bonds (€ 500 million in March 2021; € 500 million in May 2021; € 500 million in September 2021) confirming BAWAG Group's good capital markets access and the positive perception among its investors..

NET STABLE FUNDING RATIO

With the implementation by the European Parliament the Regulation (EU) 2019/876 Net Stable Funding Ratio (NSFR), initially introduced by the Basel Committee, has finally become binding requirement in the European Union. BAWAG Group as a Large Institution is obliged to present NSFR information on semi-annual basis.

The aim of NSFR is to promote stable funding structure in relation to the composition of institutions assets and off-balance sheet activities. It is achieved by limiting the possibility of overreliance on short-term funding. The regulatory limit of 100% requires bank to keep Available Stable Funding (AFS) at least in the same amount as Required Stable Funding (RSF).

As of 31.12.2021. the NSFR was at 139,42% expressing stable development in BAWAG Group ASF and RSF since first NSFR reporting under CRR II regime in June 2021 with ratio at 139,57%. The increase in RSF that has been driven by new loans has been mainly funded by customer deposits.

CONCENTRATION RISK

Article 435 (1) points (a) – (d) CRR

STRATEGIES, PROCESSES AND MANAGEMENT

The general framework for the management of concentration risk is based on estimates made by senior management coupled with specifications and recommendations made by national and international institutions engaged in bank regulation.

The Risk Management Organization (Risk Controlling) manages, limits and controls concentration risks and reports them on a monthly basis to the PSC, composed of controlling, markets and risk divisions heads.

Risk concentrations arise from large exposures in individual customer segments or from large total exposures in certain industries, countries or foreign currencies whose loss potential could endanger BAWAG Group's core business or has an impact on the risk profile.

Concentration risk at the level of individual transactions or products is dealt within the Credit Risk Policy. The management of country and industry limits is carried out as a standard process in accordance with binding internal guidelines.

STRUCTURE AND ORGANIZATION OF RELEVANT RISK MANAGEMENT FUNCTIONS

The main body is the monthly ERM, in which all Management Board members participate and in which the CEO serves as the chairperson. The CRO bears responsibility for the management of concentration risks in the Management Board. The ERM is set up as a committee at the Management Board level and is responsible inter alia for approving the methods and the processes employed for measuring concentration risks. The ERM delegates the steering and monitoring of the concentration risks to the PSC. As mentioned above, the Risk Management Organization bears responsibility for concentration risk management in coordination with the Commercial Risk Management and Retail Risk Management. divisions.

RISK MEASURING SYSTEMS AND LIMITATION

Allocated economic capital is the basis for quantifying the concentration risk at the level of individual borrowers and groups of affiliated customers as well as with concentrations in industries, countries and currencies. The quantification is part of the Portfolio Steering Framework (in place since 2015).

Appropriate limits are determined for countries, for industries for the segment Corporates, Real Estate & Public and for currencies and constitute an integral part of the efforts to control total Bank risk.

All limits are monitored on an ongoing basis and in accordance with the estimated risk potential.

If limits are exceeded, the risk management units and the Management Board agree on suitable actions to limit or reduce the risk.

To prevent losses in connection with collateral concentrations that could put the financial stability at risk or result in a material change in BAWAG Group's risk profile, appropriate warning thresholds are defined and are subject to periodic monitoring and reporting processes.

All material risk factors are depicted in scenario analyses and stress tests using VaR models in order to analyze and monitor market concentration risks. For reasons of a prudent view, conservative assumptions regarding correlations between risk factors are made.

Regarding concentrations of operational risks, the focus is on activities with a long business history, and particular emphasis is also placed on adequate assessments of new lines of business.

Active monitoring of funding requirements and broad diversification of funding sources are precautions against potential liquidity problems from risk concentrations in the investment and funding structure.

REPORTING SYSTEMS

The discussion of the Portfolio Steering Framework Report (which has separate sections focusing on concentration risks in the segments of countries, industries, currencies and customer groups) is performed in the PSC. This committee is delegated by the ERM to monitor and manage the economic capital allocated on the bottom levels of the portfolio steering framework (level 3 business sub-segments and level 4 countries and industries, up to € 40 million).

After the competent risk committee receives and approves the concentration risk report, the report is communicated to the relevant underwriting units..

RISK OF MONEY LAUNDERING AND TERRORISM FINANCING

Article 435 (1) points (a) – (d) CRR

STRATEGIES, PROCESSES AND MANAGEMENT

Based on the business model of BAWAG Group focusing on retail, small business, corporate and public sector clients in developed markets of the DACH/NL region (Germany, Austria, Switzerland and the Netherlands), Western Europe and the United States, the overall risk of money laundering and terrorism financing is low.

Strategy and processes for the prevention of money laundering and terrorism financing (abbreviated as AML/CTF in the following paragraphs) have been approved by the Management Board. As required by law, a comprehensive risk analysis of specific money laundering risks and mitigants is regularly conducted and updated.

Pertinent directives (summarized in a separate manual) and mandatory technical IT fields ensure compliance with all relevant regulations to prevent money laundering and terrorism financing under the Financial Market Money Laundering Act (FM-GwG) based on the 4th and 5th EU Anti-Money Laundering Directive (EC 849/2015 and EC 843/2018) and under the EU Regulation on information accompanying transfers of funds and repealing EC 847/2015. Furthermore, an internal control system ensures compliance with the internal account opening and transaction policies.

Customer relationships and domestic and foreign transactions are automatically monitored along AML/CTF risk classifications which follow the AML/CTF risk analysis. These customer, transaction and country screenings consider the High-Risk Country Regulation issued by delegated regulation of the European Commission and the relevant sanction guidelines of the UN, OFAC, EU, UK and the Oesterreichische Nationalbank (the Austrian National Bank).

Employees are regularly trained (self-study programs and classroom training) to sensitize them to specific typologies suspected for money laundering or terrorism financing.

STRUCTURE AND ORGANIZATION OF RELEVANT RISK MANAGEMENT FUNCTIONS

The mandatory AML Officer is supported by a department leader and specialized employees. In his function as AML Officer, the head of the Anti Money Laundering & Know Your Customer & Compliance division reports directly to the full Management Board. The organizational Anti Money Laundering and Sanctions Manual outlines the duties and responsibilities of the Anti Money Laundering & Know Your Customer division.

The main competences of the AML Officer are:
- defining the AML Group strategy as well as the review of its realization
- developing policies, controls and processes including (IT) systems to prevent money laundering and terrorism financing along regulatory developments
- comprehensive inspection and control rights (regular internal control system checks) and access to all systems
- possibility for ad hoc audits at any time
- decision to report suspicious cases to FIU and to block accounts
- decision regarding whether a critical customer relationship will be established or an existing relationship will be terminated.
- ensuring Group-wide AML/CTF and sanctions understanding and training.

RISK MEASUREMENT SYSTEMS

In addition to the yearly overall risk analysis, suspicious cases in the context of AML/CTF are continuously analyzed for new patterns to develop the AML/CTF systems. A Group-wide exchange of suspicious cases related to money laundering has been organized since 2017.

BAWAG Group operates an AML/CTF software system that classifies all customer relationships into AML/CTF risk classes (applying specific risk factors like product, domicile/residence, industry, nationality, etc.). Upon applying for a product, respective measures vary based on the assigned risk class (e.g. increased monitoring for higher risk classes). The software differentiates between low, medium, high and very high AML/CTF risk classes (such as politically exposed persons). New patterns of behavior or findings can be translated into new transaction monitoring scenarios, another module of the AML/CTF software. The third module of the applied AML/CTF software module ensures the monitoring of customers against PEP (politically exposed persons) and relevant sanctions lists.

With regard to sanction screening, the applied software ensures transaction, country and sanction screenings against relevant lists before transactions are executed.

RISK REPORTING SYSTEMS

The AML Officer reports to the full Management Board and the Audit and Compliance Committee on a quarterly basis. Furthermore, the AML annual report has to be acknowledged by the Supervisory Board. Since 2017, a Non-Financial Risk and ESG Committee has been established on the Management Board level, which meets on a regular basis.

RISK HEDGING AND MITIGATION

BAWAG Group's overall AML/CTF strategy is subject to at least an annual review and re-approval of the Management Board.

Comprehensive guidelines are summarized in the Anti Money Laundering and Sanctions Manual, and a control system is in place for the opening and monitoring of accounts and also for one-time transactions where mandatory identification duties apply. Furthermore, mandatory IT fields ensure that the required data is recorded for account opening processes and specific transactions (e.g. verification of origin for transactions, transactions requiring an ID to be shown).

Additionally, the AML Officer has established a monthly internal control system, which checks compliance of sample sets with the internal account opening and transaction policies. Any errors are redirected for correction, retraining or to take other effective measures to the person in charge.

In addition to the comprehensive Bank risk analysis that undergoes an evaluation once a year, BAWAG Group regularly analyzes suspicious cases for new behavior patterns, which may lead to software updates or other specific actions.

RESIDUAL RISK FROM TECHNIQUES OF CREDIT RISK MITIGATION

Article 435 (1) points (a) – (d) CRR

STRATEGIES, PROCESSES AND MANAGEMENT

All risks which are not already covered in other risk sections are referred to as residual risks from techniques of credit risk mitigation:

- Concentration risks for collateral
- Legal risk of realization (change in the legal situation, etc.)
- Other risks – changes affecting security and exceeding usual fluctuations and changes

Transparent risk assessment for concentrations of collateral is ensured by means of appropriately defined processes and continuous monitoring of collateral at the portfolio level and guarantor level. These activities give the management a sufficient basis of information in order to adequately control collateral concentration risks.

BAWAG Group covers legal risk and other risks by applying correspondingly conservative valuation approaches and collateral lending values.

In addition, potential credit losses due to collateral deterioration are simulated within stress testing and possible effects on the risk-bearing capacity of BAWAG Group are considered.

STRUCTURE AND ORGANIZATION OF THE RELEVANT RISK MANAGEMENT FUNCTIONS

These risks are constantly monitored within the risk organization and regularly reported to the Portfolio Steering Committee. The concept for monitoring concentration risks regulates the possible actions and the powers with regard to the imposition, execution and monitoring of concentration risks arising from collateral.

RISK HEDGING, -MITIGATION AND RISK MEASUREMENT SYSTEMS

Various steps are taken to address and ensure compliance with the requirements pertaining to residual risk from credit risk mitigation.

- The market value and lending value are assessed and estimated in the course of collateral valuation. Details on the valuation procedure are given in the Credit Collateral Catalogue.

- Stress tests are conducted to analyze the fluctuations in collateral market values and lending values and their ramifications for the risk bearing capacity. Details about these stress tests can be found in the stress test.
- The residual security concentration risk is covered in the monitoring plan entitled “Concentrations of Collateral”.

MACROECONOMIC RISKS

Article 435 (1) points (a) – (d) CRR

STRATEGIES, PROCESSES AND MANAGEMENT

Macroeconomic risks designate potential losses that may arise from changes in macroeconomic risk factors, such as the GDP trend, the unemployment rate and the oil price, but also for political reasons, such as Brexit.

Macroeconomic risks have myriad possible consequences. Unfavorable overall economic developments could result in negative repercussions for BAWAG Group such as a negative change in market prices, increased default rates, less demand for products, negative trends in the value of participations, falling savings rates (tight liquidity) and so forth.

Risk is identified during stress testing conducted to determine the type and scope of the required stress tests and to define the macroeconomic scenarios and the associated risk parameters. Stress tests are conducted periodically and fall under the responsibility of the individual specialized units of the risk organization..

STRUCTURE AND ORGANIZATION OF RELEVANT RISK MANAGEMENT FUNCTIONS

The items are addressed here in an interdepartmental manner due to the interdisciplinary topics associated with macroeconomic risks.

RISK MEASUREMENT, RISK REPORTING SYSTEM AND RISK HEDGING OR MITIGATION

Preliminary control of macroeconomic risks is done during overall Bank risk control and planning activities. Planning is completed with a defined economic environment indicated.

Within the annual Risk Self-Assessment process, macroeconomic risk is assessed and quantified. In general, macroeconomic factors are considered within the quantification of the individual risk types using validated models. Nevertheless, the Group also holds a capital buffer at the Management Board level for acquisitions and unidentified risks – a potential residual risk stemming from a negative macroeconomic development for the Group is also covered by this buffer.

Furthermore, the Group controls the impact of macroeconomic changes within the reporting of stress test results as well as during the determination of any necessary actions. Possible actions for subsequent control range from diversification and the reduction of risk positions to an increase in internal capital. Actions can also be of an organizational nature, for instance an in-depth analysis of risk drivers or also the inclusion of additional aspects in the stress tests. The actions are approved by the decision makers and carried out by the responsible organizational units.

Stress test results and any necessary actions are discussed in the dedicated ICAAP & Stress Test Committee and then presented for approval to the ERM. In addition, the Group has implemented the Macroeconomic Scenario Committee to identify appropriate scenarios for each stress test exercise and ICAAP perspectives..

PARTICIPATIONS NOT HELD IN THE TRADING BOOK

OBJECTIVES AND PRINCIPLES FOR THE MANAGEMENT OF PARTICIPATIONS

Article 435 (1) point (a) – (d) CRR

Strategies and processes

Participation risk includes potential losses from own equity provided, from risks caused by the assumption of liability (e.g. comfort letters) or from profit and loss transfer agreements (assumption of losses).

Under the participation strategy approved by the Management Board, participations are divided into the following categories:

- Majority participations in the financial services sector that are considered part of the core business and that therefore address additional groups of customers or enlarge the product range and that must satisfy minimum return requirements at least in the medium term. These minimum return requirements can be met by contributions to the Bank's commission result from dividends or service contributions.
- Minority participations in the financial services sector of strategic significance for enlarging the product range within the financial services sector. These equity exposures are measured based on direct return.
- Auxiliary undertakings that perform services for BAWAG Group in outsourced legal entities. Auxiliary undertakings are generally active in the IT sector or in payments. The participation portfolio carries auxiliary undertakings both as majority participations and as minority participations (usually collaborations with other credit institutions).
- Other participation items

BAWAG Group generally pursues the goal of achieving appropriate and lasting profitability, taking any risk mitigation into account. Any major change in the participation portfolio therefore requires the approval of the Management Board and a risk assessment from the responsible risk unit.

Structure and organization of relevant risk management functions

The risk management function for participations is integrated into the Real Estate & Institutional Clients unit within the Commercial Risk Management division. This unit reports to the Chief Risk Officer (CRO). Monthly reports on participation risk (as part of the Group Risk Report), the participation risk strategy (as a part of the risk strategy), risk assessments on risk associated with equity capital actions and value determinations during impairment tests are submitted to the respective decision-making authority.

Risk measurement systems

For material operational participations, the Controlling and Accounting units conduct a standardized analysis of target versus actual company figures during the year, with monthly reports to the relevant stakeholders.

All participations are rated at least once a year. The confirmed rating is issued by Credit Risk Management.

An impairment test for participations must be carried out annually and reviewed by Credit Risk Management. The purpose of the impairment test is to determine the recoverability of the participations and to identify hidden reserves in the participation portfolio. Impairments are taken into account in accounting and are approved by the full Management Board at year-end.

Subsequent risk control is represented by the assessment and quantification of participation risk (not-consolidated participations according to IFRS) within the annual Risk Self-Assessment process, using a simplified PD/LGD model and defining a constant buffer for the risk within the ICAAP framework.

Risk reporting systems

Participation risks are reported in the context of risk controlling on a monthly basis to the Management Board. This report is part of the Group Risk Report and contains material changes within the participation portfolio most notably with regard to acquisitions, disposals, ratings and book values.

Risk hedging and mitigation

The treatment of risks arising from participations is governed in the Participation Risk Strategy (as part of the risk strategy) and other related documents.

In addition, the Reporting & Planning department monitors the financial results of all material operational participations on an ongoing basis and monitors the performance of all other participations in the overall portfolio annually.

ACCOUNTING AND VALUATION METHODS

Article 447 point (a) CRR

UGB
The valuation of participations and shares in affiliated companies is based on acquisition costs. In the case of persistent losses, an impairment was made. Impairments will be reversed up to the historical acquisition cost at the maximum in the event that the reason for the impairment no longer applies. Details regarding the accounting and valuation methods can be found in the notes of the AGAAP solo annual report.

IFRS
The valuation of non-consolidated participations is based on the fair value. Depending on the individual classification, changes in fair value are recognized in OCI or P&L.

Item 1 in the notes to the consolidated annual report contains details on accounting and valuation methods

SECURITIZATIONS

DISCLOSURE OF EXPOSURE TO SECURITIZATION POSITIONS

Article 449 points (a), (b) CRR

The Group acts solely as an investor in securitization transactions. All securitization positions of the Group are assigned to the banking book. The portfolio includes no resecuritization positions. Based on the characteristics of the individual positions, all securitization positions are classified as non-STS. As of 31 December 2021, the Group has no securitization transactions outstanding in which it acted as the originator/issuer.

The securitization portfolio consists of collateralized loan obligations (CLOs) with risks mainly from Western and Northern European and US companies. The portfolio consists entirely of senior tranches with adequate subordination. Moreover, all positions in the securitization portfolio are AAA-rated.

The Group has established an Investment and Monitoring Policy, which represents the foundation for the risk management process of the CLO portfolio. The policy specifies criteria that must be assessed prior to an investment in individual CLO positions. It consists of both “must meet” and “should meet” criteria. “Must meet” criteria have to be fulfilled for a CLO investment to be approved. Any breach of “should meet” criteria must be appropriately assessed and documented. In addition, the policy determines the risk monitoring process, which is carried out on a regular basis after an investment has been approved.

Risk reporting consists of quarterly risk reports prepared by Risk Modeling (RM) and submitted to the Credit Approval Committee (CAC) for approval.

Quarterly reports consist of an overview of the total CLO portfolio in which key risk parameters for individual positions are summarized. This includes the seniority, weighted average life (WAL), weighted average maturity (WAM), attachment and detachment points, subordination level, expected recovery value and so forth. Moreover, RM provides an overview of key parameters in comparison to the previous quarter, as well as the analysis of the underlying collateral. In addition, stress testing of individual CLO positions is performed as part of the quarterly reports.

Article 449 point (c)
Risk-weighted exposure amounts for non-STS securitization are calculated in accordance with Article 254 (1) CRR, where BAWAG Group has chosen to apply the preference of SEC-ERBA (Art. 263 CRR) over SEC-SA (Art. 261 CRR) in line with Article 254 (3) CRR for securitization with external ratings.

Positions with no external rating from Moody’s, Standard & Poor’s or Fitch are calculated according to the SEC-SA approach (Art. 261 CRR).

Article 449 point (d)

The Group does not act as an originator or sponsor in respect to the securitization transactions. In addition, the Group does not provide any securitization-related services, such as advisory, asset servicing or management services. There are no SSPEs included in the regulatory scope of consolidation.

Article 449 point (e)

The Group does not provide support to other legal entities. Therefore, this point is considered to be irrelevant.

Article 449 point (f)

The Group does not act as an originator or sponsor in respect to the securitization transactions. As such, this requirement is not considered relevant.

Article 449 point (g)
This requirement only concerns originators of securitizations.

Article 449 point (h)

Basically, the estimated ratings of Moody's, Standard & Poor's and Fitch, regardless of the category of securitized exposure, are utilized for investment deliberations.

Article 449 point (i)
The Group has no disclosure obligations in accordance with Article 449 point (i) CRR, because it does not apply the internal assessment approach.

LEVERAGE RATIO

Article 451 CRR

The leverage ratio according to Article 429 CRR is calculated according to Article 499 (1) point (a) CRR (in consideration of transitional regulations for Tier 1 capital) and according to Article 499 (1) point (b) CRR (fully phased in the definition of Tier 1 capital) for regulatory purposes and reported to the regulators on a quarterly basis. As of 30 June 2021, the calculation was adapted to the new requirements of CRR2, which caused only minor changes in the quote.

Regulation (EU) 2019/876 (Capital Requirements Regulation – CRR2) amending Regulation (EU) No 575/2013, with the application date 28 June 2021, sets the Tier 1 capital-based leverage ratio requirement at 3% for all EU banks as per the EBA's recommendation (Article 92 (d)).

Internally, the leverage ratio is calculated and reported monthly in the Capital Management Meeting (CMM) and ERM, in which the Management Board is represented. This reporting also includes the comparison of the current indicator value with the defined alert and recovery threshold levels. In order to manage the risk of excessive leverage, the recovery plan defines procedures and processes for reacting to leverage ratio changes which can be implemented if necessary.

Due to the business model and capital structure, the share of encumbered assets measured by balance sheet volume is rather low. Therefore, asset encumbrance is not taken into account in managing the risk of excessive leverage.

REMUNERATION POLICY DISCLOSURE

Article 450 (1) points (a) – (f) CRR

BAWAG Group AG and BAWAG P.S.K. AG has established a Nomination and Remuneration Committee, which is set up as a Supervisory Board committee. The Nomination and Remuneration Committee approves the Remuneration Policy of BAWAG Group and reviews the applied remuneration practices as well as the remuneration-related incentive structure. It is responsible for the determination of terms and conditions of contracts of Management Board members and the target determination and granting of bonuses for each Management Board member.

The Nomination and Remuneration Committee approves the aggregate bonus pool for BAWAG Group, reviews the annual bonus allocation on a statistical basis and submits regular reports on its activities to the full Supervisory Board. The Nomination and Remuneration Committee consists of the chairman of the Supervisory Board, who also chairs the Nomination and Remuneration Committee, and five other Supervisory Board members including two members of the works council. One member is an expert on remuneration and one is also a member of the Risk and Credit Committee. In 2021, two meetings of the Nomination and Remuneration Committee were held.

The Remuneration Policy applies to the members of the Management Board and the employees of the BAWAG Group and is compliant with the provisions and principles of Directive 2013/36/EU (CRD IV) as amended by Directive 2019/878/EU (CRD V), the EBA guidelines on sound remuneration policies, the FMA circular on principles of remuneration policies and practices updated in January 2018 and the Austrian Banking Act.

Regarding the structure of remuneration, all remuneration and other benefits granted by BAWAG Group are qualified as either fixed or variable remuneration as defined by the regulatory framework. Criteria for fixed and variable remuneration are clear, objective, predetermined and transparent.

For employees whose activities have a material influence on the risk profile (identified staff), the Remuneration Policy provides for effective risk management. The assessment in this regard was carried out in accordance with the qualitative and quantitative criteria set forth in the applicable regulatory framework.

In accordance with the above-mentioned legal framework, identified staff receive the bonus distributed over a period of five years and at least 50% in phantom shares (based on shares of BAWAG Group AG), provided a certain amount of the variable remuneration is reached. The high proportion of (phantom) shares in the variable compensation for identified staff leads to a high level of alignment between the interests of the management and the shareholders focused on growth of the corporate value as externally communicated to the shareholders.

Bonus awards granted to non-identified staff are deferred, provided the bonus award granted exceeds a certain amount.

Malus and clawback provisions are in place in accordance with the regulatory framework.

In reviewing and deciding on any awards of variable compensation to members of the Management Board and employees, the Nomination and Remuneration Committee takes into account the market situation and market trends, the appropriateness of bonus payments, the risk trends and the strengthening of the equity base.

The aggregate bonus pool shall, absent of extraordinary circumstances, not exceed 10% of the consolidated IFRS profit before tax (PBT) of BAWAG Group AG. In the case of extraordinary circumstances (including but not limited to outperformance of targets), this self-imposed limit may be exceeded. When determining the size of the bonus pool, the following factors are considered:

- Bonus payments are appropriate and disciplined considering BAWAG Group's earnings situation
- A correlation to the development of BAWAG Group's risk-bearing ability

- Risk and compliance functions provide effective input in accordance with their roles in the setting of the bonus pool where those functions have concerns regarding the impact of employees' behavior and the riskiness of the business undertaken
- The macroeconomic risks as well as the monetary outlook

The following process shall apply for the determination of the size of the bonus pool in any year:

- Proposal of Management Board prior to approval by the Nomination and Remuneration Committee, which confirms that the proposed total bonus pool is in line with the medium-term capital targets set by the Management Board
- Approval by the Nomination and Remuneration Committee

The Remuneration Policy took the mandatory basic conditions into account as follows:

- To ensure risk adequacy, the variable remuneration must not provide an incentive to enter into inappropriate risks
- To ensure sustainability, success is determined based on a longer-term assessment. Bonus awards paid to identified staff consist of 50% cash and 50% phantom shares, and 40% to 60% of the bonus is paid upfront, provided a certain bonus amount is reached. The portion of a bonus award which is not paid upfront is deferred and vests over a period of five years.
- The appropriateness and market adequacy of remuneration are ensured, and a balanced relationship between fixed and variable components is achieved. In general, the target for variable remuneration is set at 100% of the respective fixed remuneration. In the event that there has been a significant outperformance, the variable remuneration may exceed such amount but, in any event, may not exceed the levels set by the applicable regulatory requirements, which currently stand at 200%.
- The variable remuneration is determined on the basis of the individual's success as well as on the success of the respective organizational unit and BAWAG P.S.K.

Regarding identified staff, the individual quantitative and qualitative targets are to be agreed between the employee and the relevant manager. The targets and the achievement and non-achievement of targets are documented. A clear structure in target setting is key for ensuring transparent target assessment. Therefore, the targets shall be specifically tailored for each individual function and set out with consideration of the function holder's capacity and capability. Regardless of specific contents and areas of responsibility, each target comprises of:

- a clear and transparent description of its content
- targets consist of quantitative and qualitative measurement criteria
- a reasonable timeline within the Management by Objectives process

At the end of the Management by Objectives cycle targets are assessed in a structured multi-stage procedure:

- Evaluation (by the employee and manager) of target achievement according to agreed measurement criteria
- Assessment of the targets by the employee and manager
- Documentation of the assessment and derivable consequences

In addition, the results of internal and external audits, on-site reviews by regulators and the overall fulfillment of compliance requirements shall be used as a further indicator for the individual bonus allocation.

- For risk and control function holders who are classified as identified staff, the process of target setting and target assessment differs from that of other identified staff, as KPIs or performance targets for the Group shall not be used. The targets have to be derived from the risk strategy and governance of BAWAG Group and the business unit, defined by the Chief Risk Officer together with responsible division heads. The Management by Objectives process (line manager determines targets with the employee personally) serves as a quality check of the content of the targets. However, the compensation of staff in risk and control functions is decided regardless of the success of the business units they control.

Further information on remuneration-related topics is available in BAWAG Group's consolidated annual report as well as the remuneration report.

APPENDIX (QUALITATIVE DISCLOSURE): OVERVIEW RISK-REPORT

Topic	Details	Qualitative disclosure Pages	Consolidated annual report Pages	Other publications
General principles	Scope of consolidation and consolidation methods	9-11	71-72	
Risk management	Group-wide risk management	12-16	42-44, 191-202	
	Internal capital adequacy assessment process and Group-wide stresstest	17-21	200-202	
	Capital allocation and limitation at total bank level	22	11-12	
Credit risk	Objectives and principles	23-26	202-207	
	Counterparty default risk Treasury	27-29	77-82	
	Credit risk mitigation	30-32	203, 208-209, 217	
	Value adjustments and reserves	32-34	209-217	
	Rating systems and rating processes	35-45	203, 207	
Market risk	Objectives and principles	46-47	201, 226	
	Internal models for limitation of market risk	48	226-230	
	Interest rate risk from positions not held in the trading book	48-51	226-230	
Operational risk	Strategy, processes and management	53	233-234	
	Structure and organization	53	233	
	Risk measurement systems	54-57	201-202, 234	
	Risk hedging and mitigation	57	233-234	
	Own fund requirements	57		
Other risks	Liquidity risk	58-63	201, 230-233	
	Concentration risk	64-65	205-207, 222-224	
	Risk of money laundering and terrorism financing	66-67	201-202	
	Residual risk from techniques of credit risk mitigation	68	201-202	
	Macroeconomic risks	69	199-200	
Additionals	Participations not held in the trading book	70-71	84, 235	
	Securitizations	72-73	190	
	Leverage Ratio	74	3, 25-26, 33	
	Remuneration policy disclosure	75-77	51, 261, 266	
	Company information		2-7, 10-20	Pages Internet BAWAG Group
	BAWAG Group on the Stock Market		21-22	Pages Internet BAWAG Group.
	Funding		20-21, 33, 230-231	Pages Internet BAWAG Group
	Corporate Governance		48, 254-265	Pages Internet BAWAG Group.

OWNER AND PUBLISHER

BAWAG Group AG
Wiedner Gürtel 11
A-1100 Vienna, Austria
Companies Registry number: 269842b
EU VAT number: ATU72252867
Telephone: +43 (0)5 99 05 0
Internet: www.bawaggroup.com

Investor Relations:
investor.relations@bawaggroup.com

Media:
communications@bawaggroup.com

www.bawaggroup.com