Press release DEXIA

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Dexia Group consolidated results 2018[1]

Ongoing dynamic management of the Group's resolution

- *Reduction of the Group's geographic footprint: sale of Dexia Israel, closure of the Dexia Crédit Local branch in Lisbon, continuing restructuring of the Madrid branch and signature of an agreement on the sale of Dexia Kommunalbank Deutschland*
- *Balance sheet total down by 14% in 2018 to EUR 158.8 billion: commercial asset portfolio down by EUR 14 billion and the expected impact of the deconsolidation of Dexia Kommunalbank Deutschland in the 2nd quarter (EUR -24 billion)*
- *Implementation of the agreement to outsource back office activities with Cognizant and renewal of the technological infrastructure*

Net income of EUR -473 million as at 31 December 2018

- *Significant impact of regulatory taxes and contributions (EUR -105 million)*
- *Net recurring income of EUR -210 million, integrating a strongly positive cost of risk (EUR +128 million)*
- *Negative impact of accounting volatility elements (EUR -144 million); non-recurring elements (EUR -119 million) principally associated with the proactive strategy of balance sheet reduction*

Significant impact of the first-time application of the IFRS 9 accounting standard

- *Impact of EUR +2.1 billion on the Group's Common Equity Tier 1 Capital as at 1 January 2018 due to the cancellation of the AFS reserve*
- *Dexia's Total Capital Ratio at 27.3% at the end of December 2018*

Wouter Devriendt, CEO of Dexia, stated: "*In line with the efforts engaged in 2017 for the simplification of the Group and the reduction of commercial portfolios, in 2018, we have pursued our objective of reducing the Group's balance sheet, risks and geographical footprint. After selling our Israel subsidiary and closing our Lisbon branch, we signed an agreement last December to sell our German subsidiary. This sale is an important step in the Group's orderly resolution. It will facilitate the continuation of the resolution and reduce Dexia's balance sheet by an additional 15%, beyond the 14% reduction achieved in 2018 The teams are doing a remarkable job in managing this complex resolution and I thank them for their unwavering commitment.*"

Gilles Denoyel, Chairman of the Board of Directors of Dexia, said: "*Throughout 2018, we continued to implement our strategic roadmap, whilst working on convergence towards the general supervisory framework requested by the European Central Bank and compliance with prudential requirements, which have been further strengthened in 2019. The year's achievements are remarkable. In addition to the dynamic management of the Group's risks, balance sheet and liquidity, we are constantly working to develop our Group into a more centralised and agile structure.*"

[1] *The figures given in this press release are not audited.*

Introduction

Despite the rise of political uncertainties within the euro zone and the Brexit issue, as well as the end of the accommodating policy pursued by the European Central Bank, for Dexia 2018 was characterized by a strong acceleration in the simplification and reduction of the Group. The efforts undertaken were continued and intensified, in particular including the sale of its stake in its subsidiary in Israel, the closure of Dexia Crédit Local's branch in Portugal and the signature of an agreement on the sale of its German subsidiary, Dexia Kommunalbank Deutschland. The Group also continued the reduction of its portfolio of commercial assets.

The Group's 2018 results are marked by these contextual elements. Due to its significant impact, the entry into force of the IFRS 9 accounting standard was also one of the highlights of the past financial year.

The Board of Directors of Dexia SA met on 25 February 2019 and approved the income statement and balance sheet of Dexia SA for the 2018 financial year. The Dexia Group's annual report will be published on 15 April 2019 on the website *www.dexia.com*.

1. Significant events and transactions

- *Dynamic strategy to reduce the balance sheet and risks*
- *Signature of an agreement to sell Dexia Kommunalbank Deutschland*
- *Disposal of Dexia Israel and active continuation of the simplification of the international network*
- *Implementation of the agreement on the outsourcing of back office activities with Cognizant and renewal of technological infrastructure*

A. Progress on the Group's orderly resolution plan

Dynamic management of the balance sheet and risk reduction

In 2018, Dexia continued and intensified its proactive strategy of reducing the balance sheet. This materialised in an annual reduction of the Group balance sheet total by EUR 24.9 billion, or 14%. The reduction of commercial assets is significant, at EUR 14 billion over the year, of which EUR 7.3 billion related to disposals and EUR 1.1 billion to early redemptions. The natural amortisation of the balance sheet amounts to EUR 5.4 billion.

Asset sales in 2018 related in particular to US public sector securities and French public sector loans, Spanish covered bonds and ABS on US student loans or exposures to the Japanese sovereign and local public sector.

They are characterised by a long residual life of the transferred assets (9.4 years) and by the fact that a significant proportion of these assets was denominated in currencies other than the euro, in particular the US dollar and the yen. This has made it possible to reduce the Group's funding risk in these currencies.

Dexia has strengthened its expertise in the sale of loans. After a first successful transaction in 2017, the Group sold two new portfolios of receivables from the French local public sector following a call for tenders from investors. These sales related to a total outstanding amount of EUR 1.1 billion for a total of 186 loans. The Group also disposed of social housing loans in France, in two tranches, in an amount of EUR 0.8 billion.

As part of its credit risk reduction, efforts were concentrated on the management of heavily provisioned files. In particular, the Group sold almost all of its exposure in relation to the Commonwealth of Puerto Rico[2] and obtained the redemption of debts associated with the Bulgarian railway sector. The Dexia Group's credit

[2] *Dexia's residual exposure to the Commonwealth of Porto Rico wasà EUR 5 million as at 31 December 2018. Entirely covered by a good quality monoline, that outstanding reaches maturity in 2020.*

portfolio remains globally of good quality with 91% of exposures rated in the investment grade category as at 31 December 2018.

The Group also pays particular attention to the monitoring and management of certain exposures representing a significant concentration risk. Thus Dexia remains vigilant regarding the evolution of the US local public sector, in particular the Chicago Board of Education (CBOE), which is experiencing financial difficulties due to a very high level of indebtedness, an under-financing of its pension funds and the continuous decline in student enrolment. The Group's exposure to the CBOE was EUR 432 million as at 31 December 2018. Approximately 12% of the exposure benefits from a good quality credit enhancement. Dexia also attentively follows the evolution of the economic and political situation in Italy. The Group's exposure to Italy was EUR 22 billion as at 31 December 2018.

Signature of a sale and purchase agreement concerning Dexia Kommunalbank Deutschland

On 14 December 2018[3], Dexia signed with the German banking group Helaba a sale agreement allowing Helaba to buy 100% of the shares in Dexia Kommunalbank Deutschland (DKD) for a total consideration of EUR 352 million.

Dexia Crédit Local, acting through its Dublin branch, will sell its shares in DKD after having obtained all relevant regulatory approvals. The transaction is expected to close during the second quarter of 2019. It will have a non-significant impact on Dexia's solvency and will account for a reduction of approximately 15% of its balance sheet. Detailed financial impacts will be disclosed when the transaction closes.

Pursuant to this transaction, Dexia has also terminated, with effect as of the closing date of the sale, the Letters of Support it had issued to DKD.

In accordance with the IFRS 5 accounting standard, DKD has been classified as "Activities held for sale" in Dexia's financial statements as at 31 December 2018. DKD's assets and liabilities are presented on a separate line in the Group's consolidated balance sheet. DKD's post-tax income has also been classified on a separate line in the Group's consolidated income statement.

Disposal of the 58.9% holding in Dexia Israel Bank

On 18 March 2018, Dexia Crédit Local disposed of all of its shares in Dexia Israel Bank (Dexia Israel). The sale took place at a price of NIS 674 per share and for a total amount of approximately EUR 82 million. This disposal ends Dexia's presence in Israel, where the Group had been active since 2001.

With this sale, Dexia successfully completed the mandatory programme to dispose of its main commercial franchises, as part of the undertakings made by the Belgian, French and Luxembourg States within the framework of the orderly resolution plan approved by the European Commission in December 2012. It therefore marks the end of an important stage in the implementation of Dexia's orderly resolution plan.

Closure of Dexia Crédit Local's Portuguese and Spanish branches

In 2016, from the perspective of simplifying its operational structure, the Dexia Group proceeded with the cross-border merger by absorption of Dexia Crédit Local and its subsidiary Dexia Sabadell as well as the simultaneous creation of two new branches of Dexia Crédit Local in Spain and in Portugal. On 29 June 2018, the Group closed the Dexia Crédit Local branch in Lisbon, after finalising the transfer of assets to its Paris office.

[3] *Cf. Joint Dexia/Helaba Press Release dated 14 December 2018, available at www.dexia.com.*

The same centralisation work is under way for the Madrid branch, and should enable it to be closed at the latest during the first half-year 2019.

Reinforcing the operating model: implementation of the service outsourcing agreement with Cognizant

Implementation of the service outsourcing agreement, signed between Dexia and Cognizant on 4 October 2017, continued during the first half-year 2018 with the transfer, on 1 May 2018, of the back office market and credit teams to Cognizant. The IT teams were transferred in November 2017. In total, 133 Dexia staff members were transferred under this agreement.

Dexia also chose to entrust the renewal and management of its IT system infrastructure to Cognizant. This transaction was the object of a separate agreement, also for a term of ten years. Its implementation will extend until the second quarter of 2019 and will provide the Group with better-performing IT tools and strengthen operational continuity. On the other hand, it will facilitate the actions taken by Cognizant, which will be able to work in synergy between IT applications and infrastructures.

B. Evolution of Group governance

On 16 May 2018, Gilles Denoyel was appointed director and chairman of the Board of Directors of Dexia, replacing Robert de Metz, whose mandate ended. Gilles Denoyel is also director and chairman of the Board of Directors of Dexia Crédit Local.

On 6 September 2018, the Board of Directors of Dexia appointed Giovanni Albanese as executive director and Chief Risk Officer of Dexia, replacing Johan Bohets, who had expressed his wish to leave the Group.

On 28 November 2018, the Board of Directors of Dexia appointed Bertrand Dumont as a non-executive director of Dexia, replacing Thomas Courbe, who resigned.

On 4 February 2019, the Board of Directors of Dexia appointed Claire Cheremetinski as a non-executive director of Dexia, replacing Lucie Muniesa, who resigned.

As the governance of Dexia and Dexia Crédit Local is integrated, Giovanni Albanese is also a director, Executive Vice-President and Chief Risk Officer of Dexia Crédit Local. Bertrand Dumont and Claire Cheremetinski are also directors of Dexia Crédit Local.

C. Non-renewal of the specific approach to supervision and strengthening of prudential requirements regarding solvency applicable in 2019

On 16 July 2018[4], the European Central Bank (ECB) informed Dexia that the specific approach to the tailored, pragmatic and proportionate supervision applied to the Dexia Group since 2015 would not be renewed for 2019. This decision is a part of the trend of convergence of the requirements applied to Dexia towards the general supervision framework which began in 2018.

As from 1 January 2019, Dexia must therefore meet all the regulatory requirements applicable to banking institutions supervised by the ECB, at each level of the Group's consolidation. The observance of the constraint regarding large exposures will continue to be applied as described in the communication dated 5 February 2018, i.e. the deduction from its CET1 regulatory capital of the economic impact which might be generated by remediation on a failure to respect that ratio[5].

[4] *Cf. Dexia Press Release dated 26 July 2018, available at www.dexia.com.*
[5] *Cf. Dexia Press Release dated 5 February 2018, available at www.dexia.com.*

On 14 February 2019[6], the ECB informed the Dexia Group of the qualitative and quantitative prudential requirements with regard to solvency applicable to Dexia SA and its subsidiaries as from 1 March 2019, in accordance with Council Regulation (EU) 1024/2013 dated 15 October 2013. These requirements are based in particular on the conclusions of work carried out by the ECB within the framework of the Supervisory Review and Evaluation Process, (SREP).

The Total SREP Capital Requirement (TSCR) has been set at 11% on a consolidated basis. This level includes a minimum own funds requirement of 8% (Pillar 1) and an additional own funds requirement of 3% (P2R – Pillar 2 Requirement). By including the capital conservation buffer, of 2.5%, as well as the countercyclical buffer relating to exposures in France and the United Kingdom, estimated at 0.35%, this takes the own funds requirement to 13.85%.

In addition the ECB expects Dexia to comply with Pillar 2 capital guidance (P2G) of 1%, to be held over the level of 13.85% and to be made up entirely of Common Equity Tier 1 capital (CET 1).

As a consequence, the minimum level of the CET1 ratio goes to 11.35%, taking account of P2G.

2. Annual results 2018

A – *Presentation of Dexia's consolidated financial statements as at 31 December 2018*

a – Going concern

The consolidated financial statements of Dexia as at 31 December 2018 were established in accordance with the accounting rules applicable to a going concern. This relies on a certain number of assumptions made in the business plan underlying the resolution of the Dexia Group, developed in the Appendix to this Press Release.

b – Replacement of the IAS 39 "Financial instruments: accounting and valuation" accounting standard by the IFRS 9 "Financial instruments" accounting standard as at 1 January 2018

The IFRS 9 "Financial instruments" accounting standard became applicable on 1 January 2018, replacing IAS 39. The options retained by the Group and the impacts of the first-time application of the accounting standard for the Dexia Group are detailed in the Appendix to this Press Release.

c – Classification as "Activities held for sale"

In accordance with the IFRS 5 accounting standard, DKD has been classified as "Activities held for sale" in Dexia's financial statements as at 31 December 2018. DKD's assets and liabilities are presented on a separate line in the Group's consolidated balance sheet. DKD's post-tax income has also been classified on a separate line in the Group's consolidated income statement.

[6] *Cf. Dexia Press Release dated 18 February 2019, available at www.dexia.com.*

B - Dexia Group consolidated results for 2018

- *Net income Group share of EUR -473 million, including net recurring income (EUR -210 million), a negative contribution from accounting volatility elements (EUR -144 million) and non-recurring elements (EUR -119 million)*
- *Significant impact of regulatory taxes and contributions up, at EUR -105 million, and positive cost of risk, at EUR +128 million*

a – Income statement for the period (non-audited figures)

Consolidated income statement - ANC format		
EUR million	***2017 IAS39***	***2018 IFRS9***
Net banking income	***-123***	***-232***
Operating expenses and depreciation, amortisation and impairment of tangible fixed assets and intangible assets	*-392*	*-386*
Gross operating income	***-515***	***-618***
Cost of risk	*33*	*128*
Net gains or losses on other assets	*2*	*8*
Pre-tax income	***-480***	***-482***
Income tax	*-13*	*-40*
Result from discontinued operations, net of tax (1)	*32*	*23*
Net income	***-461***	***-499***
Minority interests	*1*	*-26*
Net income Group share	***-462***	***-473***

(1) As the activity of Dexia Kommunalbank Deutschland is considered a discontinued operation in the sense of the IFRS 5 accounting standard, its post-tax income is isolated on a separate line from the Group's consolidated income statement.

Over the year 2018, the Dexia Group booked net income Group share of EUR -473 million, quite stable compared to 2017.

Over the year, net banking income was negative at EUR -232 million (cf. detail p. 8). In addition to the carrying of assets, this amount in particular includes negative impacts associated with the valuation of derivatives, as well as disposal gains and provisions for legal risk.

Costs amounted to EUR -386 million and included an increase in taxes and regulatory contributions compared to the 2017 financial year.

In total, regulatory taxes and contributions amounted to EUR -105 million as at 31 December 2018 and include in particular the contribution of Dexia Crédit Local and Dexia Crediop to the Single Resolution Fund (EUR -72 million), the tax for systemic risk (EUR -4 million), an exceptional contribution from Dexia Crediop to the Italian national resolution fund (EUR -3 million) and the contribution from Dexia Kommunalbank Deutschland to the Single Resolution Fund (EUR -13 million), recorded under the heading "result from discontinued operations, net of tax" in accordance with the IFRS 5 accounting standard.

Gross operating income amounted to EUR -618 million.

The cost of risk or net gains and losses on other assets contributed positively to the result, amounting to EUR +137 million, of which EUR +128 million attributable to the cost of risk (cf. detail p.8).

Taking these elements into account, pre-tax income amounted to EUR -482 million.

Over the year, the tax impact amounted to EUR -40 million, including EUR -42 million of deferred taxes related to asset transfers within the Group.

The result from discontinued operations, net of tax, amounted to EUR +23 million and represents the contribution of Dexia Kommunalbank Deutschland's to the Group's result.

The income attributable to minority interests amounted to EUR -26 million, leading to net income attributable to the Group for the year 2018 of EUR -473 million.

b – Analytical presentation of the results for the period (non-audited figures)

The net income Group share of EUR -473 million is composed of the following elements:

- EUR -210 million attributable to recurring elements[7];
- EUR -144 million associated with accounting volatility elements[8];
- EUR -119 million generated by non-recurring elements[9].

In order to make these results easier to understand and to assess the momentum over the year, Dexia presents the evolution of the three analytical segments retained by the Group separately.

Analytical presentation of 2018 results of the Dexia Group

EUR million	Recurring elements	Accounting volatility elements	Non-recurring elements	Total
Net banking income	**45**	**-144**	**-134**	**-232**
Operating expenses and depreciation, amortisation and impairment of tangible fixed assets and intangible assets	-369	0	-17	-386
Gross operating income	**-323**	**-144**	**-151**	**-618**
Cost of risk	128	0	0	128
Net gains or losses on other assets	0	0	8	8
Pre-tax income	**-195**	**-144**	**-143**	**-482**
Income tax	-40	0	0	-40
Result from discontinued operations, net of tax	0	0	23	23
Net income	**-236**	**-144**	**-119**	**-499**
Minority interests	-26	0	0	-26
Net income Group Share	**-210**	**-144**	**-119**	**-473**

[7] *Recurring elements associated with the carry of assets such as portfolio income, funding costs, operating charges, cost of risk and taxes.*

[8] *Accounting volatility elements associated with asset and liability fair value adjustments in particular including the impacts of the IFRS 13 accounting standard (CVA, DVA, FVA), the valuation of OTC derivatives, the various impacts relating to financial instruments booked at fait value through profit and loss (in particular non-SPPI assets) and the valuation of derivatives hedging the WISE portfolio (synthetic securitisation of a portfolio of enhanced bonds).*

[9] *Non-recurring elements, in particular gains and losses on the disposal of holdings and instruments booked at amortised cost or at fair value through equity, costs and gains associated with litigation, cost and indemnities induced by the exit of projects or contracts, restructuring costs as well as costs associated with Group strategic restructuring projects or exceptional operational taxes.*

b.1 – Recurring elements

The net income Group share from recurring elements was EUR -210 million as at 31 December 2018, compared to EUR -302 million at the end of 2017.

Over the year, net banking income reached EUR +45 million and reflects the net interest margin, which corresponds to the cost of carrying assets as well as the Group's transformation result. The net interest margin decreased, mainly due to the reduction of the asset portfolio, the deconsolidation of Dexia Israel and the lengthening of funding maturities.

Costs reached EUR -369 million. This amount includes EUR -88 million in regulatory taxes and contributions, in particular including the contribution from Dexia Crédit Local and Dexia Crediop to the Single Resolution Fund (EUR -72 million) and the tax for systemic risk (EUR -4 million). Excluding these taxes and contributions, operating costs amounted to EUR -280 million, down on the previous year, in line with the simplification efforts undertaken by the Group.

The cost of risk amounted to EUR +128 million. This strongly positive amount is mainly due to reversals of provisions following the sale of exposures related to the Commonwealth of Puerto Rico and the repayment of a receivable in Bulgaria, as well as the revaluation of provisions on some exposures, in particular the Portuguese sovereign. It is partially offset by the provisioning of the Chicago Board of Education exposure in the fourth quarter of 2018.

The tax amount was EUR -40 million, of which EUR -42 million of deferred taxes related to asset transfers within the Group.

Recurring elements		
EUR million	***2017 (1)*** ***IAS39***	**2018** **IFRS 9**
Net banking income	**26**	***45***
o/w Net interest margin	143	*50*
o/w Other	-117	*-5*
Operating expenses and depreciation, amortisation and impairment of tangible fixed assets and intangible assets	**-371**	***-369***
o/w Expenses excl. operational taxes	-296	*-280*
o/w Operational taxes	-75	*-88*
Gross operating income	**-345**	***-323***
Cost of risk	32	*128*
Pre-tax income	**-312**	***-195***
Income tax	-13	*-40*
Net income	**-325**	***-236***
Minority interests	1	*-26*
Net income Group share	**-326**	***-210***

(1) Pro forma for 2017, the contribution of DKD to Dexia's result having been classified as non recurring element.

b.2 - Accounting volatility elements

Accounting volatility elements generated a negative impact of EUR -144 million on the 2018 result.

At the end of December 2018, a charge of EUR -73 million was booked for the Funding Value Adjustment (FVA), which represents the funding cost related to non-collateralised derivatives. The negative impact of the FVA is related to an adjustment in the calculation methodology used by Dexia as well as an increase in the funding cost for the banking sector in the 4th quarter. The Credit Value Adjustment (CVA), an adjustment to the value of derivatives related to counterparty risk, was also negative at EUR -34.8 million due to a widening of credit spreads, particularly on bank counterparties.

Variations in market parameters during the year also had a negative impact on hedging inefficiencies. In particular, the valuation of derivatives was marked by the unfavourable evolution of the BOR/OIS spreads in pound sterling.

b.3 – Non-recurring elements

Non-recurring elements booked over the year amounted to EUR -119 million and in particular included:

- losses associated with asset disposals and, to a lesser extent, repurchases of liabilities in an amount of EUR -108 million;
- allocations and reversals of provisions for litigation, the net impact of which was EUR -26 million;
- provisions for restructuring costs at EUR -9 million;
- an exceptional contribution from Dexia Crediop to the Italian national resolution fund (EUR -3 million);
- the net impact of the sale of Dexia Crédit Local's shares in Dexia Israel (EUR +8 million);
- the contribution to the post-tax result of Dexia Kommunalbank Deutschland, in an amount of EUR +23 million[10].

3. Evolution of the balance sheet, solvency and the liquidity situation of the Dexia Group

A – Balance sheet and solvency

- *Reduction of the balance sheet by EUR 24.9 billion compared to the end of 2017, linked to the asset portfolio reduction strategy, the fall of interest rates and the sale of Dexia Israel*
- *Significant impact of the first-time application of the IFRS 9 accounting standard on the Group's regulatory capital*
- *Dexia's Total Capital ratio at 27.3% at the end of December 2018, against 20.4% as at 31 December 2017*
- *Estimated impact of the sale of Dexia Kommunalbank Deutschland: reduction of the Group's total balance sheet of 15%; not significant on solvency*

[10] *In accordance with the IFRS 5 accounting standard, the contribution from Dexia Kommunalbank Deutschland is isolated in the item "Result from discontinued operations, net of tax," and fully classified in the analytical segment "non-recurring elements".*

a – Annual evolution of the balance sheet

As at 31 December 2018, the Group's consolidated balance sheet total amounted to EUR 158.8 billion, down EUR -24.9 billion compared to 31 December 2017, adjusted for the first-time application of the IFRS 9 accounting standard, under the combined effect of a dynamic balance sheet management policy and the macroeconomic environment. At EUR 80 billion, the commercial asset portfolio fell by about EUR -14 billion compared to the end of December 2017, of which almost 60% due to asset disposals and early redemptions.

To recall, the first-time application of the IFRS 9 accounting standard was reflected by an increase of the balance sheet total of EUR +2.7 billion as at 1 January 2018, mainly due to the cancellation of the frozen AFS reserve (see Appendix 2 "First-time application of the IFRS 9 accounting standard").

Over the year, at a constant exchange rate, the reduction of balance sheet assets is principally attributable to:

- the EUR -14 billion reduction of the commercial portfolio, of which EUR -8.3 billion attributable to asset disposals or early redemptions and EUR -5.4 billion to natural portfolio amortisation;
- the fall in fair value of assets and derivatives of EUR -5.5 billion;
- a EUR -2.7 billion reduction of the amount of cash collateral paid by the Group to its derivatives counterparties;
- the sale of Dexia Israel (EUR -2 billion);

On the liabilities side, at a constant exchange rate, balance sheet evolution is principally attributable to:

- a EUR -17.7 billion reduction of the market funding stock;
- a EUR -5.3 billion fall in the fair value of liabilities and derivatives;
- a EUR -2 billion reduction linked to the sale of Dexia Israel.

The impact of exchange fluctuations on the annual evolution of the balance sheet is slightly positive, at EUR +0.9 billion.

In December 2018, Dexia signed an agreement on the sale of its subsidiary Dexia Kommunalbank Deutschland (DKD). The transaction is expected to be completed in the second quarter of 2019. DKD's contribution to the Group's consolidated balance sheet total amounted to EUR 24.4 billion as at 31 December 2018, including EUR 14 billion of commercial portfolios.

b – Solvency

As at 31 December 2018, the Dexia Group's Common Equity Tier 1 capital was EUR 8.1 billion, compared to EUR 6.5 billion as at 31 December 2017, The first-time application of the IFRS 9 accounting standard on 1 January 2018 led to an increase of EUR +2.1 billion in the Group’s prudential capital, mainly due to the cancellation of unrealised gains and losses recognised as equity under IAS 39 (see Appendix 2 "First-time application of the IFRS 9 accounting standard").

The group's Common Equity Tier 1 capital as at 31 December 2018 was burdened by the negative net income for the year (EUR -473 million) and also benefited from a positive evolution of the item "gains and losses directly recognized in equity" (EUR +207 million), mainly as a result of the improvement in credit spreads on American and Spanish sovereigns.

In line with European Central Bank requirements, two items are deducted from regulatory capital for a total of EUR -107 million:

- the theoretical loss amount corresponding to the remediation of the non-compliance with the large exposure constraint, which amounts to EUR -60 million[11];
- the amount of irrevocable payment commitments (IPC) to the resolution funds and other guarantee funds, for an amount of EUR -47 million.

As at 31 December 2018, risk-weighted assets decreased compared to the end of December 2017, to EUR 30.4 billion as at 31 December 2018, of which EUR 28.7 billion for credit risk, EUR 0.7 billion for market risk and EUR 1 billion for operational risk.

Considering these elements, Dexia's Common Equity Tier 1 ratio was 26.7% as at 31 December 2018, against 19.5% at the end of 2017. The Total Capital ratio was 27.3%, against 20.4% at the end of 2017, a level higher than the minimum imposed for the year 2018 by the European Central Bank within the framework of the Supervisory Review and Evaluation Process (SREP).

The Common Equity Tier 1 and Total Capital ratios of Dexia Crédit Local also meet the minimum requirements, at 23.2% and 23.6% respectively as at 31 December 2018.

On-sight inspections (OSI) by the supervisors are currently ongoing, in particular an inspection with regard to credit risk. Dexia will integrate the conclusions of such inspections, which might have an impact on the solvency ratios of Dexia Crédit Local and of the Dexia Group, when they are communicated.

B – Evolution of the Dexia Group's liquidity situation

- *Ongoing and significant reduction of the funding volume in 2018*
- *Ongoing strategy of optimising the funding mix, characterised by a lengthening of funding maturities*
- *Absence of recourse to Eurosystem funding since September 2017*
- *Comfortable liquidity reserve, for the most part pledged with central banks*

As a result of the reduction of the asset portfolio and the decrease of cash collateral (total net amount of EUR 22.7 billion as at 31 December 2018), funding outstanding decreased by EUR -18.5 billion, compared to the end of December 2017, to EUR 106 billion at the end of December 2018. The adjustment of the funding mix was achieved through the reduction of secured funding (EUR -14.1 billion compared to the end of 2017) due to the sale of the underlying assets and the termination of Crediop's domestic repo platform. There was also a reduction of unsecured funding (EUR -4.3 billion compared to the end of December 2017), half of which was due to the decrease of State-guaranteed funding, bringing the outstanding amount to EUR 65.5 billion at the end of December 2018, or 62% of the total outstanding amount of funding at that date.

Over the year, Dexia Crédit Local successfully launched various long-term public benchmark transactions in euros, US dollars and pounds sterling, raising EUR 7.3 billion at a particularly competitive funding cost. Short-term funding activity in guaranteed format was also strong, with an average maturity at issuance of 8.5 months.

The Group has made not use of central bank funding since September 2017.

[11] *Cf. Dexia press releases dated 5 February and 26 July 2017, available at www.dexia.com.*

As at 31 December 2018, the Dexia Group had a liquidity reserve of EUR 16.3 billion, of which EUR 9.1 billion in the form of cash deposits with central banks.

As at the same date, the Group's Liquidity Coverage Ratio (LCR) stood at 202%, compared with 111% as at 31 December 2017. This was also respected at the subsidiary level, each exceeding the required minimum of 100%. The Group's Net Stable Funding Ratio (NSFR), estimated on the basis of the latest proposals to amend the CRR, would be above the target threshold of 100%, as a result of the Group's efforts since 2013 to improve its funding profile.

Appendices

Appendix 1 – Going concern

The consolidated financial statements of Dexia as at 31 December 2018 were prepared in accordance with the accounting rules applicable to a going concern. This requires a number of constituent assumptions underlying the business plan for the resolution of the Dexia Group, decided upon by the European Commission in December 2012. They are listed below:

- The macroeconomic hypotheses underlying the business plan are revised as part of the half-yearly reviews of the overall plan. The update made on the basis of market data observable as at 30 June 2018 and validated by the Board of Directors of Dexia on 19 December 2018 integrates the regulatory developments known to date, including the final version of the CRD IV Directive. It also takes account of the extremely positive impact on the Dexia Group's regulatory capital of the first-time application of the IFRS 9 accounting standard as from 1 January 2018, with Dexia's Total Capital Ratio at 27.3% at the end of December 2018. Finally it takes account of the non-renewal, as from 1 January 2019, of the specific approach implemented by the European Central Bank for the supervision of the Dexia Group[12].
- The ongoing resolution assumes that Dexia retains a sound funding capacity, relying in particular on the appetite of investors for debt guaranteed by the Belgian, French and Luxembourg States as well as on the Group's capacity to raise secured funding. Since the end of 2012, Dexia has considerably reduced its funding requirement, diversified its access to different funding sources and taken advantage of favourable market conditions to extend the maturity of its liabilities, with a view to the prudent management of its liquidity. In particular, this enables the Group to maintain a level of liquidity reserves which is deemed appropriate considering the restriction of access to European Central Bank funding announced on 21 July 2017[13]. The latest update of the business plan takes account of a revision of the funding plan relying on the last observable market conditions.
- The business plan assumes the maintenance of the banking licences of the various entities and the rating of Dexia Crédit Local.

Regular revisions of the business plan lead to adjustments to the original plan and over time involve a significant change of the Group's resolution trajectory as initially anticipated, particularly in terms of profitability, solvency and funding structure. At this stage, they do not raise any question as to the nature or the fundamentals of the resolution, which justifies the decision to establish the financial statements in accordance with "going concern" principles.

However, over the duration of the Group's resolution, uncertainties remain regarding the implementation of the business plan:

- In particular, this plan is likely to be impacted by new developments in accounting and prudential rules.
- The Dexia Group is also sensitive to the evolution of the macroeconomic environment and to market parameters, particularly exchange rates, interest rates and credit spreads. An unfavourable evolution of these parameters over time could weigh on the Group's liquidity and its solvency position, for instance by increasing the amount of cash collateral paid by Dexia to its derivatives counterparties or an impact on the valuation of financial assets and liabilities and OTC derivatives, fluctuations of which are booked in the income statement and are liable to result in a fluctuation of the level of the Group's regulatory capital.

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[12] Cf. Press Release issued by Dexia on 26 July 2018, available at www.dexia.com

[13] On 21 July 2017 the European Central Bank announced the end of access to the Eurosystem for wind-down entities as from 31 December 2021.

- Discussions are ongoing between the European Commission and the Belgian and French States on the conditions of the renewal of the State guarantee as from 1 January 2022.
- If market demand for government-guaranteed debt were to decline, Dexia might need to turn to more costly funding sources which would directly impact the profitability assumed in the original business plan;
- Finally, the Group is exposed to certain operational risks, specific to the resolution environment in which it operates.

Appendix 2 – First-time application of the IFRS 9 accounting standard as at 1 January 2018

The IFRS 9 “Financial Instruments” accounting standard came into force on 1 January 2018, replacing the standard IAS 39. It has three aspects:

- The first relates to the classification and valuation of financial instruments;
- The second relates to the financial asset provisioning model;
- The third relates to hedge accounting.

Classification and valuation of financial assets

The IFRS 9 accounting standard provides for classification and valuation of assets depending on the management model retained by the bank and the characteristics of the assets concerned.

Management model

The choice of management model under IFRS 9 has an impact on the possibilities for classification of financial assets authorised by the standard and, as a consequence, on their mode of valuation. Three management models are retained by the IFRS 9 accounting standard:

- “Hold to collect” model, with financial assets held with a view to collecting contractual cash flows;
- “Hold to collect and sell” model, with financial assets held with a view to collecting contractual cash flows, as well as disposal;
- “Other” model, in the case where the management intention does not correspond to either of the two previous models (in particular trading operations).

Asset characteristics

The characteristics of the financial assets are also decisive in identification of their accounting classification. Depending on the complexity of their structure and the cash flows they generate, financial assets are considered to be either SPPI (*Solely Payments of Principal and Interest*), for simpler and less structured assets, or non-SPPI for structured and/or complex assets.

On the basis of these two elements, different accounting classifications are offered by the IFRS 9 accounting standard:

- Financial assets at amortised cost: this classification includes “hold to collect” assets considered to be SPPI. Such assets are valued at amortised cost;
- Financial assets at fair value through equity: this classification includes “hold to collect and sell”

assets considered to be SPPI. Such assets are valued at fair value and value adjustments are booked through equity (*Other Comprehensive Income* – OCI);

- Financial assets at fair value through profit and loss: this classification includes assets for which the management intention does not correspond to “hold to collect” or “hold to collect and sell”, as well as assets considered to be non-SPPI. Such assets are valued at fair value and value adjustments are booked through profit and loss.

<u>Asset classification</u>

In line with its status as an entity managed in run-off, Dexia has for the most part opted for a “hold to collect” management model. As a result, assets booked as “available for sale” (AFS) under IAS 39, have been classified in the “amortised cost” category under IFRS 9.

Furthermore, Dexia identified a portfolio of assets which may be the object of a disposal in coming years. These assets have been classified in the category “fair value through equity” under IFRS 9, as have the liquid assets held by Dexia Financial Products Services LLC.

Finally, in accordance with the standard, certain non-SPPI assets have been classified in the “fair value through profit and loss” category under IFRS 9.

<u>Consequence for Dexia</u>

Classification of the majority of Dexia’s assets in the “amortised cost” category under IFRS 9 involves a significant positive impact associated with the cancellation of latent gains and losses observed in equity under IAS 39.

This classification also results in a reduction and a change of the sensitivity of the Group’s equity to credit spread fluctuations, as the valuation of assets classified at “amortised cost” is no longer affected by credit spread fluctuations. In particular, the reduction of sensitivity is notable on Italian and Portuguese sovereigns. A residual sensitivity to credit spreads continues to exist, for assets classified in the “fair value through equity” and in the “fair value through profit and loss” category under IFRS 9. It now relates principally to American ABS as well as assets in the French and US public sectors.

Financial asset provisioning model

The IFRS 9 accounting standard defines a new credit risk provisioning model for assets booked at “amortised cost” and “fair value through equity”. Off-balance-sheet commitments are also subject to this new model.

Under IAS 39, credit risk provisioning took place when an operative event was observed. Under IFRS 9, provisioning is now made from the origination of the asset on the basis of expected credit losses.

The provisioning model defined by IFRS 9 relies on the distinction of three separate asset classes:

- The first (stage 1) corresponds to assets for which the credit risk has not deteriorated since origination. The level of provisioning of such assets corresponds to the expected loss over 12 months.
- The second (stage 2) corresponds to assets for which the credit risk has significantly deteriorated since origination, but without a default having been observed. The level of provisioning of such assets corresponds to the expected losses over the residual term.

- The third (stage 3) corresponds to assets on which there has been a default. The level of provisioning corresponds to the expected losses over the residual term. Assets acquired when they had already deteriorated are classified in this category. In this latter case, the modes of calculation of the provisioning level are specific.

Implementation of the new provisioning model by the Dexia Group

Implementation of the new credit risk provisioning model only has a limited impact at a Dexia Group level, reflected by an increase of provisions in the order of EUR 200 million.

Hedge accounting

Dexia has retained the opportunity to keep the provisions offered by IAS 39 regarding hedge accounting.

Impacts of the first-time application of the IFRS 9 accounting standard by the Dexia Group

Consolidated balance sheet

The first-time application of the IFRS 9 accounting standard is reflected by an increase of the balance sheet total by EUR +2.7 billion as at 1 January 2018, principally due to the cancellation of the frozen AFS reserve.

Furthermore, in accordance with Recommendation No 2017-02 dated 2 June 2017 of the French Autorité des Normes Comptables (ANC), certain changes have been made to the presentation of the financial statements, principally the creation and deletion of headings associated with the implementation of IFRS 9 as well as the presentation of cash collateral under the headings “Interbank/Customer loans and receivables” and “Interbank/Customer borrowings and deposits” under IFRS 9 (cf. table in Appendix 3 to the press release).

Accounting and regulatory equity – solvency ratios

The application of IFRS 9 generates a total positive net impact in the order of EUR 2.7 billion on accounting equity Group share as at 1 January 2018, associated with the asset classification and the implementation of the new provisioning model, partially offset by the adjustment to prudential treatment (EUR -0.6 billion).

As a consequence, Common Equity Tier 1 Capital and Total Capital rise by EUR 2.1 billion and EUR 2.0 billion respectively.

Risk-weighted assets increase by EUR 1.4 billion, following the increase of EAD outstanding due to the cancellation of the frozen AFS reserve.

As a consequence, Dexia’s Common Equity Tier 1 Capital and Total Capital amount to 24.9% and 25.5% respectively as at 1 January 2018 against 19.5% and 20.4% as at 31 December 2017, or an increase of 5.4% and 5.1%.

Dexia decided to opt for transitional provisions[14] enabling it to spread over five years the impact on prudential capital resulting from the implementation of the new IFRS 9 impairment model. This will enable the Group to smooth the effects on the level of impairment of the migration of an asset from one category to

[14]. In December 2017, the European Parliament amended the CRR and proposed that credit institutions use transitional provisions (phase in), which will enable them to spread over five years the impact on equity resulting from the implementation of the new IFRS 9 impairment model on solvency ratios. These provisions apply to the amount of additional provisions for credit risk as at 1 January 2018 (“static” phase in). They also apply to any additional amount of provisions associated with financial assets classified in phase 1 and phase 2 in accordance with the IFRS 9 approach, constituted during the five-year transition period (“dynamic” phase in).

another and attenuate any volatility generated by the new impairment model on prudential solvency ratios. In particular, Dexia is sensitive to any change of stage of Italian government debt.

Accounting equity as of 1 January 2018 (in EUR million)	
Accounting equity, Group share – IAS 39	**5,402**
Impact of the new credit risk provisioning model	-180
Impact of the change of accounting classes	419
Cancellation of the premium/discount associated with the reclassification of securities made historically in application of the amended IAS 39	2,485
Other	-5
Accounting equity, Group share – IFRS 9	**8,121**

Regulatory capital as at 1 January 2018 (in EUR million)	**IAS 39**	**IFRS 9**
Accounting equity, Group share	**5,402**	**8,121**
Prudential treatment	1,093	515
Common Equity Tier 1 Capital	**6,496**	**8,635**
Total Capital	**6,811**	**8,846**

Solvency ratios as at 1 January 2018 (in EUR million unless otherwise stated)	**IAS 39**	**IFRS 9**
Credit risk-weighted assets	31,371	32,750
Market risk-weighted assets	980	980
Operational risk-weighted assets	1,000	1,000
Risk-weighted assets	**33,351**	**34,730**
Common Equity Tier 1 Capital	6,496	8,635
Common Equity Tier 1 Ratio	**19.5%**	**24.9%**
Total Capital	6,811	8,846
Total Capital Ratio	**20.4%**	**25.5%**

Appendix 3 – Simplified balance sheet[15] (non-audited figures)

Balance sheet key figures			
(in EUR million)	**31/12/2017 IAS 39**	**01/01/2018 IFRS 9**	**31/12/2018 IFRS 9**
Total assets	**180,938**	**183,676**	**158,804**
of which			
Cash and central banks	10,721	10,721	9,269
Financial assets at fair value through profit or loss	13,188	17,013	13,421
Hedging derivatives	4,985	4,977	1,263
Financial assets available for sale	10,830		
Financial assets at fair value through other comprehensive income		11,757	4,916
Financial assets at amortised cost - Debt securities		50,272	45,502
Interbank loans and advances	6,144		
Financial assets at amortised cost - Interbank loans and advances (1)		30,690	23,665
Customer loans and advances	99,264		
Financial assets at amortised cost - Customer loans and advances (1)		54,320	35,158
Accruals and other assets	30,550	562	389
Non current assets held for sale (2)	2,105	2,102	24,375
Total liabilities	**175,536**	**175,555**	**150,963**
of which			
Central banks	0	0	0
Financial liabilities at fair value through profit or loss	14,193	14,912	11,872
Hedging derivatives	27,858	27,139	21,151
Interbank borrowings and deposits	31,016	30,807	20,091
Customer borrowings and deposits	6 404	10,137	4,873
Debt securities	89,654	89,654	67,960
Liabilities included in disposal groups held for sale (2)	1,894	1,894	24,055
Total equity	**5,402**	**8,121**	**7,841**
of which			
Equity, Group share	4,992	7,689	7,504

(1) As at 31 December 2017, the cash collateral was booked under "Accruals and other assets" (EUR 29,989 million). As at 31 December 2018, it is split between "Financial assets at amortised cost - Interbank loans and advances" (EUR 20,311 million) and "Financial assets at amortised cost - Customer loans and advances" (EUR 4,850 million).

(2) This item includes Dexia Israel as at 31 December 2017 and Dexia Kommunalbank Deutschland as at 31 December 2018.

[15] *In accordance with the IFRS 5 standard, Dexia Israel has been classified under "Activities held for sale" in the Dexia financial statements as at 31 December 2017. The assets and liabilities of Dexia Israel have been reclassified in a separate line in the Groups' consolidated balance sheet.*

Appendix 4 – Capital adequacy (non-audited figures)

(in EUR million)	31/12/2017 IAS 39	01/01/2018 IFRS 9	31/12/2018 IFRS 9
Common Equity Tier 1	6,496	8,635	8,119
Total Capital	6,811	8,846	8,278
Risk-weighted assets	33,351	34,730	30,365
Common Equity Tier 1 ratio	19.5%	24.9%	26.7%
Total Capital ratio	20.4%	25.5%	27.3%

Appendix 5 – Exposure to credit risk (non-audited figures)

Exposure by geographic region

(in EUR million)	31/12/2017	31/12/2018 Total	o/w continuing operations	o/w discontinuing operations (DKD)
France	28,201	22,271	22,216	54
Italy	23,002	21,883	21,046	837
United Kingdom	22,178	21,114	21,061	53
Germany	17,835	16,714	1,909	14,805
United States	17,483	15,017	14,865	152
Spain	10,136	7,421	7,393	28
Japan	6,152	5,469	5,469	0
Portugal	3,924	4,422	4,187	235
Belgium	1,648	1,936	531	1,406
Canada	2,071	1,882	1,882	0
Austria	1,058	1,023	10	1,014
Central and Eastern Europe (1)	954	889	889	0
Switzerland	357	353	353	0
South and Central America	430	345	345	0
Scandinavian countries	528	218	198	20
Southeast Asia	451	202	202	0
Netherlands	130	106	80	26
Greece	88	78	78	0
Luxembourg	38	49	49	0
Ireland	10	7	7	0
Hungary	2	2	2	0
Turkey	169	0	0	0
Other (2)	5,039	2,241	1,974	267
Total	**141,881**	**123,643**	**104,747**	**18,896**

(1) *Excluding Austria and Hungary.*

(2) *Including supranationals, Australia and Israel (deconsolidated in 2018).*

Exposure by category of counterparty

(in EUR million)	31/12/2017	31/12/2018 Total	o/w continuing operations	o/w discontinuing operations (DKD)
Local public sector	75,621	65,804	49,153	16,651
Central governments	29,701	27,081	25,416	1,666
Financial institutions	13,174	10,406	9,849	557
Project finance	11,652	10,299	10,286	14
Corporate	5,807	5,733	5,732	0
ABS/MBS	4,424	2,831	2,822	9
Monolines	1,500	1,488	1,488	0
Individuals, SME and self-employed	1	1	1	0
Total	**141,881**	**123,643**	**104,747**	**18,896**

Exposure by rating (internal rating system)	31/12/2017	31/12/2018 Total	o/w continuing operations	o/w discontinuing operations (DKD)
AAA	20.96%	19.11%	18.40%	23.04%
AA	14.93%	16.96%	8.05%	66.33%
A	25.23%	25.24%	29.19%	3.33%
BBB	29.26%	29.44%	33.56%	6.62%
Non Investment Grade	8.43%	7.85%	9.15%	0.66%
D	0.78%	1.13%	1.33%	0.00%
Not Rated	0.42%	0.27%	0.32%	0.02%
Total	**100%**	**100%**	**100%**	**100%**

Appendix 6 – Sector exposure of the Group as at 30 June 2018 (EAD on end counterparties – non-audited figures)

Group sector exposure to certain countries

(in EUR million)	*Total*	*o/w local public sector*	*o/w corporate and project finance*	*o/w financial institutions*	*o/w ABS/MBS*	*o/w sovereign exposures*	*o/w monolines*	*o/w discontinued operations (DKD)*
France	**22,271**	9,522	2,581	1,710	0	8,458	0	54
Italy	**21,883**	8,993	341	282	7	12,260	0	837
United Kingdom	**21,114**	9,918	8,006	1,131	1,312	61	686	53
Germany	**16,714**	13,983	126	2,211	0	395	0	14,805
United States	**15,017**	9,020	879	1,793	1,114	1,409	802	152
Spain	**7,421**	4,145	1,390	1,124	316	447	0	28
Japan	**5,469**	4,726	0	722	0	21	0	0
Portugal	**4,422**	1,532	70	9	15	2,796	0	235
Poland	**556**	1	0	0	0	554	0	0
Greece	**78**	1	77	0	0	0	0	0
o/w discontinued operations (DKD)	16,164	14,321	14	514	0	1,315	0	

Appendix 7 – Asset quality (non-audited figures)

Asset quality

(in EUR million)			31/12/2017 IAS 39	31/12/2018 IFRS 9
Impaired assets[(1)]			877	1,273
Specific impairments[(2)]			257	305
	Of which	*Stage 3*		299
		POCI		6
Coverage ratio[(3)]			29.30%	23.96%
Collective provisions			331	345
	Of which	*Stage 1*		*5*
		Stage 2		*340*

(1) *Outstanding computed according to the applicable perimeter defined under IFRS 9 (FV through OCI + Amortised Cost + Off Balance).*

(2) *Impairments: according to the portfolio taken into account for the calculation of the outstanding, inclusive the impairments related to POCI.*

(3) *Specific impairments-to-Impaired assets ratio*

Appendix 8 – Ratings

Ratings as at 15 February 2019			
	Long term	**Outlook**	**Short term**
Dexia Crédit Local			
Fitch	BBB+	Stable	F2
Moody's	Baa3	Stable	P-3
Moody's - Counterparty Risk (CR) Assessment	*Baa3(cr)*		*P-3(cr)*
Standard & Poor's	BBB	Stable	A-2
GBB Rating[1]	BBB	Positive	-
Dexia Crédit Local (guaranteed debt)			
Fitch	AA-	-	F1+
Moody's	Aa3	Stable	P-1
Standard & Poor's	AA	-	A-1+
Dexia Kommunalbank Deutschland (*Pfandbriefe*)			
Standard & Poor's	A-	CW Positive	-

Appendix 9 – Litigation

The most significant developments in 2018 in relation to pending litigation in which a Dexia Group entity was named as defendant are summarised below.

The following updated data are provided for comparison and should be read in conjunction with the corresponding summaries contained or mentioned in the Dexia Annual Report 2017 (available at *www.dexia.com*).

Mixed decisions of Dutch Courts in litigation relating to Dexia Nederland

Dutch Courts passed various judgements on share leasing cases involving Dexia Nederland (DNL).

The Supreme Court (*Hoge Raad*) confirmed certain legal principles in cases where share leasing agreements had been sold through intermediaries. The final outcome of the relevant cases remains dependent on the ability of plaintiffs to prove before the Courts, inter alia, that certain duty of care obligations had not been fulfilled. Other cases relating to the role of intermediaries and certain duty of care obligations which would allegedly not have been fulfilled by DNL are still pending.

At Court of Appeal level, during 2018, a number of rulings were made in which DNL's position in relation to various topics has been confirmed, such as on the calculation of legal interest, on advice which would allegedly have been given by DNL, on activities which would allegedly have qualified as cold calling, on the imputation of tax benefits on the damages suffered by clients and on the activities of the clients' representatives which could qualify for compensation as extra-judicial costs.

Generally, the Courts of Appeal also confirmed that, provided certain conditions are fulfilled, DNL is entitled to start legal proceedings so as to obtain court declarations that it has no outstanding obligations vis-à-vis its clients.

Press contacts
Press Service – Brussels
+32 2 213 57 39
Press Service – Paris
+33 1 58 58 58 49

Investor contact
Investor Relations - Paris
+33 1 58 58 82 48
Investor Relations - Brussels
+32 2 213 57 66