Understanding the 2016 EBA Stress Test Results

August 2016

Executive summary

Key takeaways

The **difference in capital impact between the base and adverse scenarios is significantly greater** in 2016 than in 2014. The average impact on the **CET1 capital ratio** across all banks was a **reduction of 380 bps**.

European banks appear to be in a **more stable position** than they were in 2014. Overall, the Banks have increased their aggregate stock of capital, both in terms of quality and amount, which we regard as a clear indicator of a **more stable and resilient banking system**.

Certain business models where the **focus is on credit and interest income, the overall capital depletion is higher**, and those **business models where higher fees and commission play a larger role, the CET1-Ratio depletion is relatively lower**.

All **Italian banks fared better** in the 2016 Stress Test results than in the 2014 Stress Test results, **except Monte dei Paschi di Sienna**, which falls to a CET1 ratio of **-2.44%** in the adverse scenario.

UK bank results were in line with the European average, RBS and Barclays saw the largest CET 1 ratio impact from this group.

Only 4 banks fared worse in the adverse scenario of the 2016 Stress Tests than in the adverse scenario of the 2014 Stress Tests.

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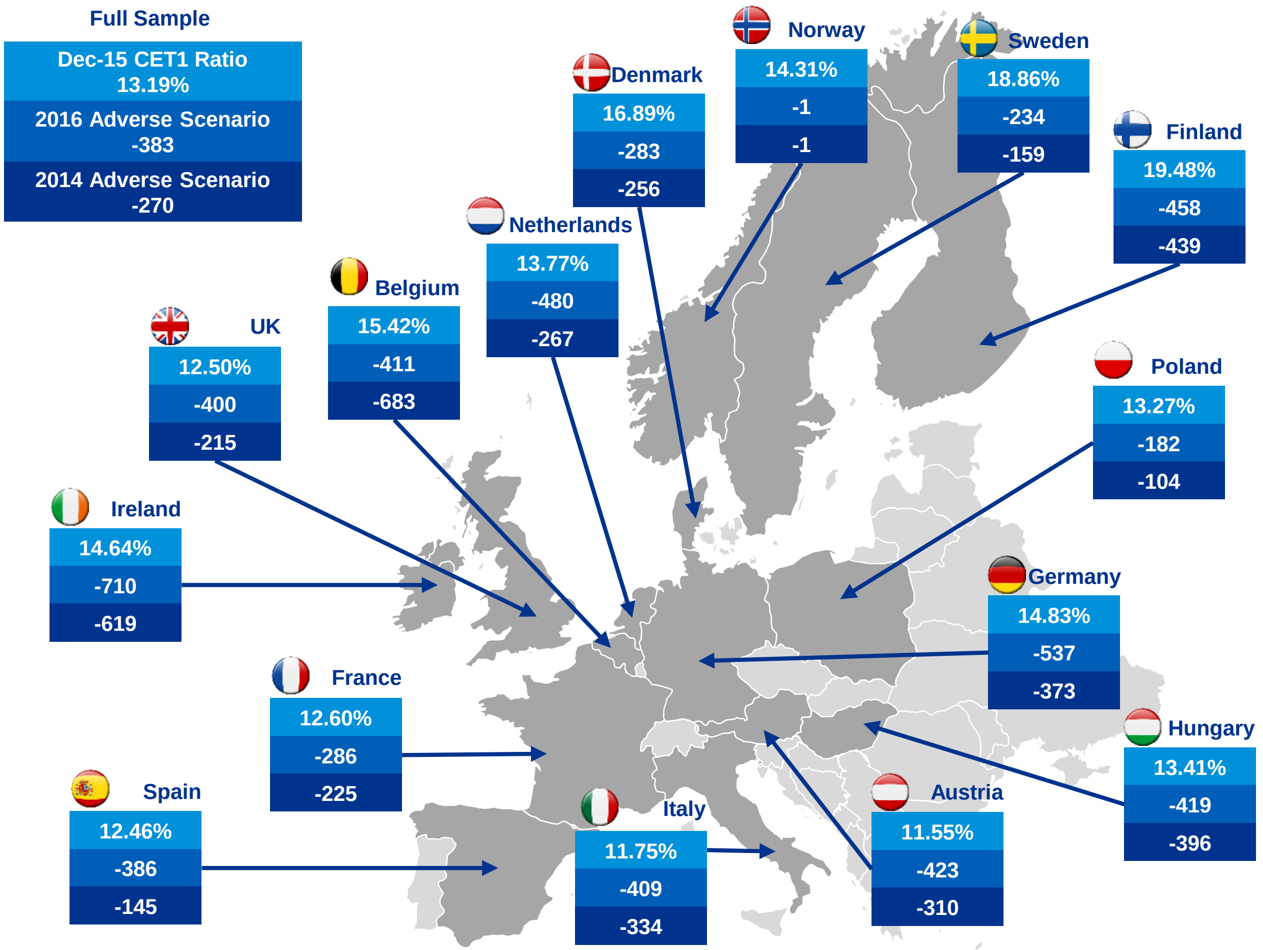
Overview of results

Overview of stress test results



Source: EBA Summary tables.

Country	# banks in stress tests
Austria	2
Belgium	2
Denmark	3
Finland	1
France	6
Germany	9
Hungary	1
Ireland	2
Italy	5
Netherlands	4
Norway	1
Poland	1
Spain	6
Sweden	4
UK	4
TOTAL	**51**

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Some business models have been hit harder

Some business models are likely to have been hit harder with regard to CET1 depletion by some of the macroeconomic and methodological changes.

In particular business models which combine a **high share of interest bearing and market-risk business in combination with a low share of commissions & fees** faced high CET1 depletion.

This hypothesis is confirmed by a **rank comparison** between CET1 reduction and NII-reduction in the adverse scenario.

	Capital depletion (CET1) in adverse scenario (31/12/2018 vs. 31/12/2015)		Change of Net Interest Income in adverse scenario (31/12/2018 vs. 31/12/2015)	
	bps	Rank	*percentage*	Rank
All banks in sample	-383	N.A.	-23.0%	N.A.
Austria	-423	4	-23.0%	6
Belgium	-411	5	-16.1%	9
Denmark	-283	10	-9.8%	11
France	-286	9	-20.7%	7
Germany	-537	2	-23.2%	5
Ireland	-710	1	-32.5%	1
Italy	-409	6	-20.2%	8
Netherlands	-480	3	-30.5%	2
Spain	-386	8	-25.1%	3
Sweden	-234	11	-24.5%	4
United Kingdom	-400	7	-12.9%	10

Source: EBA Summary tables.

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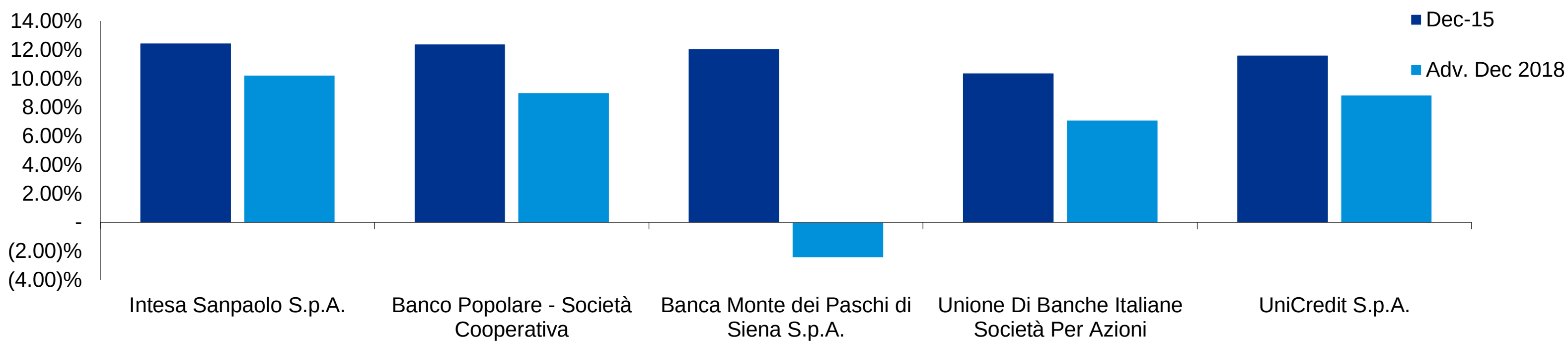
Impacts on Italian Banks' CET1 Ratio

All Italian banks fared better than expected in the 2016 Stress Test, Monte dei Paschi di Sienna was the only bank in the total population with negative capital in the results. However, plans for a capital raise were announced ahead of the results announcement.

2015 vs Adverse scenario as of EoY 2018



Source: EBA Summary charts.

Bank	Dec-15	Adv. Dec-18	Delta 2018/2015 (bps)
Intesa Sanpaolo	12.47%	10.21%	-226
Banco Popolare SC	12.39%	9.00%	-339
Banca Monte dei Paschi	12.07%	-2.44%	-1468
Unione de Banche Italiane	11.62%	8.85%	-277
Unicredit S.p.A	10.38%	7.10%	-328

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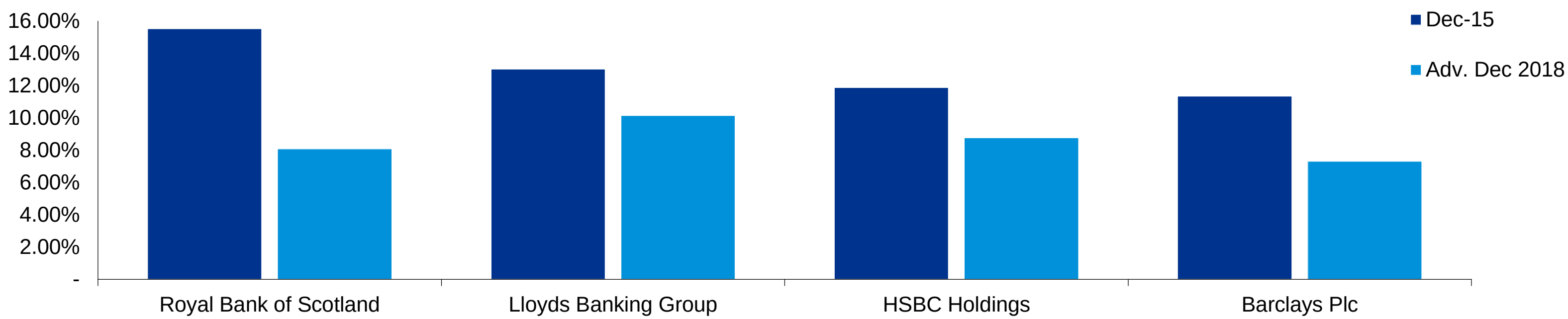
Impacts on UK Banks' CET1 Ratio

Under the adverse scenario, RBS had a CET1 impact of 745 bps, the most of any UK bank. This was primarily driven by an increased credit risk of Corporate SME loans turning into bad loans in an adverse scenario.

2015 vs Adverse scenario as of EoY 2018



Note: (*) Source EBA Summary charts.

Bank	Dec-15	Adv. Dec-18	Delta 2018/2015 (bps)
RBS	15.53%	8.08%	-745
LBG	13.05%	10.14%	-291
HSBC	11.87%	8.76%	-311
Barclays	11.35%	7.30%	-405

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Methodology

Methodology review

2016 vs 2014

The 2016 stress test includes a number of more conservative elements than 2014, which contributes to the observed pattern of larger capital impacts. The stress test methodology has been 'tightened' across a range of risk types:

- The **Operational risk** methodology prescribed by EBA is **more conservative** than 2014.
- **Conduct risk** has, for the first time been **introduced** to the Stress Test.
- A **conservative floor** (standardized approach) has been applied for **Market risk.**
- **Interest margins** have been **tightened** under stress methodology significantly through **conservative minimum increases in funding costs**, coupled with an assumed margin compression.

As in 2014, only limited management action was allowed in the downside scenario, hence the balance sheet had to remain constant even if the changed macro-situation would require a different funding mix or lending policy (static balance sheet approach).

What the EBA 2016 Stress Test did not cover

The following factors were not considered during the 2016 Stress Tests, however, they could create additional downward pressure on CET1 ratios:

- **Brexit:** The impact of the UK leaving the European Union has not been taken into account, as the methodology was published prior to the EU Referendum.
- **IFRS9:** Under the IFRS9 standards banks will have to recognize their financial instruments at "fair value", putting a further strain on their capital requirements.
- **TLAC / MREL:** The Financial Stability Board has mandated additional capital requirements for global systemically important banks, to increase their Total Loss Absorbing Capacity.
- **Basel 4:** The proposed standard requires stricter capital requirements and more transparent financial disclosure, with an aim to meet a higher maximum leverage ratio.

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Conclusions

Main Conclusions

The higher impact of the adverse scenario compared with 2014 exercise is neither to be explained by harsher macroeconomic assumptions nor by weaker banks.

More conservative and detailed Net Interest Income and Market Risk methodologies, coupled with the introduction of new risks such as Conduct Risk, have moved the needle on the adverse scenario compared with 2014.

Basel III transitional provisions in some countries, e.g. Ireland, Germany and Spain have compounded the stress test impact, given that the end of the transition period overlaps with the stress test time horizon of 2016-2018.

The overall stock of capital has increased, both in terms of quality and amount, which we regard as a clear indicator of a more stable and resilient banking system than in 2014, however more work needs to be done.

Management should consider their strategy to improve management of Non Performing Exposures and assess options to speed up the process.

For a more detailed analysis, please click here.

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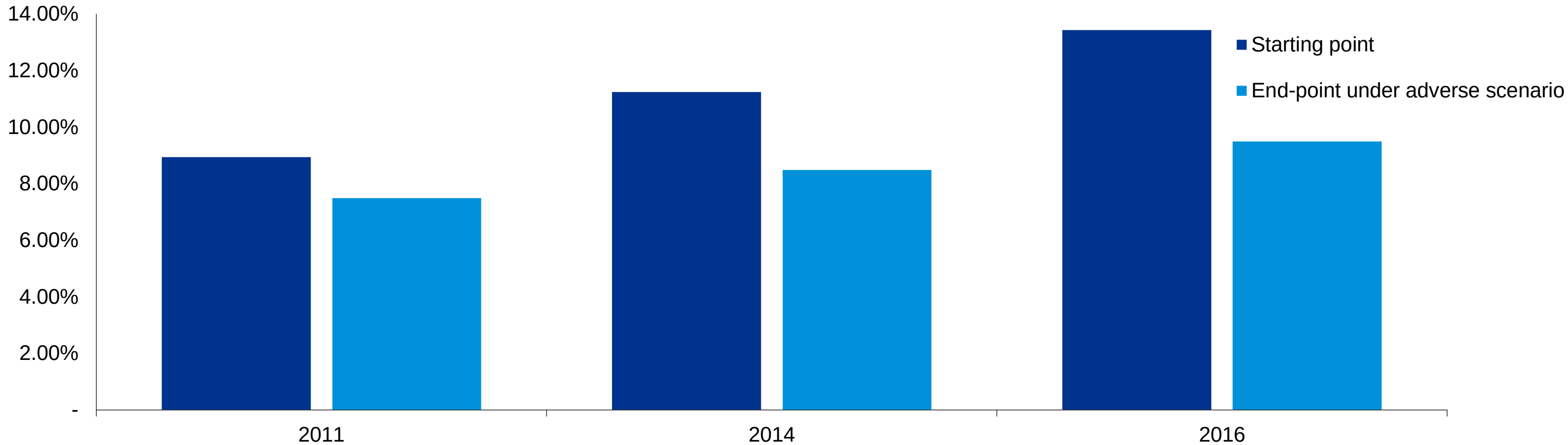
Appendices

Appendix A: Impact of the last three stress tests

EBA Stress Tests – Capital ratio start and end points



Note: EBA Stress Test – Capital ratio start and end points.
EBA, ECB and Citi Research.

With every successive stress test since the 2011 Eurozone crisis, banks have grown more resilient, while the stress tests are adopting a more conservative methodology, thereby increasing pressure on banks to maintain higher capital levels.

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Appendix B: Bank-by-Bank results

Country	Country 2015 CET1 Ratio	Bank	Adverse 2018 (ST 2016)	Adverse 2016 (ST 2014)
AT	11.55%	Raiffeisen-Landesbanken-Holding GmbH	6.12%	7.50%
		Erste Group Bank AG	8.02%	6.80%
IT	11.75%	Banca Monte dei Paschi di Siena S.p.A.	-2.44%	-3.50%
		Banco Popolare - Società Cooperativa	9.00%	3.60%
		Unicredit S.p.A.	7.10%	6.50%
		Unione Di Banche Italiane Società Per Azioni	8.85%	7.90%
		Intesa Sanpaolo S.p.A.	10.21%	7.80%
ES	12.46%	Banco Popular Español S.A.	6.62%	6.40%
		Banco Santander S.A.	8.20%	7.30%
		BFA Tenedora de Acciones S.A.U.	9.58%	8.60%
		Banco de Sabadell S.A.	8.04%	7.80%
		Banco Bilbao Vizcaya Argentaria S.A.	8.19%	8.20%
		Criteria Caixa, S.A.U.	7.81%	#N/A
UK	12.50%	The Royal Bank of Scotland Group Public Limited Company	8.08%	6.70%
		Lloyds Banking Group Plc	10.14%	6.00%
		Barclays Plc	7.30%	7.10%
		HSBC Holdings	8.76%	9.30%
FR	12.60%	La Banque Postale	9.82%	9.40%
		Groupe BPCE	9.47%	6.40%
		Groupe Crédit Agricole	10.49%	8.60%
		Société Générale S.A.	7.50%	7.10%
		BNP Paribas	8.51%	7.60%
		Groupe Crédit Mutuel	13.38%	12.80%

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Appendix B: Bank-by-Bank results (cont.)

Country	Country 2015 CET1 Ratio	Bank	Adverse 2018 (ST 2016)	Adverse 2016 (ST 2014)
PL	13.27%	Powszechna Kasa Oszczędności Bank Polski SA	11.44%	14.30%
HU	13.41%	OTP Bank Nyrt.	9.22%	12.00%
NL	13.77%	N.V. Bank Nederlandse Gemeenten	17.62%	17.40%
		ABN AMRO Group N.V.	9.53%	8.80%
		Coöperatieve Rabobank U.A.22	8.10%	7.10%
		ING Groep N.V.	8.98%	8.20%
NO	14.31%	DNB Bank Group	14.30%	11.30%
IE	14.64%	Allied Irish Banks plc	4.31%	-3.60%
		The Governor and Company of the Bank of Ireland	6.15%	2.90%
DE	14.83%	Landesbank Baden-Württemberg	9.40%	5.50%
		Commerzbank AG	7.42%	6.90%
		DekaBank Deutsche Girozentrale	9.53%	7.50%
		Norddeutsche Landesbank Girozentrale	8.62%	8.50%
		Landesbank Hessen-Thüringen Girozentrale	10.10%	7.70%
		Deutsche Bank AG	7.80%	7.00%
		Bayerische Landesbank	8.34%	7.00%
		NRW.BANK	35.40%	31.10%
		Volkswagen Financial Services AG	9.55%	6.50%

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Appendix B: Bank-by-Bank results (cont.)

Country	Country 2015 CET1 Ratio	Bank	Adverse 2018 (ST 2016)	Adverse 2016 (ST 2014)
BE	15.42%	Belfius Banque SA	11.41%	6.50%
		KBC Group NV	11.27%	6.30%
DK	16.89%	Nykredit Realkredit	13.86%	10.90%
		Jyske Bank	13.99%	13.30%
		Danske Bank	14.02%	11.10%
SE	18.86%	Skandinaviska Enskilda Banken - group	16.60%	13.00%
		Svenska Handelsbanken - group	18.55%	16.90%
		Nordea Bank - group	14.09%	12.00%
		Swedbank – group	23.05%	16.30%
FI	19.48%	OP Financial Group21	14.61%	11.20%

Four most deteriorated banks, for which the 2016 Stress Test Adverse scenario put them in a worse position than the 2014 Stress Test Adverse Scenario

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