



Understanding the 2016 EBA Stress Test Results

July 30th 2016

DRAFT





Management summary

Key takeaways

1

European banks appear to be in a **more stable position** than they were in 2014. Inter alia, for example, has increased its overall 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**.

2

Today's European banking system appears to have **deeper loss-absorbing capacity**, however this is combined with heightened **concern over profitability and a diminished appetite for equity** from investors

3

Bank capital positions have increased for each country compared with the 2014 stress test. However, the **difference in capital impact between the base and adverse scenarios is significantly greater** in 2016 than in 2014

4

Macro scenarios do not explain the more severe impact across all countries - what explains it is the much more **conservative methodology** used

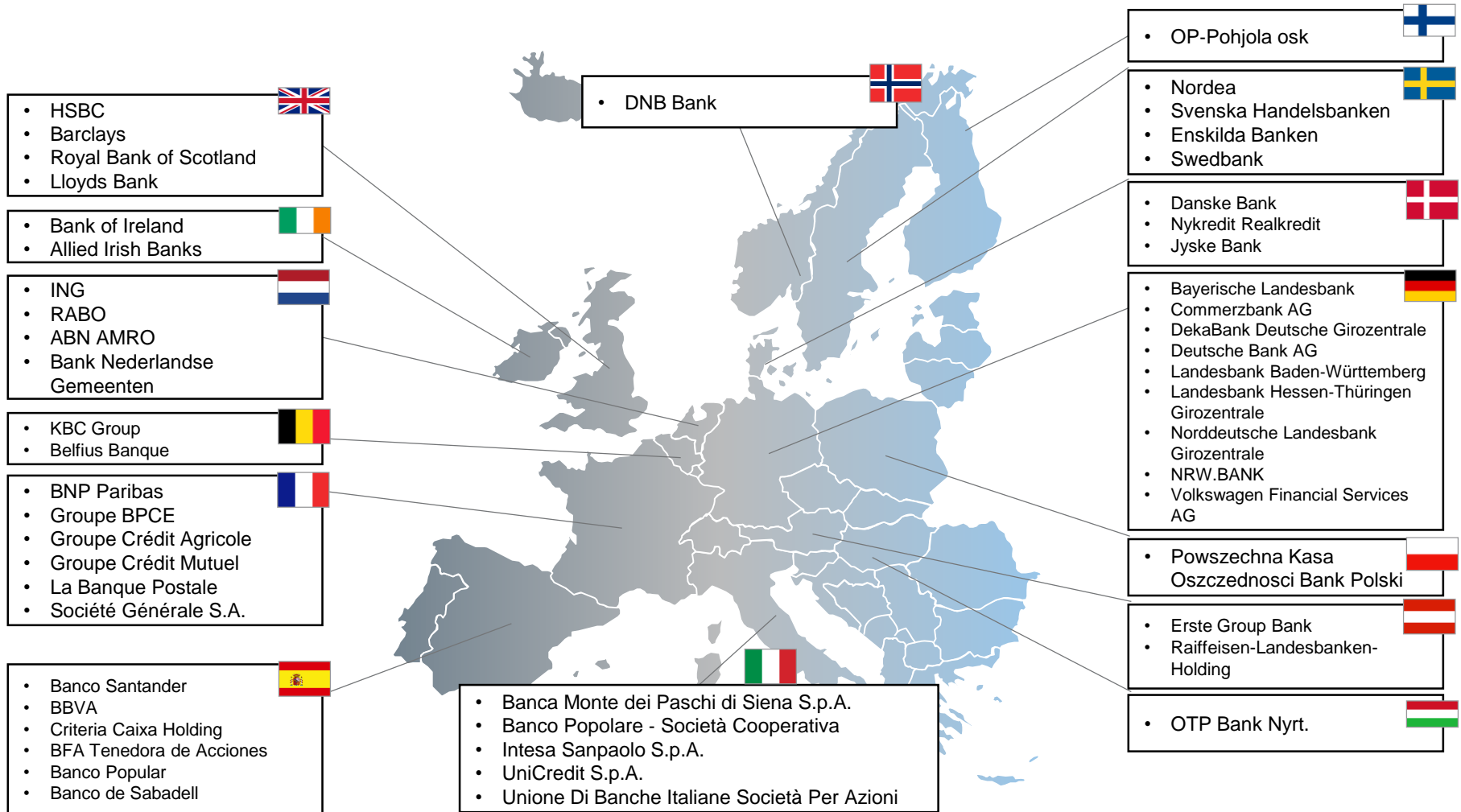
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Country-by-Country comparison shows a large degree of **heterogeneity** in the impact of the stress test. A higher capital depletion is not necessarily a sign of larger weakness. Most of the **heterogeneity can be explained by the methodological assumptions** which hit certain business models harder and different transitional provisions in the European banking law



Scope and methodology

Scope reduced to 51 banks

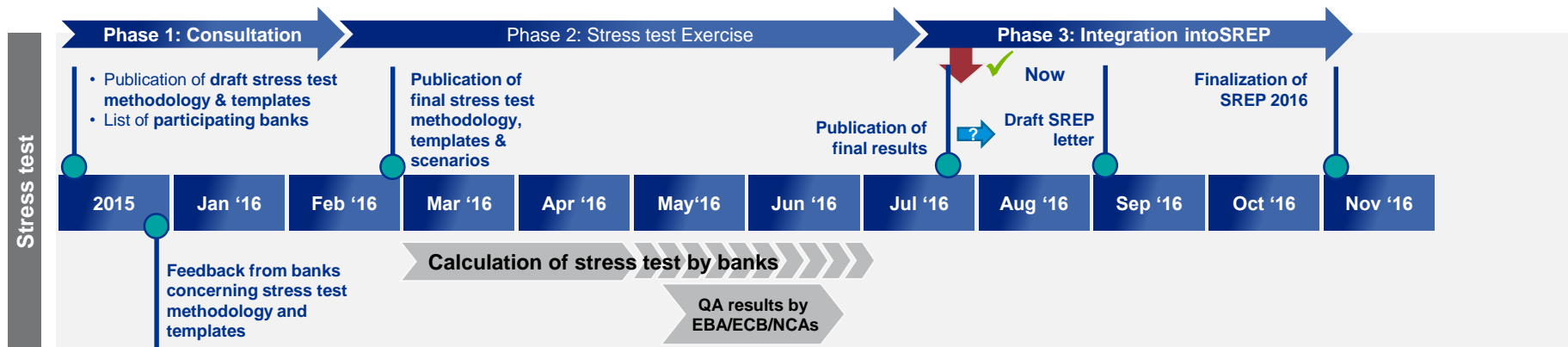


Scope of exercise and methodology

Stress test:

- to assess banks' ability to withstand adverse economic conditions;
- to inform the 2016 SREP and challenge capital plans.

Scope	<ul style="list-style-type: none"> Scope of institutions for EBA Stress Test significantly reduced: 51 in the EU (70% assets). Most likely ECB will ask significant institutions to run the exercise; stress test is run at the highest level of consolidation of the banking group and insurance activities are excluded from the scope
Macroeconomic scenarios	<ul style="list-style-type: none"> Two scenarios, a “common baseline scenario” and an “adverse macro-economic scenario” The reference date is 31.12.2015, the stress horizon covers three-years from 2016 to 2018
New business and portfolio run-down	<ul style="list-style-type: none"> “Static balance sheet” assumption
Capital requirements	<ul style="list-style-type: none"> No single/public capital threshold – banks cannot publicly pass/fail; BUT: Results will inform the 2016 SREP, so threshold might implicitly be set by SREP letter ratios, which are significantly higher than the 2014 ratios (8% baseline, 5.5% adverse)
Regulatory & accounting changes	<ul style="list-style-type: none"> New regulation / accounting changes need only be considered if legally binding & endorsed at cut-off date, i.e. IFRS 9 and „Basel IV“ changes out of scope





Overview of results

Overview of stress test results

- Bank initial **capital positions** as measured by CET1 have **increased for each country in comparison with the 2014 exercise.**
- Difference in **capital impact between the base and adverse scenarios is significantly larger** than in 2014.
- **There are substantial differences between results for each country** – e.g. Irish and Dutch banks suffer a greater capital hit than banks in other EU states.

Capital depletion in adverse scenario (CET1-ratio, change in bps)

bps / percentage	Stress Test 2016 (31/12/2018 vs. 31/12/2015)	Stress Test 2014 (31/12/2016 vs. 31/12/2013)	CET1% as EoY 2015	CET1% as EoY 2013
All banks in the sample	-391	-252	13,4%	11,3%
Austria	-424	-242	11,4%	10,3%
Belgium	-419	-530	15,5%	13,1%
Denmark	-210	-201	16,1%	14,9%
France	-316	-221	13,1%	10,6%
Germany	-540	-407	13,8%	13,2%
Ireland	-704	-511	14,6%	13,2%
Italy	-347	-339	12,1%	9,6%
Netherlands	-568	-332	14,5%	12,1%
Spain	-384	-151	12,4%	10,3%
Sweden	-230	-172	20,0%	16,4%
United Kingdom	-362	-243	12,5%	9,7%

Based on median values on country-level



Major drivers of the 2016 stress test results

Macroeconomic scenarios have changed, though severity is comparable to 2014

- **While macroeconomic scenarios have changed, the differences cannot be attributed to those changes**
- **As can be seen on the right, the scenarios severity is comparable between 2014 and 2016**
- **For example, the assumed GDP reduction for the EU is 7.1 % for this year's exercise while in 2014 it was 7.0%.** Certain asset classes, notably equity markets and commercial property, are stressed more harshly in 2016. This is offset by a relaxation of other stresses: for example a shallower reduction in demand for EU-exports from advanced economies

	Stress Test 2016	Stress Test 2014
Increase in yields	<ul style="list-style-type: none"> • + 71 / 80 / 68 bps in 2016-2018 in EU • Between 44 bps (Germany) and 234 bps (Greece) • Peak in Q1 of 1st stressed year 	<ul style="list-style-type: none"> • + 150 / 110 / 110 bps in 2014-2016 in EU • Between 137bps (Germany) and 380 bps (Greece) • Peak in Q1 of 1st stressed year
Currency fluctuations (EEA)	<ul style="list-style-type: none"> • Appreciation of EUR vs. local CEE currencies (between 8 and 24 percent) • Substantial appreciation of CHF against EUR, by 23 percent from Year 2 (not included in 2014). 	<ul style="list-style-type: none"> • Appreciation of EUR vs. local CEE currencies (between 15 and 25 percent)
Loss of demand (EU-exports)	<ul style="list-style-type: none"> • Reduction in demand by advanced economies from EU of 6.5% in a three year period. 	<ul style="list-style-type: none"> • Reduction in demand by advanced economies from EU of 11.7% over a three year period.
Stock market crash	<ul style="list-style-type: none"> • Value down by 25.4% on average for EU 	<ul style="list-style-type: none"> • Value down by 18.6% on average for EU
Property crash	<ul style="list-style-type: none"> • Residential property down 21.2% over three years. • Prime commercial property down 22.6% (both EU figures.) 	<ul style="list-style-type: none"> • Residential property down 21.2% over three years. • Prime commercial property down 14.7% (both EU figures.)
Rise in unemployment	<ul style="list-style-type: none"> • Increase in EU unemployment rates vs. base case of 2.8% over 3 years. 	<ul style="list-style-type: none"> • Increase in EU unemployment rates vs. base case of 2.9% over 3 years.

Methodological assumptions are more conservative

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)

Some business models likely to be hit harder than others

- **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 banks with a high NII-share**
- **An increase in the NII-stress level therefore most likely impacts banks in the Netherlands and Ireland** more strongly which is confirmed by a rank comparison between CET1 reduction and NII-reduction in the adverse scenario. See annex

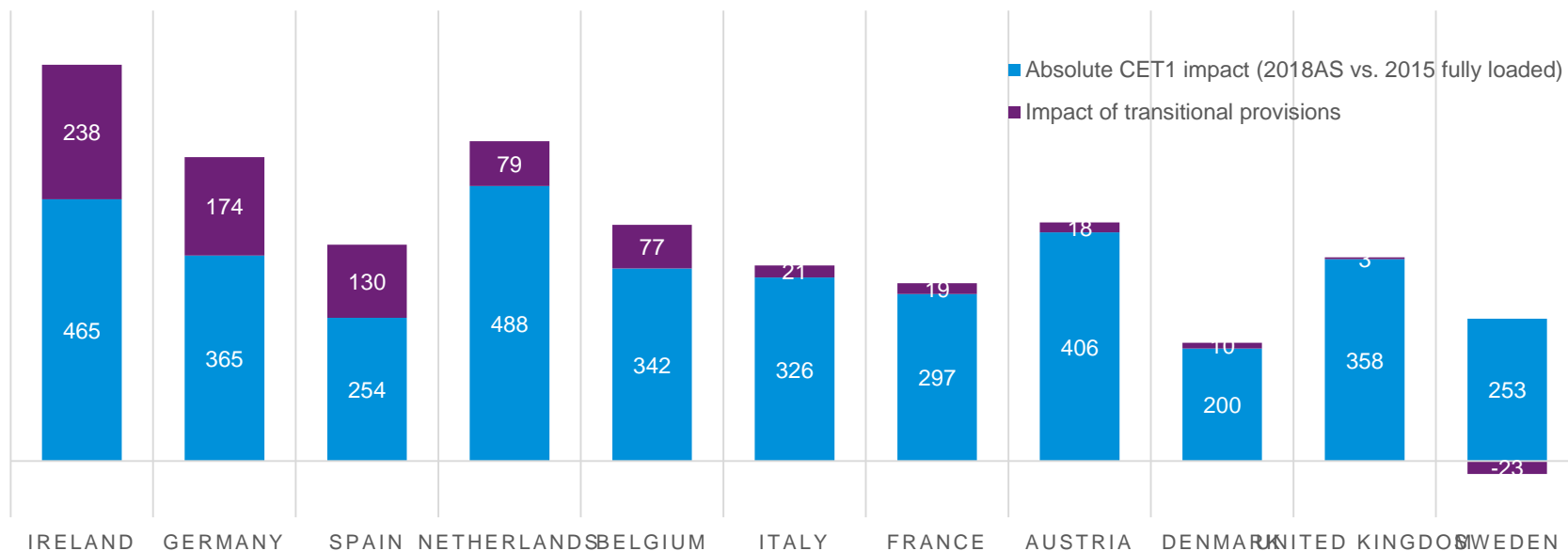
	Capital depletion (CET1) in adverse scenario (31/12/2018 vs. 31/12/2015)		Change of Net Interest Income in adverse scenario (31/12/2018 vs. 31/12/2015)	
	<i>bps</i>	Rank	<i>percentage</i>	Rank
All banks in sample	-325	N.A.	-23,0%	N.A.
Austria	-424	4	-23,0%	6
Belgium	-419	5	-16,1%	9
Denmark	-210	11	-9,8%	11
France	-316	9	-20,7%	7
Germany	-540	3	-23,2%	5
Ireland	-704	1	-32,5%	1
Italy	-347	8	-20,2%	8
Netherlands	-568	2	-30,5%	2
Spain	-384	6	-25,1%	3
Sweden	-230	10	-24,5%	4
United Kingdom	-362	7	-12,9%	10

Based on median values on country-level

Basel 3 Transitional Provisions differ between countries

The Basel 3 transitional provisions provide an additional explanation for the observed country pattern of the Stress Test results:

- The CRR allows some room for maneuver for national legislators to adopt capital rules and to transition towards a ‘fully loaded’ Basel 3 capital definition
- Whereas some national regulators allowed transition periods of maximum length, some countries enforced much shorter transition periods. Other countries range in the middle
- Results confirm that most “late” adopters face a significant higher impact from transitional provisions when compared to “early” adopters like e.g. Sweden or the United Kingdom



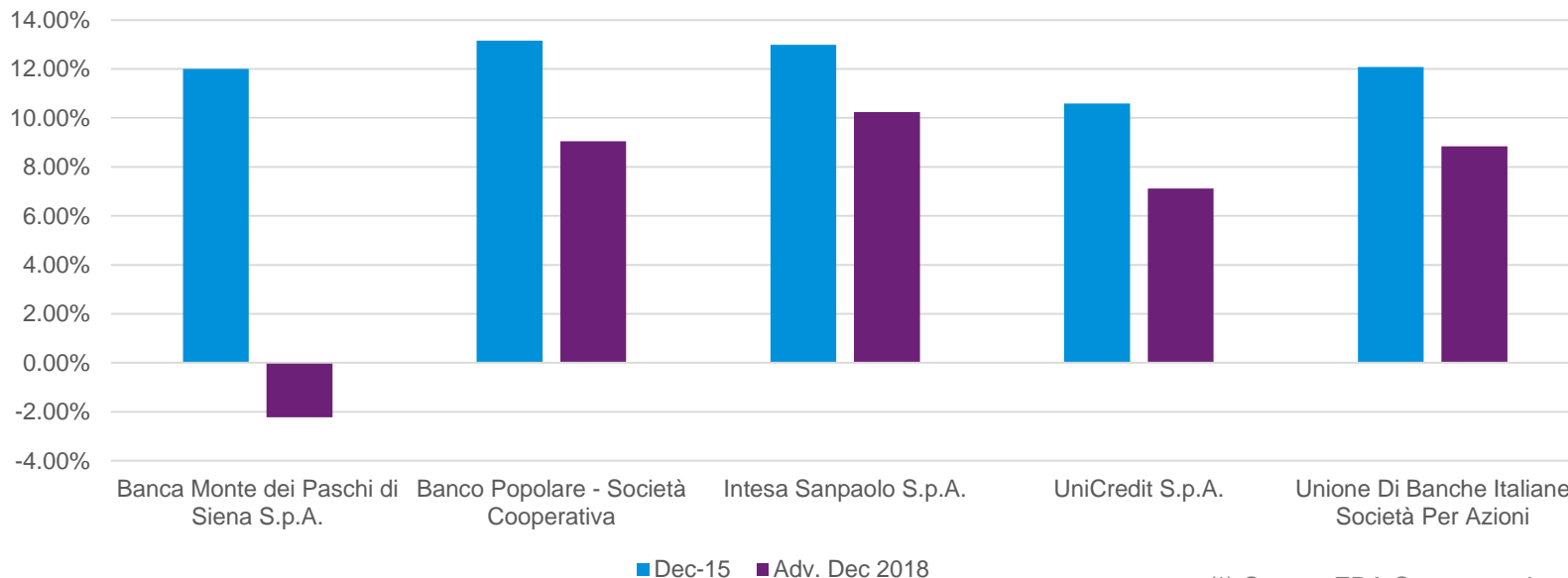
Main Conclusions

- 1 The higher impact of the adverse scenario compared with 2014 exercise is neither to be explained by harsher macroeconomic assumptions nor by weaker banks.
- 2 It appears that 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.
- 3 Basel III transitional provisions in some countries have compounded the stress test impact, given that the end of the transition period overlaps with the stress test time horizon of 2016-2018
- 4 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.



Focus on Italian Banks

Impacts on Italian Banks CET1 Ratio

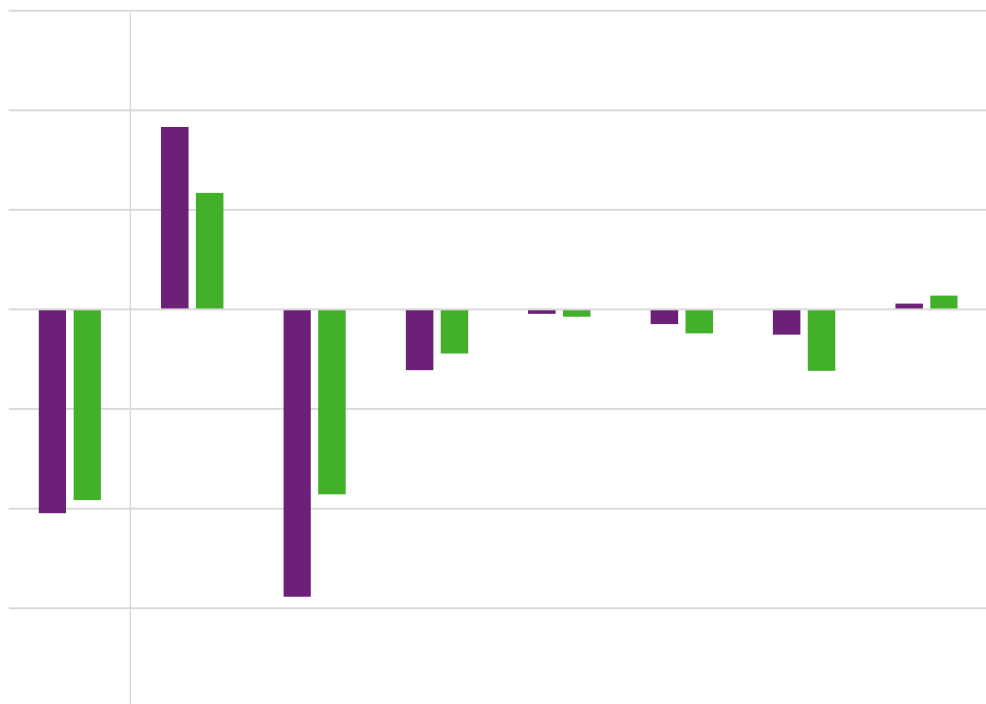


(*) Source EBA Summary charts

Bank	Dec-15	Adv. Dec 2018	Delta 2018/2015 (bps)
Banca Monte dei Paschi di Siena S.p.A.	12.01%	-2.23%	-1423
Banco Popolare - Società Cooperativa	13.15%	9.05%	-410
Intesa Sanpaolo S.p.A.	12.98%	10.24%	-274
UniCredit S.p.A.	10.59%	7.12%	-347
Unione Di Banche Italiane Società Per Azioni	12.08%	8.85%	-323
Italian Market (*)	11.75%	7.66%	-409

UE vs. Italian Banks - CET1 Ratio waterfall

Impacts on CET1 Ratio (bps)



When comparing Italian to other EU banks, the **impact waterfall on CET1%** under the adverse scenario shows that:

- **Italian Banks are able to produce higher profits** (+370bps vs +235bps)
- **Credit losses are significantly higher** for Italian banks (-580 vs -370bps)
- **Market risk impacts are higher** (-120bps vs -90bps)
- **Transitional arrangements have a lower impact** on Italian banks (-30bps vs -50bps)
- **Risk Weighted Assets increase is significantly lower** for Italian banks (-50bps vs -120bps)

Data source: EBA Summary charts





Appendix

Income Structure as per EoY 2015





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