



EUROPEAN CENTRAL BANK

EUROSYSTEM

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ECB'S IN-DEPTH REVIEW SHOWS BANKS NEED TO TAKE FURTHER ACTION

- Key results of comprehensive assessment of 130 largest euro area banks:
 - Capital shortfall of €25 billion detected at 25 participant banks
 - Banks' asset values need to be adjusted by €48 billion, €37 billion of which did not generate capital shortfall
 - Shortfall of €25 billion and asset value adjustment of €37 billion implies overall impact of €62 billion on banks
 - Additional €136 billion found in non-performing exposures
 - Adverse stress scenario would deplete banks' capital by €263 billion, reducing median CET1 ratio by 4 percentage points from 12.4% to 8.3%
- Exercise delivers high level of transparency, consistency and equal treatment
- Rigorous exercise is milestone for the Single Supervisory Mechanism starting in November

The European Central Bank (ECB) has today published the results of a thorough year-long examination of the resilience and positions of the 130 largest banks in the euro area as of 31 December 2013.

“This unique and rigorous exercise is a major milestone in the preparation for the Single Supervisory Mechanism, which will become fully operational in November,” said Vítor Constâncio, Vice-President of the ECB. “This unprecedented in-depth review of the largest banks' positions will boost public confidence in the banking sector. By identifying problems and risks, it will help repair balance sheets and make the banks more resilient and robust. This should facilitate more lending in Europe, which will help economic growth.”

The comprehensive assessment—which consisted of the asset quality review (AQR) and a forward-looking stress test of the banks—found a capital shortfall of €25 billion at 25 banks. Twelve of the 25 banks have already covered their capital shortfall by increasing their capital by €15 billion in 2014. Banks with shortfalls must prepare capital plans within two weeks of the announcement of the results. The banks will have up to nine months to cover the capital shortfall.

The AQR showed that as of end-2013 the carrying values—or book values—of banks' assets need to be adjusted by €48 billion, which will be reflected in the banks' accounts or prudential requirements. Furthermore, using a standard definition for non-performing exposures (any obligations that are 90 days overdue, or that are impaired or in default), the review found that banks' non-performing exposures increased by €136 billion to a total of €879 billion.

The comprehensive assessment also showed that a severe scenario would deplete the banks' top-quality, loss-absorbing Common Equity Tier 1 (CET 1) capital—the measure of a bank's

financial strength—by about €263 billion. This would result in the banks' median CET1 ratio decreasing by 4 percentage points from 12.4% to 8.3%. This reduction is higher than in previous similar exercises and is a measure of the rigorous nature of the exercise.

“This exercise is an excellent start in the right direction. It required extraordinary efforts and substantial resources by all parties involved, including the euro area countries' national authorities and the ECB. It bolstered transparency in the banking sector and exposed the areas in the banks and the system that need improvement,” said Danièle Nouy, Chair of the Supervisory Board. “The comprehensive assessment allowed us to compare banks across borders and business models, and the findings will enable us to draw insights and conclusions for supervision going forward.”

Since the announcement of the exercise in July 2013, the largest 30 participating banks have undertaken various measures, including capital raising to an amount of €60 billion, to strengthen their balance sheets by a total of more than €200 billion. These frontloaded measures are part of the overall successful outcome of the exercise. Some of the measures taken in 2013 reduced the insufficiencies detected by the comprehensive assessment; some measures adopted in 2014 may count toward the coverage of the capital shortfall.

Comprehensive assessment

The comprehensive assessment—which joined up the AQR and the stress test components—was aimed at strengthening banks' balance sheets, enhancing transparency and building confidence. The 130 banks that were examined accounted for assets of €22 trillion, which represents 82% of total banking assets in the euro area. It was performed under the current EU Capital Requirements Regulation and Directive (CRR/CRDIV), which include certain national discretions. These national discretions can lead to differences in, for example, the definition of capital. These differences will gradually diminish over the coming years as transitional arrangements in the relevant regulation are phased out. The ECB recognises the need to improve the consistency of the definition of capital and the related quality of capital. ECB Banking Supervision will address this as a matter of priority.

AQR

The AQR conducted by the ECB and national competent authorities (NCAs) examined whether assets were properly valued on banks' balance sheets as on 31 December 2013. It made banks comparable across national borders by applying common definitions for previously diverging concepts and a uniform methodology when assessing balance sheets. More than 6,000 experts across the Single Supervisory Mechanism examined more than 800 individual portfolios in detail, among other things thoroughly analysing the quality of the credits of 119,000 debtors of banks. The review provides the ECB with substantial information on the banks that will fall under its direct supervision and will help its efforts in creating a level playing field for supervision in the future.

Stress test

The stress test was performed by the participating banks, the ECB and NCAs in cooperation with the European Banking Authority (EBA). The EBA also designed the stress test methodology, while the adverse scenario was developed by the European Systemic Risk Board (ESRB) in cooperation with the NCAs, the EBA and the ECB. Banks were required to maintain a minimum CET1 ratio of 8% under the baseline scenario (as for the AQR) and a minimum CET1

ratio of 5.5% under the adverse scenario. The stress test is not a forecast of future events, but a prudential exercise to test banks' ability to withstand weakening economic conditions; participating banks were encouraged to make conservative projections, which were challenged according to strict quality assurance requirements. A novel element was that information acquired from the AQR was incorporated in banks' balance sheet starting points and in related stress test projections.

Bank-by-bank disclosures

In the 130 individual bank templates, the ECB distinguishes between capital shortfalls identified in the AQR and those identified under the baseline and adverse scenarios of the stress test. In the comprehensive assessment, the two items are joined up. The templates also provide important additional information on each bank, such as the issuance of capital instruments already undertaken in 2014. The full results of the stress test are also published by the EBA. The aggregate report on the full outcome of the exercise for all banks can be found at: <http://www.ecb.europa.eu/ssm/assessment/html/index.en.html>.

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