EUROPEAN CENTRAL BANK

BANKING SUPERVISION

SSM SREP Methodology Booklet

- 2016 edition -

Level playing field - High standards of supervision - Sound risk assessment

SREP – Key achievements

- **Level playing field:** SREP is currently being executed for **the second time** according to:
  - a **common methodology**
  - a **common decision-making process** allowing for peer comparisons and transversal analyses on a wide scale

- **High standards of supervision:**
  - follows the **EBA guidelines on SREP** and draws on leading practices within the SSM and as recommended by international bodies
  - **proportionality, flexibility and continuous improvement**
  - supervisory decisions – **not only additional capital but also additional measures** tailored to banks' specific weaknesses

- **Sound risk assessment:**
  - **combination of quantitative and qualitative elements**
  - **holistic assessment** of institutions' viability taking into account their specificities
  - **forward-looking perspective**, e.g. stress tests performed in 2016

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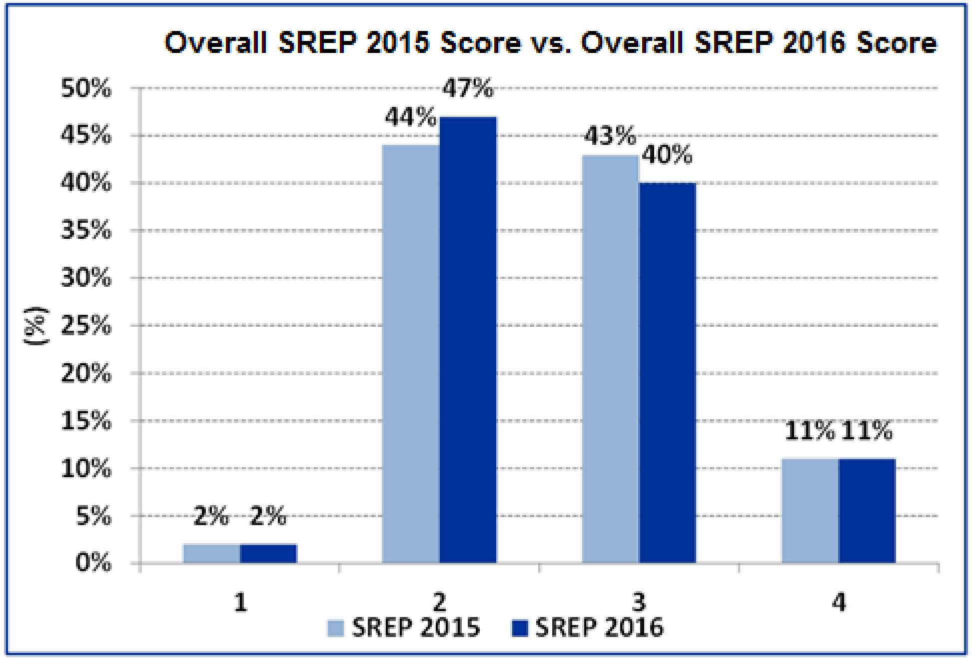
In 2016 the SSM carried out its second SREP cycle for 123 SIs in 19 countries

- Overall, the exercise revealed that the **distribution of risks in the system remains broadly stable**, with some idiosyncratic changes

SREP Outcome 2015/2016



Based on banks with a final SREP 2016 decision as of 30 November 2016

1.1. SREP 2016 Outcome – Key facts: Capital measures (1/2)

Overall consistency in CET1 demand from SREP 2015 to SREP 2016

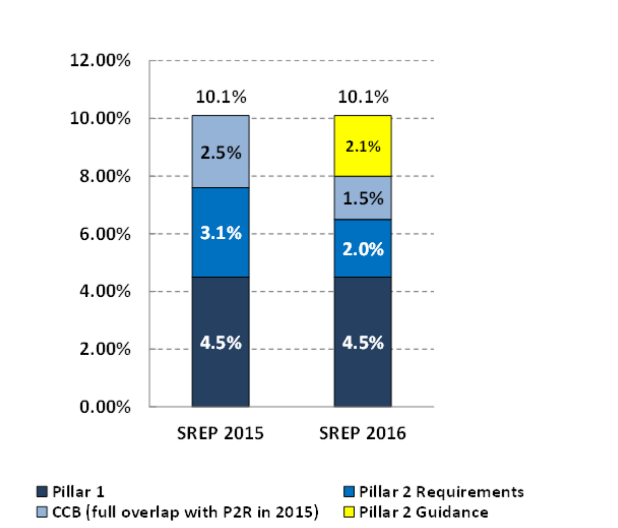
- The overall SREP CET1 demand for 2017 remained at the same level as last year.
- In a number of individual cases, the CET1 demand changed to reflect the evolution of the risk profile (up or down).
- The MDA trigger decrease, from an average of 10.2% to 8.3%, is due to a shift of capital from the 2015 Pillar 2 to the newly introduced non-MDA relevant Pillar 2 Guidance (P2G). The P2G also captures supervisory risk concerns from the outcome of stress tests. Moreover, the inclusion of the non-phased-in part of the CCB in Pillar 2 was eliminated in the 2016 approach.

Notes:

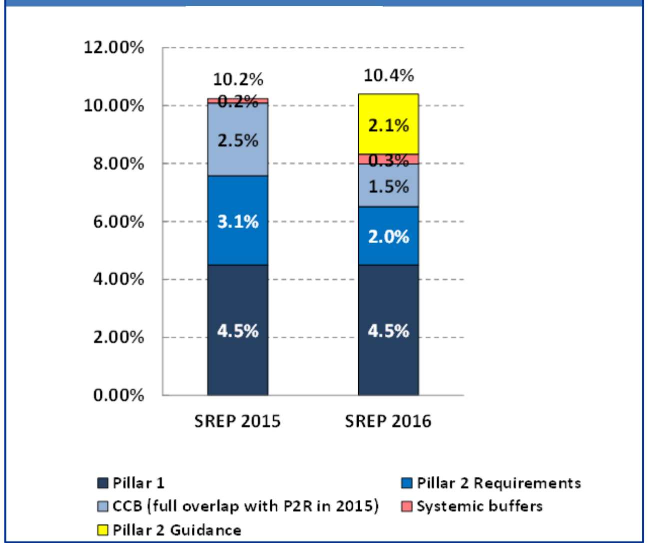
- *Simple average, computed based on the final SREP 2016 decisions as of 30 November 2016.*
- *CET1 demand is computed without taking into account the potential need to cover shortages of P1 AT1 and T2.*

[1] *excluding systemic buffers (G-SII, O-SII and systemic risk buffer)*

CET1 demand (excl. systemic buffers)



CET1 demand (incl. systemic buffers)

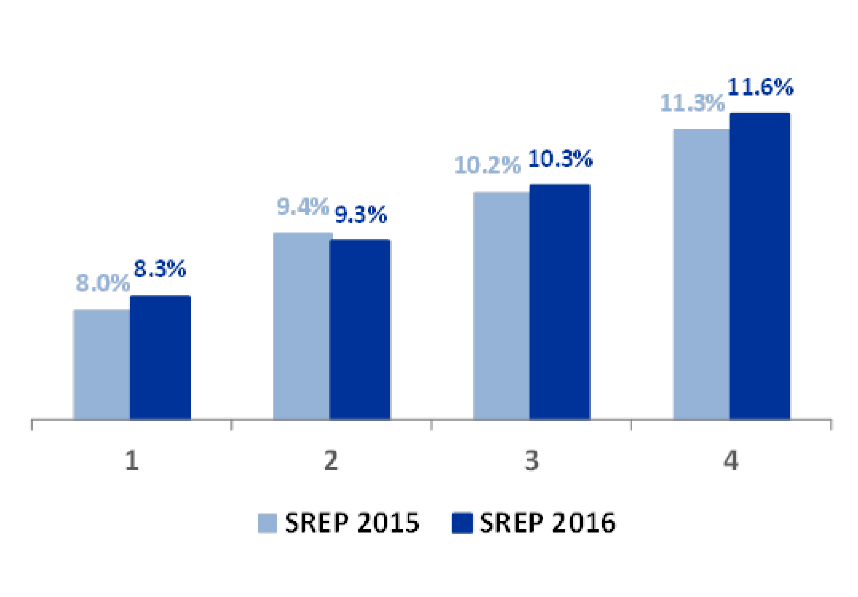


1.1. SREP – 2016 Outcome – Key facts: Capital measures (2/2)

SREP CET1 demand per score comparable to 2015

- Average and median of SREP 2016 CET1 demand[1] are around 10%, which is comparable to last year
- In line with SREP 2015 achievements, SREP 2016 CET1 demand is consistent and correlated with overall SREP scores

SREP CET1 demand[1] by overall SREP score



[1] *excluding systemic buffers (G-SII, O-SII and systemic risk buffer)*

Based on banks with a final SREP 2016 decision as of 30.11.2016

1.1. SREP – 2016 Outcome – Key facts: Other measures

Liquidity measures

- Targeted liquidity measures to address main weaknesses, such as:
  - over-reliance on wholesale short-term funding
  - liquidity risk strategy and tolerance framework to be integrated within the overall risk appetite framework
  - need to adequately monitor and manage risks associated with collateral management, especially collateral availability and collateral needs during stress
- Quantitative measures, such as:
  - LCR higher than the regulatory minimum
  - specific minimum survival period
  - minimum amount of liquid assets

Other qualitative measures

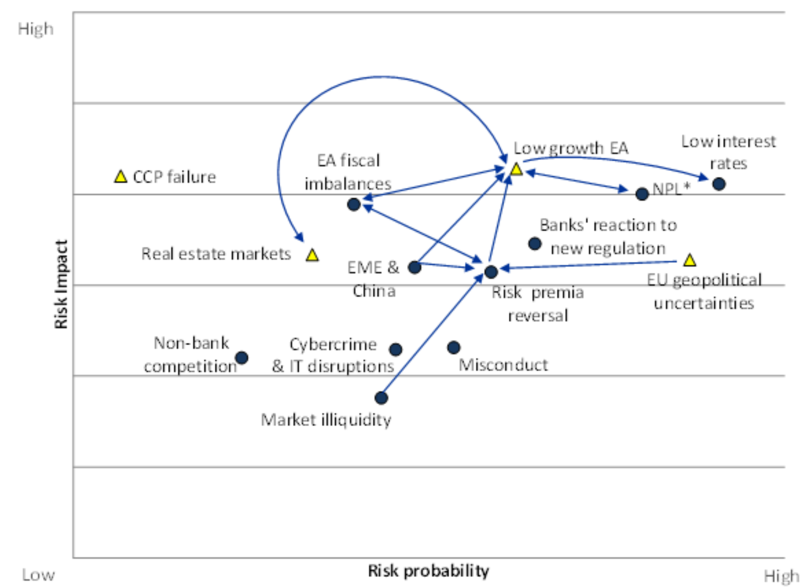
- The likelihood of qualitative measures increases with the risk profile of banks – qualitative measures for all banks with an overall score of 4
- Qualitative measures relate to all SREP elements and are bank specific, e.g. "governance still needs improvement"
  - quality and independence of the management body
  - consistency and robustness of risk appetite framework versus risk profile

1.2. SREP – 2016 Outcome: Key risks (1/2)

2016 SREP cycle highlighted challenges regarding profitability and capital adequacy

- Profitability under pressure:
  - weak economic environment
  - banks' net interest income – on average half of their total income – resilient but to come under strain
  - overcapacity and market fragmentation
- Capital adequacy still negatively affected by non-performing loans in some countries – weighing on banks' profitability

Key risks for SSM banks

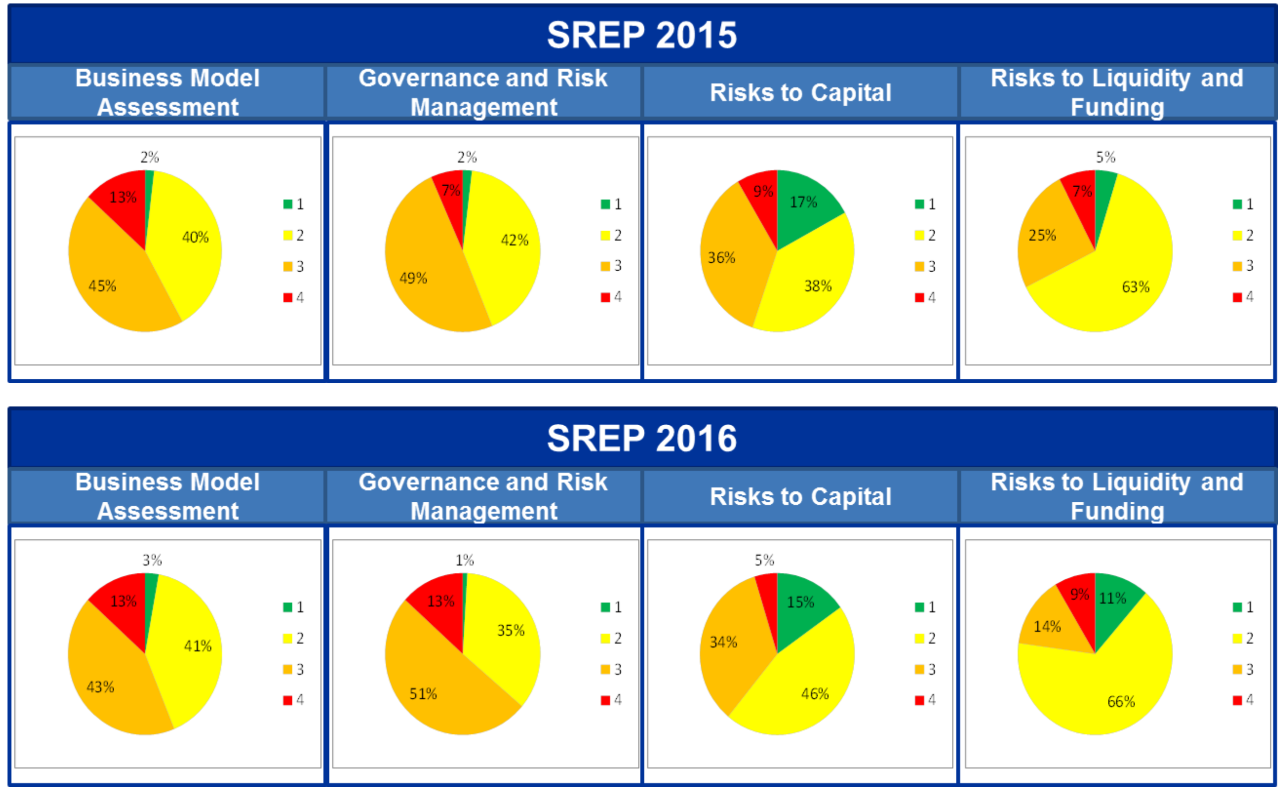


Source: ECB calculations, NCAs submissions.
* Only applicable to banks with high NPL ratios

Evolution of SREP scores per element 2015 and 2016

- The main drivers of concern remain the same as in 2015: business model, internal governance and risk management and risks to capital (especially credit risk)

- Worse scores in internal governance and risk management were based on the results of the thematic review on risk governance and risk appetite

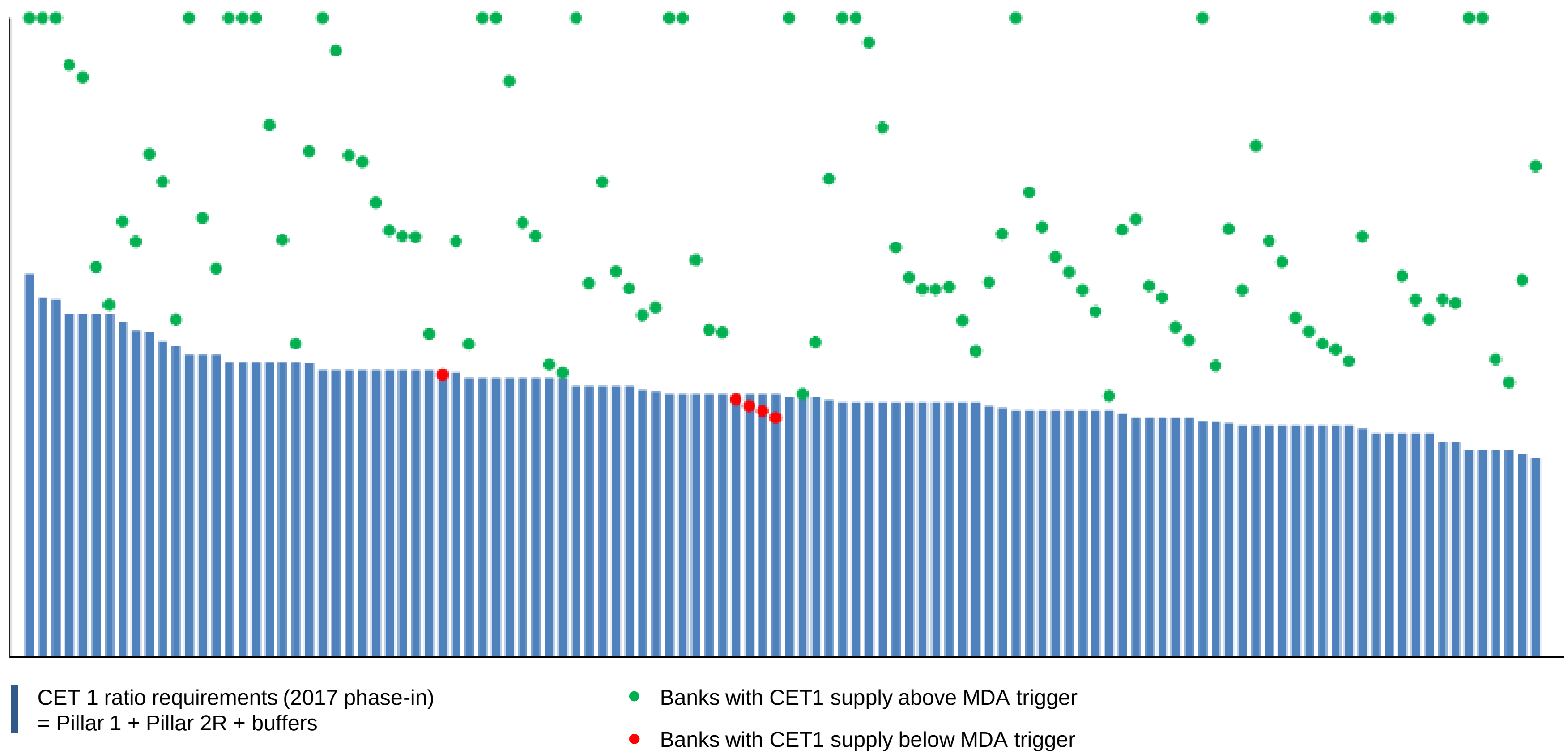


Based on banks with a final SREP 2016 decision as of 30 November 2016

1.2. SREP – 2016 Outcome: CET1 level

Most significant institutions currently have capital levels above CET1 requirements and buffers*

Capital supply compared to MDA trigger



* Based on capital supply in Q2 2016 (CET1: without Pillar 1 AT1/T2 shortages)

Based on banks with a final SREP 2016 decision as of 30.11.2016

2. Legal Basis

The SSM SREP methodology implements Union law, EBA Guidelines and supervisory best practices

SREP in CRD IV – Article 97

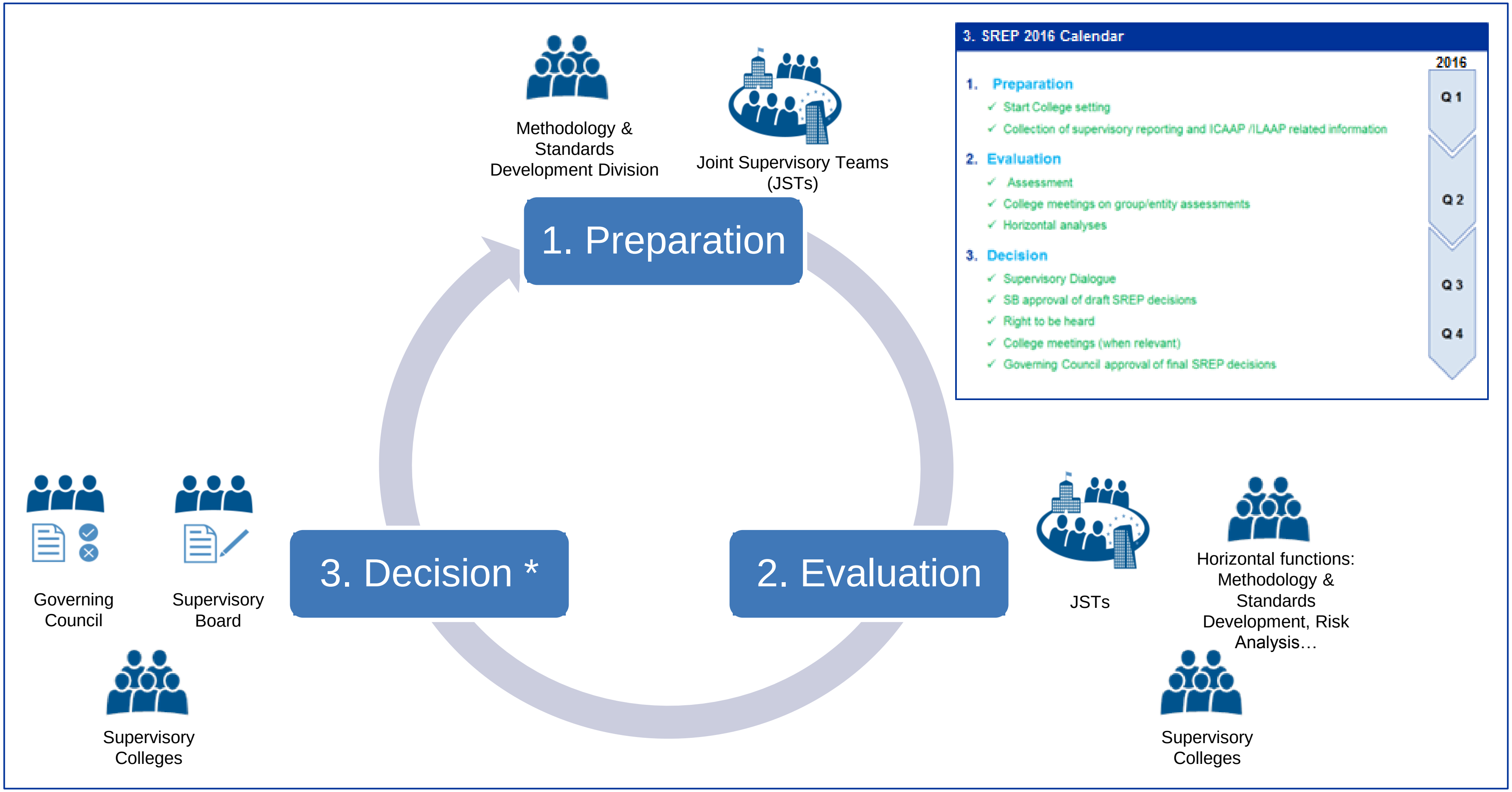
...the competent authorities shall review the arrangements, strategies, processes and mechanisms implemented by the institutions and evaluate:
(a) risks to which the institutions are or might be exposed;
(b) risks that an institution poses to the financial system; and
(c) risks revealed by stress testing taking into account the nature, scale and complexity of an institution's activities.

RTS, ITS and EBA Guidelines

- *Implementing Technical Standards (ITS) on joint decisions on prudential requirements – 16 October 2015*
- *Regulatory Technical Standards (RTS) and ITS on the functioning of colleges of supervisors – 16 October 2015*
- *Guidelines on common procedures and methodologies for the SREP (EBA/GL/2014/13) – 19 December 2014*
- *Opinion of the European Banking Authority on the interaction of Pillar 1, Pillar 2 and combined buffer requirements and restrictions on distributions – 16 December 2015*
- *EBA clarification of the use of 2016 EU-wide stress test results in the SREP process – 1 July 2016*

BCBS and FSB Principles

Supervisors at ECB and in 19 countries jointly prepared SREP decisions for SSM significant institutions through a common process



** Note: decision finalised after right-to-be-heard procedure and Governing Council non-objection*

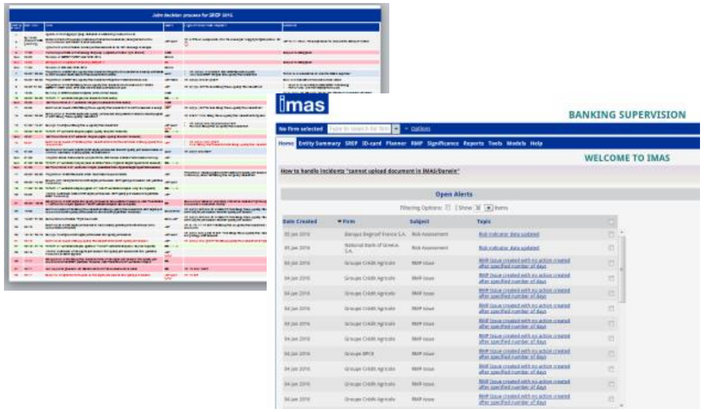
Underlying infrastructure built in less than one year

- common integrated IT system
- secured Information flow between all supervisors
- bank data quality controls at two levels: NCAs and ECB
- full use of NCA and ECB resources
- in-depth field testing of the methodology

Experienced supervisors from the ECB and NCAs:
- **19 Member States involved**
- **26 national authorities involved**

SREP managed as a key project

- common timeline
- steering by Senior Management
- project management, methodology development and horizontal consistency ensured by the ECB's DG MS IV
- full use of ECB and NCA expertise – especially in methodology development – through thematic workshops and dedicated Q&A sessions delivered by DG MS IV



Execution **fully in line** with plan
SREP completed in IT system

4.1. SREP – Methodology: common framework (1/3)

Building block approach in line with EBA Guidelines

SREP methodology at a glance: four key elements

SREP Decision

- Quantitative capital measures
- Quantitative liquidity measures
- Other supervisory measures

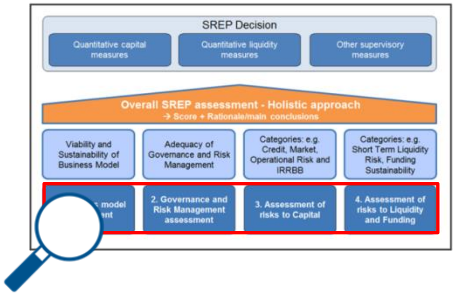
Overall SREP assessment – holistic approach

→ Score + rationale/main conclusions

1. Business model assessment	**2. Governance and risk management assessment**	**3. Assessment of risks to capital**	**4. Assessment of risks to liquidity and funding**
Viability and sustainability of business model	Adequacy of governance and risk management	Categories: e.g. credit, market, operational risk and IRRBB	Categories: e.g. short-term liquidity risk, funding sustainability

Feeds into the Supervisory Examination Programme (SEP)

All four SREP elements follow a common logic ensuring a sound risk assessment



Three phases in on-going risk assessment for each of four elements

Phase 1 Data gathering	Phase 2 Automated anchoring score	Phase 3 Supervisory judgement
Main sources: • quarterly ITS • STE reports	• Scoring risk level • Formal compliance checking of risk control	Adjustments based on additional factors and considering banks' specificities and complexity

Risk level (RL) vs. risk control (RC)

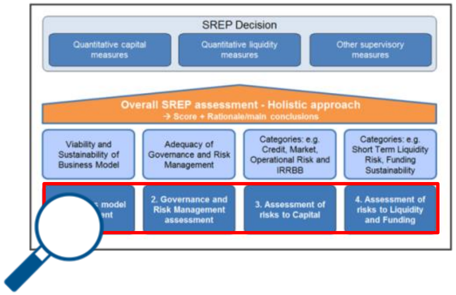
	1. Business model	2. Internal governance and RM	3. Assessment of capital risks	4. Assessment of liquidity risks
RL	✓	n/a	✓	✓
RC	n/a	✓	✓	✓

➡ **Combined score (RL + RC)**

n/a: not applicable

The intensity of the supervisory engagement is decided based on banks' risk profile and size

4.1. SREP – Methodology: common framework (3/3)



Constrained judgement

- Fair flexibility on a four-grade scale where Phase 2 score can be improved by one notch and worsened by two notches based on supervisory judgement

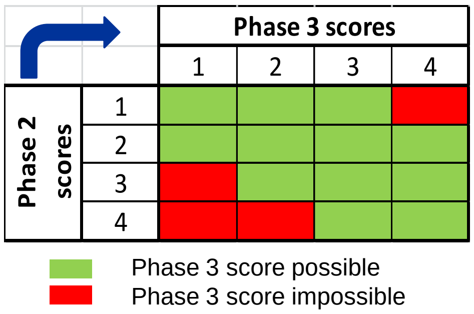
- Ensures the right balance between:
  - a common process, ensuring consistency across SSM banks and defining an anchor point
  - the necessary supervisory judgment, to take into account the specificities and complexity of an institution

- Adjustments go in both directions and are fully documented by the JST in the integrated IT system

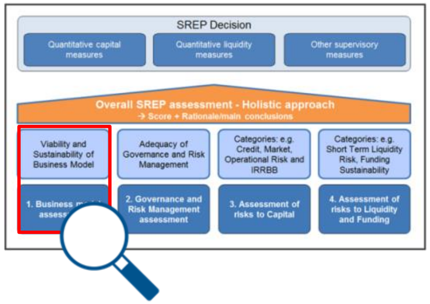
- Departing from constrained judgement not allowed as a rule

- Constrained judgment used ***effectively*** by JSTs for ***all*** risk categories ***in both directions*** – improving as well as worsening Phase 2 scores

Scale of the constrained judgement



4.2. SREP – Methodology: Element 1 (1/2)



Business model

- ➢ Identification of the areas of focus (e.g. main activities)
- ➢ Assessment of the business environment
- ➢ Analysis of the forward-looking strategy and financial plans
- ➢ Assessment of the business model
  - viability (within one year)
  - sustainability (within three years)
  - sustainability over the cycle (more than three years)
- ➢ Assessment of the key vulnerabilities

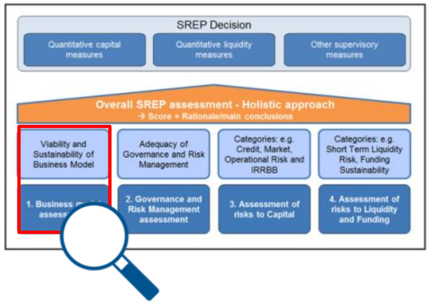
In line with EBA SREP Guidelines, § 55-57

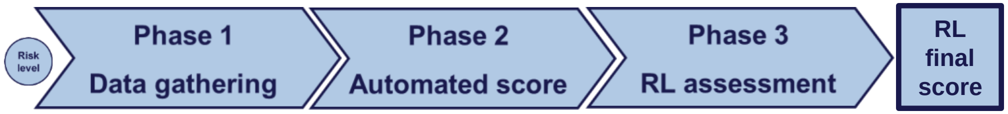
Examples of identified business models

- ➢ custodian
- ➢ diversified lender
- ➢ retail lender
- ➢ small universal bank
- ➢ specialised lender
- ➢ universal bank

4.2. SREP – Methodology: Element 1 (2/2)

Business model

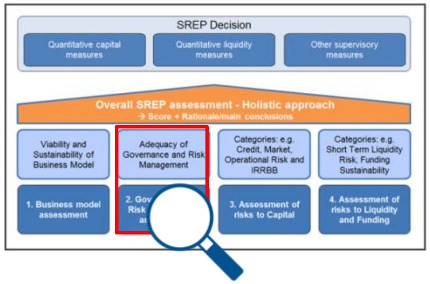




Phase 1	Phase 2	Phase 3
➢ **Information gathering and understanding materiality of business areas**	➢ **Automated anchoring score based on indicators, such as ROA, cost-to-income ratio, etc.**	➢ **Comprehensive analysis** ➢ **Used to adjust Phase 2 score taking into consideration the bank's specificities**

4.3. SREP – Methodology: Element 2 (1/2)

Internal governance and risk management



- Internal governance framework (including key control functions such as risk management, internal auditing and compliance)
- Risk management framework and risk culture
- Risk infrastructure, internal data and reporting
- Remuneration policies and practices

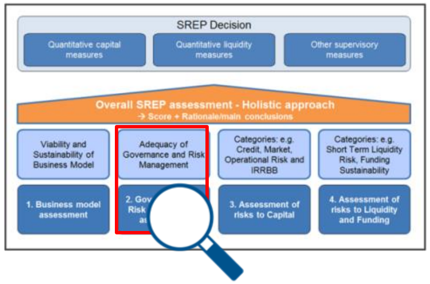
In line with EBA SREP Guidelines, § 81-82

Two examples of key questions

- Is there a compliance function in place that is hierarchically and functionally separate and operationally independent from any business activity responsibilities?
- Are there mechanisms in place to ensure that senior management can act in a timely manner to effectively manage, and where necessary mitigate, material adverse risk exposures, in particular those that are close to or exceed the approved risk appetite statement or risk limits?

4.3. SREP – Methodology: Element 2 (2/2)

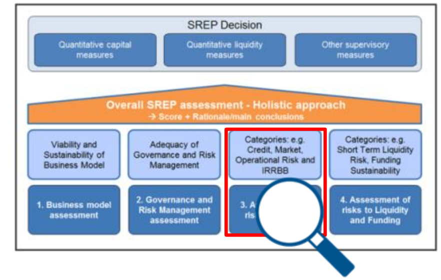
Internal governance and risk management



Risk control → **Phase 1** Information gathering → **Phase 2** Formal compliance checking → **Phase 3** RC main assessment → **RC final score**

Phase 1	Phase 2	Phase 3
➢ **Information gathering e.g. through the thematic review on risk governance and risk appetite (RIGA)**	➢ **Check compliance with CRD provisions** ➢ **Specific analysis of, for example:** • organisational structure • internal audit • compliance • remuneration • risk appetite • risk infrastructure • reporting	➢ **Comprehensive analysis** ➢ **Adjustment of Phase 2 check taking into consideration the bank's specificities** ➢ **Use of findings from thematic review on risk governance and risk appetite**

4.4. SREP – Methodology: Element 3 Overview



Risks to capital

Three different perspectives ("3 Blocks")

Block 1 Supervisory perspective	Block 2 Bank's perspective	Block 3 Forward-looking perspective
Four risk categories: credit risk, market risk, operational risk, IRRBB ✓ Information gathering ✓ Anchoring scores on risk categories ✓ Comprehensive analysis	✓ Information gathering: e.g. ICAAP reports ✓ Anchoring assessment: with proxies in line with the EBA Guidelines* ✓ Comprehensive analysis	✓ Information gathering: bank internal stress tests ✓ Anchoring assessment: supervisory stress tests ✓ Comprehensive analysis

For SREP 2016

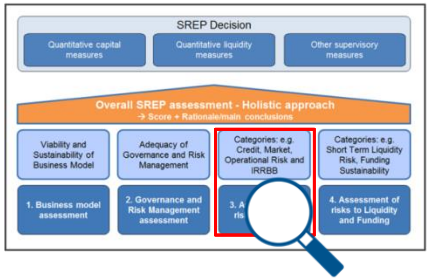
- ✓ Supervisory stress tests complemented the SREP tools
- ✓ ICAAP submission still very heterogeneous

In line with EBA SREP Guidelines

** SSM proxies implement the concept of supervisory benchmarks set out in the EBA Guidelines on SREP (§ 335)*

4.4.1. SREP – Methodology: Element 3 Block 1

Risks to capital – Block 1



Risk level	Phase 1 Data gathering	Phase 2 Automated score	Phase 3 RL assessment	RL final score
Risk control	Phase 1 Information gathering	Phase 2 Formal compliance checking	Phase 3 RC main assessment	RC final score

Deep-dive into a given risk factor: **credit risk** (example)

Phase 1

- **Risk level**
  - subset of pre-defined indicators calculated from ITS and STE data
- **Risk control**
  - information gathering

Phase 2

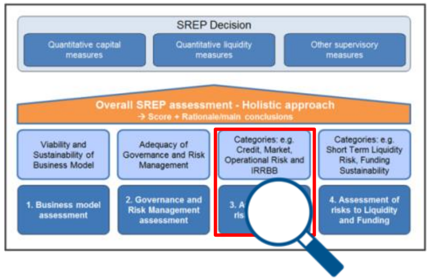
- **Risk level**
  - automated score given through different dimensions, such as:
    - quality (e.g. non-performing loans ratio)
    - coverage (e.g. provisions)
- **Risk control**
  - compliance checks relating to internal governance, risk appetite, risk management and internal audit of credit risk in particular

Phase 3

- **Risk level**
  - **comprehensive analysis, e.g.:**
    - current risk position and trend
    - forward-looking view
    - peer comparison
  - **in-depth analysis of various sub-categories, e.g.:**
    - non-financial corporate portfolios
    - household portfolios
- **Risk control**
  - deeper analysis, notably thanks to dedicated meetings with the bank

4.4.2. SREP – Methodology: Element 3 Block 2 (1/3)

Risks to capital – Block 2

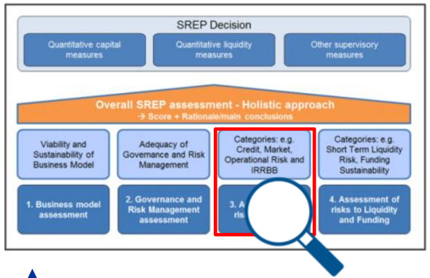


- ICAAP reliability assessment
- Following ECB ICAAP expectations published on 8 January 2016, JSTs:
  - assess reliability of the whole process – *qualitative assessment*
  - challenge ICAAP figures with SSM proxies – *quantitative assessment*
  - come up with Block 2 assessment to feed the overall capital adequacy assessment

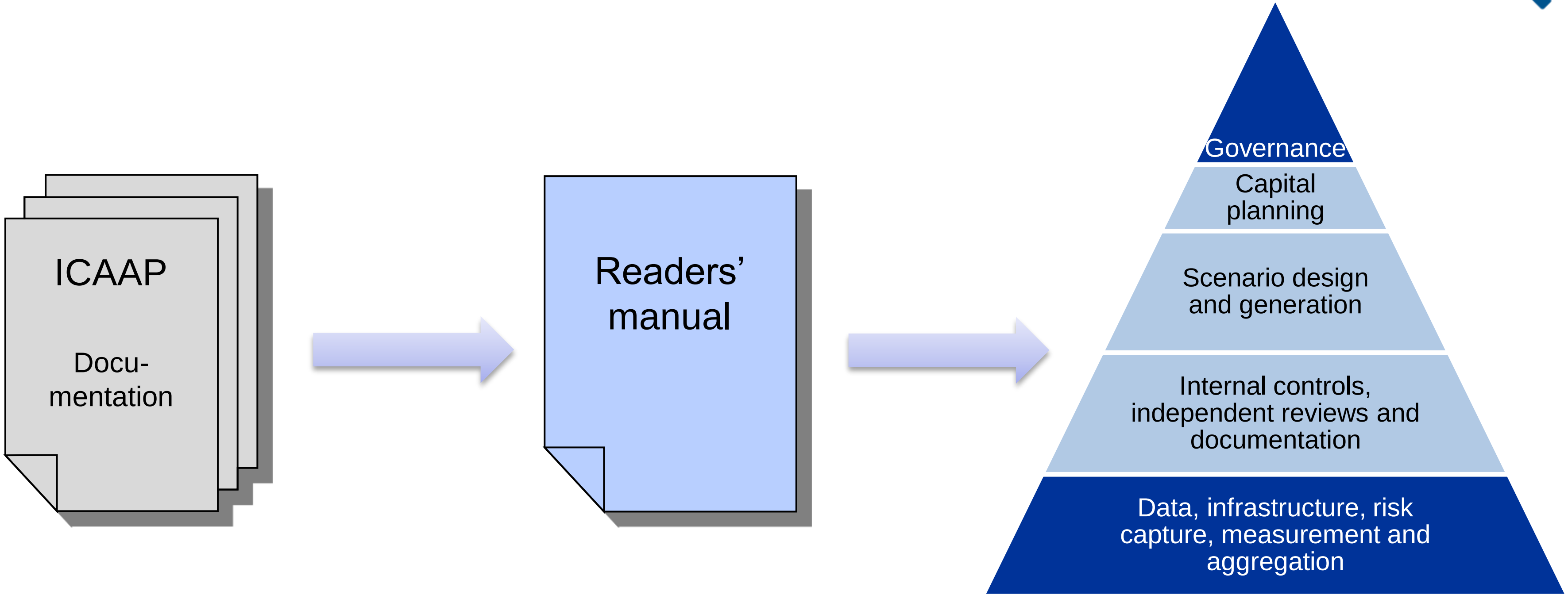
ECB ICAAP expectations

- Content as described in EBA Guidelines on ICAAP and ILAAP information
- Internal documentation together with a "readers' manual"
- Risk data template
- Reconciliation between Pillar 1 and ICAAP figures
- Conclusions in form of capital adequacy statements supported by analysis of ICAAP outcomes and signed by management body

4.4.3. SREP – Methodology: Element 3 Block 2 (2/3)



ICAAP – Qualitative assessment



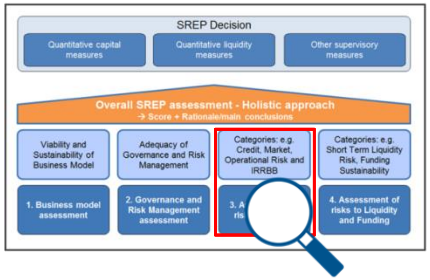
Bank-internal documents as set out in EBA GL

Mapped to EBA GL structure to facilitate JST access to bank-internal information

JST assessment

→ **Decision on ICAAP reliability**

4.4.4. SREP – Methodology: Element 3 Block 2 (3/3)



ICAAP – Quantitative assessment

ICAAP risk data

Risk definition and ICAAP estimates according to banks' own risk taxonomy

Mapping of internal risk categories to SSM risk map and information on internal capital

Please provide the information and data only as internally available. Do not change or produce internal numbers only for filling column 1.5 of the template. If the cell is not applicable to the institution, please complete as "na" for not applicable. Only white cells can be filled in.

SSM Risk Map		ICAAP information				
1.1 Risk categories	**1.2 Risk sub-category** (thereof: ...)	**1.3 Name of internal risk category as currently covered in ICAAP** (please use categories and sub-categories as available internally and map them to the given risk categories and sub-categories as possible; for risk categories or sub-categories not covered in the SSM risk map please use the rows named "other")	**1.4 Short description of internal Risk category** (including sub-categories that may be included)	**1.5 ICAAP estimate - internal capital needed (ly view) in EUR** (please only provide numbers as internally available)	**1.6 Have there been material changes in scope or quantification methodology for this risk category / sub-category since the last reporting date? (y/n)**	**1.7 Pl**
Credit risk						
	credit risk (please use this row in case several sub-categories are quantified together, i.e. no separate estimates are available)					
	default risk					
	credit concentration risk					
	FX lending risk					
	Securitisation risk					
	Country risk (includes transfer & other risks)					
	settlement and delivery risk					
	residual risk					
	migration risk					

Proxies*

- Give rough quantification of capital demand
- Allow JSTs to put institutions' estimates in perspective and underpin supervisory dialogue
- Do not provide a single figure, but indicative ranges for JSTs to derive risk-by-risk capital figures based on their judgement

* *Concentration risk (single name and sectoral), market risk, credit risk, IRRBB*

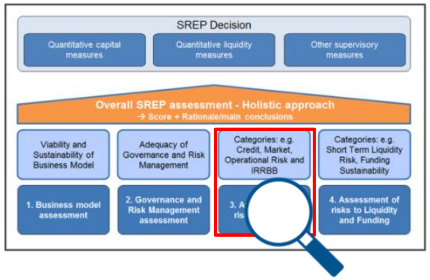
Assessment

Internal capital-adjusted figure (capital requirements)

- Pillar 1 as floor
- No inter-risk diversification

Dialogue with banks

4.4.5. SREP – Methodology: Element 3 Block 3 (1/4)



Risks to capital

- Forward-looking perspective
- In 2016, two large-scale stress test exercises

EU-wide EBA stress test

- **37 SSM Significant Institutions**
- **Publication** of results
- EU-wide exercise under **EBA coordination**, in cooperation with EU-COM, ESRB, ECB and NCAs
- Timeline: March-July **2016**

SSM SREP stress test

- **56** other **SSM Significant Institutions**[1]
- Results are **not public**
- Under **ECB/SSM coordination**
- Timeline and methodology **broadly aligned with EBA Stress Test**

Objectives

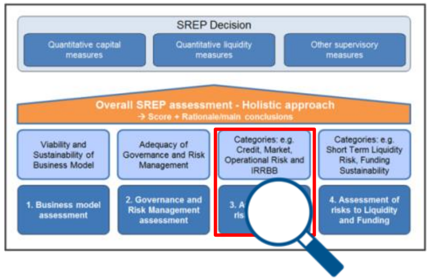
- Assessed the **resilience of financial institutions** to adverse market developments
- **Contributed to the overall SREP** to ensure institutions' capital and liquidity adequacy, as well as sound risk coverage and internal processes
- Ensured **consistent treatment** of all SIs supervised by the SSM

The results of both exercises fed into the SSM SREP

1) Combined number of SIs included in EBA and SSM SREP stress test samples does not equal total number of SIs under SSM supervision, as some exceptions apply (e.g. banks that were subject to a comprehensive assessment in 2015 or will be in 2016, or SIs that are subsidiaries of other SSM SIs, already covered at the highest level of consolidation).

4.4.5. SREP – Methodology: Element 3 Block 3 (2/4)

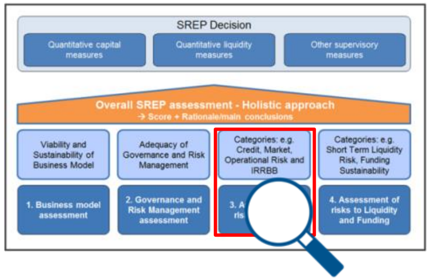
Risks to capital



As communicated by the EBA on 1 July 2016, SREP decisions of 2016 are composed of a **Pillar 2 Requirement (P2R)** and **Pillar 2 Guidance (P2G)**

- Banks are **expected to meet the P2G**, which is set **above the level of binding capital** (minimum and additional) requirements and on top of the combined buffers
- If a bank **will not meet its P2G**, this will **not result in automatic action of the supervisor** and will **not be used to determine the MDA trigger**, but will be used in fine-tuned measures based on the individual situation of the bank
- In order to assess the final measures taken, the **Supervisory Board will assess every case of a bank not meeting its P2G**

4.4.5. SREP – Methodology: Element 3 Block 3 (3/4)



Risks to capital

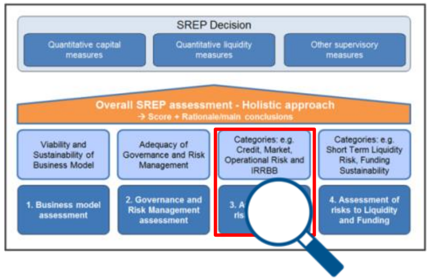
The stress test is used as a crucial input into the SREP process:

- **Qualitative outcome** of the stress test is **included in the determination of the P2R**, especially in the element of risk governance
- **Quantitative impact** of the adverse stress test is one **input factor into determining the level of P2G**

When setting P2G different elements are taken into account in a **holistic view**, for example:

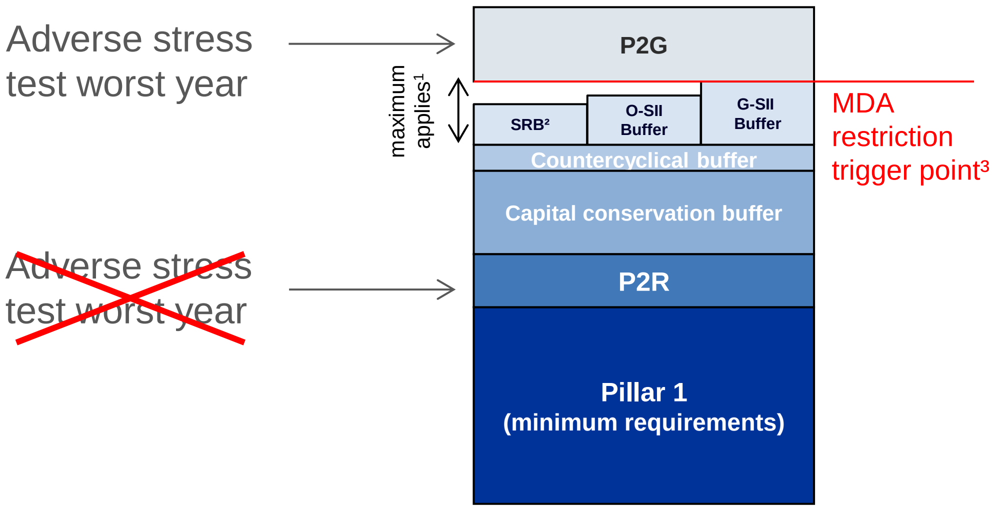
- in general, the **depletion of capital** by the stress test in the hypothetical **adverse scenario**
- the **specific risk profile** of the individual institution and its **sensitivity towards the stress scenarios**
- **interim changes in its risk profile** since the cut-off date (31 December 2015) and **measures taken by the bank** to mitigate risk sensitivities, such as relevant sale of assets, etc.

Implement adverse stress test results for the worst year only in P2G



Adverse stress test results for the worst year only in P2G

** Scale not meaningful*



1 Most common case; specific calculation may occur depending on implementation of CRD IV Article 131(15) by Member State

2 Systemic risk buffer

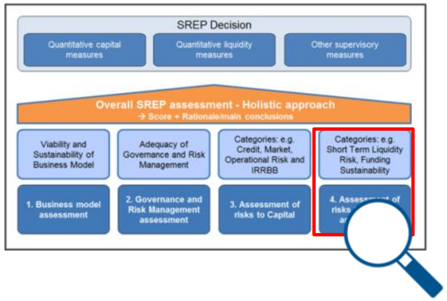
3 The ECB draws attention to the following:

- Under Regulation (EU) No 596/2014 of the European Parliament and of the Council (MAR), those institutions that have publicly traded securities are expected to evaluate whether Pillar 2 requirements meet the criteria of inside information and should be publicly disclosed
- The EBA opinion of 16 December 2015 which says "Competent Authorities should consider using the provisions of Article 438 (b) of the CRR to require institutions to disclose MDA-relevant capital requirements […], or should at least not prevent or dissuade any institution from disclosing this information"

In the light of the above, the ECB neither prevents nor dissuades institutions from disclosing MDA-relevant capital requirements.

Note: Implementation of EBA opinion on MDA and 1 July 2016 press release

4.5. SREP – Methodology: Element 4 Overview



Risks to liquidity

Three different perspectives ("3 Blocks")

Block 1 Supervisory perspective	Block 2 Bank's perspective	Block 3 Forward-looking perspective
Short-term liquidity, funding sustainability ✓ Information gathering ✓ Anchoring scores on short-term liquidity and funding sustainability risks ✓ Comprehensive analysis	✓ Information gathering: e.g. ILAAP reports ✓ Anchoring assessment: challenge the institution's internal estimates ✓ Comprehensive analysis: e.g. of ILAAP reliability	✓ Information gathering: bank internal stress tests ✓ Anchoring assessment: supervisory stress tests ✓ Assessment of supervisory stress test results and of bank's internal stress tests

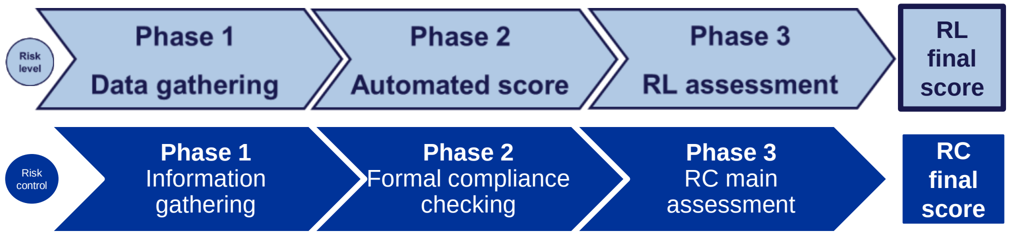
For SREP 2016

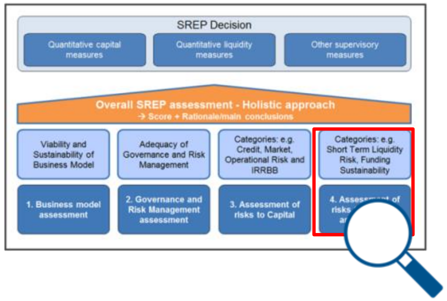
- ✓ Strongest weight on Block 1
- ✓ Block 2 – a lot of heterogeneity in ILAAP
- ✓ Block 3 not yet fully fledged

In line with EBA SREP Guidelines, § 370-373

4.5.1. SREP – Methodology: Element 4 Block 1

Risks to liquidity – Block 1





Deep-dive into a given risk factor: **short-term liquidity** (example)

Phase 1

- **Risk level**
  - subset of pre-defined indicators based on ITS and STE data
- **Risk control**
  - information gathering

Phase 2

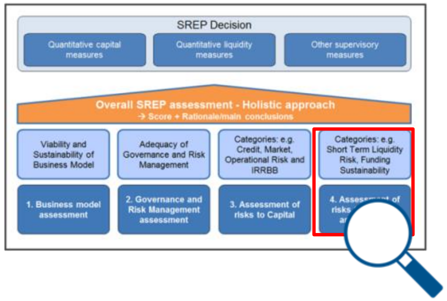
- **Risk level**
  - automated score given through several indicators, such as:
    - liquidity coverage ratio
    - short-term funding/total funding
- **Risk control**
  - compliance checks relating to internal governance, risk appetite, risk management and internal audit

Phase 3

- **Risk level**
  - **deeper analysis:**
    - short-term wholesale funding risk
    - intraday risk
    - quality of liquidity buffers
    - structural funding mismatch
- **Risk control**
  - deeper analysis, notably thanks to dedicated meetings with the bank

4.5.2. SREP – Methodology: Element 4 Block 2 and 3 (1/2)

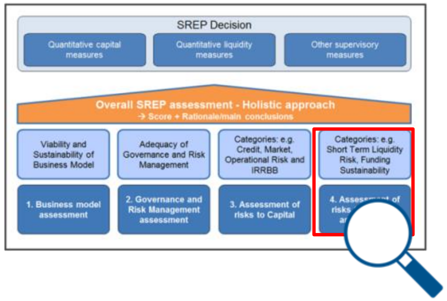
Risks to liquidity – Block 2 and 3



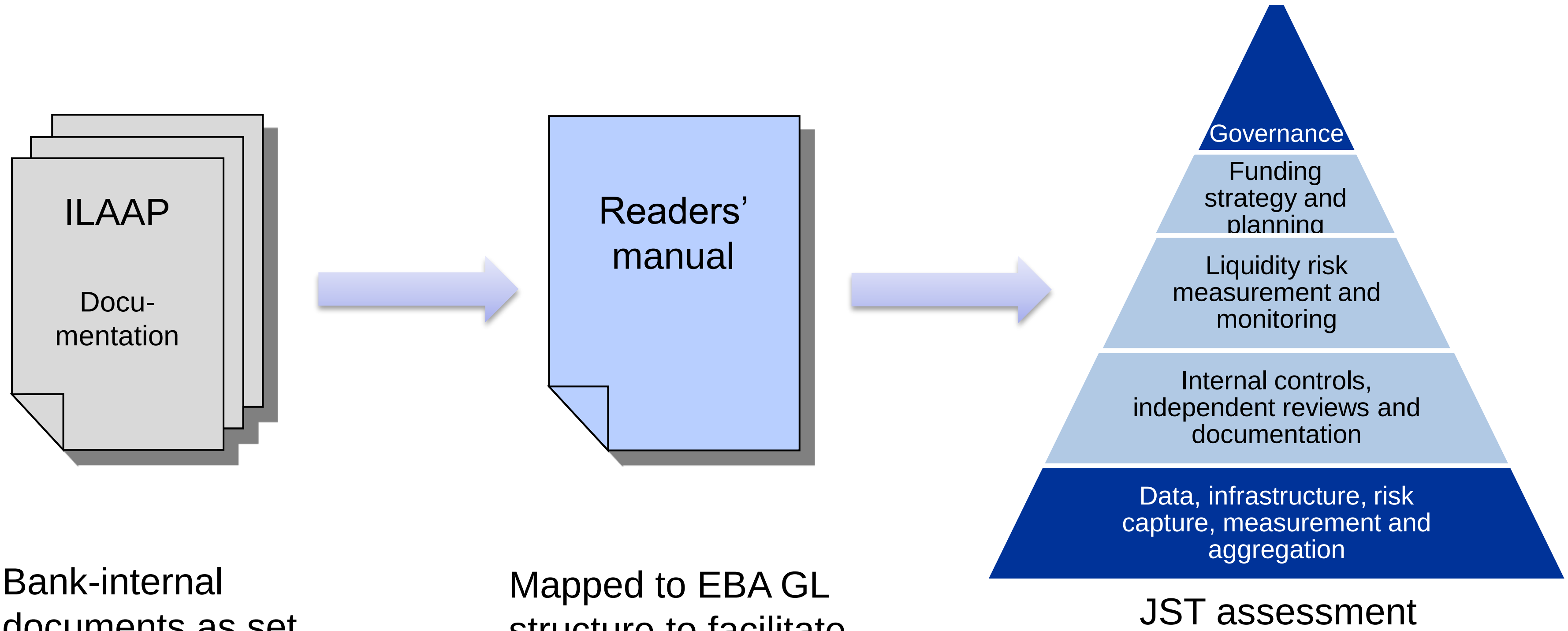
- ILAAP reliability assessment
- Following ECB ILAAP expectations published on 8 January 2016, JSTs:
  - assess reliability of the whole process – *qualitative assessment*
  - challenge ILAAP needs and stress test assumptions with SSM proxies – *quantitative assessment*
  - come up with Block 2 and 3 assessment to feed the overall liquidity adequacy assessment

ECB ILAAP expectations

- Content as described in EBA Guidelines
- Internal documentation together with a “readers’ manual”
- Conclusions in the form of liquidity adequacy statements supported by analysis of ILAAP outcomes and signed by management body



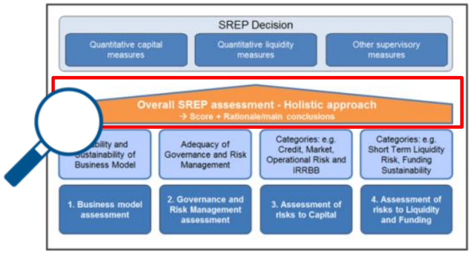
ILAAP – Qualitative assessment



Bank-internal documents as set out in EBA GL

Mapped to EBA GL structure to facilitate JST access to bank-internal information

→ Decision on ILAAP reliability



The overall SREP assessment (holistic view)

- Provides synthetic overview of an institution’s risk profile:
  - based on the assessment of all four elements (not the simple sum)
  - as a starting point, the four SREP elements are considered equally important
- Takes into account:
  - the institution’s capital/liquidity planning to ensure a sound trajectory towards the full implementation of CRD IV/CRR
  - peer comparisons
  - the macro environment under which the institution operates

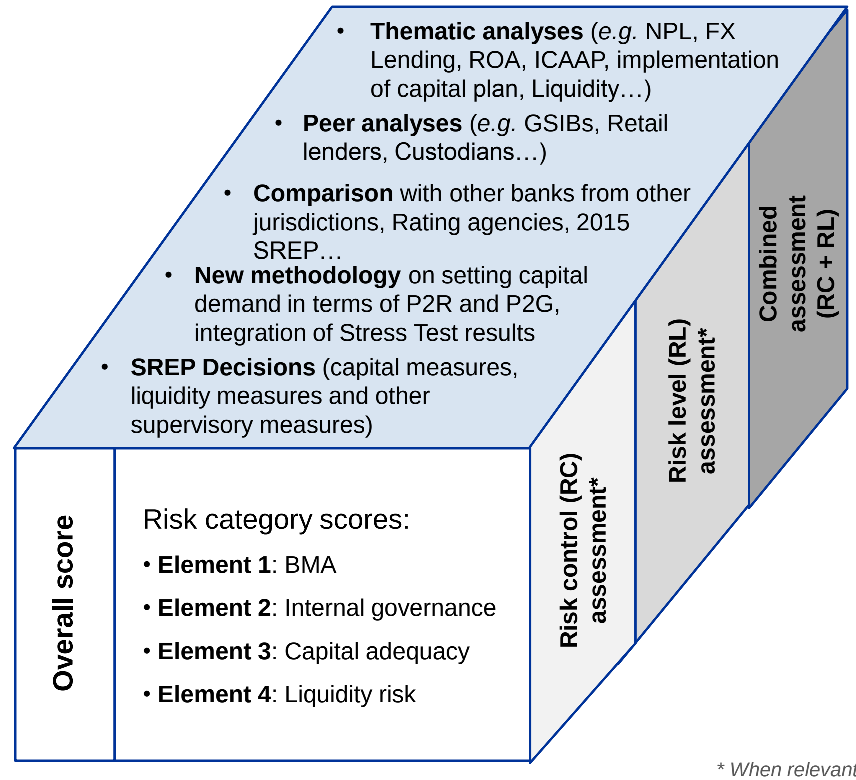
In line with the EBA SREP Guidelines (table 13, pp. 170 and 171), the overall SREP score reflects the supervisor’s overall assessment of the viability of the institution: higher scores reflect an increased risk to the viability of the institution stemming from one or several features of its risk profile, including its business model, its internal governance framework, and individual risks to its solvency or liquidity position

An institution’s risk profile is necessarily **multi-faceted**, and many risk factors are **inter-related**

Consistent and fair treatment

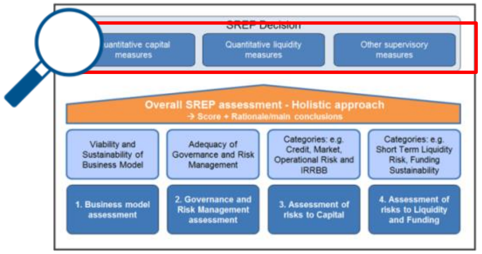
- **High number of horizontal analyses** performed when preparing assessments and decisions in order to provide:
  - additional perspectives to JSTs
  - support for policy discussions and the decision-making process

SREP Horizontal Analysis: multi-dimension analyses



** When relevant*

Extensive peer comparisons and transversal analyses were possible on a wide scale, allowing all institutions to be assessed in a **consistent manner** and thus promoting a **more integrated single banking market**.



The overall SREP is the basis for assessing capital and liquidity adequacy and for taking any necessary supervisory measures to address concerns

- SREP decisions by the Supervisory Board (followed by Governing Council non-objection procedure)
- SREP decisions may include:

Own fund requirements

- total SREP Capital Requirement (TSCR) composed of minimum own fund requirements (8%[1]) and additional own fund requirements (P2R[2])
- combined buffer requirements (CBR[2])
- recommendation to follow a linear path towards "fully loaded" ratios

Institution-specific quantitative liquidity requirements

- LCR higher than the regulatory minimum
- higher survival periods
- national measures

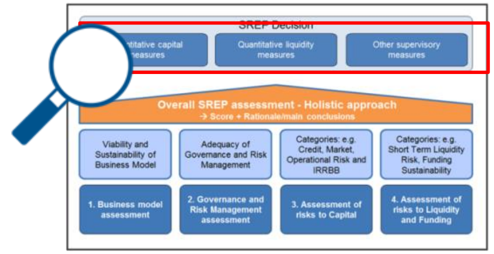
Other, qualitative supervisory measures

- additional supervisory measures stemming from Article 16(2) of the SSM Regulation include, for example, the restriction or limitation of business, the requirement to reduce risks, the restriction or prior approval to distribute dividends and the imposition of additional or more frequent reporting obligations

- SREP communication also includes P2G expressed as CET1 ratio add-on

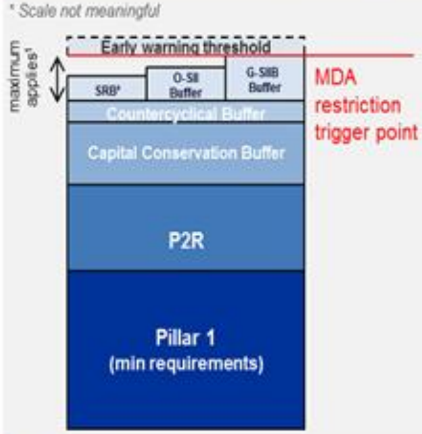
[1] At least 56.25% in CET1
[2] CET 1 only

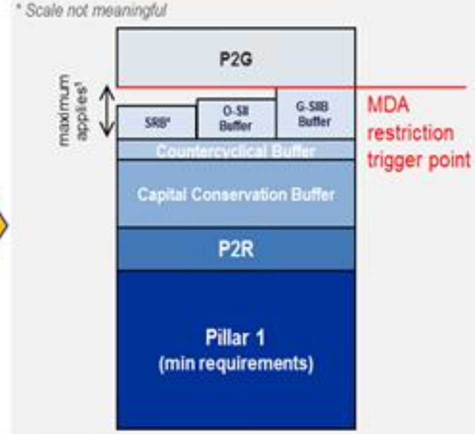
SREP decision – capital measures



	SREP 2015	SREP 2016
Pillar 2	• Pillar 2 (MDA relevant)	• Pillar 2 Requirements (P2R) (MDA relevant) • Pillar 2 Guidance (P2G) (not MDA relevant)
Capital Conservation Buffer (CCB)	• Overlap with Pillar 2 (Gross Pillar 2)	• No overlap with Pillar 2

CET1 Stacking order





	SREP 2015	SREP 2016
Capital composition	• Pillar 2: 100% CET1	• P2R & P2G: 100% CET1
SREP decision	• CET1 ratio	• P2R: CET1 ratio and Total SREP Capital Requirements (TSCR)[3] • P2G: CET1 ratio add-on

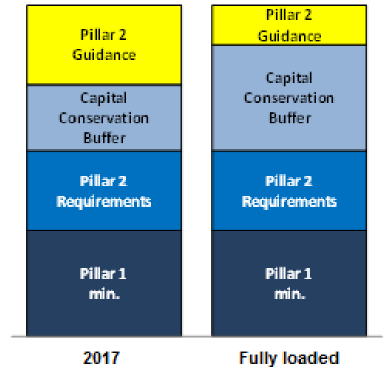
1 Most common case; specific calculation may occur depending on implementation of CRD IV Article 131(15) by Member State
2 Systemic risk buffer
3 If there is a shortfall of Pillar 1 (AT1/T2) requirement, this has to be covered by additional CET1 in P2R (but, for 2017, not in P2G)
Note: Implementation of EBA opinion on MDA and 1 July 2016 press release

4.8. SREP – Methodology: SREP decision and capital planning (3/5)

All things being equal, the current capital demand in the system also provides an indication for the future

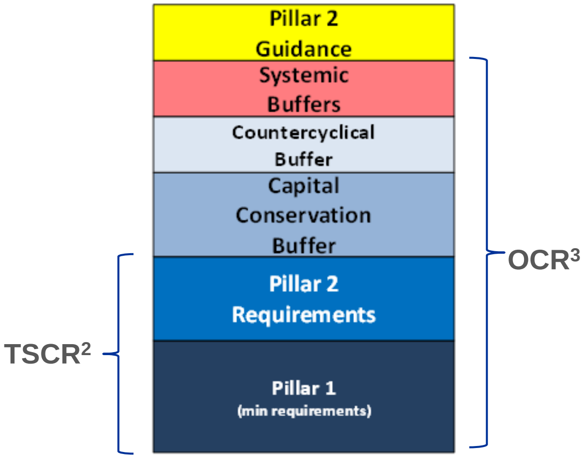
- All other things being equal, the capital demand can be expected to remain broadly stable[1]
- If a credit institution operates or expects to operate below Pillar 2 Guidance it should immediately contact its joint supervisory team
- Banks also need to take into account the systemic buffers (G-SII, O-SII and systemic risk buffers) and the countercyclical buffer that are part of the capital stack

SREP CET1 demand[1]



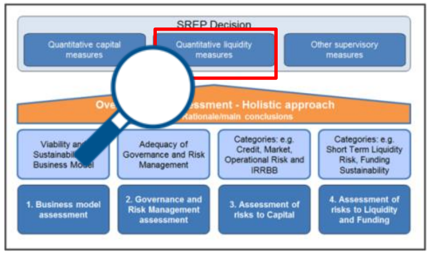
* Scale not meaningful

Capital Stack



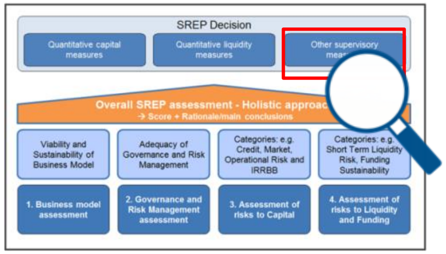
* Scale not meaningful

[1] Capital demand means Pillar 1 plus P2R, CCB and P2G. Irrespective of the phasing-in of the CCB, banks should also expect to have positive P2G in the future.
[2] *TSCR: total SREP capital requirements*
[3] *OCR: overall capital requirements*



SREP decision – liquidity measures

- LCR requirements came into force on 1 October 2015
- Examples of specific liquidity measures include:
  - LCR higher than the regulatory minimum
  - specific minimum survival period
  - minimum amount of liquid assets



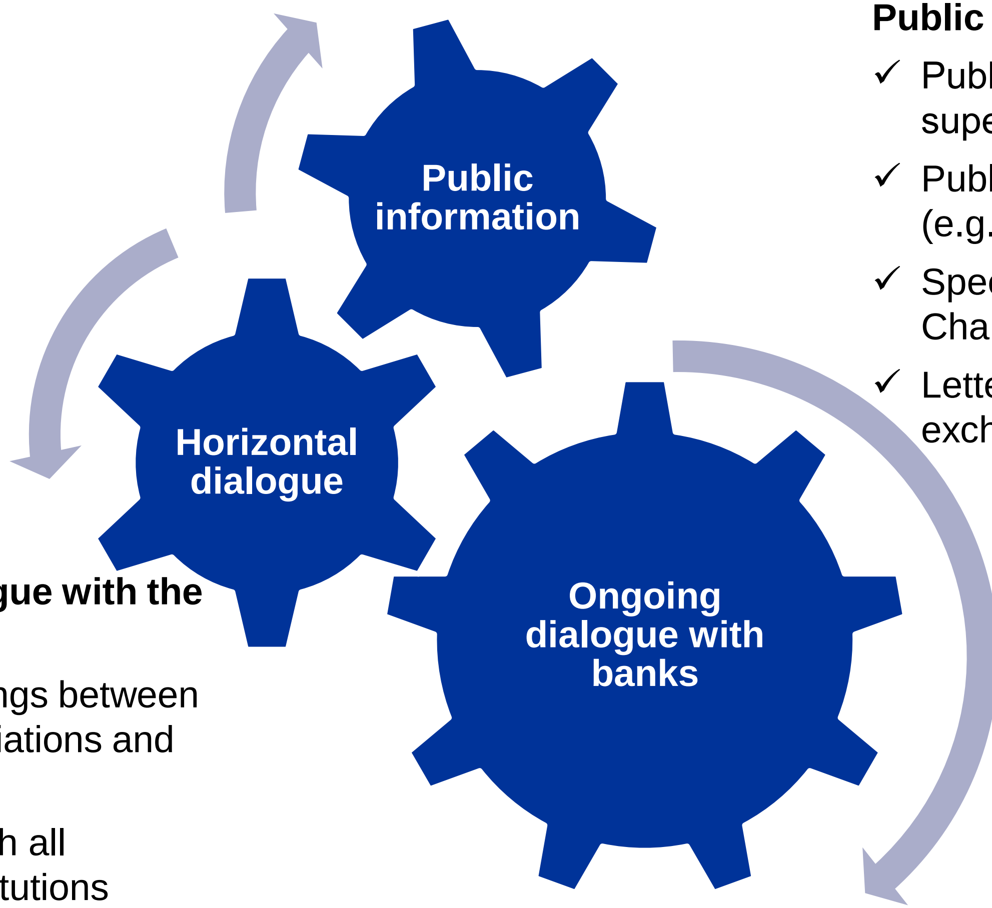
SREP decision – other supervisory measures

Article 16(2) of the SSM Regulation

The ECB has the following powers:

(a) to require institutions to hold own funds in excess of the capital requirements
(b) to require the reinforcement of the arrangements, processes, mechanisms and strategies
(c) to require institutions to present a plan to restore compliance with supervisory requirements and set a deadline for its implementation (…)
(d) to require institutions to apply a specific provisioning policy or treatment of assets in terms of own funds requirements
(e) to restrict or limit the business, operations or network of institutions or to request the divestment of activities that pose excessive risks to the soundness of an institution
(f) to require the reduction of the risk inherent in the activities, products and systems of institutions
(g) to require institutions to limit variable remuneration (…)
(h) to require institutions to use net profits to strengthen own funds
(i) to restrict or prohibit distributions to shareholders, members or holders of Additional Tier 1 instruments where the prohibition does not constitute an event of default of the institution
(j) to impose additional or more frequent reporting requirements (…)
(k) to impose specific liquidity requirements, including restrictions on maturity mismatches between assets and liabilities
(l) to require additional disclosures
(m) to remove at any time members from the management body of credit institutions

4.9. SREP – Methodology: SREP communication and transparency (1/3)



Public information

- ✓ Published "Guide to banking supervision"
- ✓ Publication of ECB stances (e.g. on MDA, remuneration, etc.)
- ✓ Speeches by Supervisory Board Chair and Vice-Chair
- ✓ Letters to MEPs, hearings and exchange of views with MEPs

Horizontal dialogue with the industry

- ✓ Regular meetings between banking associations and DG MS IV
- ✓ Workshops with all significant institutions

Ongoing dialogue with banks

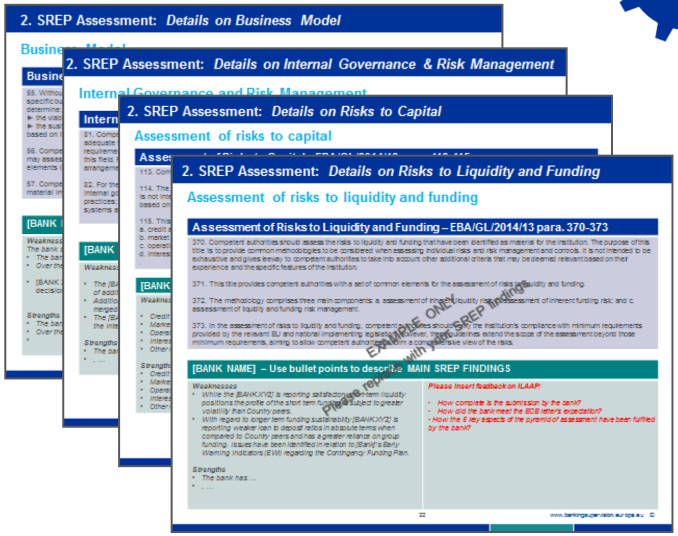
- ✓ Supervisory Examination Programme
- ✓ Meetings between banks and JSTs (especially ahead of SREP decision – supervisory dialogue)
- ✓ SREP decisions (right to be heard)

Banks have:

- ✓ the necessary clarity to understand the methodology and risk assessment, and to take the measures required to improve
- ✓ the necessary certainty to perform their capital planning

4.9. SREP – Methodology: SREP communication and transparency (2/3)

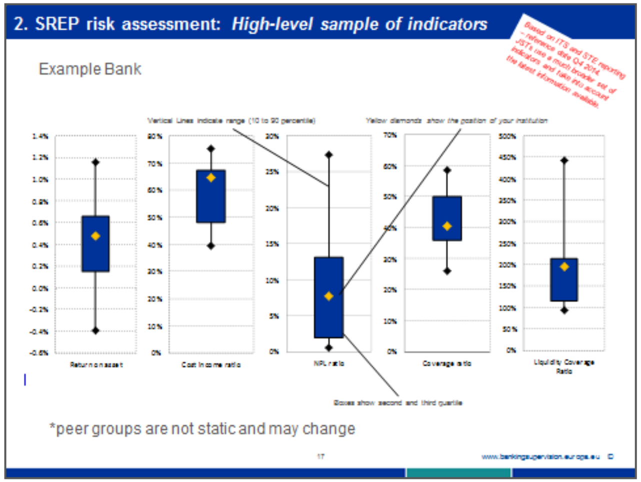
Enhanced ongoing dialogue with banks



SREP communication pack

Shared with all significant institutions to ensure consistency and quality across the euro area:

- indication of the key drivers of the possible decisions (e.g. capital, liquidity and other qualitative specific measures)
- review of the stress test outcomes
- peer comparison of key indicators

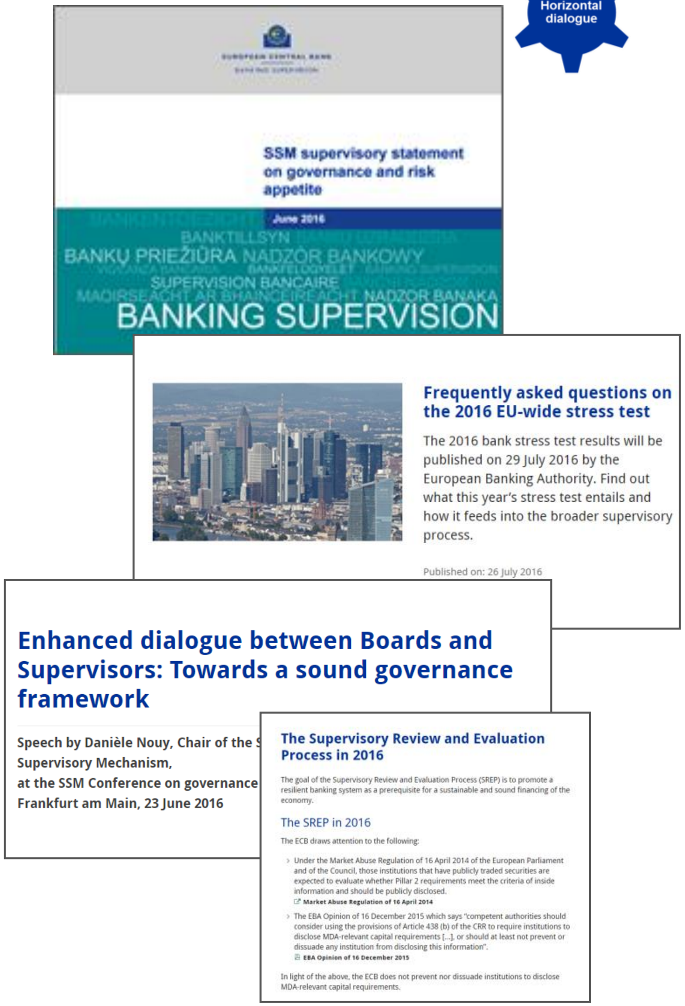


4.9. SREP – Methodology: SREP communication and transparency (3/3)

Enriched public communication and horizontal dialogue

During the 2016 SREP cycle the SSM increased the transparency of the process as well as that towards new developments and priorities:

- January: publication of SSM priorities
- January: SREP Workshops with CEOs
- June: ECB report on governance and risk appetite framework
- July: detailed communication on the 2016 stress test results and impacts on SREP – conference calls with banks' heads of communications, analysts and media
- September: implementation of EBA opinion on disclosure of SREP results
- November: Chair's hearing at the European Parliament
- Throughout the cycle, many meetings with banking associations



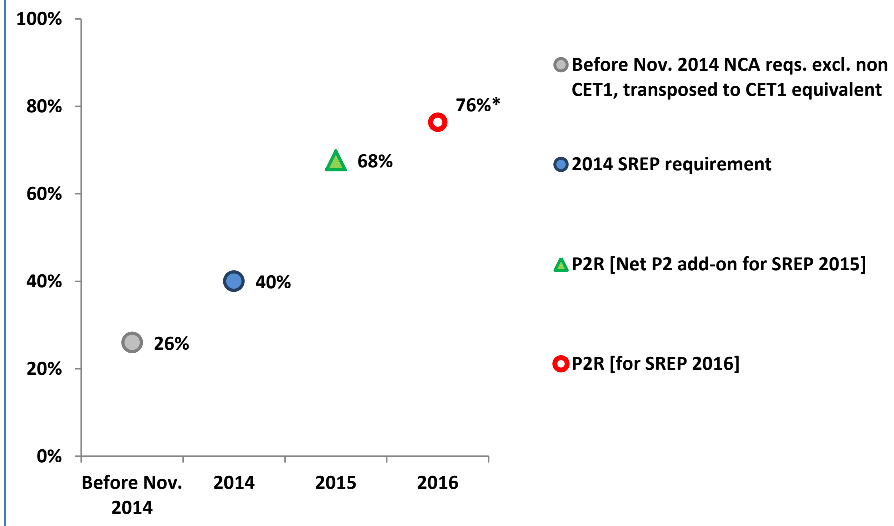
5. SREP – Where do we stand?

The second SREP cycle could be performed efficiently and promoted a level-playing field

- **Significant harmonisation**
  - constrained judgment was used effectively
  - stronger correlation between risk profile of institutions and capital requirements

- **In 2016 certain aspects of the SREP methodology are being refined, such as:**
  - liquidity and funding risk assessment
  - more harmonised framework for the assessment of ICAAP
  - 2016 stress tests and the introduction of capital guidance

Correlation between P2R and overall SREP scores



* Correlation is lower for 2016 when compared with the total CET1 demand (including P2G)

- **The SREP methodology will continue to evolve so as to adequately monitor banking activities and risks in a forward-looking manner**

Based on banks with a final SREP 2016 decision as of 30 November 2016