



EUROPEAN CENTRAL BANK

BANKING SUPERVISION

SSM SREP Methodology Booklet

- 2017 edition – to be applied in 2018 -

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

- **Level playing field:** SREP is currently being executed for **the third 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

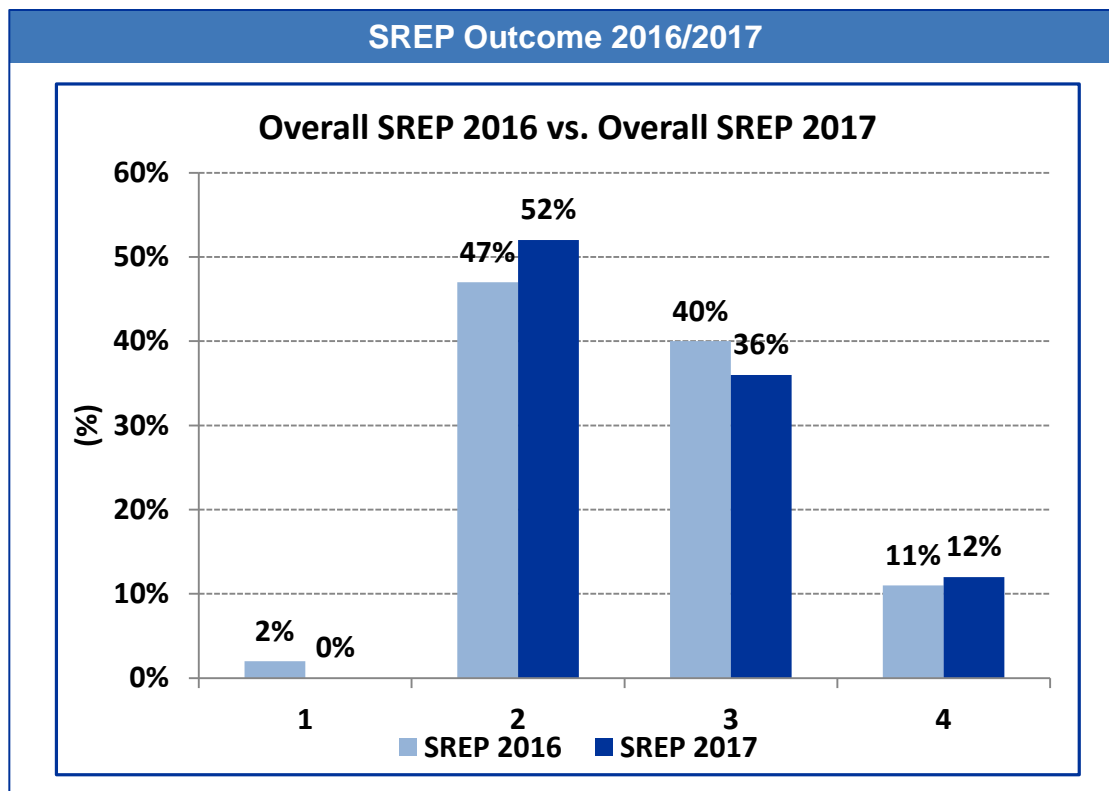
- **Sound risk assessment:**
 - **combination of quantitative and qualitative elements**
 - **holistic assessment** of institutions' viability taking into account their specificities
 - **forward-looking perspective**, e.g. stress tests performed in 2016, Sensitivity Analysis of IRRBB – Stress test 2017

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In 2017 the SSM carried out its third SREP cycle for SIs in 19 countries

- Risks fairly stable compared to last year, leading to a relatively stable aggregate risk profile, but:
 - Profitability remains an issue
 - High Level of NPL is still a point of attention
 - ICAAP and ILAAP to be further improved by banks



Notes:

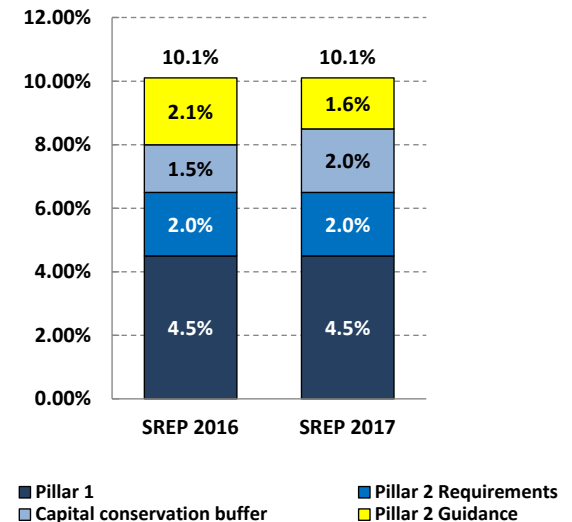
- SREP 2017 values based on 105 banks with SREP 2017 decisions finalised as of 30 November 2017.
- SREP 2016 values based on 106 banks with SREP 2016 decisions finalised as of 30 November 2016 and presented in the SSM SREP Methodology Booklet – 2016 edition.

Overall consistency in CET1 demand from SREP 2016 to SREP 2017

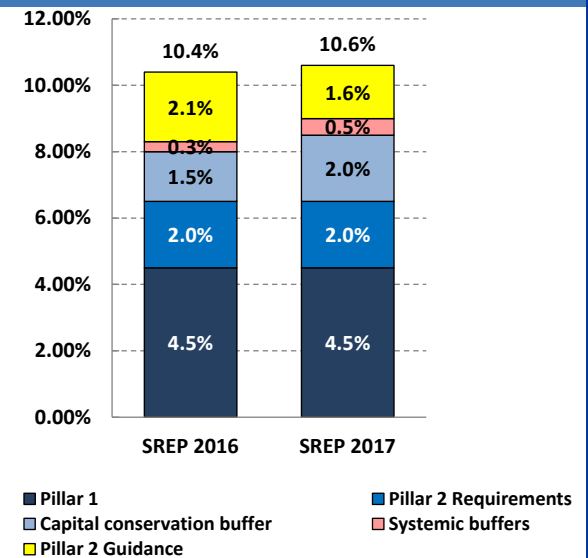
- Overall, envisaged CET1 demand (excluding systemic buffers) is stable compared to last year (10.1%).
- Beyond the stability of the overall CET1 capital demand, there is a significant number of idiosyncratic changes up and down

- Notes:
- Simple averages. Using RWA weighted averages, CET1 demand, excl. systemic buffers, increases also by 10 bp, from 9.5% to 9.6%.
 - CET1 demand is computed without taking into account the need to cover also Pillar 1 AT1/T2 in case of shortage of AT1 and T2.
 - SREP 2017 values based on SREP 2017 decisions finalised as of 30 November 2017.
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CET1 demand (excl. systemic buffers)

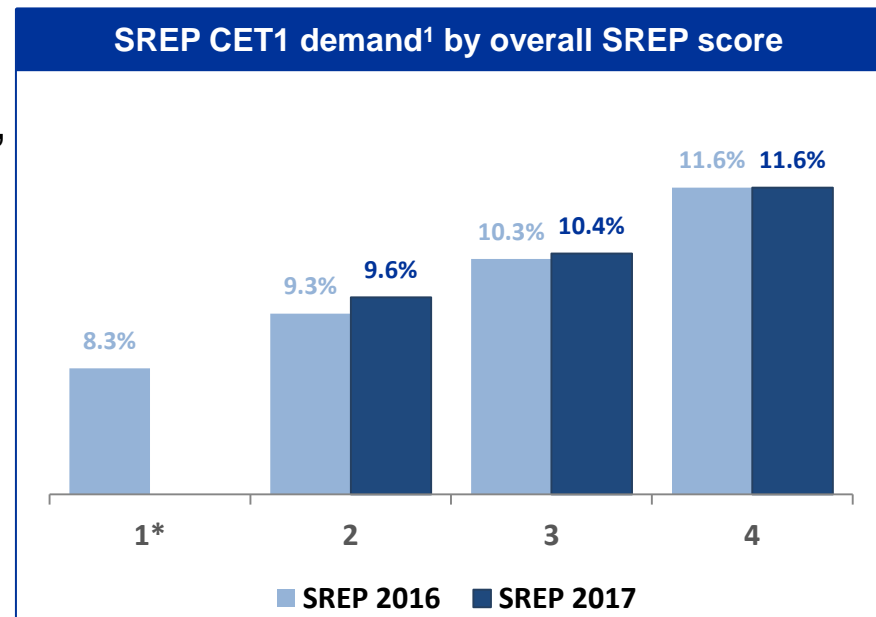


CET1 demand (incl. systemic buffers)



SREP CET1 demand per score comparable to 2016

- In line with SREP 2016 achievements, SREP 2017 CET1 demand increases consistently with higher SREP scores



Notes:

¹ Pillar 1 + Pillar 2 Requirement + Capital conservation buffer + Pillar 2 Guidance. Excludes systemic buffers (G-SII, O-SII and systemic risk buffer)

Notes:

- SREP 2017 values based on SREP 2017 decisions finalised as of 30 November 2017.
- SREP 2016 values based on SREP 2016 decisions finalised as of 30 November 2016 and presented in the SSM SREP Methodology Booklet – 2016 edition.

* No institution with SREP overall score of 1 in SREP 2017.

Liquidity measures

39 banks with envisaged **liquidity related measures** have been identified

- There are 35 banks with only qualitative liquidity SREP requirements. The requirements are diverse and relating to a broad area of topics within liquidity risk management e.g. improvement of the ILAAP
- There are 2 banks with both qualitative and quantitative liquidity SREP requirements (e.g. FX-denominated liquidity buffers)
- There are 2 banks with only quantitative liquidity SREP requirements

Other qualitative measures

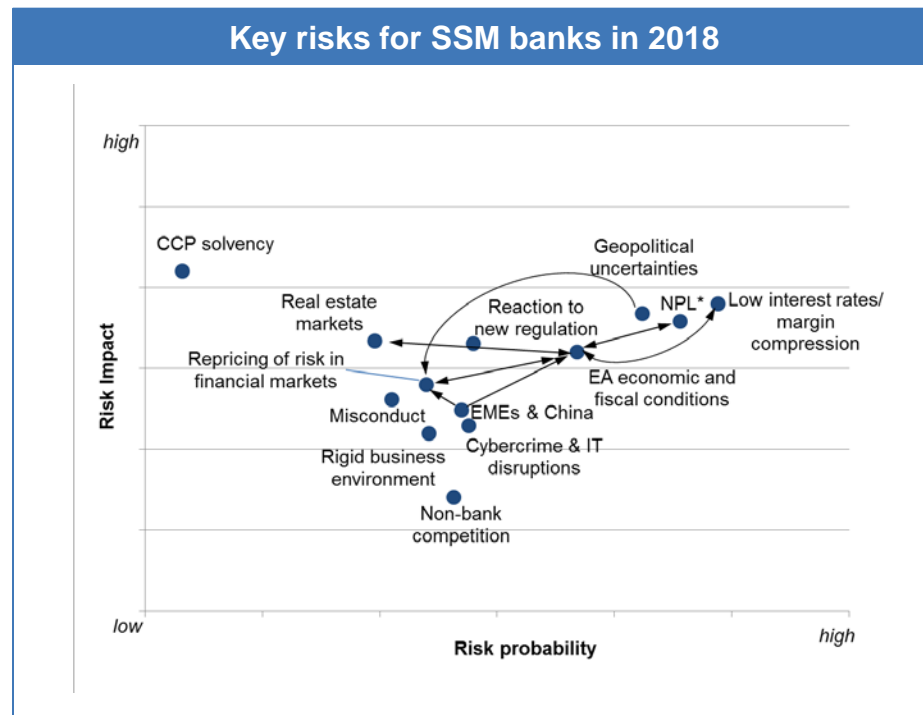
84 banks with envisaged **qualitative measures**

- Qualitative measures are envisaged for most banks scored 4 in SREP 2017, while other supervisory actions have been implemented for the remaining banks
- The envisaged measures cover the whole range of assessed banks
- They cover a wide range of weaknesses (e.g. NPL, Internal Governance, IFRS 9, BCBS 239, Data Quality, Operational risk, IRRBB)

On top of qualitative measures in SREP, JSTs often apply various supervisory actions such as operational acts or follow-up letters e.g. on IRRBB

2017 SREP cycle highlighted challenges regarding profitability and capital adequacy

- Continued period of **low interest rates** puts pressure on interest rate margins challenging banks' profitability.
- **NPL** ratios declined over the last year, however the number of high-NPL banks in the euro area remains substantial.
- While **euro area economic and fiscal conditions** improved, some countries still face debt sustainability concerns, making them vulnerable to a potential repricing in bond markets.
- This is particularly relevant against historically high levels of **geopolitical uncertainty** which could lead to a sudden repricing of risk in financial markets. Political uncertainty around Brexit creates additional challenges, including business continuity and transitional risks, as well as macroeconomic and regulatory risks.



Source: ECB and national supervisory authorities.

Note: Risks are not independent and might trigger or reinforce each other – indicated by arrows on the chart which represent the main transmission channels.

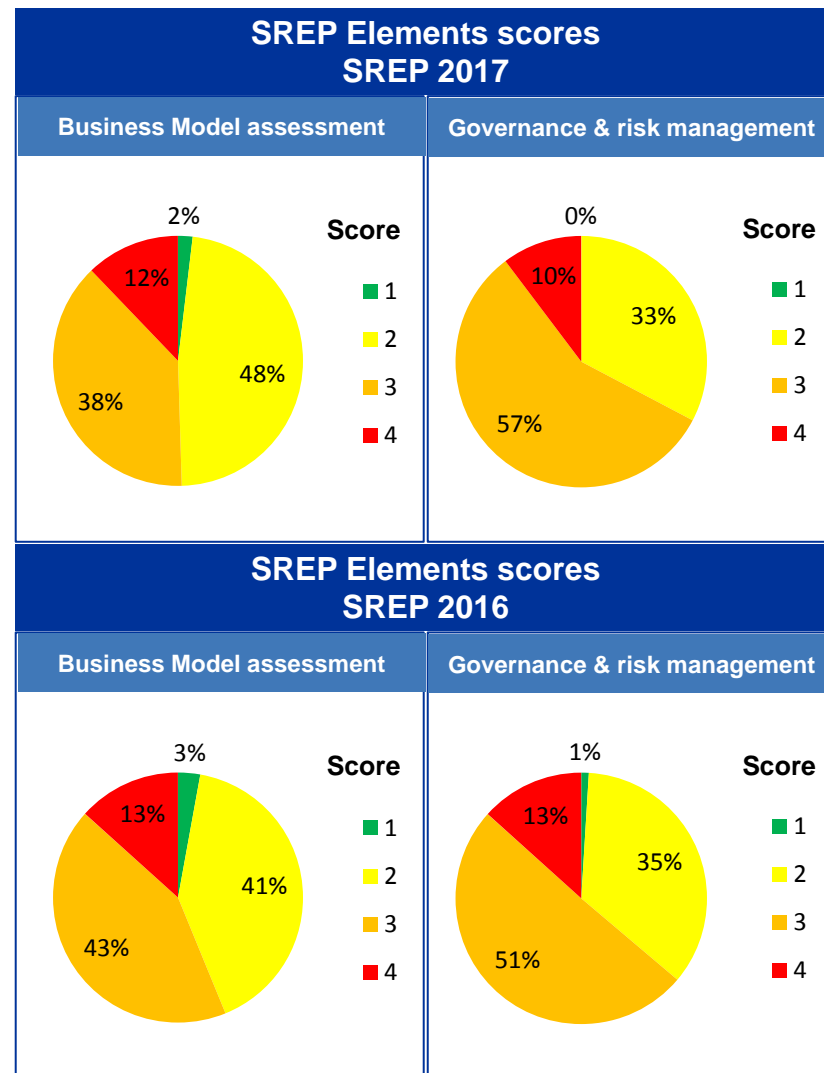
(*) NPLs: this risk driver is only relevant for euro area banks with high NPL ratios

Evolution of SREP scores per element 2016 and 2017

- Profitability remains an issue**
 - stable number of loss-making institutions; 7 institutions not profitable since SSM inception;
 - on the positive side, 24 institutions from 12 different countries have been showing a relatively good level of profitability for the last 3 years
- Many institutions still with challenges in risk management**
 - Especially in risk infrastructure, data aggregation and reporting capabilities, and internal audit

Notes:

- SREP 2017 values based on SREP 2017 decisions finalised as of 30 November 2017.
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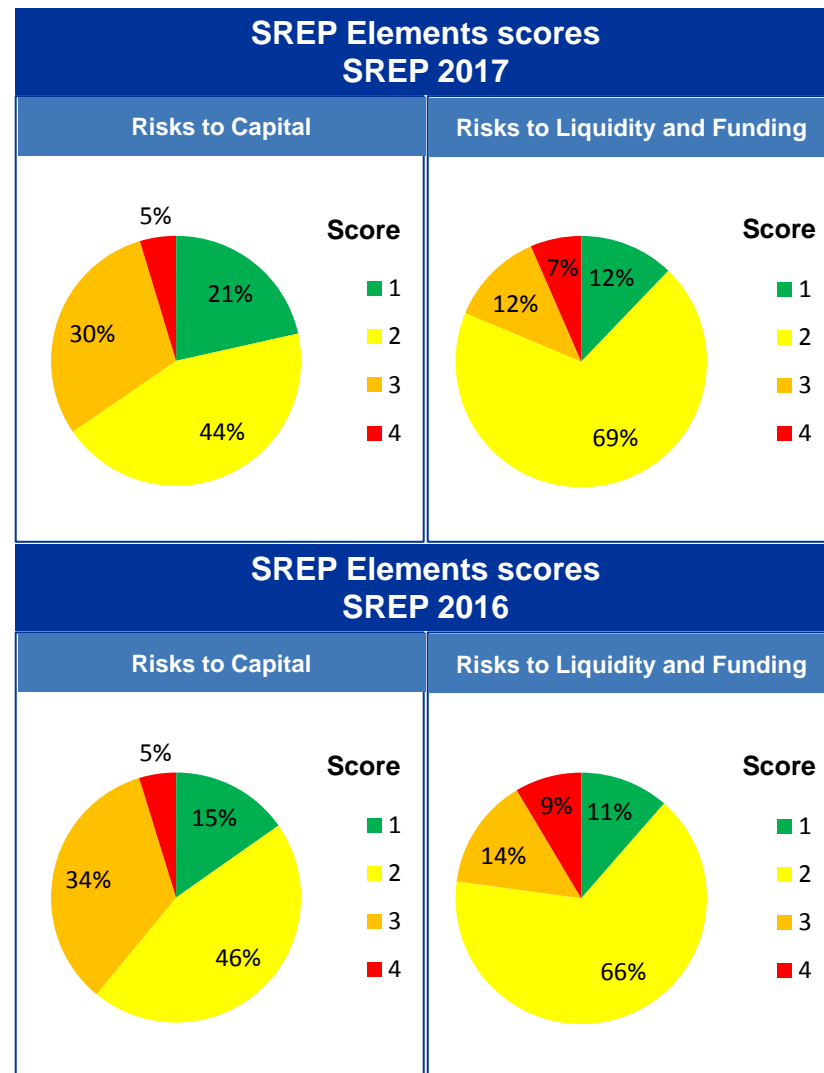


Evolution of SREP scores per element 2016 and 2017

- **In terms of Risks to Capital high Level of NPL is still a point of attention**
 - notably the 34 institutions whose reporting on the matters requested in the SREP 2016 letters show remaining issues
- **In terms of Risks to Liquidity and Funding, the risk management framework of a number of banks needs to be improved e.g. in terms of ILAAP**

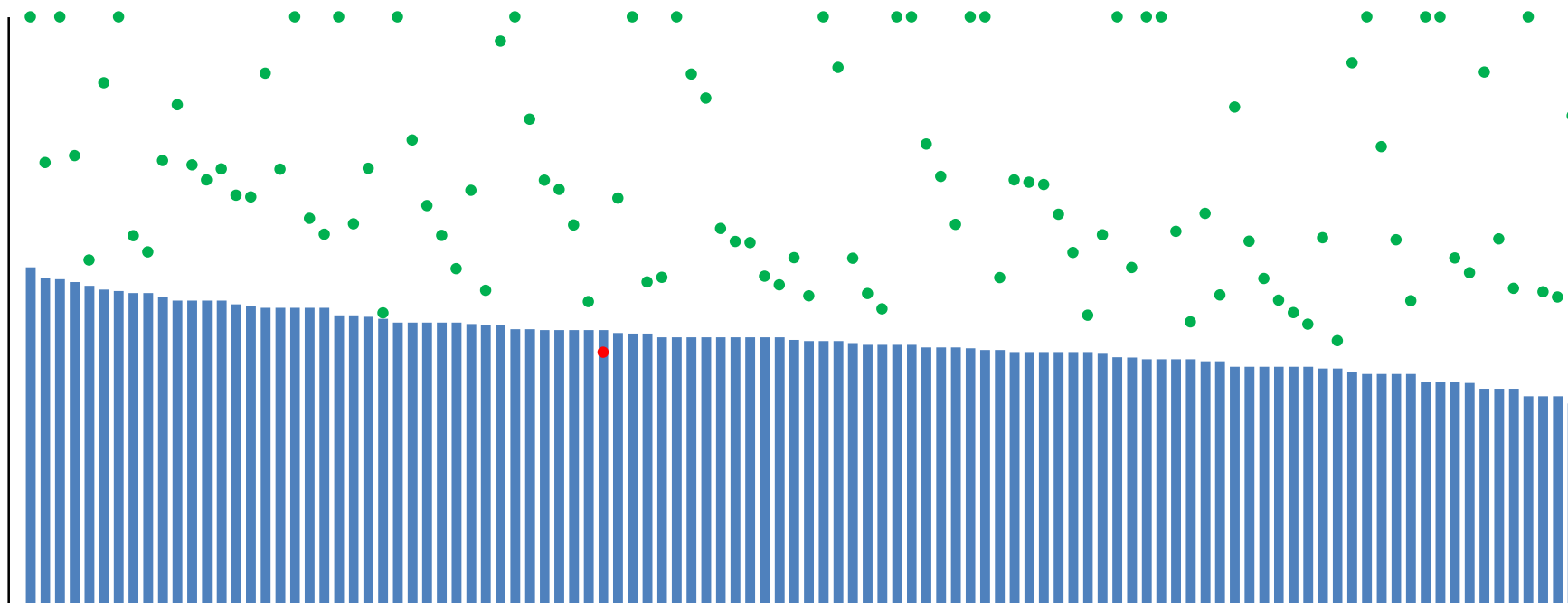
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Most significant institutions currently have capital levels above CET1 requirements and buffers*

Capital supply compared to MDA trigger



█ CET 1 ratio requirements (2017 phase-in)
 = Pillar 1 + Pillar 2R + Capital Conservation Buffer
 + Countercyclical Buffer + Systemic Buffers

● Banks with CET1 supply above MDA trigger
● Banks with CET1 supply below MDA trigger

* Based on capital supply in Q2 2017 (CET1 after covering shortfall of Pillar 1 AT1/T2 shortages)

For 2016 results please refer to the 2016 SREP Booklet on the web site: https://www.bankingsupervision.europa.eu/ecb/pub/pdf/srep_methodology_booklet_2016.en.pdf

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.*

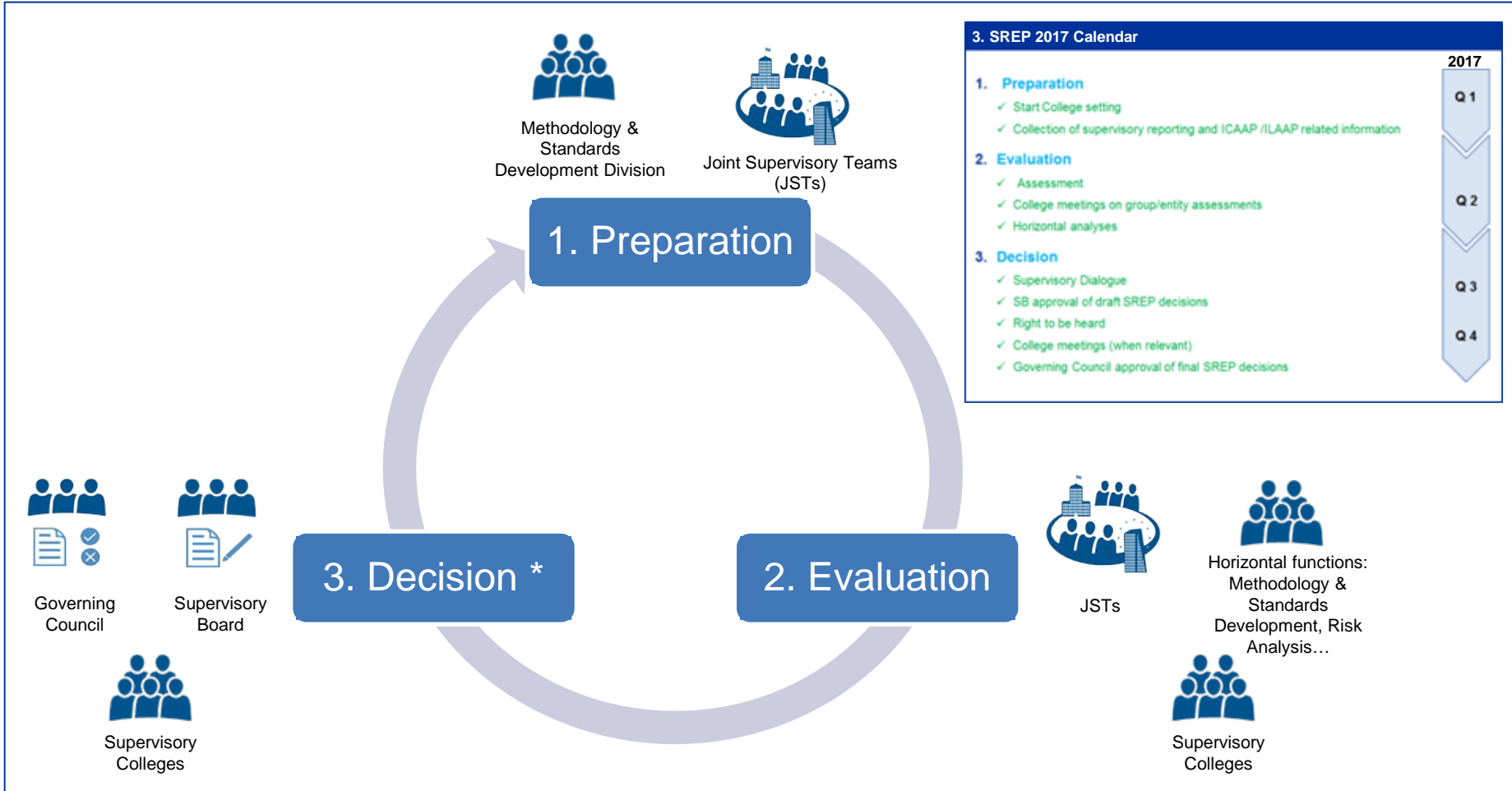
RTS, ITS and EBA Guidelines

- 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*

BCBS and FSB Principles

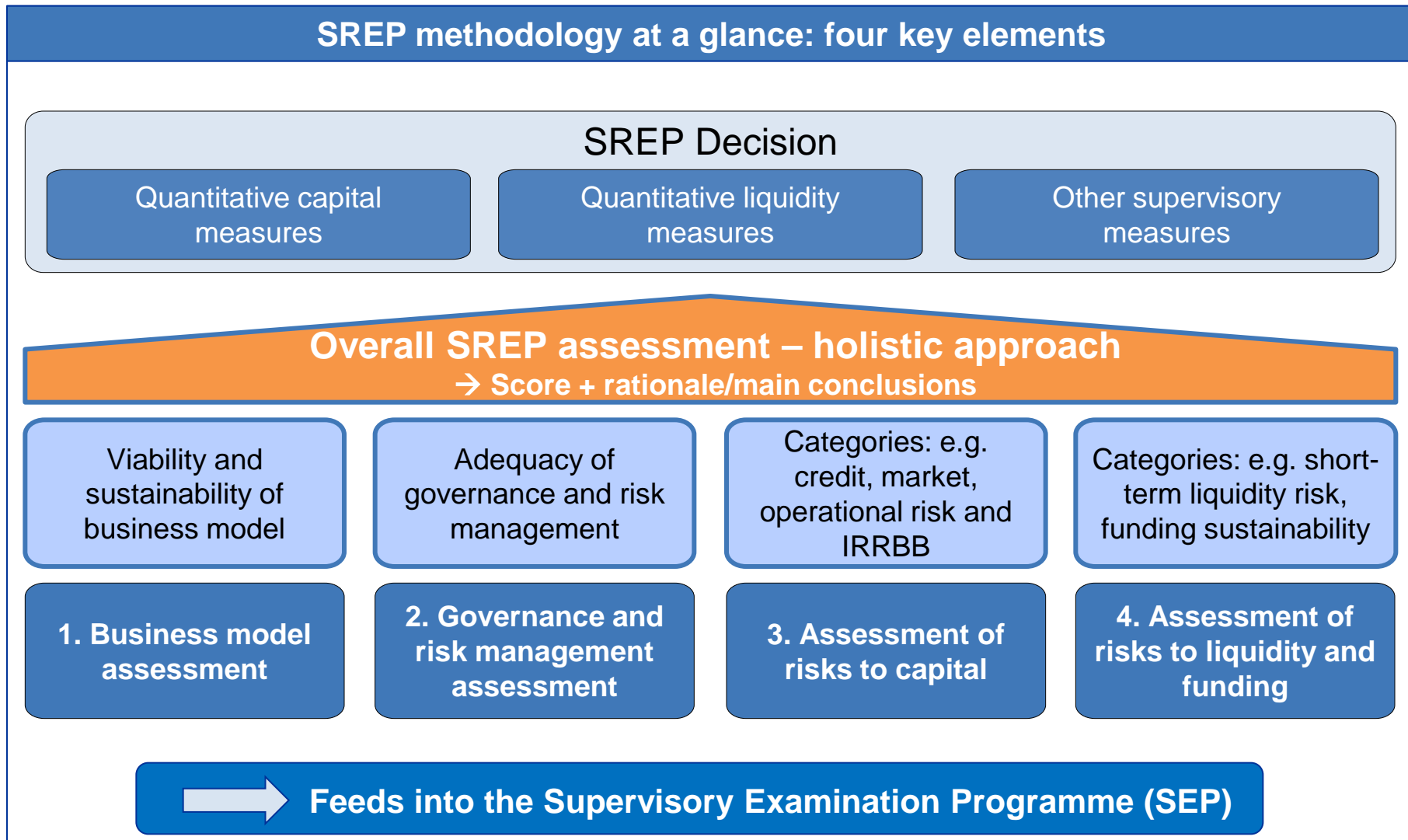


Supervisors at ECB and in 19 countries jointly prepared SREP decisions for SSM significant institutions through a common process

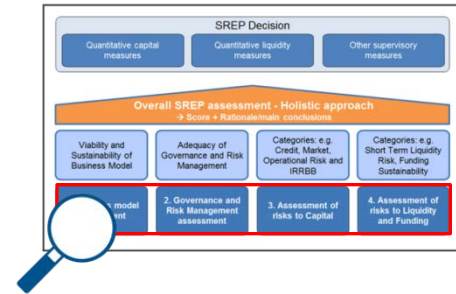


* Note: decision finalised after right-to-be-heard procedure and Governing Council non-objection

Building block approach in line with EBA Guidelines



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
<p>Main sources:</p> <ul style="list-style-type: none"> • quarterly ITS • STE reports 	<ul style="list-style-type: none"> • Scoring risk level • Formal compliance checking of risk control 	<p>Adjustments based on additional factors and considering banks' specificities and complexity</p>

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	✓	✓	✓

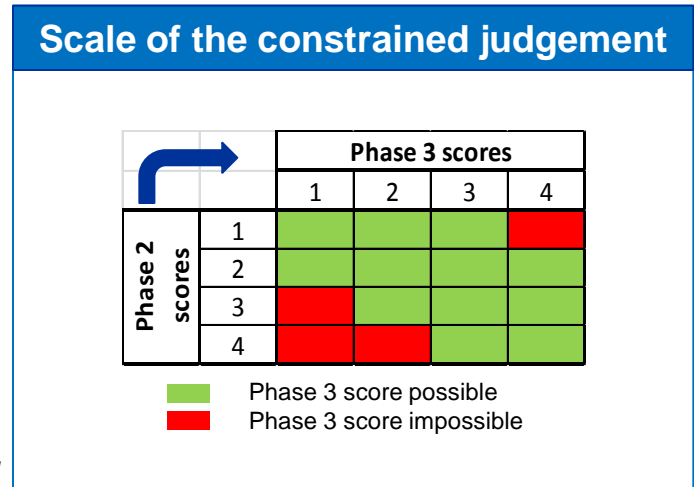
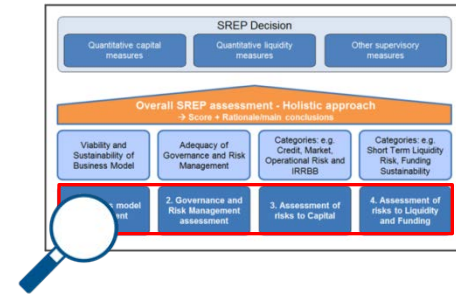
Combined score (RL + RC)

n/a: not applicable

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

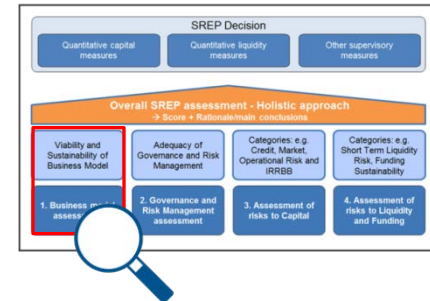
Constrained judgement

- 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



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



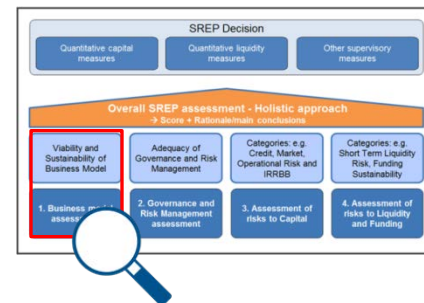
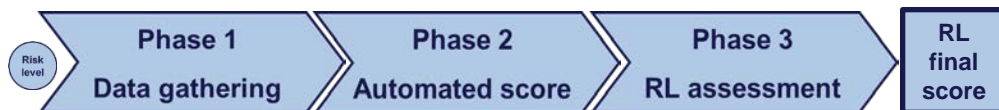
Examples of identified business models

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



**In line with EBA SREP
Guidelines, § 55-57**

Business model



Phase 1

- **Information gathering and understanding materiality of business areas**

Phase 2

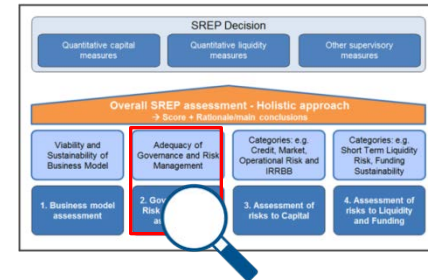
- **Automated anchoring score based on indicators, such as ROA, cost-to-income ratio, etc.**

Phase 3

- **Comprehensive analysis**
- **Used to adjust Phase 2 score taking into consideration the bank's specificities**

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, data and reporting
- Remuneration policies and practices



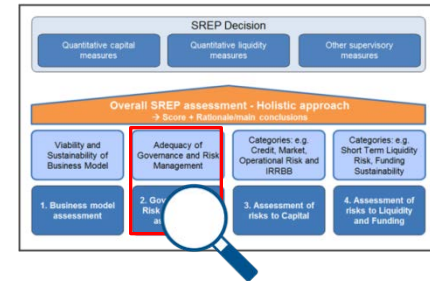
Two examples of key questions

- 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?



In line with EBA SREP
Guidelines, § 81-82

Internal governance and risk management



Phase 1

- **Information gathering e.g. through the thematic review on risk governance and risk appetite (RIGA)**

Phase 2

- **Check compliance with CRD provisions**
- **Specific analysis of, for example:**
 - organisational structure
 - internal audit
 - compliance
 - remuneration
 - risk appetite
 - risk infrastructure
 - reporting

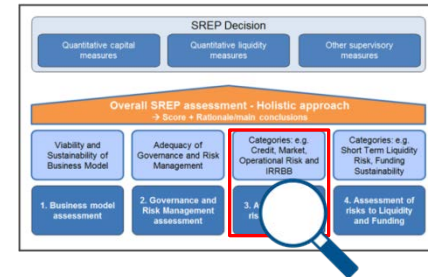
Phase 3

- **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**

Risks to capital

Three different perspectives (“3 Blocks”)

Block 1 Supervisory perspective	Block 2 Bank’s perspective	Block 3 Forward-looking perspective
<p>Four risk categories: credit risk, market risk, operational risk, IRRBB</p> <ul style="list-style-type: none"> ✓ Information gathering ✓ Anchoring scores on risk categories ✓ Comprehensive analysis 	<ul style="list-style-type: none"> ✓ Information gathering: e.g. ICAAP reports ✓ Anchoring assessment: with proxies in line with the EBA Guidelines* ✓ Comprehensive analysis 	<ul style="list-style-type: none"> ✓ Information gathering: bank internal stress tests ✓ Anchoring assessment: supervisory stress tests ✓ Comprehensive analysis



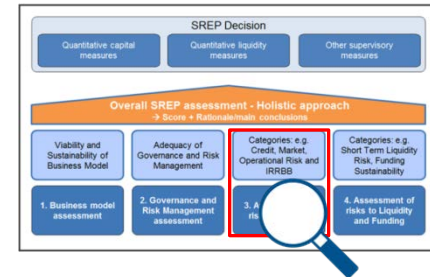
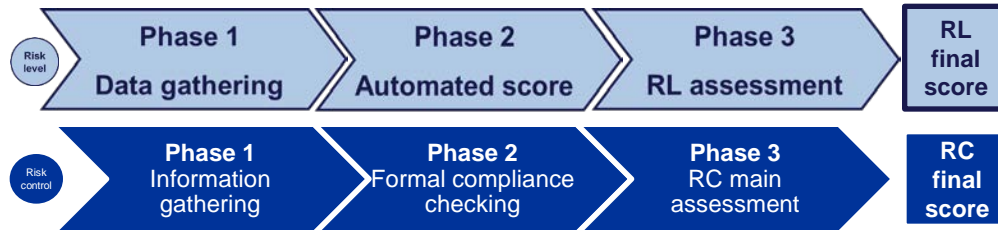
For SREP 2017

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

 See also EBA SREP Guidelines

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

Risks to capital – Block 1

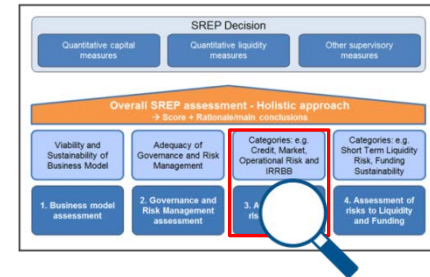


➔ Deep-dive into a given risk factor: **credit risk** (example)

Phase 1	Phase 2	Phase 3
<ul style="list-style-type: none"> ➤ Risk level <ul style="list-style-type: none"> • subset of pre-defined indicators calculated from ITS and STE data ➤ Risk control <ul style="list-style-type: none"> • information gathering 	<ul style="list-style-type: none"> ➤ Risk level <ul style="list-style-type: none"> • automated score given through different dimensions, such as: <ul style="list-style-type: none"> • quality (e.g. non-performing loans ratio) • coverage (e.g. provisions) ➤ Risk control <ul style="list-style-type: none"> • compliance checks relating to internal governance, risk appetite, risk management and internal audit of credit risk in particular 	<ul style="list-style-type: none"> ➤ Risk level <ul style="list-style-type: none"> • comprehensive analysis, e.g.: <ul style="list-style-type: none"> • current risk position and trend • forward-looking view • peer comparison • in-depth analysis of various sub-categories, e.g.: <ul style="list-style-type: none"> • non-financial corporate portfolios • household portfolios ➤ Risk control <ul style="list-style-type: none"> • deeper analysis, notably thanks to dedicated meetings with the bank

Risks to capital – Block 2

- Ongoing multi-year plan on SSM Guides on ICAAP*
- ICAAP reliability assessment

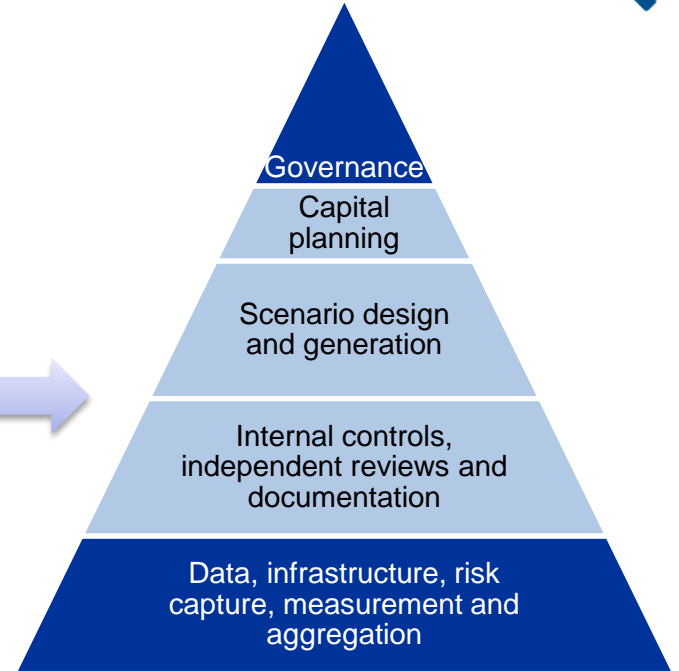
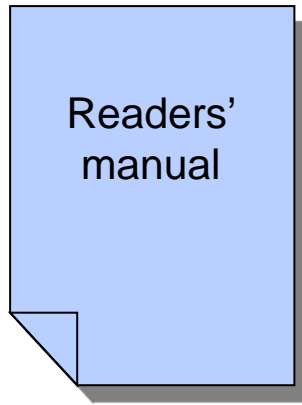
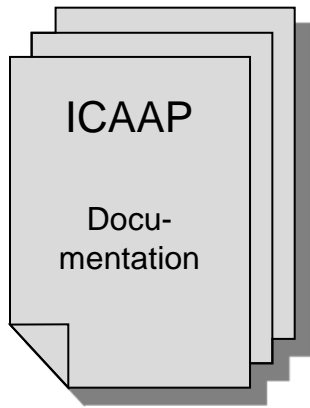


ECB ICAAP expectations

- 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

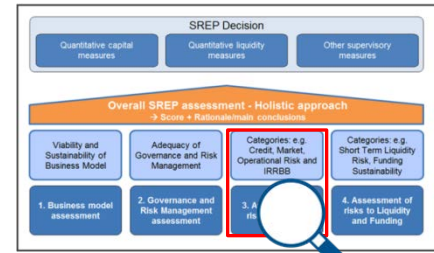
• https://www.bankingsupervision.europa.eu/ecb/pub/pdf/170220letter_nouy.en.pdf

ICAAP – Qualitative assessment



JST assessment

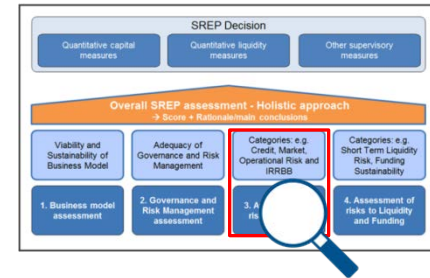
→ **Decision on ICAAP reliability**



Bank-internal documents as set out in EBA GL

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

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 15 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				
11 Risk categories	12 Risk sub-categories (where applicable)	13 Name of internal risk categories as normally covered in ICAAP (please use available internal numbering system, include name of category and risk categories as possible for risk categories or sub-categories not covered in SSM risk map (please be precise and specific))	14 Short description of internal Risk category (include sub-categories but not included)	15 ICAAP estimate - internal capital needed (in value) in EUR (please only provide numbers as internally available)	16 Have there been material changes in scope or quantification methodology for this risk category / sub-category since the last reporting date? (Yes/No)	17 PI link to form used (please provide the ID of the template)
Credit risk						
		credit risk (please use the same name as sub-categories as specified in table 11, or use separate sub-categories as available)				
		default risk				
		credit concentration risk				
		PI ending risk				
		Operational risk				
		Country risk (includes transfer of funds)				
		bankruptcy and delivery risk				
		residual risk				
		regulatory 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 risk 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

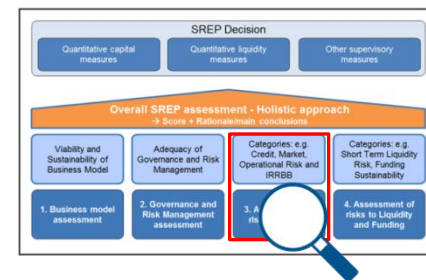
Internal capital-adjusted figure (capital requirements)

- Pillar 1 as floor
- No inter-risk diversification

Dialogue with banks

Risks to capital

- Forward-looking perspective
- In 2017, no large-scale EBA stress test but IRRBB Sensitivity Analysis
- In 2016, two large-scale stress test exercises – will be used again in 2018



2016 stress test: EBA Stress Test exercise

- **Two** consistent **macro-economic scenarios** (baseline and adverse)
- Testing **multiple risk factors**
 - Credit risk
 - Market risk, counterparty credit risk
 - Net interest income
 - Conduct risk and other operational risks
 - Non-interest income, expenses and capital
- Amongst which **IRRBB partially captured via net interest income**

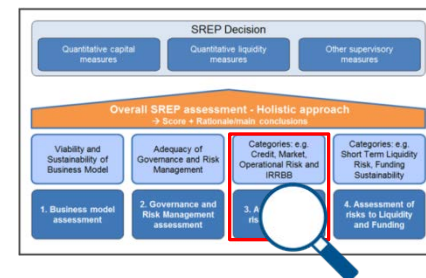
2017 stress test: IRRBB Sensitivity Analysis*

- **Multiple** heuristic instantaneous **interest rate shocks**
- Exclusively **testing interest rate risk in the banking book (IRRBB)** by focusing on interest income and interest expenses
- With **two perspectives**:
 - **Net interest income (NII)**
 - **Economic value of equity (EVE)**

* The exercise was carried out in compliance with CRDIV requirements for competent authorities to conduct annual supervisory stress tests.

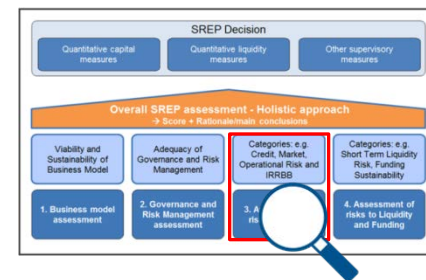
Risks to capital

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**

2017 – Risks to capital: the results of the Sensitivity Analysis of IRRBB – Stress test 2017 have contributed to the overall SREP 2017 in several ways

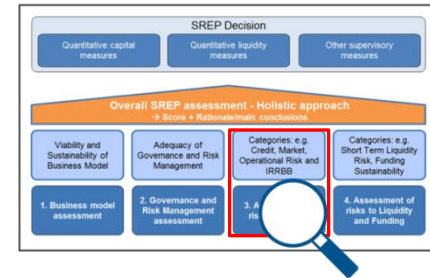


- Quantitative impact of interest rate risk on the **Economic Value of Equity to adjust up or down the level of 2016 Pillar 2 Guidance**. Three dimensions considered:
 - **Impact of the IR shocks excluding parallel up and parallel down** (already assessed in SREP as part of IRRBB review)
 - Exposure to **customer behaviour risk**
 - Risks related to **mark-to-market fluctuations** of banking book IR derivatives
- **Qualitative information** (data availability, timeliness, quality) as well as **quantitative information** (impact of interest rate risk on **Net Interest Income**) were used to **enrich P2R and qualitative measures**

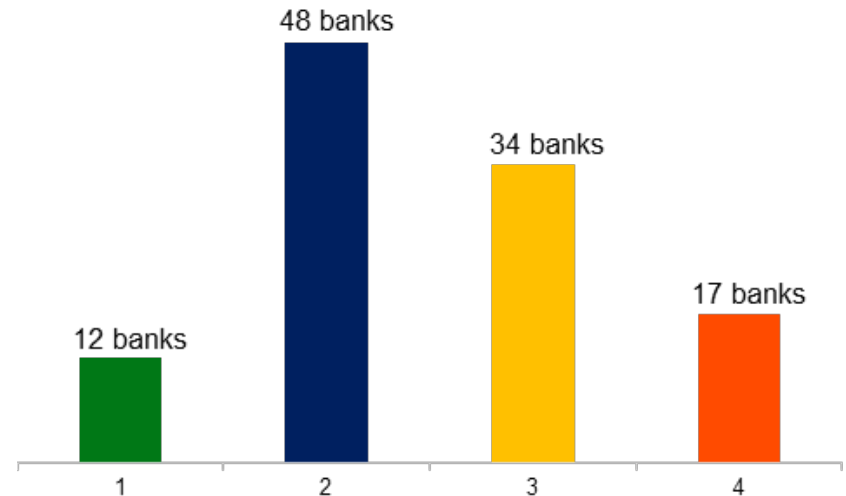
Incorporation of results ensured no double-counting

2017 – Risks to capital: the Stress test 2017 results related to Economic Value of Equity informed the calibration of Pillar 2 Guidance

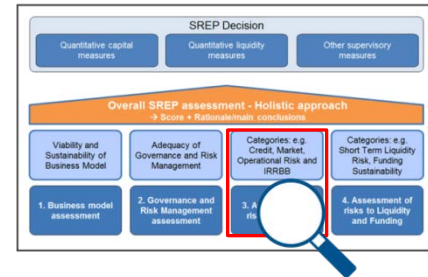
- The **Pillar 2 Guidance (P2G) starting point** reflected supervisory **risk assessment** including results from the last **EU-wide 2016 stress test**
- In the Sensitivity Analysis of IRRBB – Stress Test 2017, **anchoring scores from 1 to 4** were used by **JSTs to adjust P2G in a +25/-25 bps range**
- **In addition**, JSTs have taken into account **other information sources to adjust P2G**, e.g.:
 - Special circumstances regarding IRRBB
 - New developments from firm-wide ICAAP stress tests if relevant
 - Horizontal analyses



Anchoring scores informing P2G adjustments
(x-axis: bank score)

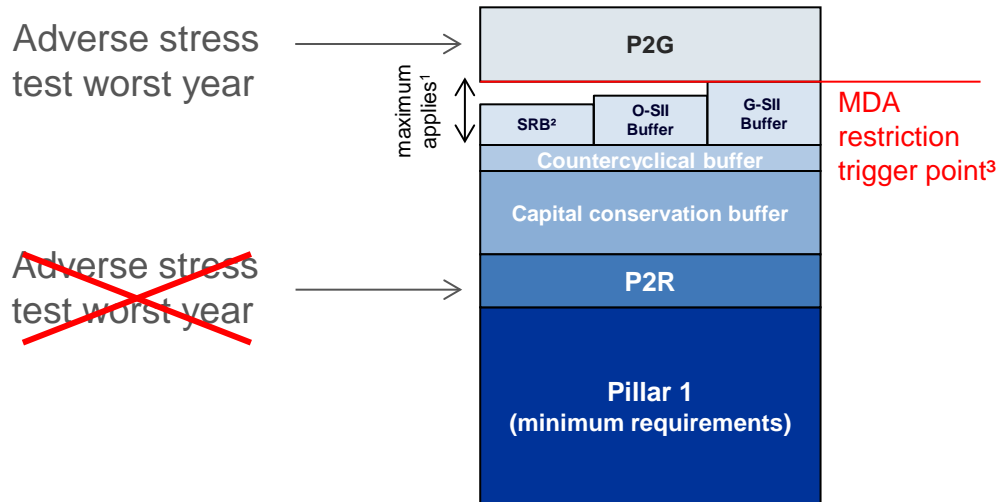


In years of large EBA stress test exercise (2016 and 2018), implement adverse stress test results for the worst year only in P2G



Adverse stress test results for the worst year only in P2G

* Scale not meaningful



Approach used in years of EBA stress test exercises (so it was not used in 2017, but will be used in 2018 again)

- 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

Risks to liquidity

Three different perspectives (“3 Blocks”)

Block 1 Supervisory perspective

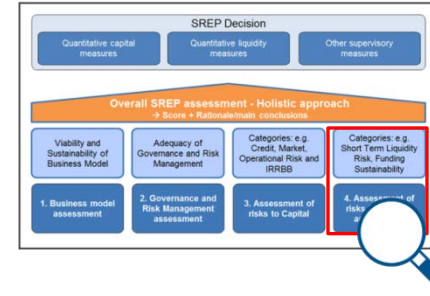
- Short-term liquidity, funding sustainability
- ✓ Information gathering
- ✓ Anchoring scores on short-term liquidity and funding sustainability risks
- ✓ Comprehensive analysis

Block 2 Bank’s perspective

- ✓ Information gathering: e.g. ILAAP reports
- ✓ Anchoring assessment: challenge the institution’s internal estimates
- ✓ Comprehensive analysis: e.g. of ILAAP reliability

Block 3 Forward-looking perspective

- ✓ Information gathering: bank internal stress tests
- ✓ Anchoring assessment: supervisory stress tests
- ✓ Assessment of supervisory stress test results and of bank’s internal stress tests



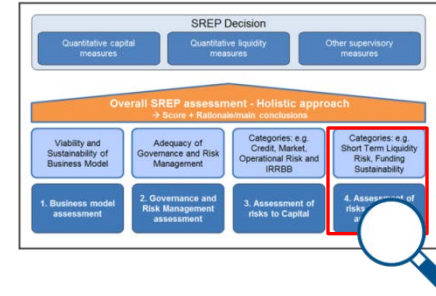
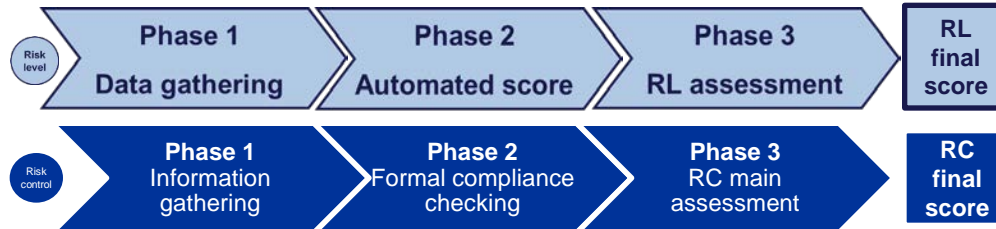
For SREP 2017

- ✓ 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

Risks to liquidity – Block 1

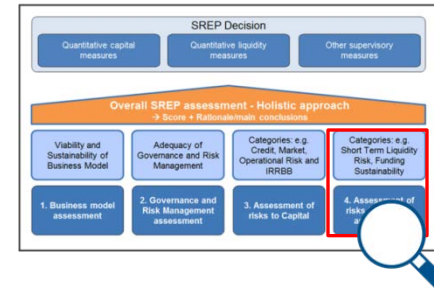


➔ Deep-dive into a given risk factor: **short-term liquidity** (example)

Phase 1	Phase 2	Phase 3
<ul style="list-style-type: none"> ➤ Risk level <ul style="list-style-type: none"> • subset of pre-defined indicators based on ITS and STE data ➤ Risk control <ul style="list-style-type: none"> • information gathering 	<ul style="list-style-type: none"> ➤ Risk level <ul style="list-style-type: none"> • automated score given through several indicators, such as: <ul style="list-style-type: none"> • liquidity coverage ratio • short-term funding/total funding ➤ Risk control <ul style="list-style-type: none"> • compliance checks relating to internal governance, risk appetite, risk management and internal audit 	<ul style="list-style-type: none"> ➤ Risk level <ul style="list-style-type: none"> • deeper analysis: <ul style="list-style-type: none"> • short-term wholesale funding risk • intraday risk • quality of liquidity buffers • structural funding mismatch ➤ Risk control <ul style="list-style-type: none"> • deeper analysis, notably thanks to dedicated meetings with the bank

Risks to liquidity – Block 2 and 3

- Ongoing multi-year plan on SSM Guides on ILAAP*
- ILAAP reliability assessment

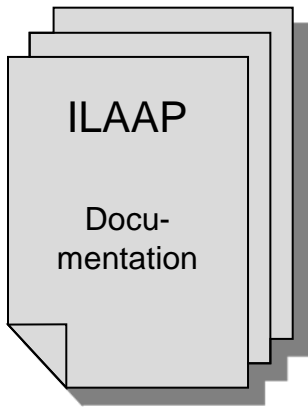
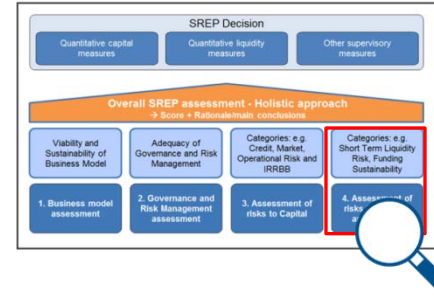


ECB ILAAP expectations

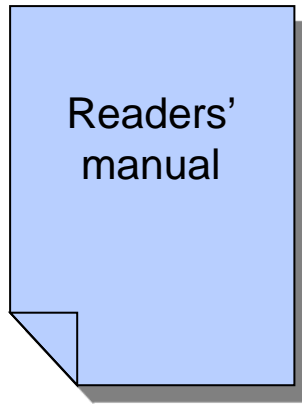
- Content as described in EBA Guidelines
- Internal documentation together with a “readers’ manual”
- Conclusions in the form of liquidity adequacy statements supported by analysis of ILAAP outcomes and signed by management body

• https://www.bankingsupervision.europa.eu/ecb/pub/pdf/170220letter_nouy.en.pdf

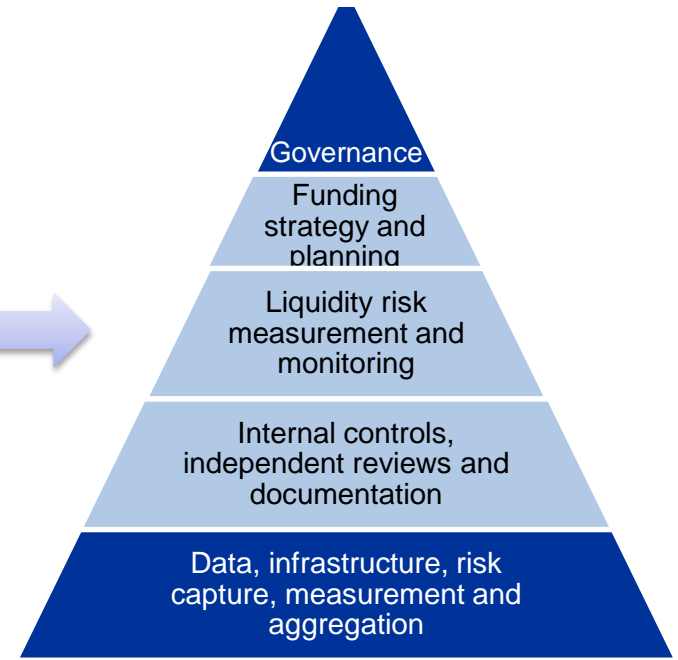
ILAAP – Qualitative assessment



Bank-internal documents as set out in EBA GL



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

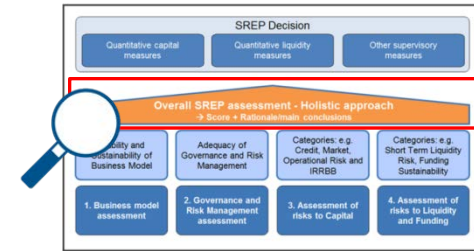


JST assessment

→ 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

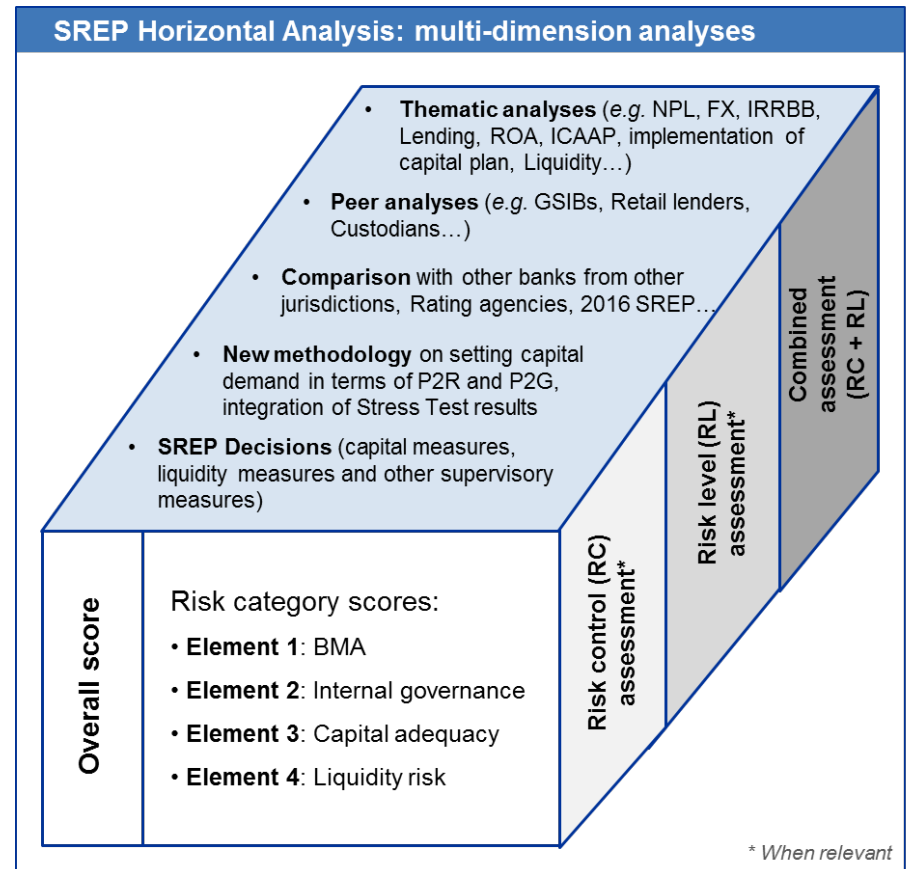


In line with the EBA SREP Guidelines (table 13, pp. 170 and 171), the overall SREP score reflects the supervisor's overall assessment of the viability of the institution: higher scores reflect an increased risk to the viability of the institution stemming from one or several features of its risk profile, 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



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**.

4.8. SREP – Methodology: SREP decision (1/5)

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 (P2R²)
- combined buffer requirements (CBR²)
- recommendation to follow a linear path towards “fully loaded” ratios

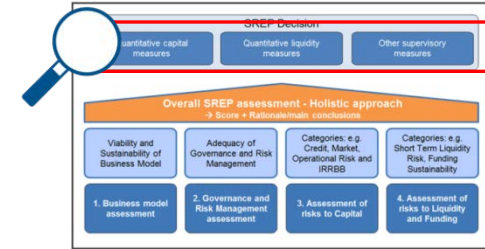
Institution-specific quantitative liquidity requirements

- 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

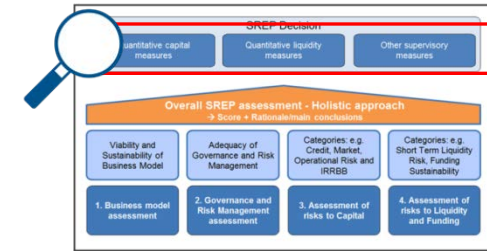
- SREP communication also includes P2G expressed as CET1 ratio add-on



¹ At least 56.25% in CET1

² CET 1 only

SREP decision – capital measures



	SREP 2015	SREP 2016	SREP 2017
Pillar 2	<ul style="list-style-type: none"> Pillar 2 (MDA relevant) 	<ul style="list-style-type: none"> Pillar 2 Requirements (P2R) (MDA relevant) Pillar 2 Guidance (P2G) (not MDA relevant) 	<ul style="list-style-type: none"> Pillar 2 Requirements (P2R) (MDA relevant) Pillar 2 Guidance (P2G) (not MDA relevant)
Capital Conservation Buffer (CCB)	<ul style="list-style-type: none"> Overlap with Pillar 2 (Gross Pillar 2) 	<ul style="list-style-type: none"> No overlap with Pillar 2 	<ul style="list-style-type: none"> No overlap with Pillar 2
CET1 Stacking order	<p><i>*Scale not meaningful</i></p>	<p><i>*Scale not meaningful</i></p>	<p><i>*Scale not meaningful</i></p>
Capital composition	<ul style="list-style-type: none"> Pillar 2: 100% CET1 	<ul style="list-style-type: none"> P2R & P2G: 100% CET1 	<ul style="list-style-type: none"> P2R & P2G: 100% CET1
SREP decision	<ul style="list-style-type: none"> CET1 ratio 	<ul style="list-style-type: none"> P2R: CET1 ratio and Total SREP Capital Requirement (TSCR)³ P2G: CET1 ratio add-on 	<ul style="list-style-type: none"> P2R: CET1 ratio and Total SREP Capital Requirement (TSCR)³ P2G: CET1 ratio add-on

No changes

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

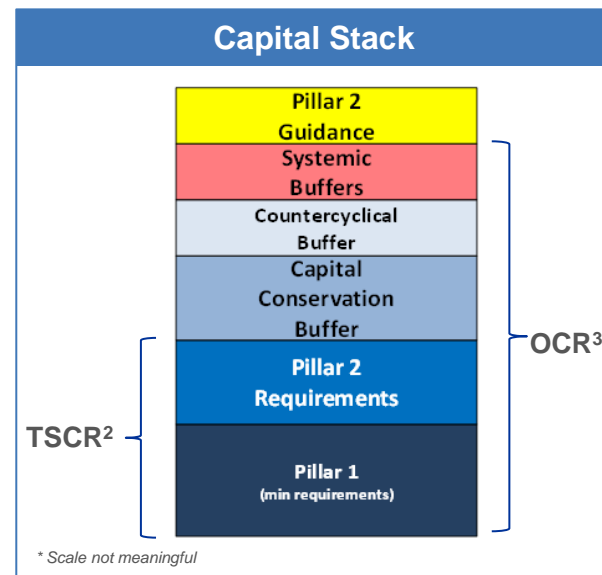
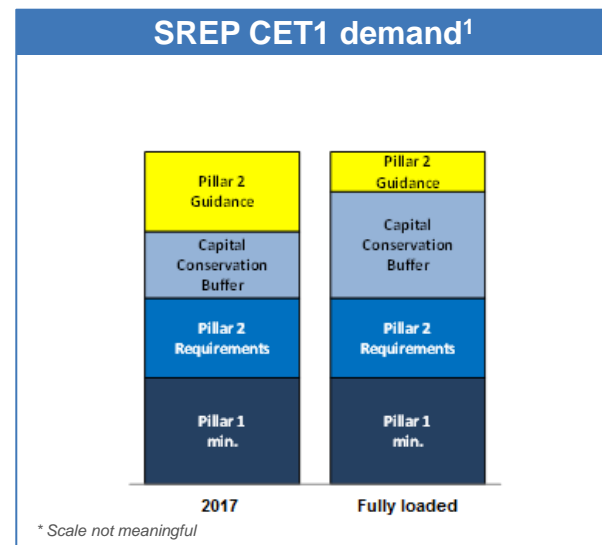
- All other things being equal, the capital demand can be expected to remain broadly stable¹
- If a credit institution operates or expects to operate below Pillar 2 Guidance it should immediately contact its joint supervisory team
- Banks also need to take into account the systemic buffers (G-SII, O-SII and systemic risk buffers) and the countercyclical buffer that are part of the capital stack
- The ECB considers that those components of the own funds requirements which, pursuant to Article 92(1) of Regulation (EU) No 575/2013, are not required to be met with Common Equity Tier 1 [i.e. CET1 held by banks used to meet Pillar 1 AT1/T2 requirements] can be counted also towards the Pillar 2 capital guidance to the extent that these components are, in fact, met in the form of Common Equity Tier 1. In view of the ongoing work of the EBA, it is expected that this stance will be amended⁴

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

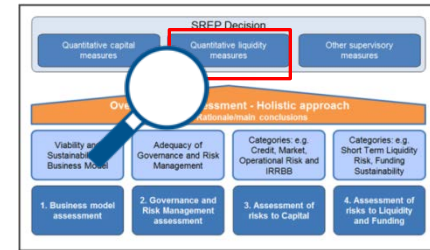
³ OCR: overall capital requirements

⁴ EBA SREP GL under consultation, §400: Competent authorities should also communicate to the institutions that own funds held for the purposes of P2G cannot be used to meet any other regulatory requirements (Pillar 1, P2R or the combined buffer requirements), and therefore cannot be used twice: to cover P2G and to cover for any shortfall of AT1 or T2 instruments to cover TSCR revealed by the outcome of the stress test.”



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

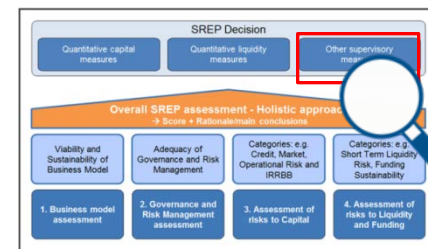


SREP decision – other supervisory measures

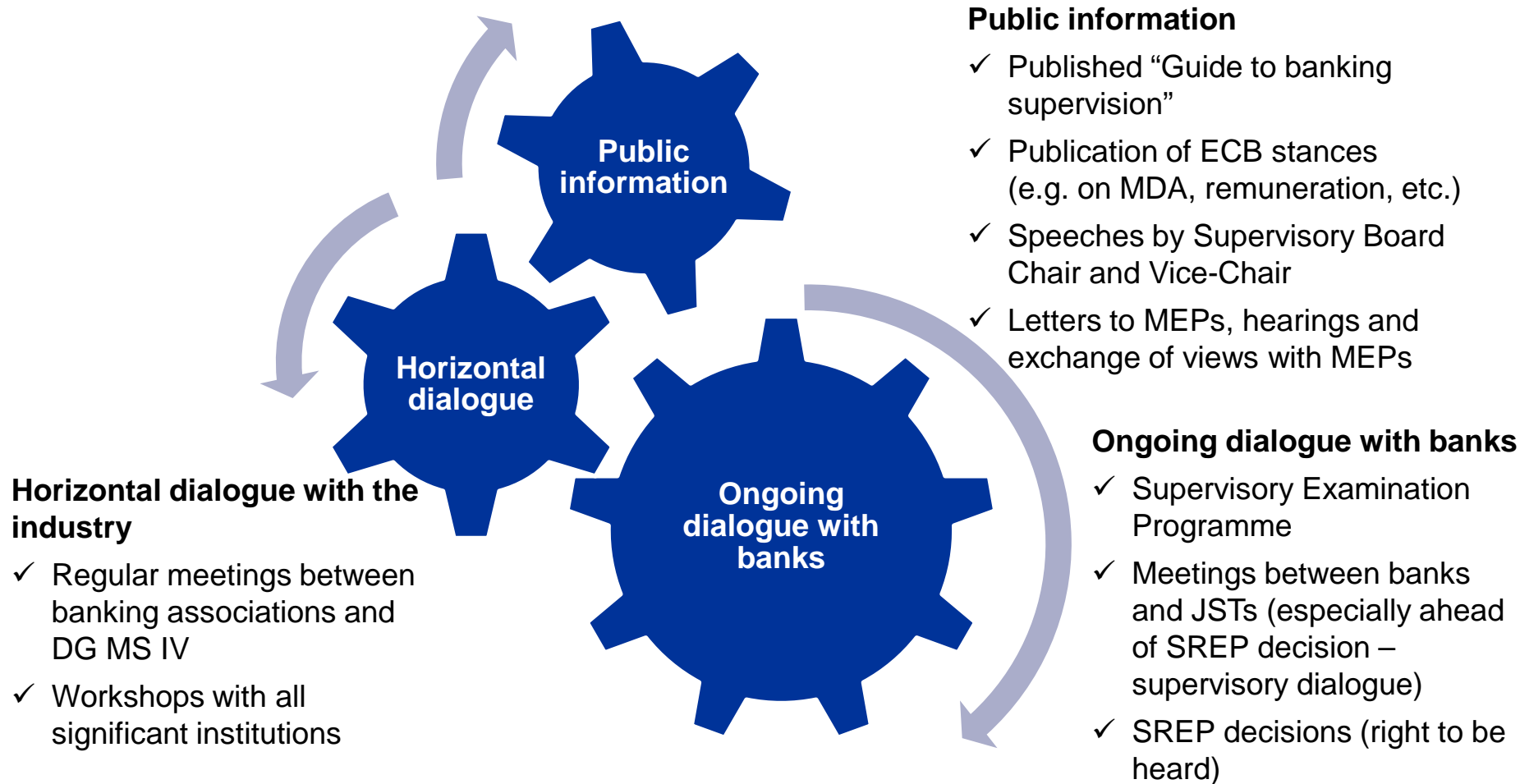
Article 16(2) of the SSM Regulation

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)



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

2. SREP Assessment: Details on Risks to Liquidity and Funding

Assessment of risks to liquidity and funding

Assessment of Risks to Liquidity and Funding – EBA/GL/2014/13 para. 370-373

370. Competent authorities should assess the risks to liquidity and funding that have been identified as material for the institution. The purpose of this title is to provide common methodologies to be applied when assessing individual risks and risk management controls. It is not intended to be exhaustive and gives leeway to competent authorities to take into account other additional criteria that may be deemed relevant based on their experience and the specific features of the institution.

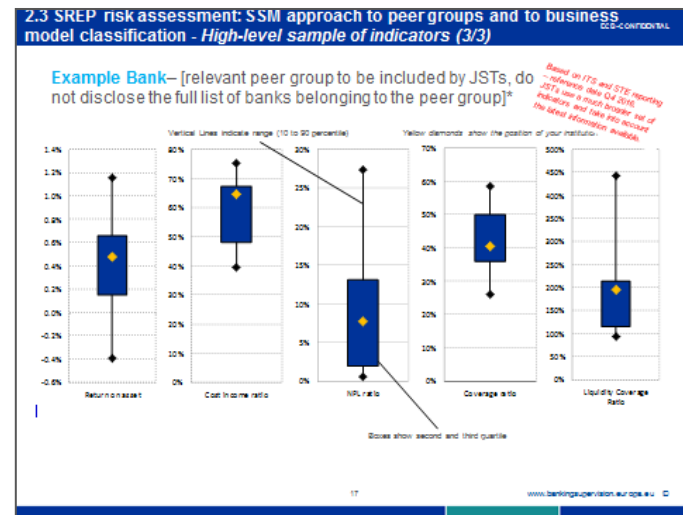
371. This title provides competent authorities with a set of common elements for the assessment of risks to liquidity and funding.

372. The methodology comprises three main components: a. assessment of the liquidity risk; b. assessment of interest funding risk; and c. assessment of funding and funding risk management.

373. In the assessment of risks to liquidity and funding, competent authorities should assess institutions' compliance with minimum requirements provided by the relevant EU and national implementing legislation. Institutions should also extend the scope of the assessment beyond these minimum requirements, aiming to achieve a comprehensive view of the risks.

[BANK NAME] – Use bullet points to describe MAIN SREP FINDINGS

Weaknesses	Please insert feedback on ILAAP:
<ul style="list-style-type: none"> • While the [BANK NAME] is reporting adequate short-term liquidity positions the profile of the short term funding is exposed to greater volatility than Country peers. • With regard to longer term funding sustainability [BANK NAME] is reporting weaker than its peers ratios in absolute terms when compared to Country peers and has a greater reliance on long-term funding. Issues have been identified in relation to [BANK NAME]'s Early Warning Indicators (EWI) regarding the Contingency Funding Plan. 	<ul style="list-style-type: none"> - How complete is the submission by the bank? - How did the bank meet the ECI letters expectation? - How the ECI aspects of the submission have been funded by the bank?
Strengths	
<ul style="list-style-type: none"> • The bank has ... 	



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

Enriched public communication and horizontal dialogue



During the 2017 SREP cycle the SSM increased the transparency of the process as well as that towards new developments and priorities:

- December 2016: publication of SSM supervisory priorities 2017
- February: Multi-year plan on SSM Guides on ICAAP and ILAAP
- February: Launch of ECB Sensitivity Analysis of IRRBB – Stress test 2017
- March: Publication of guidance to banks on tackling non-performing loans
- October: detailed communication on the 2017 stress test results and impacts on SREP – conference calls with banks' heads of communications, analysts and media
- November: Chair's hearing at the European Parliament
- Throughout the cycle, many meetings with banking associations



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

➤ Significant harmonisation

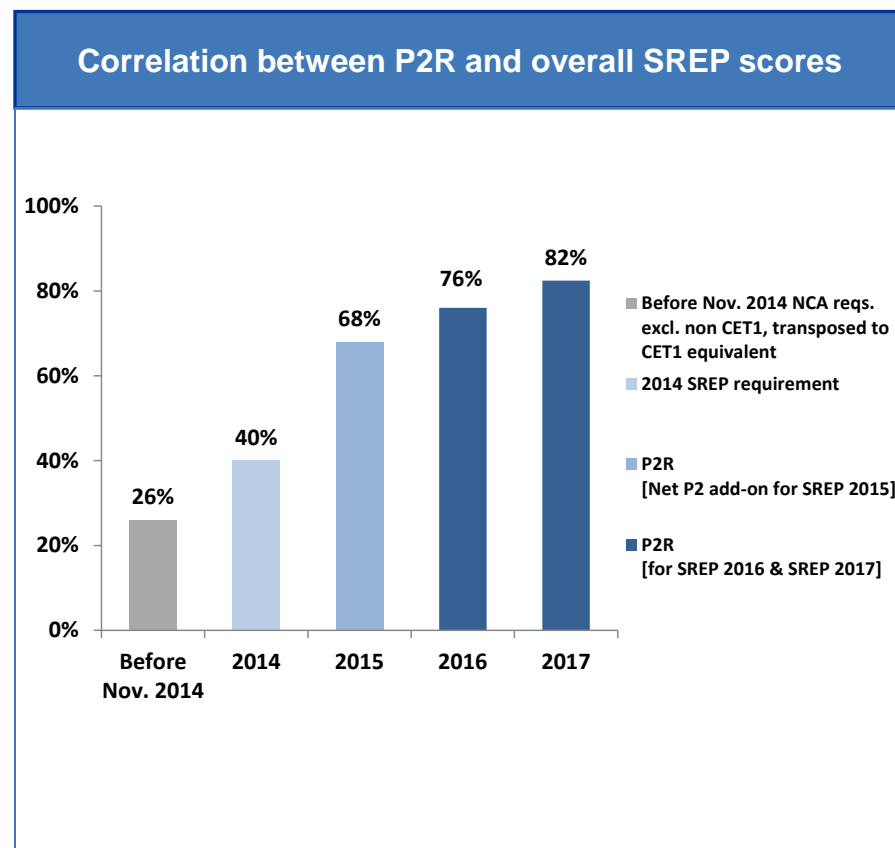
- constrained judgment was used effectively
- stronger correlation between risk profile of institutions and capital requirements

➤ Initiatives already launched:

- In 2017, Sensitivity Analysis of IRRBB – Stress test 2017
- Multi-year plan on SSM Guides on ICAAP and ILAAP

➤ Continuous improvement:

- 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 2017 decision as of 30 November 2017

Note:

Correlation cannot reach 100% due to the facts that risks can also be addressed by other measures e.g. qualitative measures