

Frequently asked questions on the 2018 stress test of Greek Significant Institutions

1. The Greek banks are part of the 2018 EU-wide stress test. Why have the results for the Greek banks been announced earlier?

The 2018 stress test of the Greek Significant Institutions was conducted following exactly the same approach as for the European Banking Authority's (EBA) upcoming stress tests. The only difference was the timeline, which was accelerated so that the results would be ready before the end of the third European Stability Mechanism (ESM) Programme for Greece (20 August 2018). Frontloading the exercise ensured that any necessary follow-up action could be taken before the ESM Programme expires.

2. What was this exercise testing? Did the methodology for the Greek banks differ in any way from the methodology for the other banks?

The Greek stress test aimed to assess the resilience of banks to adverse market developments assuming a static balance sheet. The risk areas covered by the stress test are defined in Section 1.3.10 of the EBA methodology¹. Finally, the methodology for the Greek banks was exactly the same as that used for the other banks participating in the EBA exercise.

3. What was the cut-off date of the stress test?

The reference date for the Greek stress test was 31 December 2017. Furthermore, end-2017 figures were restated to take into account the implementation of the International Financial Reporting Standard 9 (IFRS 9). Due to the static balance sheet assumption, divestments not completed before end-2017 were not taken into account in the stress test, even if already agreed upon. This might have resulted in lower capital ratios than if divestments with a positive capital impact had been considered.

4. Why was the capital depletion higher in this stress test than in 2015?

The differences in capital depletion between the 2018 and 2015 exercises can be attributed to the following main factors:

- differences in the methodology, especially for credit risk (i.e. the introduction of IFRS 9);
- the use of a static balance sheet approach in 2018 rather than a dynamic balance sheet approach as in 2015;
- differences in the stress test projection horizon (two-and-a-half years in 2015 against three years in 2018).

¹ <http://www.eba.europa.eu/documents/10180/2106649/2018+EU-wide+stress+test+-+Methodological+Note.pdf>



5. What is a static balance sheet assumption?

The static balance sheet is a standard assumption adopted in the EU-wide stress test exercises. In particular, according to the EBA 2018 stress test methodology, the static balance sheet assumes that:

- assets and liabilities that mature within the time horizon of the exercise are replaced with similar financial instruments in terms of type, currency, credit quality at date of maturity, and original maturity as at the start of the exercise;
- no workout or cure of NPEs (e.g. Stage 3 assets) is performed;
- no capital measures are taken after the reference date (31 December 2017).

6. What would have happened if a bank scored below the unofficial hurdle rate of 8% in the baseline scenario or 5.5% in the adverse scenario? By how much would banks need to increase their capital?

Following the same approach as in the previous EU-wide stress test exercise held in 2016, and in line with Section 1.3.6 of the EBA methodology, the 2018 exercise is not a pass or fail exercise. No predetermined capital thresholds that would trigger a need for recapitalisation were specified. Any recapitalisation decision will be taken on a case-by-case basis, after assessing each bank's situation in the light of the results of the stress test and any other relevant supervisory information, following a holistic approach.

7. Why is there no pass or fail threshold? How does the ECB's Supervisory Board determine the need for a capital increase without a predetermined hurdle rate?

According to the EBA, there is no pass or fail threshold in this exercise and the supervisory authorities will use the results of the exercise in the Supervisory Review and Evaluation Process (SREP). The main focus of the current stress test exercise is to update the assessment of banks' resilience under baseline and adverse conditions. Following the same approach as in the previous EBA stress test in 2016, the current stress test does not include any hurdle rates. The 2018 exercise aims to assess vulnerabilities and understand the impact of hypothetical adverse economic dynamics on banks rather than to identify possible capital shortfalls and require immediate recapitalisation actions.

In order for the ECB Supervisory Board to decide on a possible recapitalisation, several factors are taken into account. Any recapitalisation decision is made on a case-by-case basis, also considering the results of the stress test in conjunction with other relevant supervisory information in a holistic approach. In this regard, it is important to emphasise that the stress test is not a forecast of future events but a prudential exercise, based on a specific methodology and a number of assumptions and scenarios, to address banks' ability to withstand weaker economic conditions. It is a crucial but not the only factor determining the assessment of potential capital needs. The same holistic approach will be used for all participating banks to avoid any arbitrary treatment.



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8. What is the other supervisory information that supervisors look at?

Other relevant supervisory information may include among other parameters, assessments and institution-specific elements such as the risk profile of a bank, findings of possible inspections (e.g. on-site inspections or viability plans), material changes occurring after the cut-off date of the stress test and risk mitigating measures taken by the bank in the meantime. In short, a wide range of tools is available, which can be applied on a case-by-case basis in the assessment of a bank.

9. How will the stress test results be factored into the SREP?

If the Supervisory Board decides that there is no need for a recapitalisation, then the results of the stress test will be factored into the definition of supervisory measures and, in particular, will be used as one of the inputs for determining Pillar 2 guidance (P2G), in line with the common procedures and methodologies for the SREP, which applies to all banks supervised by the ECB. More specifically, the quantitative outcome of the stress test will be assessed in a non-mechanistic way, together with other relevant supervisory information (assessments and institution-specific elements, such as the risk profile of the bank, inspection findings, material changes occurring after the cut-off date of the stress test, risk-mitigating measures taken by the bank in the meantime). In short, supervisors have a wide range of tools available, which will be applied on a case-by-case basis when assessing banks' adequacy of capital and in particular their ability to meet their own funds requirements over the economic cycle.

10. Did the actions of Greek banks to improve their balance sheets in recent months result in a better performance in the stress test?

Because of the static balance sheet assumption, divestments not completed before the cut-off date (31 December 2017) were not taken into account in the stress test, even if already agreed upon and with respective impairments booked in 2017. This resulted in lower capital ratios than if these divestments with a positive capital impact had been considered.