2021 EU Bank Stress Test:
More Demanding, Better Resilience

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S&P Global
Ratings

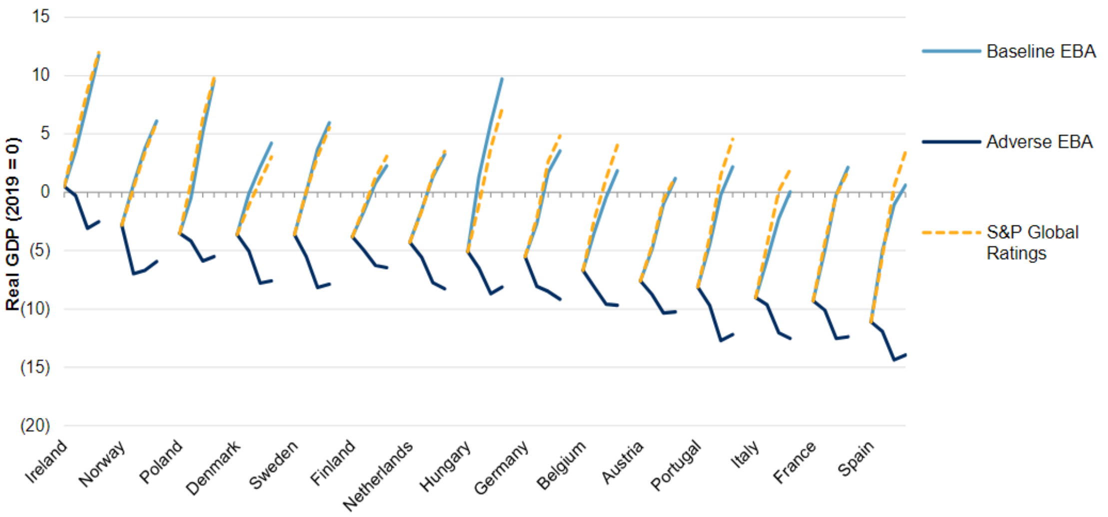
Key Takeaways

1. Banks Demonstrated **Resilience in a Tougher Adverse Scenario,** Although There is Divergence around the Average.
2. No Major Surprises: Stress Test Results **Unlikely To Lead to Rating Actions**.
3. Regulatory Consequences: **Easing of Dividend Restrictions** for Most, **Higher Capital Requirements** for a Minority.
4. **Profitability** to Remain European **Banks' Achilles Heel**.
5. **Different Disclosure** Standards by the EBA and the SSM.
6. **Hybrids** Face a **High Risk of Payment Deferral** in Situations of Stress.

EU Banks Proved Resilient Under Tougher Macroeconomic Assumptions

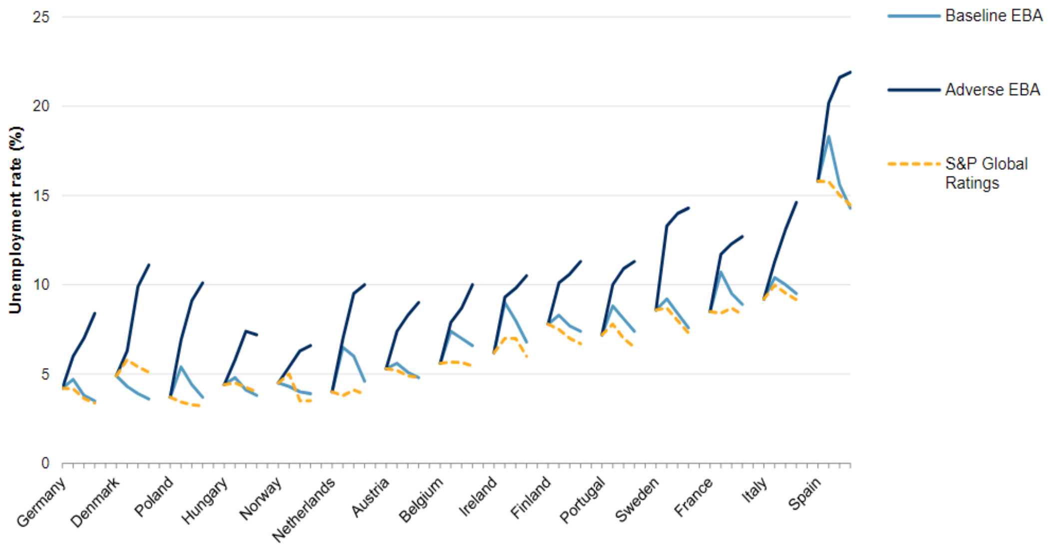
- Aggregate capital depletion of 500 bp under the adverse scenario, but CET1 capital ending at 10%, thanks to a stronger starting point.
- Only 2 Banks in the EBA sample would see their capital falling below regulatory requirements, and one of them just by the margin.
- More than half of the banks would manage to maintain CET1 above 10% post shock.

GDP Recovery Scenarios: EBA's Baseline Similar To Our Forecast, While Adverse Contemplates A Persistent 'Double Dip'
Scenarios for real GDP growth paths 2020a-2023f



a--Actual. f--Forecast. Source: EBA, S&P Global Ratings.

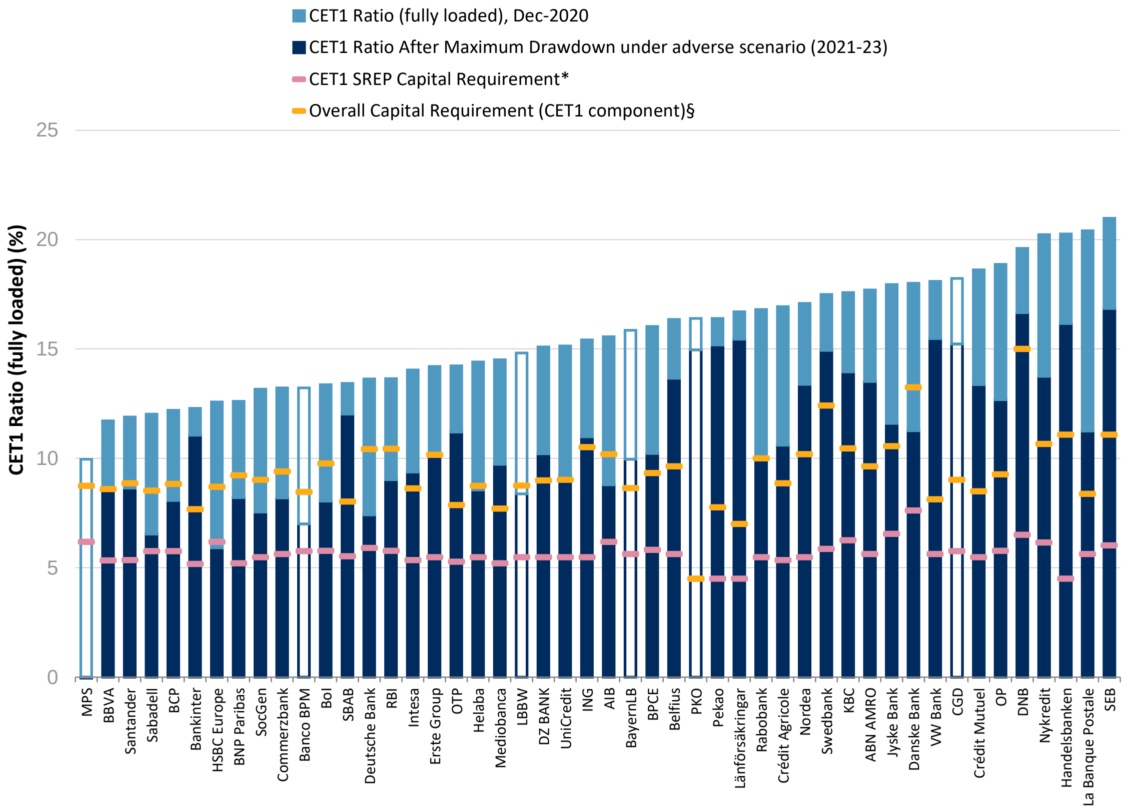
Unemployment Scenarios: EBA's Baseline Somewhat More Pessimistic Than Ours
Scenarios for unemployment rates 2020a-2023f



a--Actual. f--Forecast. Sources: EBA, S&P Global Ratings.

Results Show Divergence Around the Average

Both in the EBA and SSM samples



Banks rated by S&P Global Ratings with filled bars. BNG Bank N.V. and Nederlandse Waterschapsbank N.V.not shown (no SREP breach, highly capitalized).

More impact ← → Less impact

Maximum CET1 Ratio Depletion in adverse scenario

Minimum CET1 Ratio in adverse scenario (More capital buffer ↑ ↓ Less capital buffer)

	>900bps	600 to 899 bps	300 to 599 bps	< 300bps
CET1R ≥ 14%	Bpifrance de Volksbank N.V. Hamburg Commercial Bank AG Kuntarahoitus Oyj SFIL S.A. The Bank of New York Mellon SA Ulster Bank Ireland DAC	RBC Investor Services Bank S.A.	Argenta Bank- en Verzekeringsgroep NV Banque et Caisse d'Epargne de l'Etat, Luxembourg Biser Topco S.à.r.l.	C.R.H. - Caisse de Refinancement de l'Habitat Citibank Holdings Ireland Ltd State Street Europe Holdings Germany S.à.r.l. & Co. KG
11% ≤ CET1R < 14%	Bank of America Europe DAC	AXA Bank Belgium SA/NV Banque Degroof Petercam SA Münchener Hypothekenbank eG RCB Bank Ltd	Deutsche Apotheker- und Ärztebank eG Deutsche Pfandbriefbank AG HASPA Finanzholding J.P. Morgan Bank Luxembourg S.A. Kutxabank, S.A.	BAWAG Group AG Credito Emiliano Holding S.p.A.
8% ≤ CET1R < 11%	Aareal Bank AG Bank of Valletta plc	Alpha Services and Holdings S.A. Banca Popolare di Sondrio, Società Cooperativa per Azioni RCI Banque SA Sberbank Europe AG	ABANCA Corporación Bancaria S.A. DekaBank Deutsche Girozentrale Erwerbsgesellschaft der S-Finanzgruppe mbH & Co. KG Ibercaja Banco, S.A. Nova Ljubljanska Banka d.d. Ljubljana Raiffeisenbankengruppe OÖ Verbund eGen Volksbanken Verbund	
CET1R < 8%	Banca Carige S.p.A. - Cassa di Risparmio di Genova e Imperia Hellenic Bank Public Company Limited HSBC Bank Malta PLC Quintet Private Bank (Europe) S.A	Bank of Cyprus Holdings PLC Banque Internationale à Luxembourg S.A. MDB Group Ltd National Bank of Greece S.A. Novo Banco, S.A. Piraeus Financial Holdings S.A.	Banco de Crédito Social Cooperativo, S.A. Eurobank Ergasias Services and Holdings S.A.	

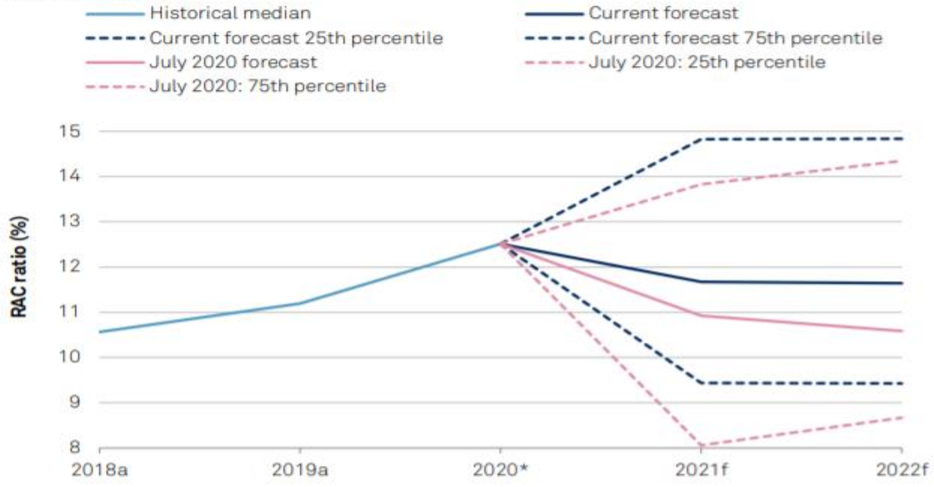
Source: S&P Global Ratings.

Our Ratings Unlikely to Be Challenged by the Stress Test Outcome

- Base Case projections confirmed **that a severe capital depletion post-pandemic** due to persistent high credit losses **is not likely**. Rather the persistence of **structurally weak profitability is of a greater risk** to European bank credit quality.
- **Only 10% of our ratings** on Top 100 European Banks **are on Negative outlook**, from 43% in mid 2020, reflecting that downward rating pressures have receded.
- Our ratings already take **a forward-looking view of a moderate reduction in capital ratios** as distributions get resumed.
- The **risk of coupon stoppage for AT1 instruments** under adverse macroeconomic developments is **not theoretical**: 22 of the 50 banks included in the EBA exercise would face constraints on coupon distributions under the adverse case.
- **One-to-one discussions with banks to follow** to take advantage of the detailed information disclosed, particularly for the EBA sample.

Capital Probably Peaked in 2020, but Will Decline only Mildly Going Forward

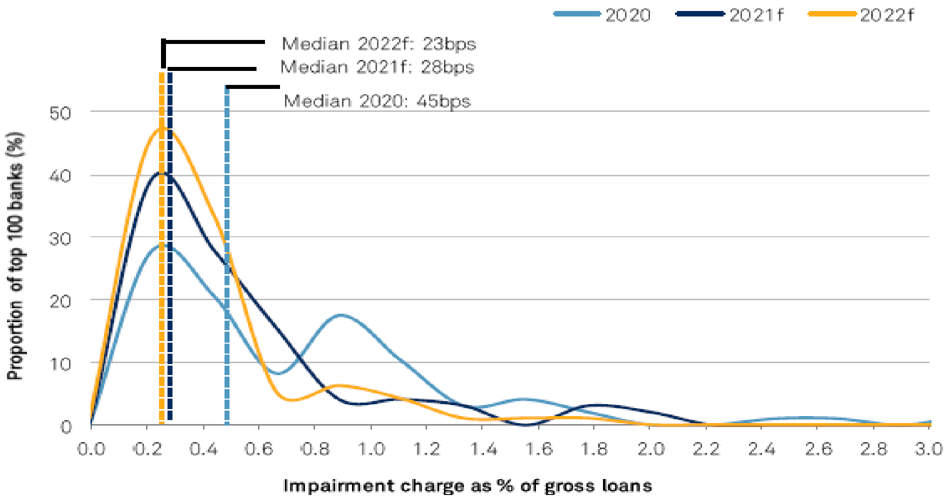
European top 100 banks' RACs: Median and middle 50% of distribution



*Data as of June 24, 2021. *2020 data are actual as far as available; we used estimates for a few entities. a--Actual. f--Forecast. RAC--Risk-adjusted capital. ECB--European Central Bank. Source: S&P Global Ratings.*

While Asset Quality Deterioration Has Yet to Come, Credit Costs Will Decline from the 2020 Peak and Would be Comfortably Absorbed

Distribution of projected credit costs for top 100 European banks



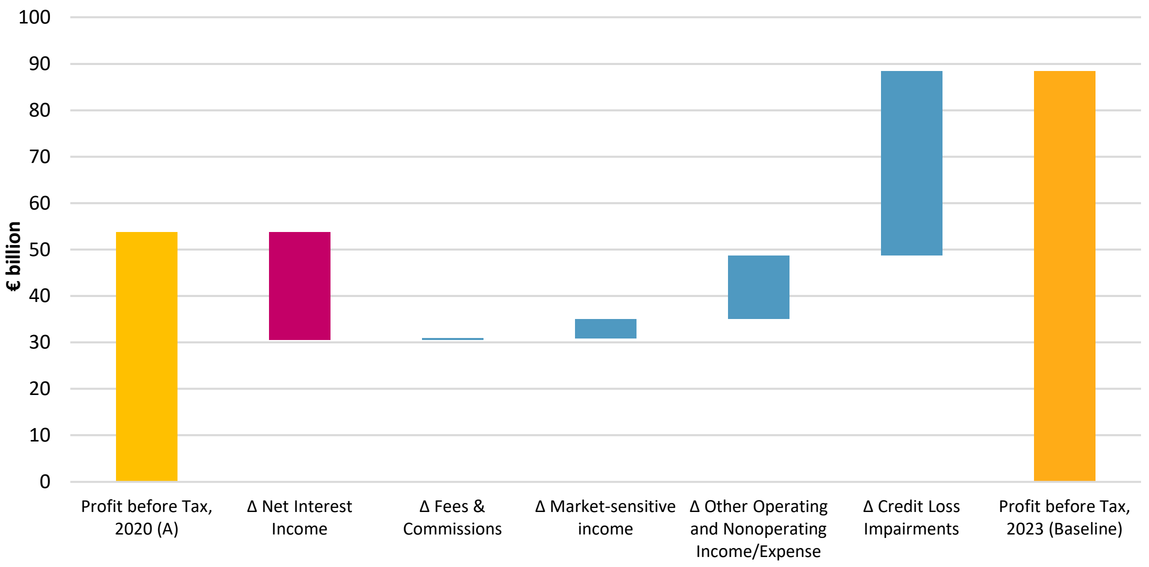
Data as of June 24, 2021. bps--Basis points. f--Forecast. Source: S&P Global Ratings.

Profitability Remains Banks’ Achilles Heel

While we remain mindful of the limitations of the EBA exercise's assumptions and methodological constraints, the aggregated and granular disclosures together provide an instructive picture.

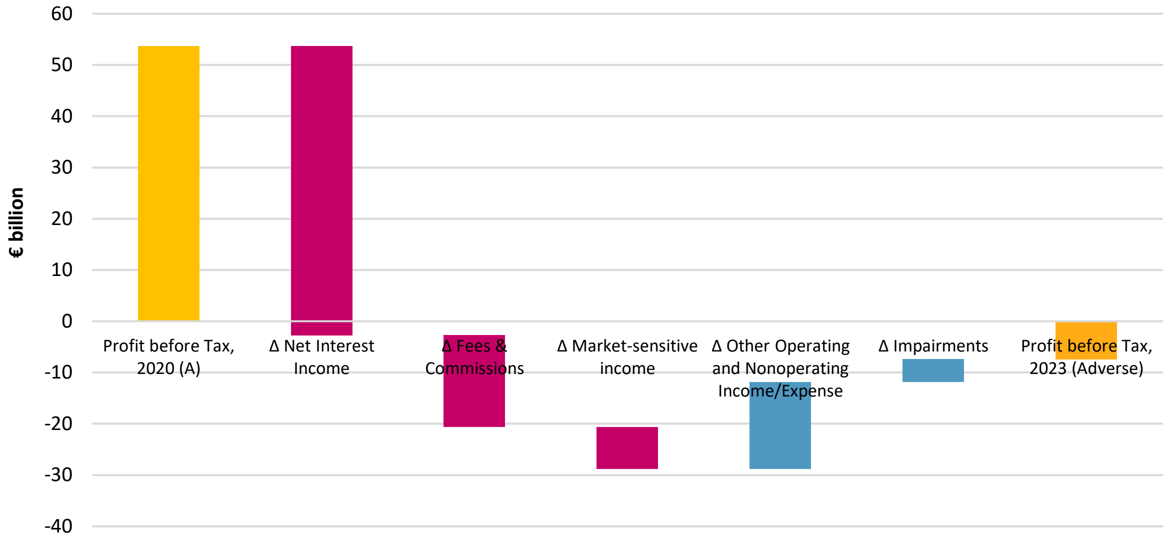
Weak Profitability Under the Base Case, Undermined by Low rates, with RoE standing at 5%-6% and no Signs of Improvement by 2023

Aggregate Changes in Selected P&L Items 2020 (A) vs. 2023 (Baseline Scenario)



In the Adverse Case Falling Income Drives Earnings into the Negative Territory Even Once Impairments Recede

Aggregate Changes in Selected P&L Items 2020 (A) vs. 2023 (Adverse Scenario)



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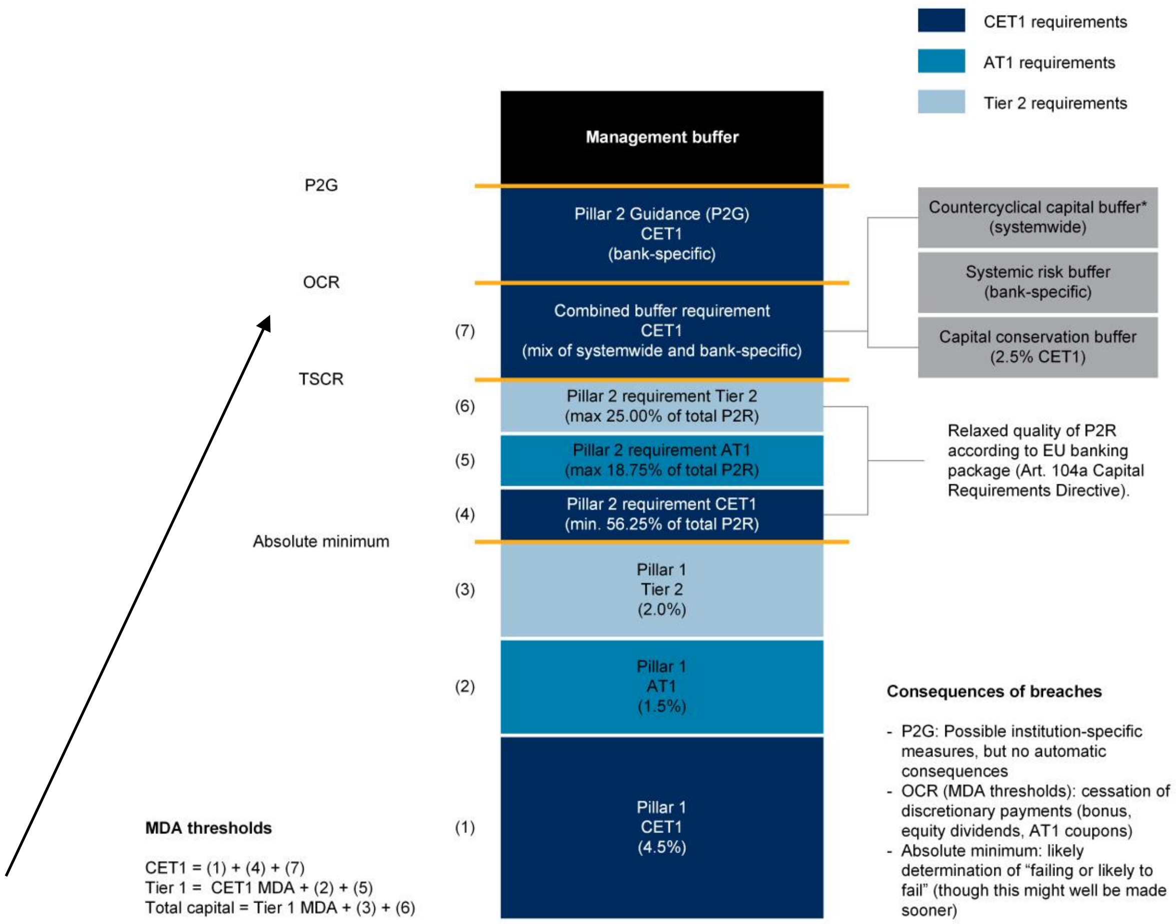
Footnote to charts: Market sensitive income compromises dividend income, Gains or losses on financial assets and liabilities held for trading and trading financial assets and trading financial liabilities. "Deltas" shown are the change modelled for 2023 relative to 2020. Sources: EBA, S&P Global Ratings.

Regulatory Consequences Only For A Minority

- ***No formal pass or fail,*** but the outcome will inform regulatory decisions, namely:
- ***Shareholder distributions***: For many, the stress test results will help regulators accept banks' distribution plans to shareholders. Only those that performed poorly will struggle to win regulatory approval to pay material dividends, or their dividend plans could be constrained.
- ***Remedial actions***: The poorest performers could be compelled to take remedial action to bolster resilience, particularly where they breached the absolute minimum requirements under stress. In practice, we expect capital-raising only for Monte dei Paschi (not rated).
- ***Capital-setting***: The exercise informs the next SREP.
  - If banks showed materially weaker or stronger data and risk governance than supervisors expected, regulators could adjust their Pillar 2 requirement (P2R).
  - Banks that show weaker modelled resilience to stress could see changes in their Pillar 2 guidance (P2G).
- In both cases, banks could see a rise (or fall) in minimum capital they are likely to hold, but the consequences of a future breach differ. Unlike P2R, P2G sits above the OCR, so a breach would not increase the risk of these banks facing mandatory restrictions of coupon payments on hybrids.

A Summary Of EU And U.K. Capital Requirements



Note: Banks may meet lower quality capital requirements with eligible higher quality capital components (i.e. Tier 2 with CET 1 or AT1, AT1 with CET1). TSCR--Total SREP capital requirement (P1R + P2R). OCR--Overall capital requirement (TSCR + CBR). MDA--Maximum distributable amount. ADI--Available distributable items. *CCyB includes sector-specific add-ons imposed under macroprudential interventions.
Source: S&P Global Ratings.

SREP—annual supervisory review and evaluation process used to determine institution-specific requirements and guidance

2021 EU Bank Stress Test: Additional Publications for Reference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2021 EU Bank Stress Test: More Demanding, Better Resilience

August 2, 2021

(**Editor's Note:** *This report was republished on Aug. 5 to include chart 10 in the Appendix.*)

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Key Takeaways

- The 101 banks that participated in the EBA and ECB's stress tests generally performed well under assumptions that were tougher than the last exercise in 2018.
- For many, this will support regulatory acceptance of their shareholders' distribution plans after the ECB's recent removal of its 2020 prohibition of such payments.
- Banks that fared less well could face tougher regulatory capital requirements and guidance; though this would typically mean that only a desired capital return may be curtailed.
- We don't expect the results of the stress tests, including possible capital return, to have a rating impact, as our ratings typically already incorporate a forward-looking expectation of a moderate reduction in capital ratios.

The latest EU bank stress tests suggest the vast majority of European banks should remain comfortably profitable during 2021-2023, even if they have to make significant top-ups to credit provisions. While structural profitability may still prove vulnerable under certain scenarios, the banks are showing improved resilience overall.

At this point, we don't expect the results of the stress tests, including possible capital return, to lead us to change ratings on any of the banks that were tested. While we will dig deeper into the results on individual banks and discuss the results with management, we saw no major surprises in the results. Our ratings typically already incorporate a forward-looking expectation of a moderate reduction in capital ratios as distributions restart.

The European Banking Authority (EBA) published the results of its 2021 stress test exercise on Friday, July 30. The publication covered 50 banking groups from 15 countries in the EU and Norway, and between them cover broadly 70% of the region's banking sector by total assets. The European Central Bank (ECB), as supervisor of the largest eurozone banks, carried out a parallel stress exercise on a further 51 banks and also announced the results on July 30.

Following the end of the post-Brexit transition period, U.K. banks were excluded from the exercise

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European Banks' 2021 Stress Test Contemplates A Tough Adverse Macroeconomic Scenario

February 1, 2021

Key Takeaways

- The European Banking Authority (EBA) has formally launched its 2021 stress test for banks. The results will be published by July 31, 2021.
- The adverse scenario sees a protracted economic contraction over 2021-2023, caused by a prolonged COVID-19 pandemic and a shock to confidence.
- Market participants will benefit from the additional disclosure of information the stress test will bring, particularly given the high uncertainty surrounding the impact of the pandemic on banks' books.
- Although the goal is to test banks' resilience should they have to absorb a much sharper than expected rise in credit losses, thus highlighting potential capital shortfalls, the stress test will likely offer insights on the Achilles' heel of many European banks—that of persistently weak profitability.

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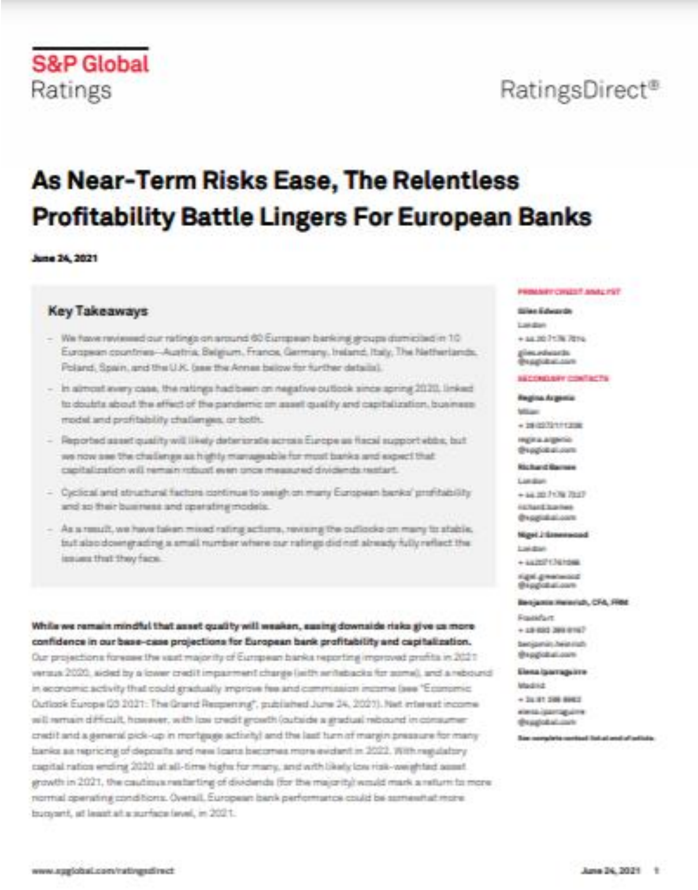
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As Near-Term Risks Ease, The Relentless Profitability Battle Lingers For European Banks

June 24, 2021

Key Takeaways

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