EUROPEAN CENTRAL BANK

BANKING SUPERVISION

Danièle NOUY

Chair of the Supervisory Board

COURTESY TRANSLATION

Dr Michael Meister
Parliamentary State Secretary
German Federal Ministry of Finance
Wilhelmstraße 97
10117 Berlin

Frankfurt am Main, 25 July 2017

Re: Your letter in line with the right of national parliaments in the banking union to ask questions

Honourable Parliamentary State Secretary, dear Dr Meister,

Thank you for your letter dated 22 June 2017 submitting a number of questions relating to Banco Popular Español S.A. from Member of the German Parliament Dr Gerhard Schick in line with the right of national parliaments to pose questions to ECB (European Central Bank) Banking Supervision.[1]

Please note that any reporting obligations are subject to the relevant professional secrecy requirements, as outlined in the Capital Requirements Directive IV[2]. These rules also apply to information about banks which the ECB determined failing or likely to fail. While I cannot disclose confidential information, let me nevertheless provide you with some relevant considerations in response to your questions.

The recent liquidity crisis experienced by Banco Popular Español S.A. was idiosyncratic and was triggered by a series of events over the recent months, including:

- in February 2017 the institution disclosed the need for extraordinary provisions amounting to €5,700 million, leading to losses of €3,485 million in 2016, and appointed a new chairman;
- on 10 February 2017 DBRS downgraded the rating of the institution;
- on 14 February 2017 Fitch downgraded the rating of the institution;
- on 3 April 2017 the institution released an ad hoc public statement on the outcome of several internal audits with a potentially significant impact on its financial statements and confirmed that it would replace its chief executive officer after less than one year in office;
- on 7 April 2017 Standard & Poor's downgraded the rating of the institution;
- on 10 April 2017 the institution announced that it would not pay dividends and that a capital increase or a corporate transaction could be required owing to the group's tight capital position and the level of its non-performing assets;

1 In line with Article 21(2) of Council Regulation (EU) No 1024/2013.

2 Directive 2013/36/EU of the European Parliament and of the Council.

- on 21 April 2017 Moody's downgraded the rating of the institution;
- on 3 May 2017 the group disclosed its quarterly results for the first quarter of 2017, which underperformed market expectations;
- on 31 May 2017 it was disclosed in the media that the bank could face a wind-down process if the ongoing sale process was not finalised in the very short term;
- on 6 June 2017 DBRS and Moody's downgraded the rating of the institution.

The ECB has continuously monitored the situation, increasing the frequency of that monitoring when the situation became more critical, i.e. daily since the beginning of April. In particular, the monitoring of the liquidity coverage ratio (LCR)[3], to which you refer in your question 6, was one of the supervisory tools used to assess liquidity risk.

In response to your questions 1, 2 and 4, on 6 June 2017 the significant deterioration of the liquidity situation of Banco Popular Español S.A. led to the determination that the entity would have, in the near future, been unable to pay its debts or other liabilities as they fell due. This situation made it impossible to delay the failing-or-likely-to-fail decision until the weekend, as there were no alternative supervisory or early intervention measures available which could have prevented the failure. Moreover, on 6 June, the entity notified the ECB in accordance with Article 21(4) of Law 11/2015[4] that it was failing. Consequently, the ECB determined that the bank was failing or likely to fail in accordance with Article 18(1) of the Single Resolution Mechanism Regulation (SRMR)[5] and duly informed the Single Resolution Board (SRB), which adopted a resolution scheme entailing the sale of business.

Regarding your question 5, the resolution by sale of business was implemented by the resolution authorities having regard to the results of the valuation of the institution which was carried out specifically for that purpose in accordance with Article 20 of the SRMR. This type of valuation, which is consistent with the goals of the resolution, is transaction-specific and, thus, should not be considered as an assessment of the capital position of Banco Popular Español S.A. on a stand-alone basis.

The aforementioned ECB decision that the bank was failing or likely to fail was taken on the basis of insufficient liquidity. At this time, the objective elements[6] were not sufficient for the ECB to determine that the institution was failing or likely to fail on the basis of its capital position. Of course, the ECB had been closely monitoring not only the liquidity but also the capital position of the bank. Its structural problems (high level of non-performing assets, low coverage, poor profitability) were reflected in commensurate capital requirements established by the ECB.

As regards our interaction with Banco Popular Español S.A., which you mention in your question 3, the ECB conducts ongoing off-site supervision, which involves several forms of interaction with the bank, including

[3] LCR disclosure guidelines were issued by the European Banking Authority (EBA) in March 2017, to be applied from 31 December 2017. Currently, no public information is disclosed on the LCR ratio level and consequently the ECB cannot comment on its level for a specific institution.

[4] Law 11/2015 of 18 June on the recovery and resolution of credit institutions and investment firms, transposing the Bank Recovery and Resolution Directive into Spanish law.

[5] Regulation (EU) No 806/2014 of the European Parliament and of the Council.

[6] Following the EBA Guidelines on the interpretation of the different circumstances when an institution shall be considered as failing or likely to fail under Article 32(6) of Directive 2014/59/EU: https://www.eba.europa.eu/documents/10180/1085517/EBA-GL-2015-07+GL+on+failing+or+likely+to+fail.pdf

face-to-face meetings throughout the year, as well as telephone calls and written communication. This is complemented by on-site inspections on targeted topics, with the on-site team maintaining a continuous presence at the bank's premises for the duration of the inspection.

Finally, please note that your questions relating to the resolution process (the valuation, the sale process, the information available to the SRB, etc.) will be answered by the SRB.

Yours sincerely,

[signed]

Danièle Nouy