



EUROPEAN CENTRAL BANK
BANKING SUPERVISION

Danièle NOUY

Chair of the Supervisory Board

COURTESY TRANSLATION

President of the German Bundestag
Dr Wolfgang Schäuble
Platz der Republik 1
11011 Berlin

Frankfurt am Main, 12 July 2018

Re: Your letter of 13 June 2018

Honourable President, dear Dr Schäuble,

Thank you for your letter of 13 June 2018, in which you submit a number of questions from the Member of the German Parliament, Mr Schäffler, some of them falling into the area of competence of the ECB.

As regards the request (question 1) to provide data on Italian banks, and on banks' exposures to the Italian sovereign, I would like to refer you to the EBA's 2017 EU-wide transparency exercise.¹ This exercise provides data on a bank-by-bank basis for 132 banks across 25 countries of the European Union and the European Economic Area, including Italy. The data are exclusively based on supervisory reports and are published at the highest level of consolidation for the reference dates of 31 December 2016 and 30 June 2017. They have been subject to a thorough data quality assurance process and provide answers to the questions asked by Mr Schäffler.

Specifically, the EBA data show that the volume of loans extended by the Italian banks in the EBA sample stood at €1.7 trillion as of the second quarter of 2017. The gross non-performing exposures (NPEs) of these banks totalled €199.7 billion in the same period, resulting in a gross NPE ratio of 12.0%. Their total exposure to the Italian sovereign amounted to €142.6 billion (of which €23.8 billion were loans and advances and €118.8 billion were debt securities) in the second quarter of 2017. These exposures represented approximately 119% of the banks' CET1 capital.²

With regard to the holdings of Italian government bonds by other banks, please note that the exposure of non-Italian banks in the EBA sample to the Italian sovereign amounted to €150.4 billion as at 30 June 2017. This represented approximately 10% of their CET1 capital.³

¹ <https://www.eba.europa.eu/risk-analysis-and-data/eu-wide-transparency-exercise/2017/results>

² Net of deductions and after applying transitional adjustments.

³ Net of deductions and after applying transitional adjustments.

On the question 3 of how increases in the yield on Italian government bonds are incorporated into stress tests, please note that the re-emergence of public debt sustainability concerns is included in the list of main financial stability risks in the 2018 EBA adverse scenario narrative and this is reflected in a material widening of the spreads in the scenario calibration. While a similar widening of spreads was indeed included in the scenarios of previous EBA exercises, it should be noted that several other factors and shocks play a role in determining the EBA exercise results, apart from developments in sovereign bond yields.

In addition to the EBA exercise, the ECB conducts other stress test analyses based on the current risk assessment, the results of which are published in the biannual Financial Stability Review (FSR). In the May 2018 issue of the FSR, the re-emergence of public debt sustainability concerns was also included in the main financial stability risks and hence taken into account in the stress test analyses.

Finally, in 2017, ECB Banking Supervision conducted a sensitivity analysis on interest rate risk in the banking book covering, inter alia, a 200 basis point upward interest rate shock. While bank-specific results cannot be disclosed, the analysis showed that interest rate risk is well managed by most European banks. The results were also used to inform the 2017 Supervisory Review and Evaluation Process (SREP), to adjust the level of 2016 Pillar 2 Guidance and to enrich Pillar 2 Requirements and qualitative measures.

On the question (3a) of the yield at which banks would be declared “failing or likely to fail”, let me state the following.

The ECB applies the criteria established by law and specified in the EBA's Guidelines on failing or likely to fail.⁴ These guidelines provide a set of objective elements that should support the determination that an institution is failing or likely to fail. However, the identification of a single objective element specified in these guidelines in respect of a particular institution does not lead to the automatic determination that it is in fact failing or likely to fail. Rather, the relevant authorities should decide in each case whether an institution is failing or likely to fail on the basis of a comprehensive assessment of both qualitative and quantitative objective elements, taking into account all other circumstances and information relevant to the specific institution.

Given the number of factors to be taken into account when assessing whether a bank is failing or likely to fail, it is not possible to determine ex ante a level of government bond yields at which banks would be failing or likely to fail or would pose a threat to financial stability (question 3b). There are numerous factors that affect the resilience of the banking sector and financial stability in the euro area. Looking back, the government bond yields observed during the sovereign debt crisis of 2011-12 proved problematic for banks. However, the banking systems of the euro area countries have changed substantially since then and, in particular, their resilience has markedly increased. As a result, European institutions are now better equipped to deal with a crisis of this kind.

As regards the other questions, let me clarify that the ECB designs scenarios for stress test analyses based on the current risk assessment. The scenarios should be severe and plausible in order for the assessment of the resilience of the banking system to be credible. As the ECB President has stressed on numerous occasions, the euro is irrevocable and it is not appropriate for the ECB to engage in reflections on hypotheses not provided for in the Treaty on the Functioning of the European Union.⁵

⁴ https://www.eba.europa.eu/documents/10180/1156219/EBA-GL-2015-07_EN_GL+on+failing+or+likely+to+fail.pdf

⁵ For example: https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter170608_zanni.en.pdf

Finally, I should inform you that the questions falling into the area of competence of the Single Resolution Board (SRB) will be answered by the SRB.

Yours sincerely,

[signed]

Danièle Nouy