



EUROPEAN CENTRAL BANK

BANKING SUPERVISION

ECB-PUBLIC

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ECB report on recovery plans

Finansinspektionen, 12 June 2019

Overview

- 1 Background
- 2 Overview of the report – Five key topics

ECB published a report to share with SIs SSM recovery plan experiences

- *Purpose of the report:*

Present lessons learned and best practices after 3 successive cycles of ECB recovery plan assessments in order to **help SIs further improve their plans and make them more operational**

- *Important disclaimers*

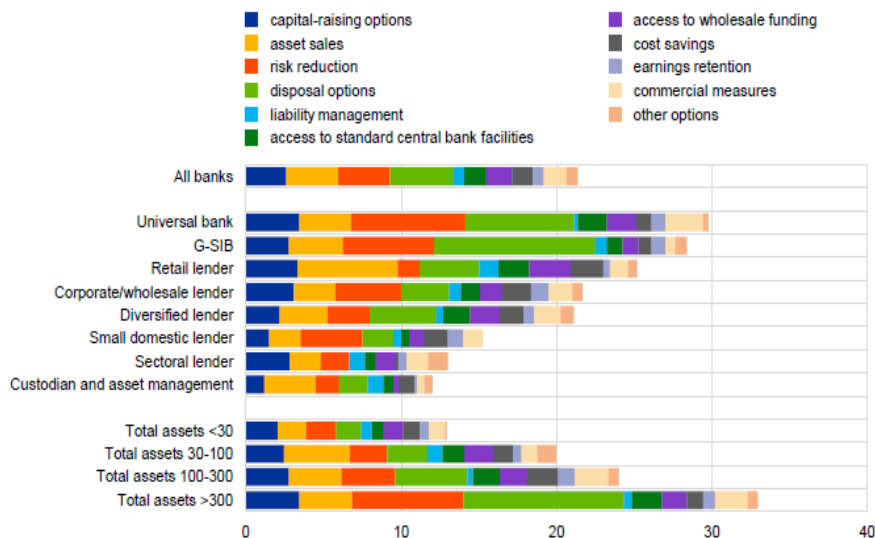
- The report **does not**
 - impose additional requirements (beyond requirements in legislation)
 - create additional ‘supervisory expectations’
- Although banks are encouraged to consider this report when updating their recovery plans, it is stressed that they should rely on their individual feedback letters for bank-specific feedback
- All graphs/figures/tables presented in the report are only indicative examples

The report focuses on five key topics which are described in more detail in the following slides

- 1. Recovery options**
- 2. Overall recovery capacity**
- 3. Indicators**
- 4. Playbooks**
- 5. Dry-runs**

Improving the feasibility of recovery options remains key as banks often do not provide a comprehensive analysis

Number of recovery options by business model



The **benchmarking analysis** has shown that the number of options has overall increased but some banks fail to provide:

- A sufficient description **of the impact of each recovery option**
- Adequate evidence to support the **feasibility** of their recovery options, including the **timeline** required to implement them

Source: Benchmarking of 2017 cycle recovery plans – data of 95 standardized reporting templates

A comprehensive presentation of options is one of the key elements for enhancing the credibility of a recovery plan

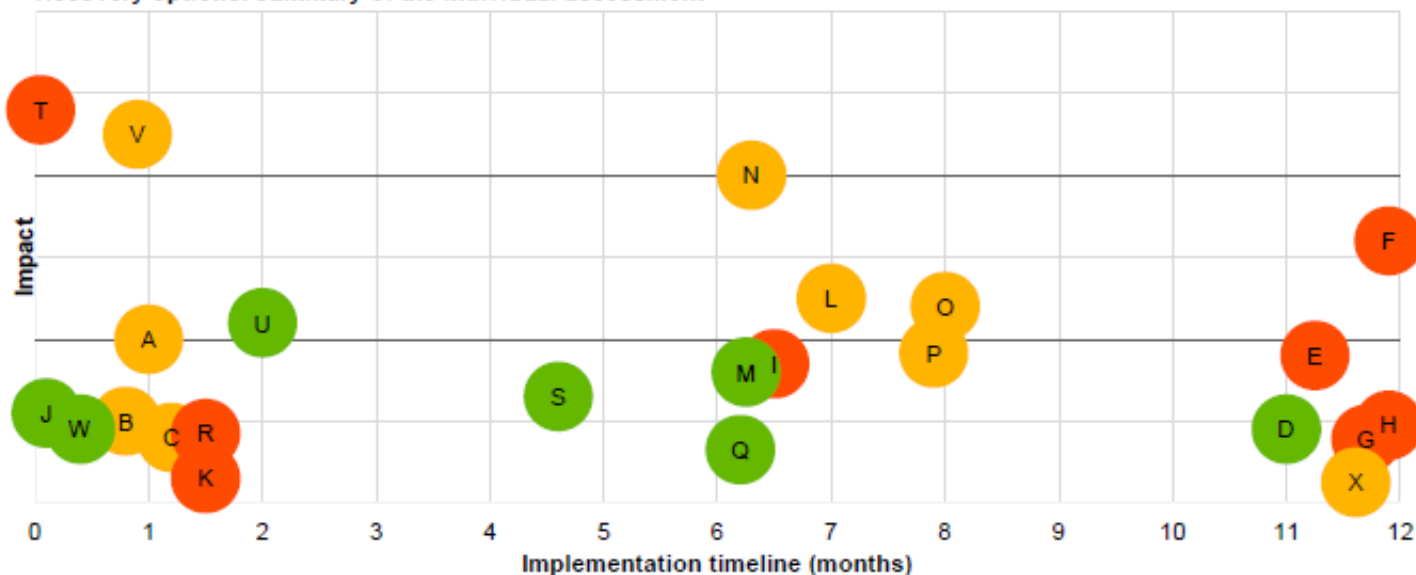
The report stresses the importance of:

- **A sufficiently wide range of recovery options**
- **A comprehensive presentation of options**
 - Best practice: consistent presentation using an overview
 - Best practice: detailed analysis of selection criteria
- **Clear evidence/justification to support feasibility analysis**
 - Best practice: anticipation of potential impediments and timeline for implementation
 - Best practice: overview table of feasibility analysis
- **Take into account market conditions when assessing feasibility**
- **Impact assessment of options on capital, liquidity & profitability**
 - Best practice: overview table incl. range of impacts under different scenarios
- **Realistic and plausible assumptions for valuation of options**
 - Best practice: concise description of valuation methodology / past experience

Example of how to present the selection criteria for recovery options

- low complexity
- medium complexity
- high complexity

Recovery options: summary of the individual assessment



Example of how to present an overview of the impact of each recovery option

#	Measure	Capital (EUR millions / basis points)				Liquidity (EUR millions)		RWA (EUR millions)		Impact on profitability	Impact on business model	Timing (days)		Owner (Function)
		Min.	Max.	Min.	Max.	Min.	Max.	Prep.	Effects					
1	Option A	1378	164 bps	1726	188 bps	1 000	2 100	n.a.	n.a.	Low	Low	119	112	Treasury
2	Option B	174	12 bps	1189	82 bps	400	420	n.a.	n.a.	Neutral	Neutral	60	10	Treasury
3	Option C	1493	103 bps	3176	219 bps	3 260	6 500	-4 800	-7 000	Low	Low	119	30	Treasury
4	Option D	1306	297 bps	1480	300 bps	5 800	7 000	n.a.	n.a.	Low	Low	119	112	Treasury
5	Option E	1740	120 bps	1 131	78 bps	3 600	4 300	-5 100	-7 400	Low	Low	28	5	Mgmt Board
6	Option F	58	4 bps	218	15 bps	100	400	n.a.	n.a.	Low	Low	32	3	Mgmt Board
7	Option G	667	46 bps	899	131 bps	n.a.	n.a.	n.a.	n.a.	Neutral	Low	90	10	Mgmt Board
8	Option H	116	8 bps	319	22 bps		400	-2 000	-5 900	Neutral	Neutral	25	7	Mgmt Board
9	Option I	0	0 bps	479	33 bps		17 000	-4 800	-6 800	Low	Low	90	5	Treasury
10	Option J	276	19 bps	276	19 bps	n.a.	n.a.	-5 800	-5 800	Low	Low	92	59	Treasury
11	Option K	276	19 bps	421	29 bps	1 900	2 180	-2 000	-5 900	Neutral	Neutral	25	59	HR
12	Option L	232	16 bps	304	21 bps	2 000	5 000	-5 700	-7 000	Low	Low	25	25	HR

Impact on capital, liquidity and RWAs; implementation timeline; impact on profitability and business model

■ High/Fast/Low
 ■ Medium/Medium/Neutral
 ■ Low/Slow/Significant

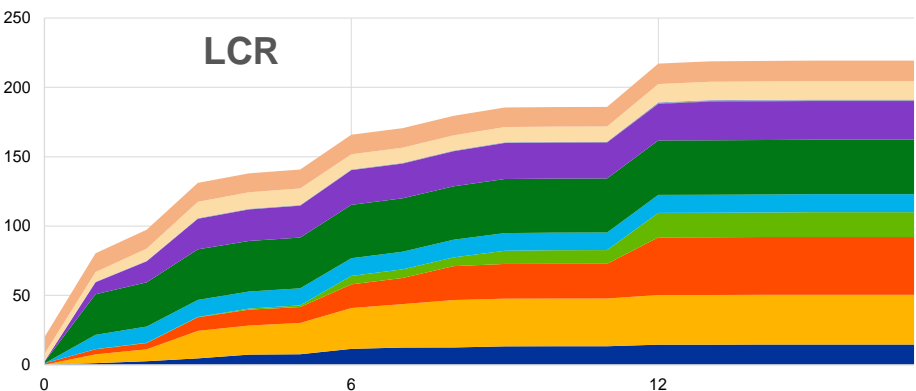
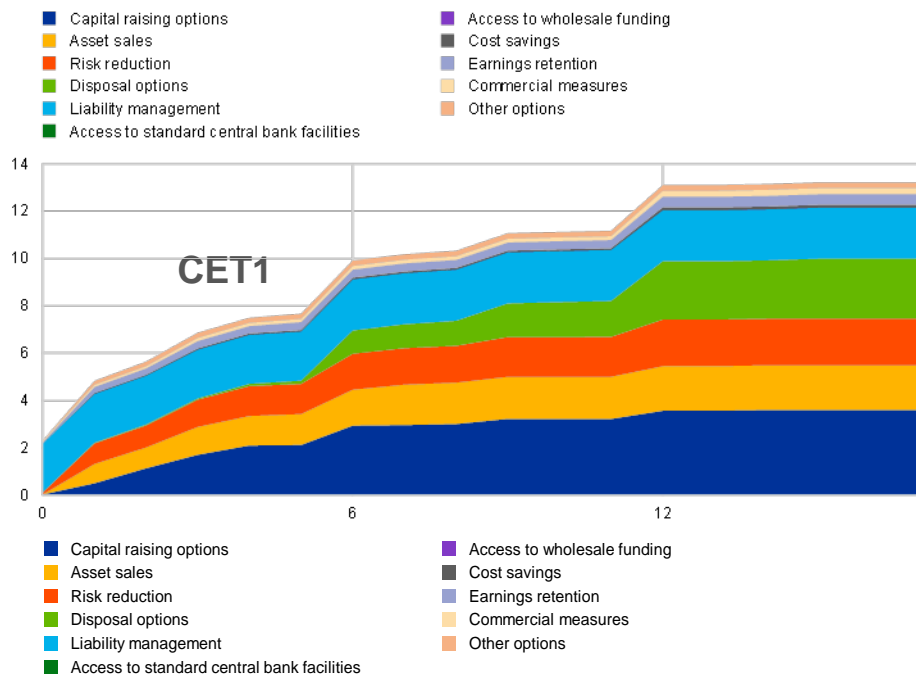
Example of how to present the feasibility of recovery options

#	Measure	Experience	Possible impediments/risk factors					Time frame	Feasibility
		YES/THEORETICAL/NO	Legal	Operational	Financial	Reputational	Business/ Group structure		
1	Option A	YES	Medium	High	Low	Medium	Low	immediate	Low
2	Option B	YES	Low	Low	Medium	Medium	Low	immediate	Medium
3	Option C	YES	Low	Low	Low	Low	Low	immediate	High
4	Option D	NO	Low	High	Low	Low	Low	1-2 months	Low
5	Option E	YES	Medium	High	High	Medium	Low	1-2 months	Low
6	Option F	NO	Low	Low	Low	Medium	Medium	2-3 months	Low
7	Option G	NO	Low	Low	Low	Medium	Low	2-3 months	Low
8	Option H	YES	Medium	Low	Low	Medium	Low	3-6 months	Medium
9	Option I	YES	Low	Medium	Medium	Low	Low	3-6 months	Medium
10	Option J	THEORETICAL	Low	Low	High	Low	Low	9 months	Low
11	Option K	THEORETICAL	Low	Low	Low	Medium	Low	12 months	Medium
12	Option L	YES	Low	Low	Low	Low	Low	12 months	High

Impediments / feasibility

High/Fast/Low
 Medium/Medium/Neutral
 Low/Slow/Significant

Banks tend to largely overstate their overall recovery capacity



Source: Benchmarking of 2017 cycle recovery plans – data of 95 standardized reporting templates

ECB report on recovery plans

The **benchmarking analysis** has shown that banks report that in a crisis they could, on average, increase

- CET1 by approx. 13 ppt ...
- LCR by 230 ppt ...
- ... in less than 13 months.

When estimating their ORC, **some banks seem to neglect basic concepts:**

- Summing up mutual exclusive options
- Fire sales without any haircuts
- Parallel disposals of major parts of the balance sheet without any impact on business model or haircuts

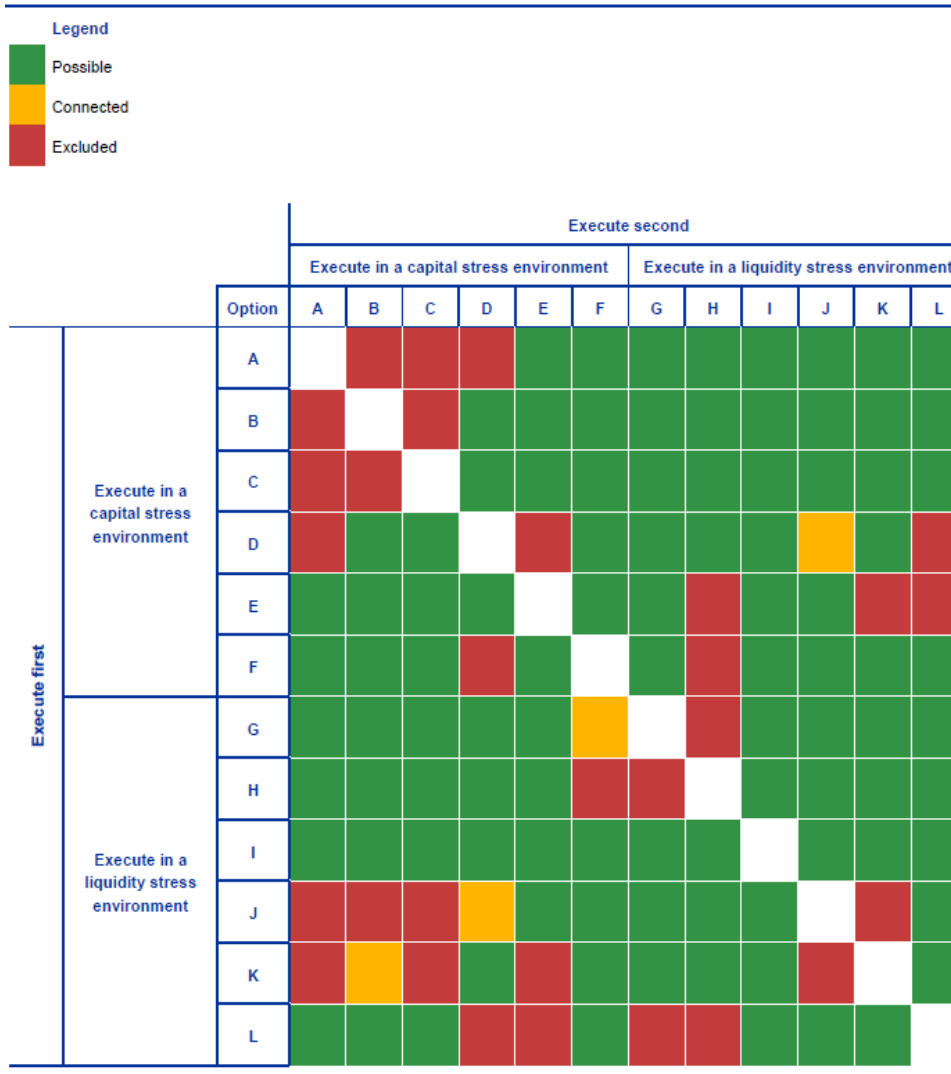
An adequate estimation of ORC is key for assessing whether a bank can overcome a crisis by implementing its recovery options

Based on the ECB experience a realistic overview of banks' ORC usually considers the following elements:

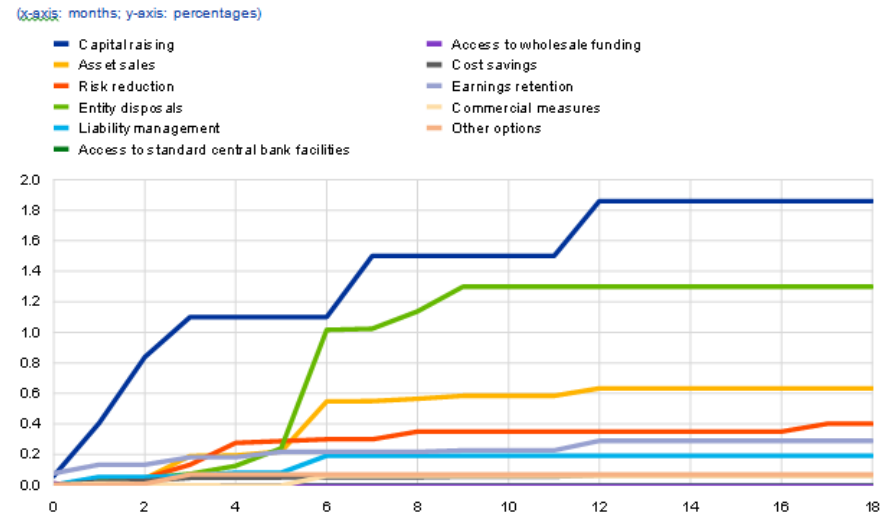
- 1. Mutual exclusivity**
- 2. Interdependencies between various recovery options**
- 3. Capacity to implement under idiosyncratic versus system-wide events**
- 4. Reputational effects**
- 5. Operational capability**
- 6. Consequences for the business model**
- 7. Proper testing of the set of options**
- 8. Optimising for capital and liquidity crisis situations**

The report also provides several examples of how to present the ORC

Example of how to present the qualitative interrelations/interdependencies between individual recovery options

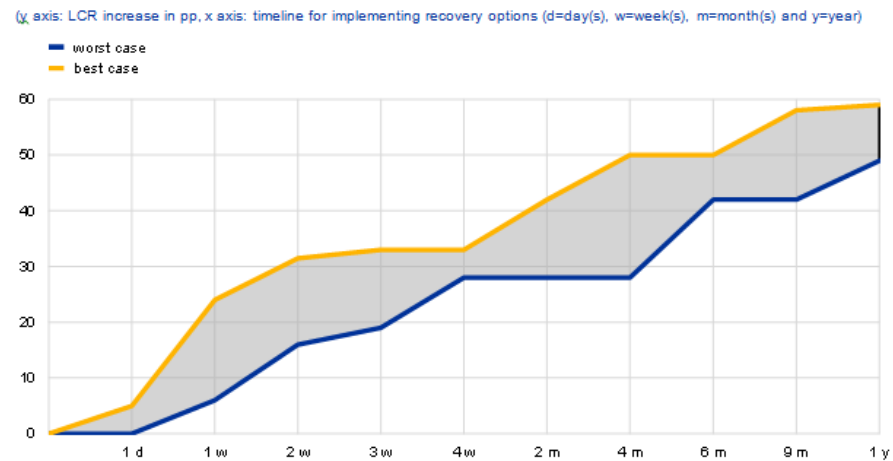


Example of how to present the aggregate impact of ORC in terms of the CET1 ratio



Source: Based on compilation of best practices adopted by several SIs. All data are fictitious.

Example of how to present the build-up of ORC over time



Source: Based on compilation of best practices adopted by several SIs. All data are fictitious.

The usage of indicators from the EBA minimum list needs improvement Only capital indicators and LCR are widely used (green)

Usage of indicators from EBA minimum list (heatmap)

Bank category	Capital			Liquidity			Profitability		Asset quality		Market-based			Macroec.	
	CET1 ratio	TC ratio	Leverage ratio	LCR	MSFR	Cost of wholesale funding	RoE or RoA	Significant operational losses	NPL Growth rate	Coverage ratio	Rating downgrade/ negative review	CDS spread	Stock price variation	GDP variations	CDS of sovereigns
All banks	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Retail lender	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
G - SIB	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Small domestic lender	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Corporate-/Wholesale-lender	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Sectoral lender	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Universal bank	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Diversified lender	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Custodian and asset management	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Total assets < 30	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Total assets 30 - 100	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Total assets 100 - 300	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow
Total assets > 300	Green	Green	Green	Green	Yellow	Orange	Green	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow	Yellow

The **benchmarking analysis** has revealed that institutions often:

- Do not include indicators that reflect their key vulnerabilities and risk factors adequately
 - banks with high credit risk → no asset quality indicator
 - banks with significant operational risk losses → no indicator for operational risk
 - listed banks → no market-related indicators
- Do not calibrate the thresholds of their recovery indicators at adequate levels in line with EBA Guidelines
- Do not adequately integrate the recovery indicators within their Risk Management Framework

dark green = all SIs in peer group use the indicator
dark red = no SI in peer group uses the indicator

Source: Benchmarking of 2017 cycle recovery plans- data of 95 standardized reporting templates

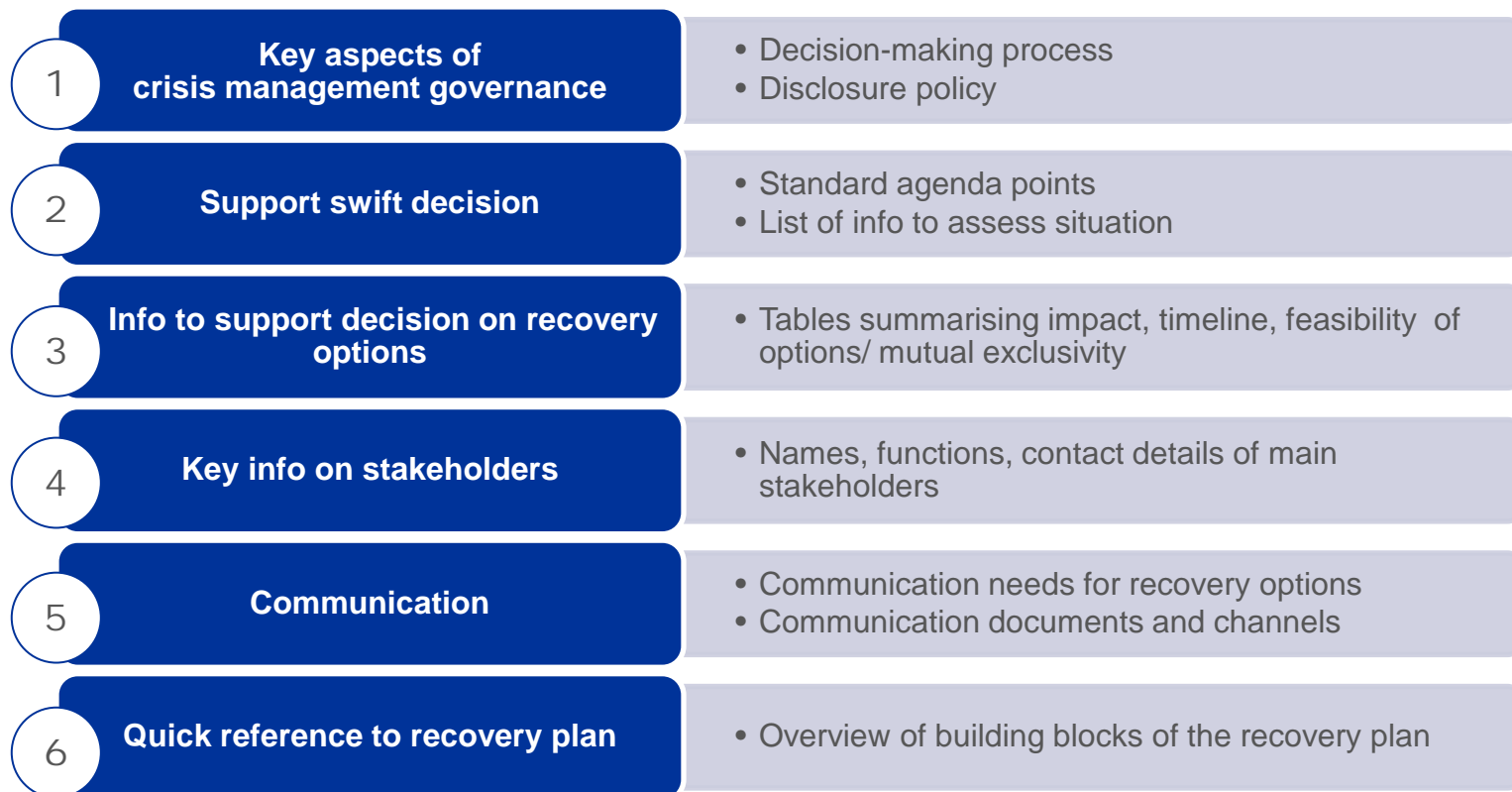
Selecting the right set of indicators (and thresholds) is key for effective recovery

The report stresses the importance of:

- better aligning banks' recovery indicator frameworks with the **EBA minimum list** but without limiting them to the minimum list
- capturing **key factors of banks' business and risks** and considering forward looking indicators (e.g. asset encumbrance indicator)
- including at least **all indicators that are based on regulatory requirements**
 - Banks are also encouraged to include the **MREL indicator**, at the latest when the MREL becomes binding and applicable to them
- calibrating **indicator thresholds** with the aim to foster adequate reaction time and capacity, ensuring **full compliance with the EBA guidelines**
- taking into account the **continuity of the risk management framework** and aligning the recovery framework with the overall risk management framework
- ensuring that **management/supervisors are informed without delay**

Playbooks have been identified as a best practice that can make recovery plans more operational

The report presents examples that are indicative of good playbooks



Example of recovery options overview table

Nr.	Description	Experience with measure	Min - max Impact capital (EUR bn)	Min - max Impact liquidity (EUR bn)	Time to prepare	Time to implement	Applicability in stress		Responsible for Execution
							Bank specific		
							Fast	Slow	
1	Disposal option 1	Practical experience	2378 - 2726	150 - 210	3 months	< 1 month			Treasury
2	Earnings retention	Practical experience	174 - 1189	400 - 420	1 day	O/N			Treasury
3	Capital increase 1	Practical experience	1493.5 - 3175.5	3260 - 6500	< 1 month	< 4 weeks			Treasury
4	Capital increase 2	Theoretical experience	4306.5 - 6380	9800 - 13000	< 1 month	< 4 weeks			Treasury
5	Disposal option 2	No experience	1740 - 1131	3600 - 4300	< 4 months	< 1 month			Mgmt Board
6	Liability Management	Theoretical experience	n.a.	100 - 400	O/N	O/N			Sales Dep.
7	Risk reduction	Theoretical experience	116 - 319	0 - 400	< 2 weeks	< 1 day			CRO
8	Asset sales	Practical experience	n.a.	0 - 17000	< 2 days	< 2 weeks			Treasury
9	Cost savings	Practical experience	275.5 - 420.5	1900 - 2180	< 1 month	< 1 day			HR
10	Use of central bank facilities	Theoretical experience	n.a.	14500 - 25500	1 day	O/N			Mgmt Board

Example of potential agenda items

No	Agenda Point	Person to act
1	Summarise current situation (potential severity, known facts)	Person/Function X
2	Discuss relevant report summarising the situation, including the following aspects: <ul style="list-style-type: none"> I Status of indicators II Possible causes for recovery indicators breaching threshold(s) III Comprehensive information on specific weaknesses IV Assessment of possible crisis scenarios and the consequences thereof V Initial assessment of possible measures to be taken VI Summary of the potential immediate consequences of the decision to initiate crisis processes/recovery options VII Advice on whether disclosure is necessary 	Person/Function Y
3	Take a decision based on the operating environment, the financial position, viability and recoverability.	Person/Function Y
4	Document the decision of whether or not to activate the recovery plan in the minutes along with supporting arguments	Person/Function Z
5	If decision is made to initiate the recovery plan, implement crisis processes/playbook	Person/Function Y

Dry-runs complement playbooks as best practices to improve the usability of recovery plans

The report presents some examples of good practices – based also on experience of institutions that have already conducted dry-runs

- **Elements of good practices include:**



Thank you

<https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.reportrecoveryplans201807.en.pdf>