SRB – BANKING INDUSTRY DIALOGUE MEETING

Update on MREL policy 2021 and Resolvability Assessment

Presenter: **Sebastiano Laviola**

Monday, 14 June 2021

Single Resolution Board

AGENDA

MREL POLICY 2021

1. MREL targets and build-up
2. Covid-19 impact on cost of funding and Issuances
3. SRB MREL Policy: what is already in place and 2021 update
4. MREL Maximum Distributable Amount (M-MDA)
5. SRB Permission regime to reduce eligible liabilities under Art. 78a CRR
6. Reporting: What data will the SRB collect in 2021?
7. Outlook for next Resolution Planning Cycles

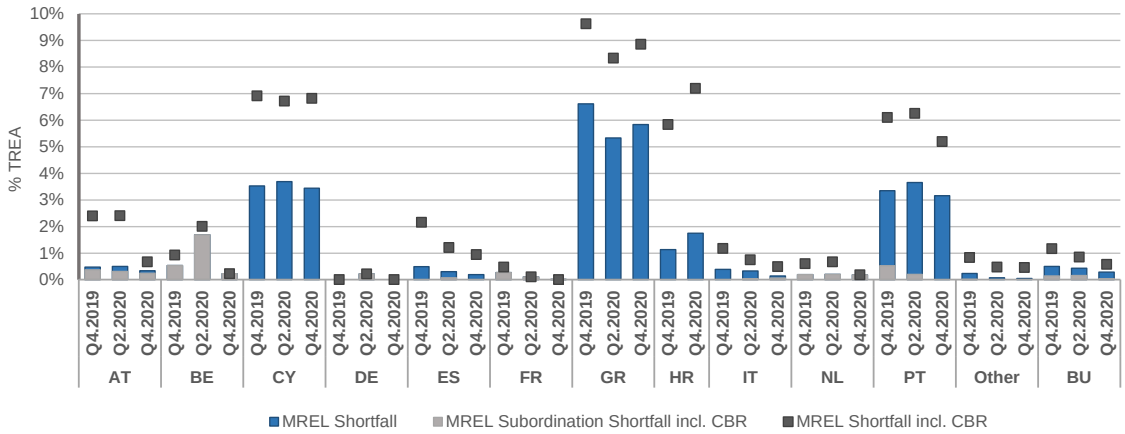
SRB approach to resolvability assessment

1. Expectations for banks
2. The resolvability “heat-map”
3. Monitoring and benchmarking analysis
4. “Incentive-compatible” approach
5. Areas of focus for 2021 RPC

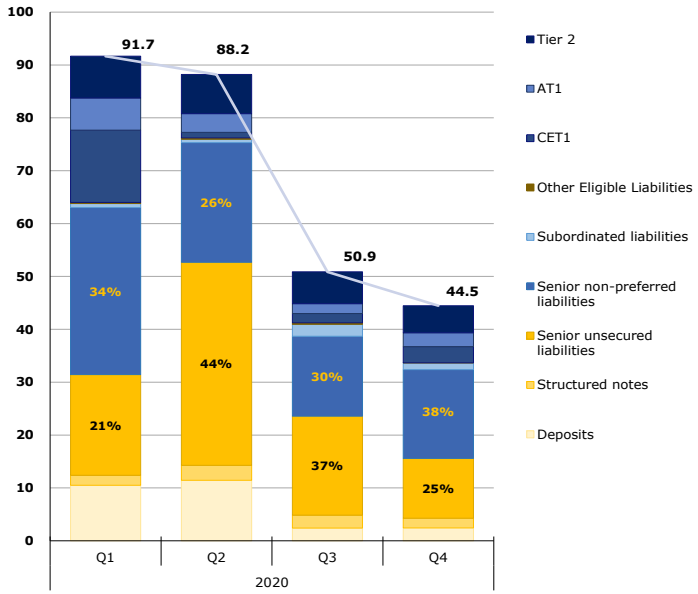
MREL POLICY 2021

1. MREL TARGETS AND BUILD-UP

BRRD 2 MREL shortfall against final targets (of which subordination), % TREA



MREL issuances by instrument (EUR bn)



▶ Average BRRD2 MREL metrics as of December 2020

- MREL target including CBR accounted for 26.0% TREA (EUR 1774 bn) – of which 17.1% TREA (EUR 1165 bn) for the subordination part.
- MREL instruments outstanding accounted for 31.2% TREA (EUR 2131 bn)
- MREL shortfall (against final target) including CBR was 0.6% TREA, i.e. EUR 39.6 bn

▶ MREL build-up over 2020

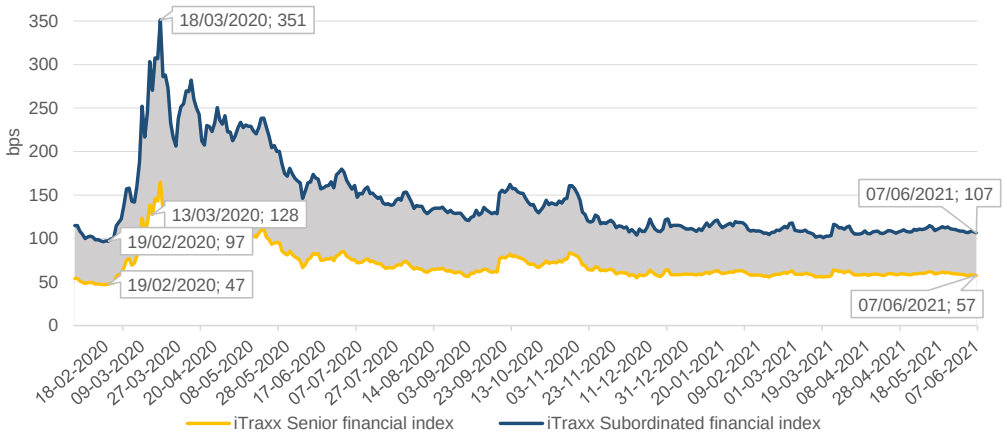
Gross yearly issuance was EUR 275.2 bn of MREL liabilities and own funds, with a decrease in pace during the last quarter.

Source: SRB Q4 2020 MREL dashboard

2. COVID-19 IMPACT ON COST OF FUNDING AND ISSUANCES

- The cost of funding has strongly decreased after the peak reached in March 2020, reaching nearly pre-Covid-19 levels.
- As of end-May 2021, the index of subordinated debt and of senior debt were 1.1 and 1.2 times pre-Covid-19 levels, respectively.

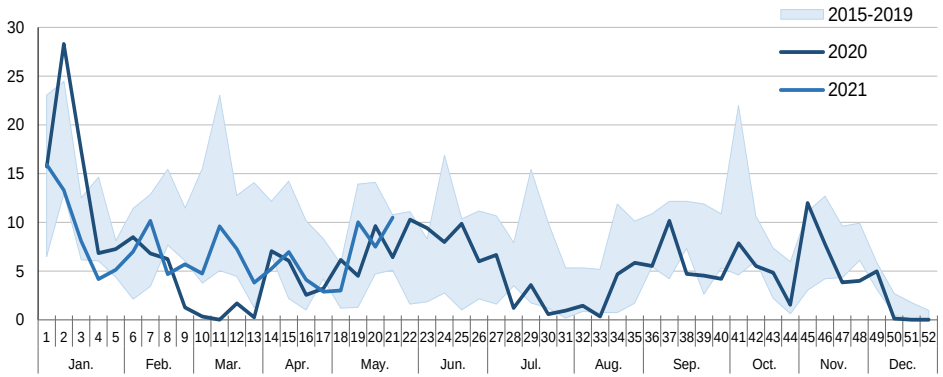
iTraxx on EU financial Subordinated and senior instruments



Source: Bloomberg Finance L.P.

- After a slow start during the first quarter of 2021, banks' issuance activity recovered since March, remaining higher than last year after the Covid-19 outbreak and hitting the year's highest level in May.

Weekly euro-banks issuances (EUR bn)



Source: Dealogic, ECB calculations

3. SRB MREL POLICY: WHAT IS ALREADY IN PLACE?

- In May 2020, **the SRB published its MREL policy** implementing the vast majority of changes introduced by the applicable **SRMR2, BRRD2 and CRR2 rules.**

- The policy covered the following aspects:
  - MREL requirements for Global Systemically Important institutions (G-SIIs);
  - Changes to the calibration of MREL, including introducing MREL based on leverage ratio exposure (LRE) and based on risk-weighted exposure (TREA);
  - Changes to the quality of MREL (subordination);
  - Dedicated rules for certain business models, such as cooperatives, and for resolution strategies, such as multiple point of entry (MPE);
  - Provisions on internal MREL;
  - Clarifications on third-country issuances; and
  - Phasing-in provisions.

3. SRB MREL POLICY: 2021 POLICY UPDATE

- The SRB published on 26 May 2021 the updated MREL Policy.

- The update refines the 2020 MREL Policy and introduces new elements:
  - Waivers from internal MREL: Criteria for systemic subsidiaries for which no internal MREL waiver is possible
  - Internal MREL: Revised thresholds (from 4% to 3%) for relevant legal entities
  - P2R post resolution: Based on SREP score and further adjusted based on bank risk profile
  - MREL calibration on preferred vs variant strategy: Based exclusively on the preferred resolution strategy
  - MREL calibration for liquidation entities: Can increase LAA beyond the default adjustment proportionately to financial stability concerns
  - MREL eligibility: New chapter on MREL eligibility conditions and management sign off form*
  - MREL maximum distributable amount (M-MDA): New chapter on M-MDA restrictions that may be applied in cases of MREL breaches

4. MREL MAXIMUM DISTRIBUTABLE AMOUNT (M-MDA)

- In accordance with **Article 10a SRMR**, the SRB may set restrictions preventing entities from distributing more than the MDA related to MREL (M-MDA) via various actions (incl. dividend payments on CET1, variable remuneration and payments on AT1 instruments).

- The M-MDA may be applied where:
  - ✓ the entity **meets the combined buffer requirement (CBR) in addition to the own funds requirements** (i.e. no prudential MDA),
  - ✓ but **fails to meet the CBR in addition to the MREL expressed in risk exposure amount (TREA)**.

What is expected from the banks in case of a shortfall on CBR?

- Once the entity is in shortfall, it shall immediately notify the national resolution authority and the SRB.
- Banks should not wait until breaches occur and should signal expected breaches.
- Banks are expected to provide all the necessary data to the SRB to perform the monthly assessments. *[Specific data templates will be provided by the SRB]*
- The M-MDA may also be applied in case of MREL breaches.

4. MREL MAXIMUM DISTRIBUTABLE AMOUNT (M-MDA)

Interplay with prudential MDA

- **Common features:** The M-MDA shares many features with the prudential MDA-regime of Article 141 CRD (where the CBR has to be met in addition to Pillar 1 and Pillar 2 requirements), e.g. the computation methodology.
- **No automaticity:** Unlike the prudential MDA, the M-MDA regime is not automatic and its application is subject to a discretionary decision of the resolution authority, which needs to follow specific procedural steps and assessment criteria.
- **Precedence of prudential MDA**

4. MREL MAXIMUM DISTRIBUTABLE AMOUNT (M-MDA)

How will the SRB assess whether to impose M-MDA?

Notification by the bank

9 months later

Stage I:

SRB assesses whether to exercise the M-MDA power, taking into account all of the elements set out in Article **10a(2) SRMR**

Stage II:

SRB in principle exercises the M-MDA power, <u>except</u> where it finds that at least two of the conditions set out in Article **10a(3) SRMR** are fulfilled

A formal consultation with the ECB will run during each stage.

5. SRB PERMISSION REGIME TO REDUCE ELIGIBLE LIABILITIES UNDER ART. 78A CRR

Time line to updated Permission Regime

Ongoing transitional phase

No permission required due to Art. 12k SRMR2 – see SRB publication on 18 Dec 2020

Update of SRB Permission Regime by end 2021

EBA RTS - Delegated Regulation integrated into SRB Permission Regime

1 January 2022

Updated SRB Permission Regime applies (including enlarged scope of liabilities and contents of EBA RTS)

6. REPORTING: WHAT DATA WILL THE SRB COLLECT IN 2021?

- **Quarterly monitoring of MREL and TLAC capacity**
  - SRB collects on a quarterly basis data on MREL/TLAC issuances and outstanding stock, to monitor banks' MREL build-up
  - Key changes throughout the 2021 quarters to reflect the BRRD2 framework, and the implementation of the EBA ITS on MREL TLAC reporting

1. *Q1.2021 reference date*:
    1. BRRD2 framework
    2. Submission deadline: 30 June 2021
2. *Q2.2021* reference date:
    1. Collection of the templates in XBRL format in line with EBA ITS on MREL TLAC Reporting
    2. Additional excel-based templates on quarterly MREL issuances and forecasts (not included in EBA ITS templates)
    3. Submission deadline for both: 30 September 2021

7. OUTLOOK FOR NEXT RESOLUTION PLANNING CYCLES

The SRB will continue completing and refining the MREL policy, in particular in the following areas:

- **NCWO approach:** the SRB will assess the possibility to reflect more elements in the NCWO methodology, notably the evolution of the bank's balance sheet and the potential impact of the discretionary exclusions
- **Further work on transfer strategies:** the SRB will enhance the MREL policy for these resolution strategies.
- **Implementing new EBA RTSs into the SRB policy:** the SRB will revise the MREL policy once new EBA RTSs will be endorsed, e.g. on prior-permissions and on daisy-chains.

SRB APPROACH TO RESOLVABILITY ASSESSMENT

1. EXPECTATIONS FOR BANKS

- In April 2020, the SRB published the **"Expectations for Banks"**, setting out the actions, steps and capabilities that banks should take to show that they are resolvable.
- The Expectations are structured along **seven dimensions** (and 28 underlying **principles**), representing the core conditions to be met by banks to be deemed resolvable (Governance; Loss Absorption and Recapitalisation; Liquidity and Funding in resolution; Operational continuity and access to FMI services; Information Systems; Communication; Separability and Restructuring).
- The "Expectations for banks" are general in nature, and are **tailored to the bank's business model and resolution strategy** to ensure proportionality and level playing field.
- They are gradually **phased-in**, until end-2023, to provide sufficient time to the banks for implementing such capabilities and for providing the underlying evidence.

2. THE RESOLVABILITY "HEAT-MAP"

- The SRB will assess and monitor banks' capabilities using the "**Resolvability Heat-map**". The Heat-map classifies banks according to the progress made on each resolvability condition and the impact of each condition on the feasibility of the resolution strategy.

Impact

Progress

	High impact	Medium impact	Low impact	N/A
Level 0 « No progress »	Potential candidates for substantive impediments		No or minor impediment	No impediment
Level 1 « Limited progress »		Impediment	No or minor impediment	
Level 2 « Advanced progress »	No or minor impediment	No or minor impediment	No impediment	
Level 3 « Full progress »	Best practice	Best practice	Best practice	
Grey progress	Potential impediment		No impediment	

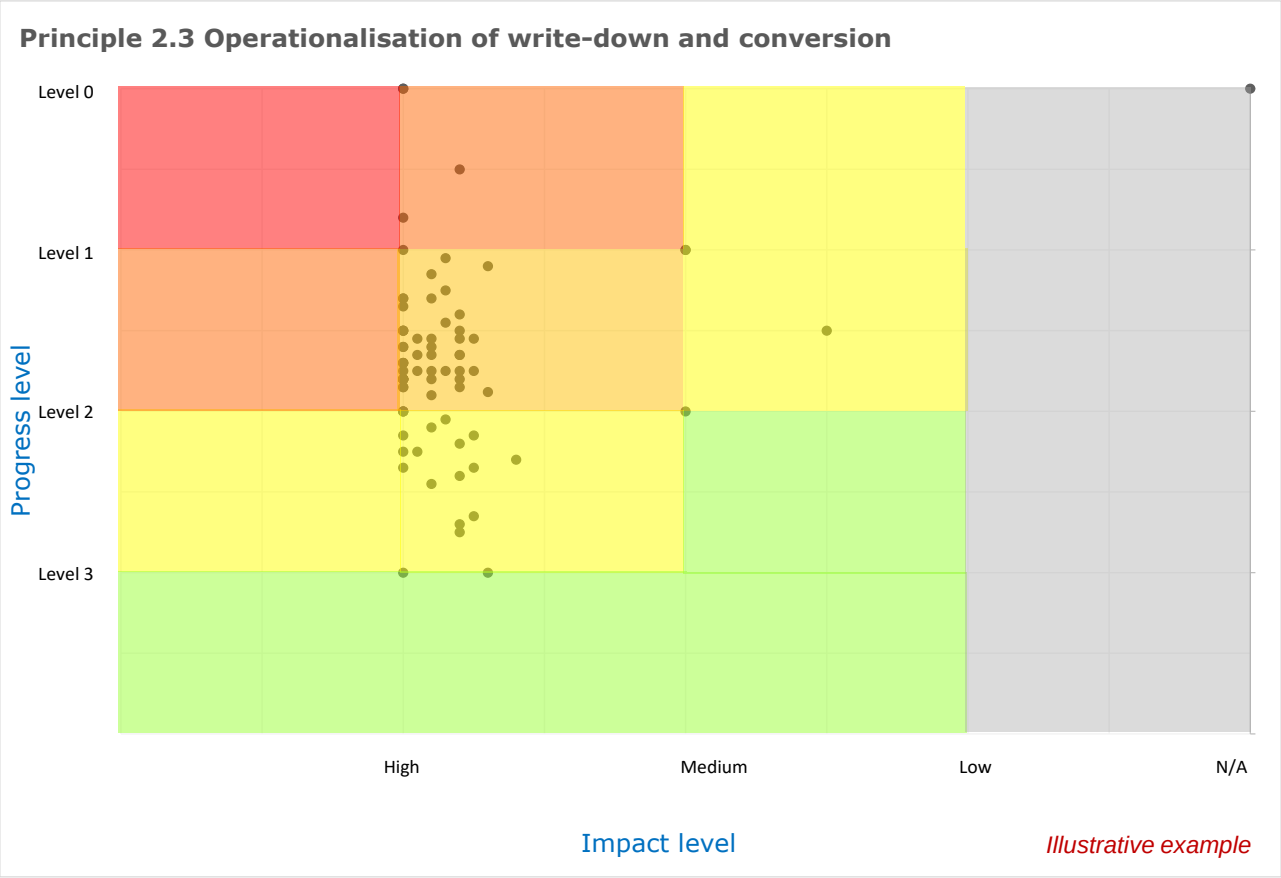
<u>Impact levels</u> take into account business model and the specificities of the resolution strategy, to ensure proportionality in the application of the Expectations for Banks and in the resolvability assessment.

<u>Progress levels</u> are consistent with the phase-in of the Expectations for Banks **and** the MREL **transition periods,** allowing appropriate time for banks to develop adequate capabilities.

14 June 2021

3. MONITORING AND BENCHMARKING ANALYSIS

- The Heat-map allows monitoring of progress on resolvability, peer group benchmarking and the identification of « outliers ».



In an illustrative example few banks are classified as "negative outliers", with progress levels between 0 and 1, while two banks emerge as "positive outliers", reaching best practice.

4. “INCENTIVE-COMPATIBLE” APPROACH

The approach should work as a strong incentive for banks to become compliant:

- Progress towards resolvability is also relevant for the purposes of MREL calibration, as concerns the adjustments from the baseline formula (case by case approach).
- Where insufficient progress is noted, the assessment may lead to the identification of impediments to resolution at different degrees of materiality, including triggering the formal procedure for removing substantive impediments to resolvability.

5. AREAS OF FOCUS FOR 2021 RPC

- In the 2021 RPC, progress monitoring will focus on the Expectations for Banks phased-in in 2021 and follow-up on the capabilities phased-in in previous cycles, mainly:

  - Loss absorbing and recapitalization capacity (mainly bail-in playbooks, quality and level of MREL)
  - Operational continuity arrangements and FMI contingency plans to support the continuity of Critical Functions and some work extended Core Business Lines in 2021
  - Estimation of liquidity needs in resolution
  - MIS capabilities (self-assessment) to produce the dataset for valuation and for bail-in execution
  - Governance and communication plan arrangements
  - Any other bank or resolution-strategy specific priorities (e.g. separability for transfer tools)

THANK YOU!

Single
Resolution Board