The Bank Recovery and Resolution Directive – implementation challenges from an institutional point of view

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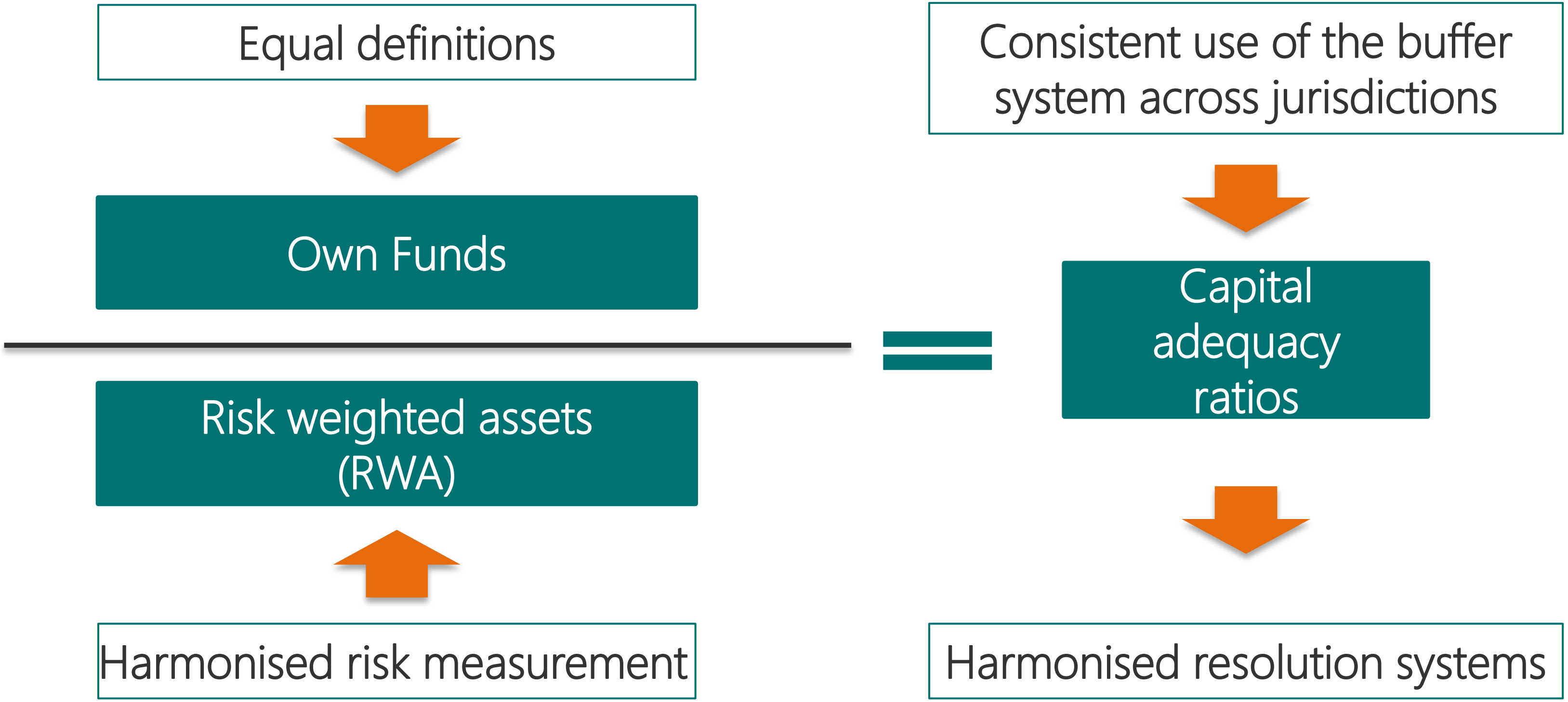
Agenda

1) Some remarks on the implementation of the BRRD

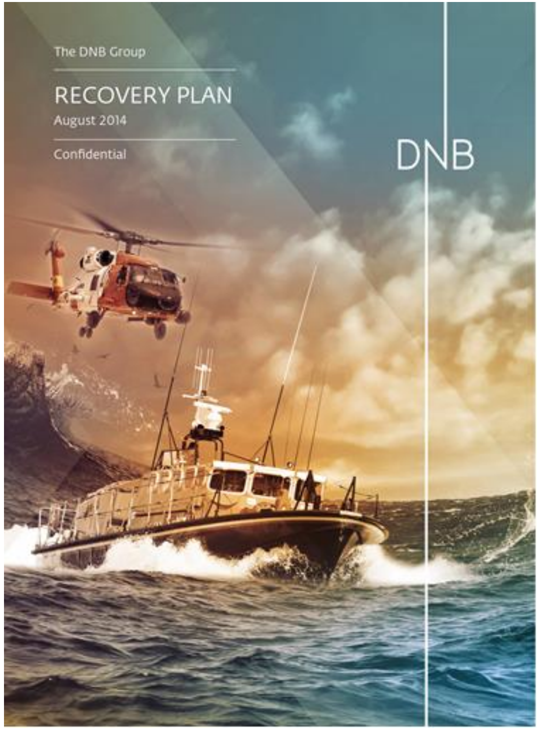
2) Recovery planning
   - Experiences so far
   - Challenges going forward

3) Funding costs and capital structure
   - Observed pricing effects of the BRRD

A level playing field requires strict harmonisation of all elements



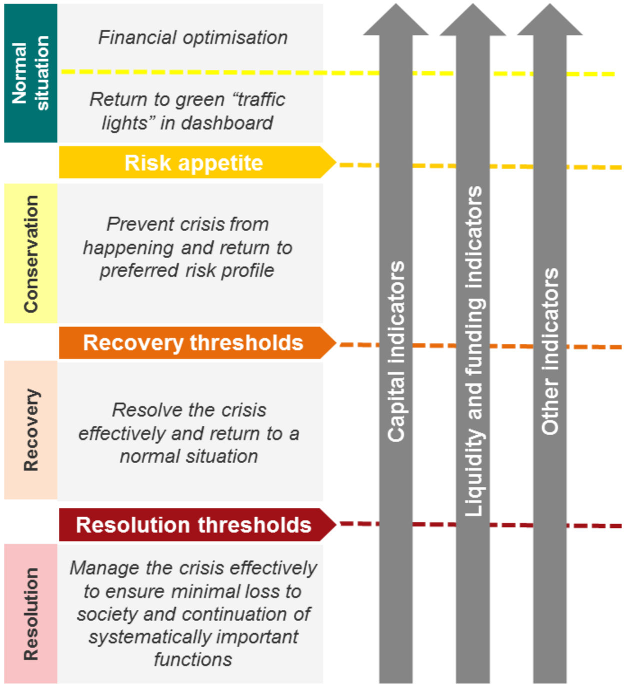
Recovery planning in DNB



- Initiated by EBA and the Norwegian FSA in January 2013
- First version December 2013
  - Internal resources only
  - Feedback in April 2014
- Second version August 2014
  - DNB College discussion October 2014
  - Feedback in March 2015
- Annual update
  - DNB College – joint decision according to BRRD procedures
  - Compliance with EBA Guidelines
  - Recovery plan for DNB Lithuania from 2015

Key issues to consider

- The role of the Recovery plan in the overall risk management system
  - Risk appetite
  - Contingency planning
- The recovery situation means severe stress
  - Indicators
  - Options
  - Scenarios



DNB's recovery plan is structured in six chapters

Governance	• Integration in overall corporate governance and risk management • Recovery indicators • Roles and responsibilities
Description of the Group	• Legal and financial structure • Core business lines • Critical functions
Scenarios	• Specific scenarios of financial stress
Recovery options	• Identification and assessment of possible recovery options
Preparatory measures	• Changes and actions to facilitate effective recovery
Communication plan	• Internal and external communication plan • Communication guidelines for the various recovery options

The available recovery options fall in four categories

Share capital increase

Divestment of subsidiaries

Divestment of portfolios

Other measures

New EBA guidelines on recovery indicators introduce extensive minimum requirements

DNB's current recovery indicators

	Recovery indicators	Early warning indicators
Liquidity	1. Liquidity Coverage Ratio (LCR)	• Senior debt spread • Availability of Commercial Papers • Maturity of senior debt
Capital	1. Total capital ratio 2. Solvency ratio	• Watch list • Significant write-downs due to economic conditions • Sharp drop in real estate prices
Other	1. Price / book 2. Long-term rating downgrade	• Negative development in share price relatively to peers

Minimum list of required indicators (EBA 2015)

1. Capital indicators
   a) Common Equity Tier 1 ratio
   b) Total Capital ratio
   c) Leverage ratio
2. Liquidity indicators
   a) Liquidity Coverage Ratio
   b) Net Stable Funding Ratio
   c) Cost of wholesale funding
3. Profitability indicators
   a) (Return on Assets) or (Return on Equity)
   b) Significant operational losses
4. Asset quality indicators
   a) Growth rate of gross non-performing loans
   b) Coverage ratio
5. Market-based indicators
   a) Rating under negative review or rating downgrade
   b) CDS spread
   c) Stock price variation
6. Macroeconomic indicators
   a) GDP variations
   b) CDS of sovereigns

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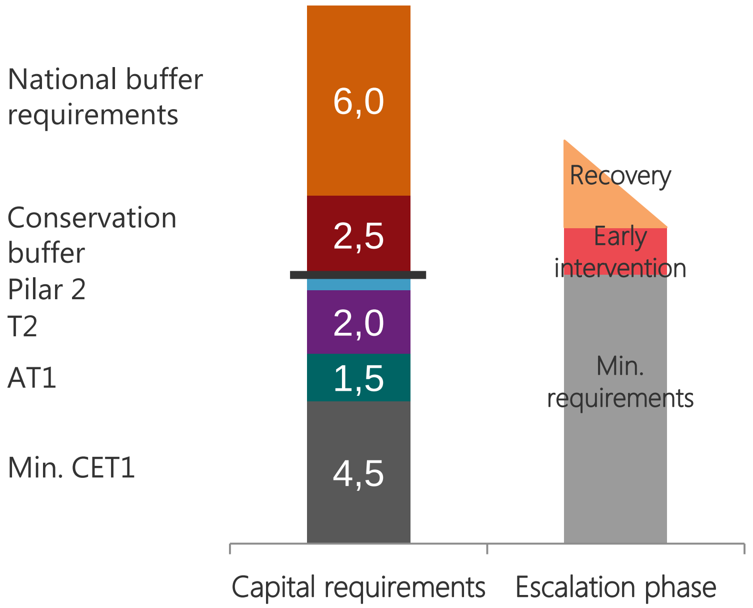
Deciding the appropriate capital indicator

Capital and possible trigger levels



BRRD on Early Intervention:
"Where an institution infringes or, due inter alia to a rapidly deteriorating financial condition, including deteriorating liquidity situation, increasing level of leverage, non-performing loans or concentration of exposures, as assessed on the basis of a set of triggers, which may include the institution's own funds requirement plus 1,5 percentage points"

EBA – Guidelines on Recovery Plan Indicators (2015):
"The thresholds for indicators based on regulatory capital requirements should be calibrated by the institution at adequate levels in order to ensure a sufficient distance from a breach of the capital requirements applicable to the institution (including minimum own funds requirements and additional own funds requirements ***but without taking into account any buffer requirements*** *set out in Chapter 4 of Title VII of Directive 2013/36/EU). "*

Some crucial parts of the BRRD implementation are yet to come - how to make “bail-in” workable

- Total Loss-Absorbing Capacity (TLAC) / Minimum Requirement for own funds and Eligible Liabilities (MREL)
  - Size / calibration
  - National discretion
- How to make senior unsecured funding eligible for TLAC / MREL
  - Ranking order / subordination by legislation (Germany)
  - Ranking order / subordination by contractual terms (Spain)
  - Mandatory use of a HoldCo as the issuing entity - structural subordination
- Single point of entry vs multiple point of entry for resolution

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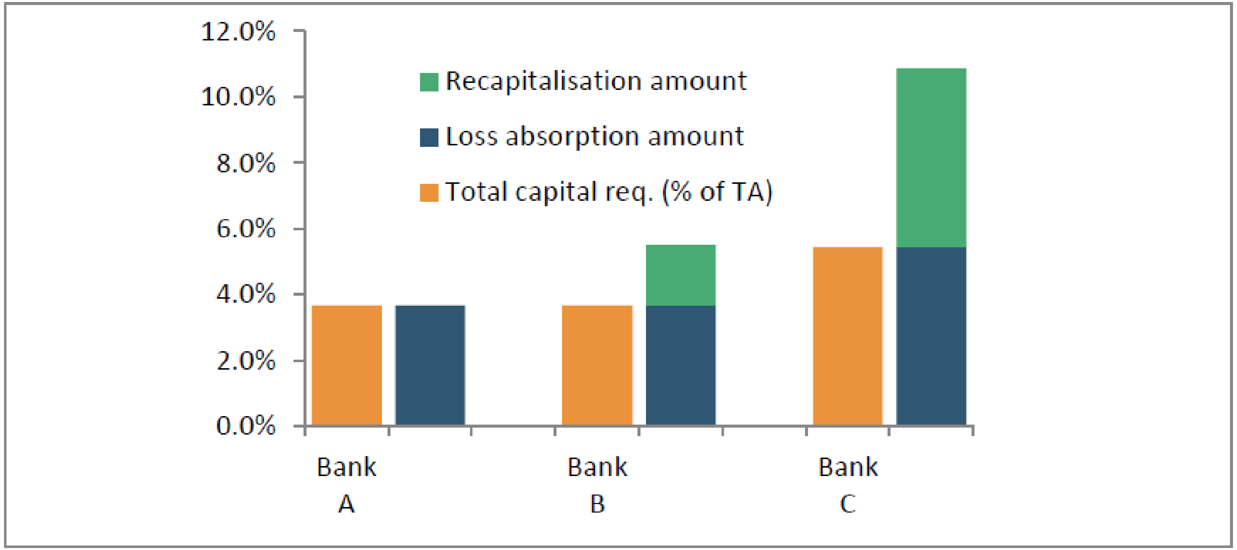
EBA draft Regulatory Technical Standard on MREL - examples



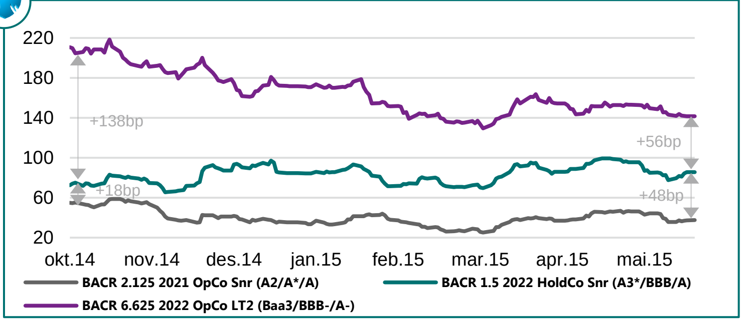
A: Small bank, RWA: 35% liquidation

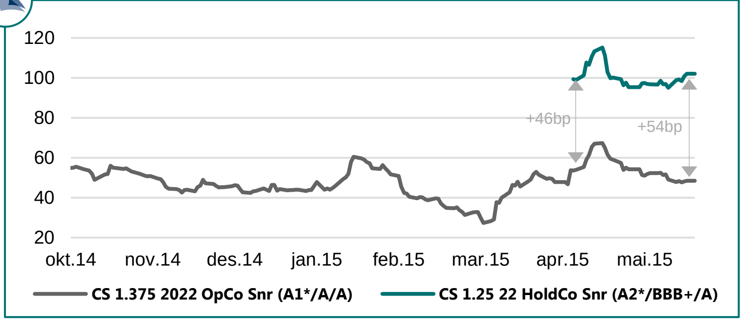
B: 50% systemic, RWA: 35%, partly refinancing, partly liquidation

C: Large systemic, RWA: 35%, refinancing

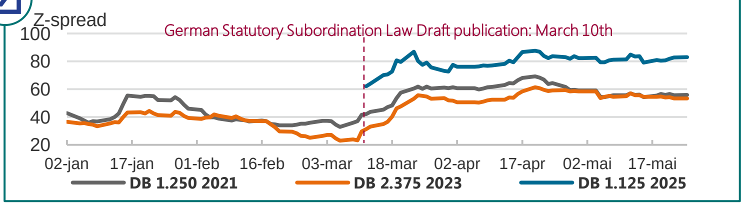
Market Reaction to TLAC Subordination Strategies

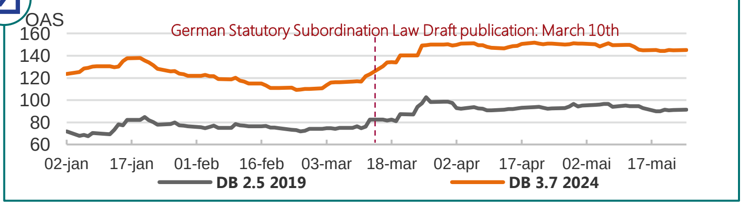
EUR Securities





DB Securities





DB EUR Securities	Spreads increase (bp)*
DB 1.25 2021	6
DB 2.375 2023	26
DB 1.125 2025	32

DB USD Securities	Spreads increase (bp)*
DB 2.5 2019	28
DB 3.7 2024	33

Short-dated senior is less sensitive to subordination than longer term debt

HoldCo senior spreads lie inside OpCo Tier 2 and above OpCo senior; the differential over OpCo senior has widened during the course of 2015 as the market considers down-streaming for TLAC

*Increase from 9th March up to widest levels on 24th March.
Source: Barclays Chart, as of 6th May 2015

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