



EUROPEAN CENTRAL BANK
BANKING SUPERVISION

Danièle NOUY

Chair of the Supervisory Board

Mr Ernest Urtasun
Mr Sven Giegold
Member of the European Parliament
European Parliament
60, rue Wiertz
B-1047 Brussels

Frankfurt am Main, 3 August 2017

Re: Your letters (QZ-055-58 and QZ-065)

Honourable Members of the European Parliament, dear Mr Urtasun, dear Mr Giegold,

Thank you for your letters relating to Banco Popular Español's resolution, which were passed on to me by Mr Roberto Gualtieri, Chairman of the Committee on Economic and Monetary Affairs, accompanied by a cover letter dated 29 June 2017.

As laid down in the Interinstitutional Agreement between the European Parliament and the ECB, any reporting obligations vis-à-vis the European Parliament are subject to the relevant professional secrecy requirements, as outlined in the Capital Requirements Directive IV¹. These rules also apply to information about banks which the ECB determined failing or likely to fail. While I cannot disclose confidential information, including the specific supervisory measures taken, let me nevertheless provide you with some relevant considerations in response to your question.

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 chairman²;
- On 10 February 2017, DBRS downgraded the rating of the institution;
- On 14 February 2017, Fitch downgraded the rating of the institution;

¹ Directive 2013/36/EU of the European Parliament and of the Council.

² The Court of Justice of the European Union's ruling on floor clauses was one of several factors referred to by Banco Popular Español S.A. in its 2016 Annual Report, which resulted in an increase in provisions. As disclosed in the annual report, Banco Popular Español S.A. recorded a provision of €229 million to cover this contingency (€511 million in total).

- 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 who, at that time, had been in office for less than one year;
- 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;
- On 21 April 2017, Moody's downgraded the rating of the institution;
- On 3 May 2017, Banco Popular Español disclosed its group quarterly results for the first quarter of 2017, which underperformed market expectations;
- On 31 May 2017, it was disclosed in the media that the institution could face a wind-down process if the on-going 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 is one of the supervisory actions to assess liquidity risk.

On 6 June 2017, the significant deterioration of the liquidity situation of Banco Popular Español S.A. led to the determination that the institution 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 failure³. Consequently, the ECB determined that the institution was failing or likely to fail in accordance with Article 18(1) of the Single Resolution Mechanism Regulation (SRMR)⁴ and duly informed the Single Resolution Board (SRB), which adopted a resolution scheme entailing the sale of business. In this context, the SRB would be better placed to answer your questions regarding the resolution process, including the valuation conducted.

The aforementioned ECB decision that the institution was failing or likely to fail was taken on the basis of insufficient liquidity. At this time, the objective elements⁵ 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 institution. Its structural problems (e.g. high level of non-performing assets, low coverage, poor profitability) were reflected in commensurate capital requirements established by the ECB. This capital demand reflected, inter alia, the results of the 2016 EBA stress test, which revealed that Banco Popular Español S.A. would suffer a significant impact under a stress scenario. The bank performed the worst in Spain, and the third worst in the whole sample, in terms of its CET1 ratio under the adverse scenario in the 2016 EBA stress test. This outcome was mainly

³ Considerations concerning emergency liquidity assistance and particular deposit withdrawals are subject to confidentiality.

⁴ Regulation (EU) No 806/2014 of the European Parliament and of the Council.

⁵ 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>

driven by the impact of credit quality, but also by the impact of ongoing litigation classified as conduct or operational risks.⁶

The sale to Banco Santander S.A. as part of the resolution scheme decided by the SRB was executed in accordance with Spanish law. In particular, the fiscal treatment of the related deferred tax assets (DTAs) is governed by Spanish corporate tax regulation and its compliance is ensured by the relevant competent authorities at national level. The ECB is responsible for monitoring balance sheet dynamics and for ensuring that DTAs are properly reported for prudential purposes, in line with the Capital Requirements Regulation⁷.

Finally, I refer to your question regarding the public statement made by the Deputy Governor of the Banco de España. Let me first and foremost point out that I generally do not comment on such statements. Moreover, they relate to the provision of central bank liquidity, which falls outside the scope of ECB Banking Supervision.

Yours sincerely,

A handwritten signature in black ink, consisting of several overlapping loops and strokes, characteristic of Danièle Nouy's signature.

Danièle Nouy

⁶ 2016 EU-wide stress test results are available at:
http://www.eba.europa.eu/documents/10180/1519983/EBA_TR_ES_80H66LPTVDLM0P28XF25.pdf

⁷ Regulation (EU) No 575/2013 of the European Parliament and of the Council.