

EUROPEAN SYSTEMIC RISK BOARD

DECISION OF THE EUROPEAN SYSTEMIC RISK BOARD

of 11 December 2015

on the assessment of materiality of third countries for the Union's banking system in relation to the recognition and setting of countercyclical buffer rates

(ESRB/2015/3)

(2016/C 97/11)

THE GENERAL BOARD OF THE EUROPEAN SYSTEMIC RISK BOARD,

Having regard to Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board ⁽¹⁾, and in particular Article 3(2)(a) and (b), and Article 15 thereof,

Having regard to Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC ⁽²⁾, and in particular Article 138 thereof,

Having regard to Commission Implementing Regulation (EU) No 680/2014 of 16 April 2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No 575/2013 of the European Parliament and of the Council ⁽³⁾, and in particular Annexes I and II thereto,

Having regard to Decision ESRB/2015/2 of the European Systemic Risk Board of 21 July 2015 on the provision and collection of information for the macroprudential oversight of the financial system within the Union and repealing Decision ESRB/2011/6 ⁽⁴⁾,

Whereas:

- (1) The European Systemic Risk Board (ESRB) is responsible for carrying out macroprudential oversight in order to contribute to the prevention or mitigation of systemic risks within the Union.
- (2) In order to discharge its responsibilities, the ESRB needs to assess macroprudential risks stemming from developments within the Union and in third countries. Such risks could arise from cross-border exposures of the Union's banking system to third countries, which might serve as a contagion channel into the Union. In particular, excessive credit growth in a given third country could, if not addressed by means of macroprudential policies taken by that country, lead to large losses for the banking sector within the Union and, ultimately, pose a threat to financial stability within the Union.
- (3) Article 138 of Directive 2013/36/EU provides the ESRB with a specific mandate to address risks arising from excessive credit growth in third countries. Specifically, when actions taken by authorities in a third country are deemed insufficient, the ESRB can act to protect the Union's banking sector from risks stemming from excessive credit growth in that third country. In particular, the ESRB may, by means of a recommendation, provide guidance to designated authorities within the Union on the appropriate countercyclical buffer rate for exposures to third countries.
- (4) In order to discharge this mandate, third countries to which the Union's banking system has material exposures (hereinafter 'material third countries') need to be identified. The impact that excessive credit growth in a given third country might have on the Union's banking system depends on the size and nature of the exposures of banks which have their head offices in the Union towards that third country. Given that the ESRB does not have the capacity to monitor developments in all third countries around the world, it considers that it can best discharge its mandate under Article 138 of Directive 2013/36/EU by monitoring only those third countries to which the exposures of the Union's banking system are material for signs of excessive credit growth.

⁽¹⁾ OJ L 331, 15.12.2010, p. 1.

⁽²⁾ OJ L 176, 27.6.2013, p. 338.

⁽³⁾ OJ L 191, 28.6.2014, p. 1.

⁽⁴⁾ OJ C 394, 27.11.2015, p. 4.

- (5) In order to identify material third countries, the ESRB intends to use supervisory data collected by the European Banking Authority (EBA) in accordance with Decision EBA/DC/2015/130 of the European Banking Authority of 23 September 2015 ⁽¹⁾. Decision EBA/DC/2015/130 provides detailed information on exposures in the banking book of a sample of the largest 191 banks in the Union to all third countries globally. Although the data do not include exposures in the trading book, and do not cover all banks in the Union, the ESRB considers that the data are adequate for the purpose of identifying material third countries. Focusing on exposures in the banking book is considered adequate because they represent the majority of exposures. Moreover, netting arrangements and the use of, inter alia, derivatives and short positions make it difficult to allocate an exposure in the trading book to a given third country. Focusing on a sample of the largest banks is considered adequate because these banks tend to have the largest volume of cross-border activities and are, therefore, the banks that would be most affected if excessive credit growth in a third country was not being addressed. In 2014, the 191 banks in the sample accounted for around 92 % of the total assets of the Union's banking system. As the ESRB does not need bank-specific exposure data for the purpose of identifying material third countries, it intends to request from the EBA the data gathered in accordance with Decision EBA/DC/2015/130 aggregated to country level. Such data requests are governed by Decision ESRB/2015/2.
- (6) The ESRB will identify material third countries on the basis of three exposure metrics: risk-weighted assets, original exposure and defaulted exposures in relation to third countries. The main purpose of using a number of metrics is to reflect a comprehensive view of the nature of the exposures to third countries. Focusing solely on risk-weighted assets could result in a situation in which significant exposures with low risk weights would not be given due consideration. By capturing the size of the exposures before risk weights are applied, original exposure compensates for this. Finally, defaulted exposures aim to capture those exposures which pose a greater credit risk to the banks.
- (7) The ESRB typically defines a third country as material when exposures of the Union's banking system to that third country are at least 1 % for at least one of the above three metrics. Compared to non-financial corporations, banks' equity levels tend to be small relative to their assets. This means that, even for what might appear to be small exposures when compared with the size of the balance sheet of a bank, losses can reach levels that threaten the solvency of banks and/or create doubt among the public about their solvency. This argument would require the setting of a low threshold, as adverse developments in a given third country could materially impact the capital position of banks. At the same time, the threshold used to identify material third countries should not consider third countries to which only one Member State is exposed, unless such exposures are large enough to pose a risk to the Union, beyond the individual Member State in question. To minimise these occurrences, a high threshold should be set, which ensures that only the largest exposures across Member States are captured. The ESRB considers that a threshold of 1 % of total exposures achieves the right balance between the two desirable outcomes above.
- (8) The ESRB will compile a list of material third countries and update this list annually on the basis of criteria that govern additions to and deletions from that list. Banking exposures evolve over time, reflecting both cyclical and structural developments in economic and financial integration across the world. The process of identifying material third countries needs to reflect this evolution. To that end, criteria that govern additions to and deletions from the list of material third countries have been defined. They are designed to be: (a) conservative — for a third country to be added to the list is easier than to be deleted from it; and (b) transparent — criteria for adding to and deleting from the list are based on simple rules. In addition, the ESRB can exercise discretion when determining whether a third country is material for the banking sector of the Union. Such discretion is most likely to be exercised in cases where a third country is on the verge of meeting the materiality criteria.
- (9) The General Board will be asked to approve each revision of the list of material third countries via written procedure. If an objection is raised, the General Board will vote. The ESRB Secretariat will, on an annual basis, prepare a draft list of material third countries based on the application of the addition and deletion criteria. The Advisory Technical Committee will be able to exercise its discretion and amend the draft list prior to submission to the General Board.
- (10) Material third countries identified in accordance with this Decision will be monitored by the ESRB Secretariat. Other third countries might be monitored by other jurisdictions in the Union depending on their materiality for the domestic banking system of a given Member State. Expertise gained from the Risk Dashboard and from earlier work on the countercyclical capital buffer will be used to identify those indicators which are more relevant in terms of the early identification of excessive credit growth.

⁽¹⁾ Decision EBA/DC/2015/130 of the European Banking Authority of 23 September 2015 on reporting by competent authorities to the EBA, published on the EBA's website at www.eba.europa.eu.

- (11) The ESRB has initially identified six third countries as material, based on supervisory data with a reference date of 30 June 2014. The third countries initially identified as material are the Federative Republic of Brazil, the Hong Kong Special Administrative Region of the People's Republic of China, the People's Republic of China, the Republic of Turkey, the Russian Federation and the United States of America. Amendments to this list of material third countries should be published on the ESRB's website.
- (12) The first revision of the list of material third countries, as identified by the ESRB, will take place in the second quarter of 2017, using supervisory data with a reference date of 31 December 2016. This reflects the need to have sufficient data to apply the addition criteria. Due to the fact that there will be insufficient data to apply the deletion criteria, this first revision will consider only potential additions to the list of material third countries.
- (13) Subsequent revisions to the list of material third countries will take place using supervisory data with a reference date of the 31 December of each relevant calendar year. Once sufficient data to apply the deletion criteria are available, subsequent revisions will also consider potential deletions from the list of material third countries,

HAS ADOPTED THIS DECISION:

Article 1

Scope

The Decision defines the ESRB's procedures for assessing the materiality of third countries for the Union's banking sector in relation to the recognition and setting of countercyclical buffer rates in accordance with Directive 2013/36/EU.

Article 2

Definitions

For the purposes of this Decision, the following definitions shall apply:

- (a) 'countercyclical buffer rate' has the same meaning as in Article 128(7) of Directive 2013/36/EU;
- (b) 'exposure' has the same meaning as in Article 5(1) of Regulation (EU) No 575/2013 of the European Parliament and of the Council⁽¹⁾;
- (c) 'monitoring/monitored by the ESRB Secretariat' means the governance, maintenance and regular update of a set of indicators and quantitative tools by the ESRB Secretariat to signal potentially excessive credit growth in material third countries;
- (d) 'third country' has the same meaning as in point 1(g) of Section 2 of Recommendation ESRB/2015/1.

Article 3

Collection of data

1. For the purposes of assessing which third countries are material for the Union's banking sector and in accordance with Article 15 of Regulation (EU) No 1092/2010, the ESRB Secretariat shall request from the EBA aggregated supervisory data, as provided in Annex I to Implementing Regulation (EU) No 680/2014, collected by the EBA in accordance with Decision EBA/DC/2015/130.
2. In assessing whether a third country is material for the Union's banking sector, the following metrics shall be considered:
 - (a) risk-weighted exposure amounts;
 - (b) original exposures; and
 - (c) defaulted exposures.

⁽¹⁾ Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

3. In particular, on a quarterly basis, the following data points of the supervisory data referred to in paragraph 1 shall be collected by the ESRB for each relevant third country:

(a) Template C 09.01: intersection of rows 070, 080, 090, 100, 110, 120, 130, 140, 150, 160, and columns 010, 020 and 080; and

(b) Template C 09.02: intersection of rows 030, 060 and 140, and columns 010, 030 and 110.

4. The ESRB Secretariat shall liaise with the EBA as regards the submission of the data points referred to in paragraph 3, and in relation to possible future amendments to the reporting templates.

Article 4

Assessment of materiality

1. A third country shall be identified as material for the Union's banking sector, and added to the list of material third countries in the following circumstances:

(a) the arithmetic mean of exposures to the third country in the eight quarters preceding the reference date was at least 1 % for at least one of the metrics listed in Article 3(2); and

(b) the exposures in each of the two quarters preceding the reference date were at least 1 % for at least one of the metrics listed in Article 3(2).

2. A country shall be deleted from the list of material third countries where:

(a) the arithmetic mean of exposures to that country in the 12 quarters preceding the reference date was less than 1 % for all metrics listed in Article 3(2); and

(b) the exposures in each of the two quarters preceding the reference date were less than 1 % for all the metrics listed in Article 3(2).

3. A third country that is identified as material for the Union's banking sector on the basis of the criteria set out in paragraph 1 shall be monitored by the ESRB Secretariat.

4. The list of material third countries shall be revised annually by the ESRB Secretariat, which shall submit a proposal to the Advisory Technical Committee. This proposal shall be based on supervisory data collected for the 12 quarters preceding 31 December of the relevant calendar year. The proposal shall be submitted to the Advisory Technical Committee by 30 June of the relevant year. The Advisory Technical Committee may exercise its discretion and amend the proposal before submitting it to the General Board for approval, in particular in those cases where the ESRB has issued a recommendation in accordance with Article 138 of Directive 2013/36/EU and the third country subject to that recommendation should be deleted from the list of material third countries.

5. The General Board shall adopt a decision on amendments to the list of material third countries based on the proposal of the Advisory Technical Committee. Any amendments to the list of material third countries shall be published on the ESRB's website.

Article 5

Transitional provisions

1. The initial list of material third countries, compiled on the basis of reference data for the second quarter of 2014, comprises the Federative Republic of Brazil, the Hong Kong Special Administrative Region of the People's Republic of China, the People's Republic of China, the Republic of Turkey, the Russian Federation and the United States of America.

2. In the 2017 revision of the list of material third countries using supervisory data with a reference date of 31 December 2016, the criteria set out in Article 4(2) for deleting countries from the list shall not be used.

*Article 6***Entry into force**

This Decision shall apply from 1 January 2016.

Done at Frankfurt am Main, 11 December 2015.

The Chair of the ESRB

Mario DRAGHI
