

Position Paper

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Swedbank response to the EBA consultation of Guidelines for the estimation of LGD appropriate for an economic downturn

Introduction and general comments

First of all, we welcome the opportunity to provide our feedback to the EBA consultation on its draft regulatory technical standards (RTS) specifying an economic downturn and on its set of Guidelines related to the estimation of loss given default (LGD) appropriate for conditions of an economic downturn. Swedbank fully supports the responses to the consultation from the Swedish Bankers' Association and from the European Savings and Retail Banking Group, where we are active members of the specialist committees that have studied the EBA proposals.

The robustness of internal models has during the past years of post-crisis regulation been questioned by some decision makers in the EU involved in financial markets regulation, against the backdrop of variability of risk weights between IRB banks in different EU member states, but also within individual member states.

As a solution, the EBA has since 2016 developed several new Guidelines (GL) and Regulatory Technical Standards (RTS) to ensure consistency in models' outputs and the comparability of risk-weighted exposures, some of which have already been adopted. The changes have been structured in four main phases; (1) IRB assessment methodology, (2) harmonizing definition of default, (3) risk parameter estimation and (4) credit risk mitigation. Banks using IRB models ("IRB-banks") in the EU will have to comply with the new rules by the end of 2020.

The proposed guideline on estimation of LGD appropriate for conditions of an economic downturn currently under consultation is one important component of the overhaul of the phase (3) risk parameter estimation.

In addition to the changes proposed by the EBA, the recent agreement on the final revision of Basel III will have to be implemented at EU level. A key component are the so called input floors. These will have similar and additional

effects on IRB risk weighted exposures as the ongoing EBA overhaul of IRB modelling.

Swedbank proposes a cumulative impact assessment and postponement of date of compliance

Several of the changes, in particular estimation of PD and LGD, as well as downturn LGD estimation and the input floors, will have a deep impact on regulatory capital and risk assessment in large parts of the European banking sector. Some of these proposals may not have a large impact on a stand-alone basis, but the cumulative effect of all the measures together is more pronounced. We are of the opinion that because the changes have been proposed and consulted individually and at different points in time this has led to banks and supervisors underestimating the total effects of the entire package.

Swedbank therefore strongly recommends the EBA to conduct a thorough quantitative impact study of the cumulative effect of *both* the overhaul of the IRB modelling proposed by the EBA *and* the input floors. This could be done by national supervisors requiring banks to estimate the effects of the changes and the EBA analyzing the results at the European level. Given the need for such an impact study, we also propose that the date of application of the new rules should be postponed to at least 2022. If postponed, the date of application would coincide with the application of the input floors following from the revision of Basel III.

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