



EUROPEAN CENTRAL BANK

EUROSYSTEM

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“Stabilising and Healing the Irish Banking System: Policy Lessons”

Discussion

*Joint CBI, CEPR, IMF Conference,
Dublin, 19 January 2015*

Much to agree with in “Stabilising and Healing the Irish Banking System: Policy Lessons” by D. Schoenmaker

- Minsky diagnosis
 - Importance of rigorous, multi-faceted PCAR 2011 to address:
 1. Solvency concerns;
 2. Asset quality problems;
- } Schoenmaker (2015)

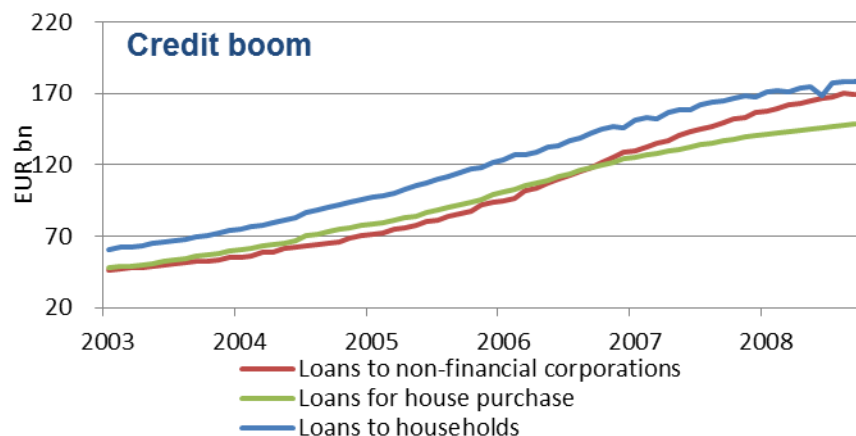
But two other important aspects of the Financial Measures Programme 2011:

3. “Right-sizing” the banking system;
 4. Addressing funding challenges;
- } Focus of the discussion

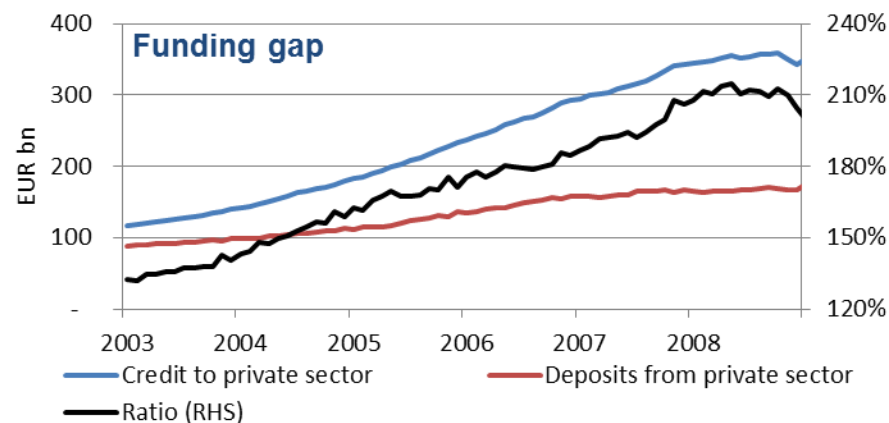
Recall: unprecedented scale of challenges in 2010; “high-risk programme” with bank-sovereign and other adverse feedback loops amongst these 4 elements in evidence

“Right-sizing”, funding and liquidity challenges

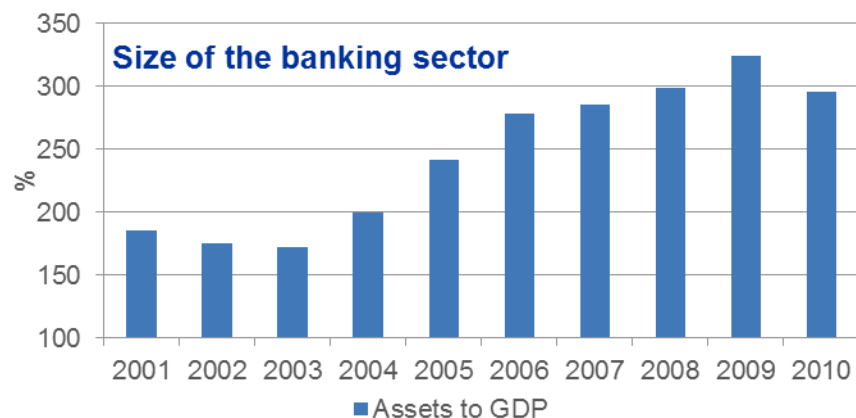
Unsustainable credit growth was fuelled by a burgeoning funding gap, in tandem with an unstable and unsustainable funding composition ...



Source: Central Bank of Ireland. Note: outstanding loans to Irish residents, including securitised loans.



Source: Central Bank of Ireland. Note: domestic market group, loans and deposits to Irish residents.



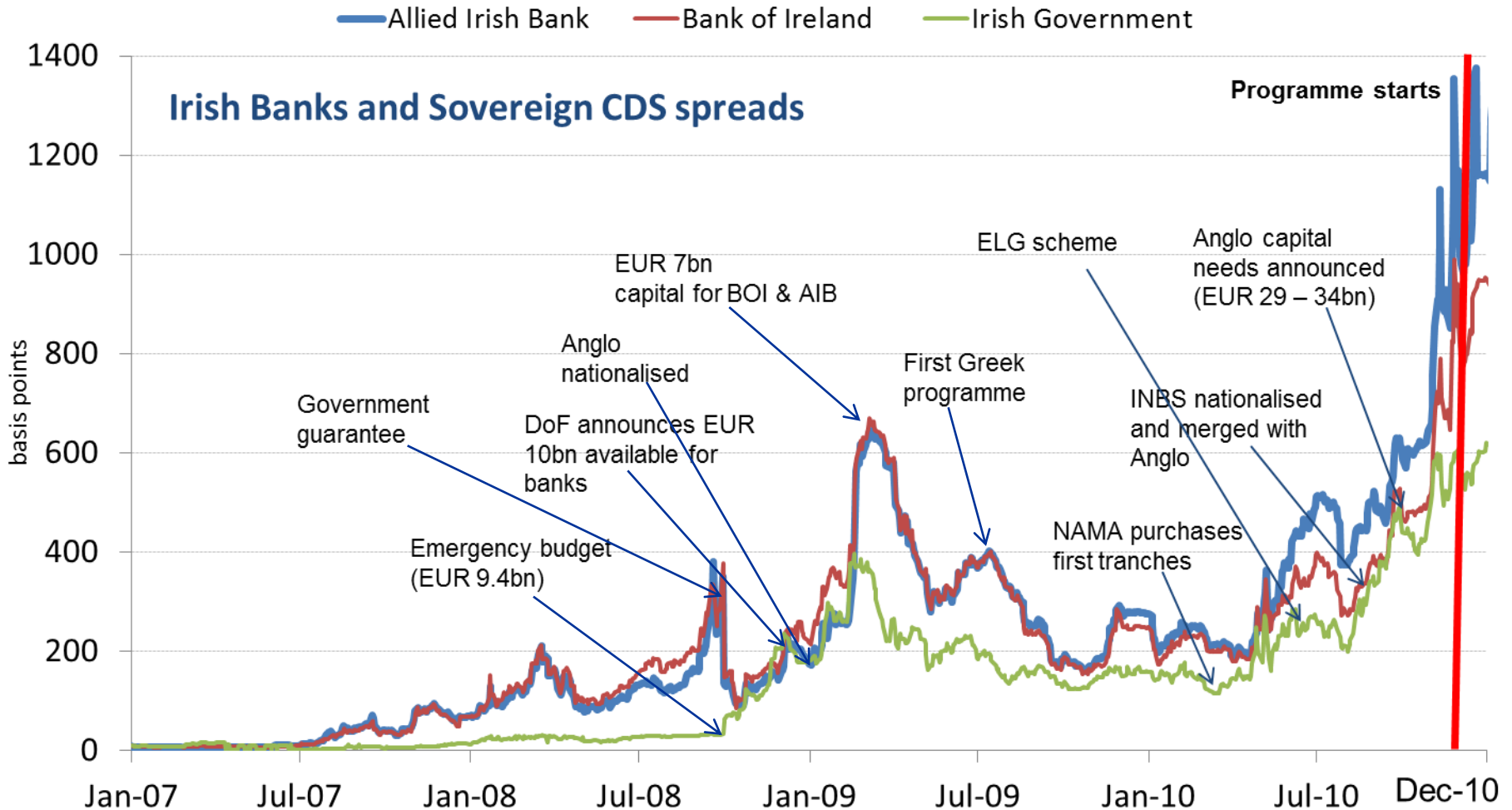
Source: Central Bank of Ireland, Financial Measures Programme Report. Note: data for six covered banks.

Wholesale funding as % of total liabilities (2010)	
ILP	64%
Anglo	62%
EBS	49%
INBS	41%
AIB	39%
BOI	35%

Source: Central Bank of Ireland.

Feedback loops – evidence

Sovereign-bank feedback loop emerged in late 2008 and deepened in 2010...
...as fears for ever-growing losses from the banking sector impacted the sovereign

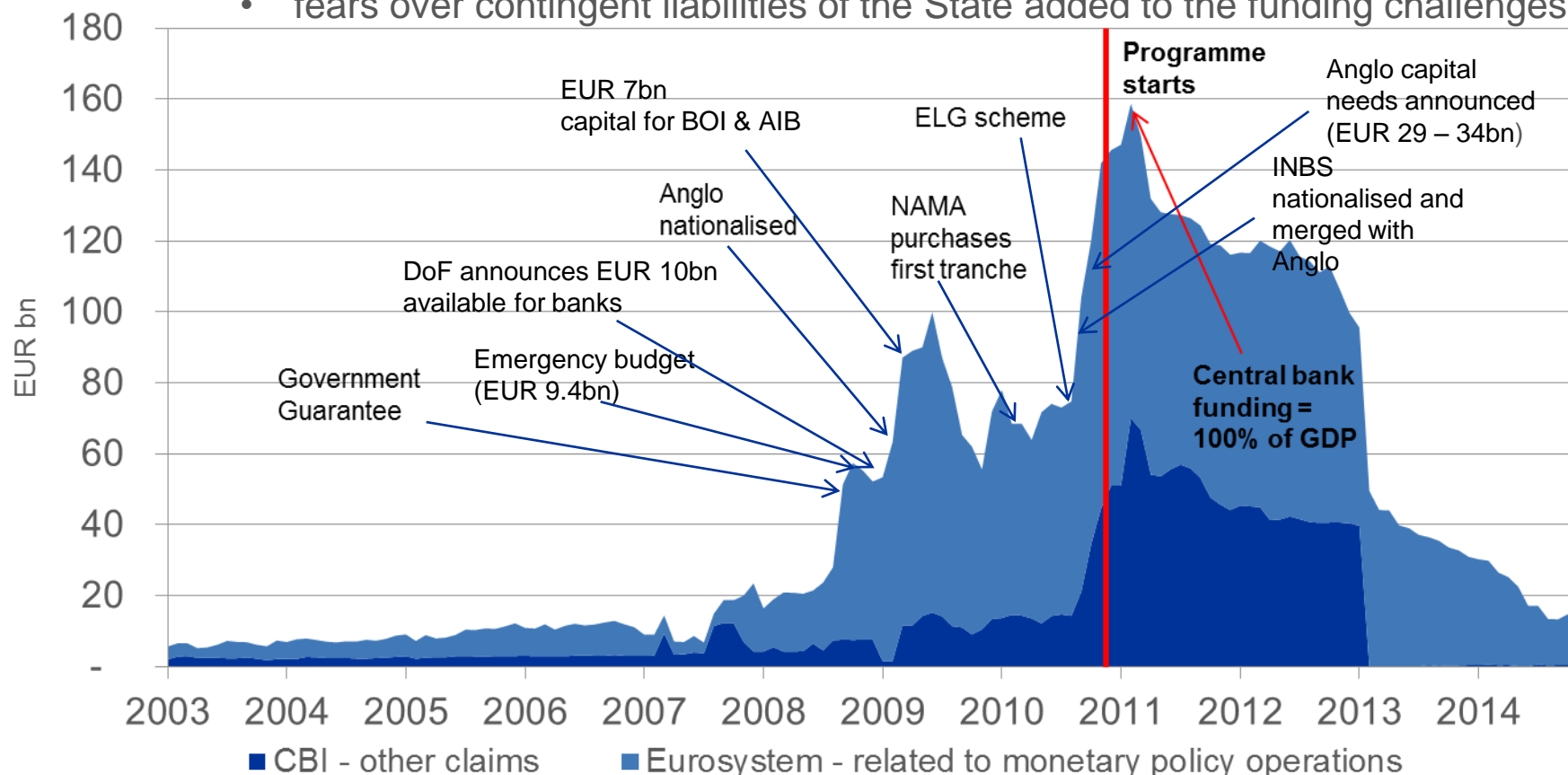


Source: Bloomberg and IMF

Feedback loops – evidence

A funding-solvency adverse feedback loop was in evidence too...

- funding vulnerabilities were exposed by global market developments;
- which the guarantee could not fully offset;
- asset quality concerns (including of sovereign) were impacting collateral availability; and
- fears over contingent liabilities of the State added to the funding challenges



Solvency & Asset Quality

- ✓ Rigorous AQR
- ✓ Bottom-up stress test
- ✓ Minimum capital ratios

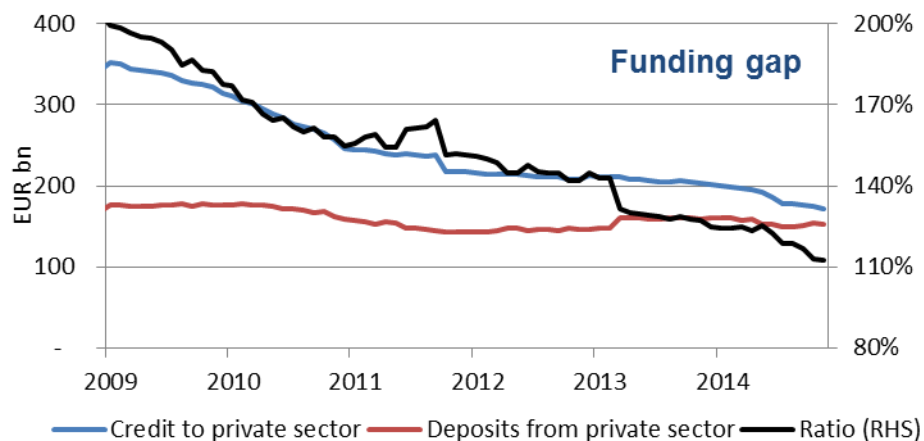
“Right-sizing” & Funding

- ✓ PLAR programme
- ✓ Deleveraging of non-core
- ✓ Funding support & waiver

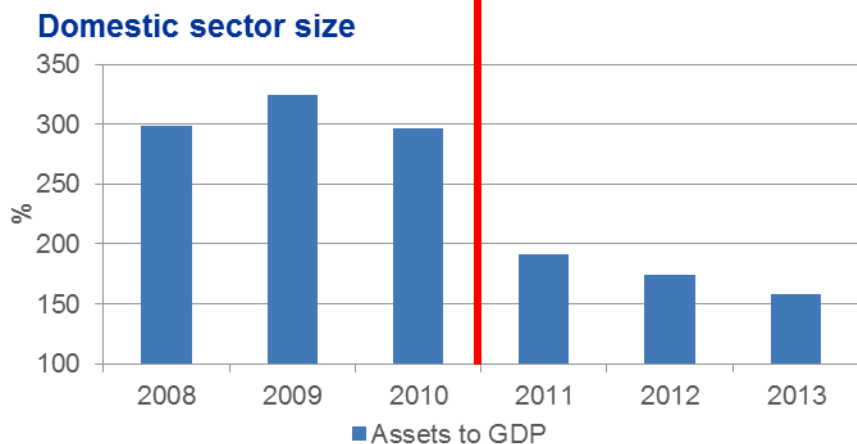
- ✓ Confidence restored
- ✓ Solvency-funding feedback loop reversed
- ✓ Sovereign-bank correlation reduced

Outcomes

Funding gap has closed, funding composition and solvency have improved while domestic bank assets have been significantly reduced ...



Source: CBI, Domestic Market Group, Loans and Deposits - Irish residents.



Source: CBI, From 2011 – three covered banks (AIB, BOI, PTSB).

Stabilising Ireland's banking sector in 2011.

Loan-to-deposit ratios

	DEC 2010	JUN 2014
AIB	166%	96%
BOI	176%	112%
PTSB	248%	141%

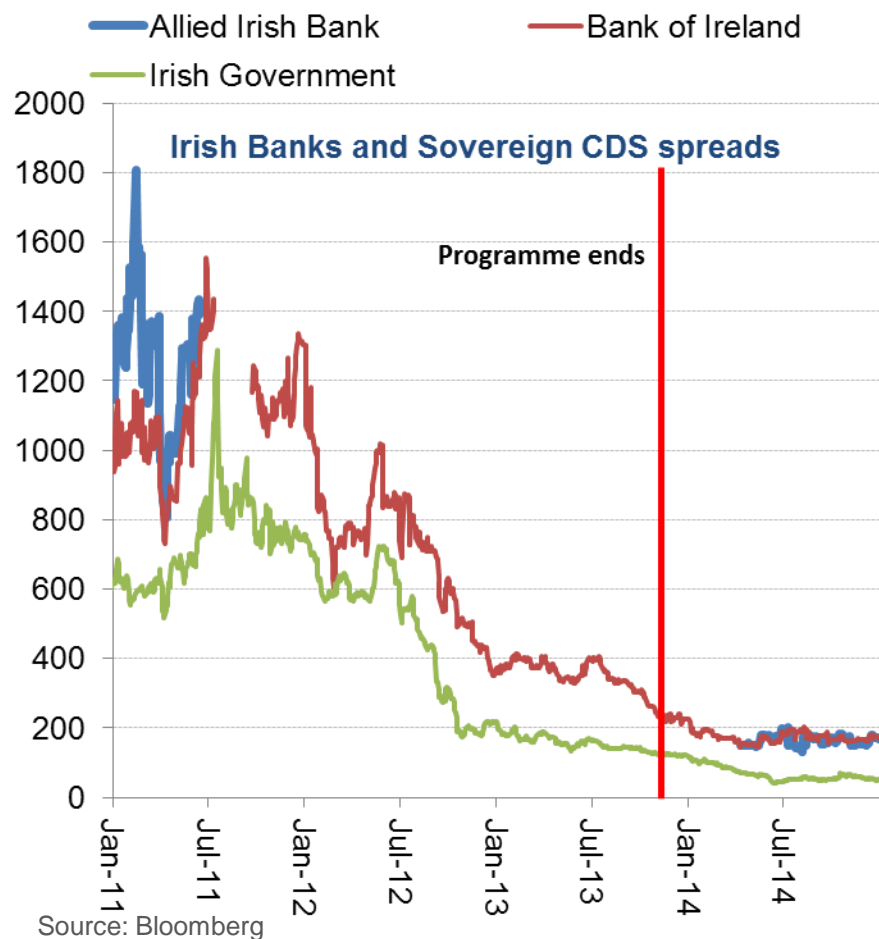
Source: FMP report, Banks semi-annual reports.

CA outcome

%	CET1 (2013)	AQR CET1	CET1 ratios 2016	
			Baseline	Adverse
AIB	14.99	14.64	14.29	10.26
BOI	12.40	11.80	12.43	9.31
PTSB	13.13	12.84	8.82	0.97

Source: European Central Bank. Note: capital quality under the comprehensive assessment based on more stringent definitions than previous exercises.

Improvements have also been seen for funding, market access and profitability and, as a consequence, the bank-sovereign loop poses much lower risk ...



Banks' profits after tax

EUR mn	Jun-2014	2015 (f)	2016 (f)
AIB	411	665	819
BOI	344	567	838
PTSB	-200	-54	-3

Source: Banks semi-annual report
 Note: Forecast from Davy Research (DEC 2014)

Allied Irish Banks (AIB) and Bank of Ireland (BoI) together issued over €5.2 billion in the first nine months of 2014, including €750 million of Tier 2 capital by BoI.