AGENDA

• The liquidity in resolution
• Policy proposals
• A different approach
THE LIQUIDITY IN RESOLUTION

Before
- Loss of mkt access
- FOLTF (bank holiday)
- Resolution scheme adopted
- Reopening of the bank

After
- Possible providers of liquidity
  - Markets
  - Eurosystem (MPO)*
- Prospect of viability
  - YES = bail in + recap
  - NO = Liquidation
- Viable
  - SRF
  - ESM

Gaps
- Weak market confidence
- Insufficient collateral
- Viable
  - Markets
  - Eurosystem (MPO)*
THE LIQUIDITY IN RESOLUTION: US & UK VS. EU

• In US there is a direct facility from the US Treasury
• In UK there is a similar facility from HM-Treasury
• In Europe there is not an European Treasury
• Solution has to
  • be fiscally neutral
  • provide sufficient resources
THERE ARE MANY POLICY PROPOSALS UNDER DISCUSSION…

<table>
<thead>
<tr>
<th>Refinements of current practices</th>
<th>Public Sector Schemes</th>
<th>Private sector schemes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asset encumbrance ratios in resolution plan</td>
<td>ECB proposal: SRB provides a guarantee to the bank</td>
<td>ESM Collateral Pool</td>
</tr>
<tr>
<td>Liquidity stress test</td>
<td>* first demand</td>
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<tr>
<td>Timely FOLT</td>
<td>* interest and principal</td>
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<tr>
<td>Liquidity MREL</td>
<td>* Standing guarantee</td>
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<tr>
<td>Maturity extension</td>
<td>EC/SRB proposal: ESM guarantees the ECB and SRB counterguarantees</td>
<td></td>
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<tr>
<td>Voluntary bank funding + SRB guarantee</td>
<td>SRB Bond (+ Guarantee)</td>
<td></td>
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<tr>
<td>...</td>
<td></td>
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</tbody>
</table>
PUBLIC SCHEMES ARE A VARIATION OF A COMMON IDEA...

• First demand
• interest and principal
• Standing guarantee

BUT
• ESM cannot provide guarantees under the current framework
SRB ISSUES BONDS TO PROVIDE COLLATERAL TO BANKS...

- Unsecured bonds
- 3-10 yrs
- Super senior claim from the bank to SRB

Problems:
- SRB’s rating can pro-cyclical
- Complicate the use of the backstop

Resolved Bank

ECB
Or
Private Repo market

SRB

Bond

Bond

liquidity
A PRIVATE SECTOR LED SOLUTION: COLLATERAL POOL

Collateral Pool
Investment grade assets on-balance sheet

Resolved Bank

Collateral top-up (OP. A)
Collateral top-up (OP. B)

Bank
Bank
Bank
Bank

Markets OR EUROSYSYSTEM

Fees to donor banks
Liquidity
## POTENTIAL CET1 COST OF COLLATERAL POOL REQUIREMENTS...

<table>
<thead>
<tr>
<th>Assumptions</th>
<th>€ bn</th>
<th>Sovereign/Supra €bn)</th>
<th>Bank Issued Bonds (€bn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Collateral</td>
<td>284</td>
<td>AAA</td>
<td>0%</td>
</tr>
<tr>
<td>Cash Equivalent (HC 5%)</td>
<td>270</td>
<td>AAA to AA-</td>
<td>20%</td>
</tr>
<tr>
<td>Total EA Banks' Assets</td>
<td>33,000</td>
<td>A+ to A-</td>
<td>30%</td>
</tr>
<tr>
<td>Total EA Banks' Credit Rating</td>
<td></td>
<td>BBB+ to BBB-</td>
<td>50%</td>
</tr>
<tr>
<td>Total Interest Bearing Assets</td>
<td>28,050</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Collateral/TA</td>
<td>0.86%</td>
<td>0</td>
<td>5.7</td>
</tr>
<tr>
<td></td>
<td></td>
<td>56.8</td>
<td>8.5</td>
</tr>
<tr>
<td></td>
<td></td>
<td>142.1</td>
<td>14.2</td>
</tr>
</tbody>
</table>

- **Cash Equivalent (HC 5%)**
- **Total EA Banks' Assets**
- **Total EA Banks' Credit Rating**
- **Total Interest Bearing Assets**
- **Collateral/TA**
- **CET1 Cost (19% of RWA)**
THE COLLATERAL POOL CONTAINS MORE BENEFITS THAN RISKS...

**Strenghts**

- It can utilise existing (ECB) technology
- It adheres to the main principle of fiscal neutrality.
- The impact on P&L should be neutral and only a minimal increase in capital absorption.
- Appropriate fee calculated at market value and reflecting the credit risk.
- Transparent structure.
- Given that it is purely privately led, should not breach EU Competition rules.

**Weaknesses**

- Affects banks’ unencumbered asset ratios.
- The assets could absorb a (small) amount of regulatory capital.
- To further explore the accounting effect on banks’ P&L in case of a default of the resolved bank.
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