EBA capital exercise

Thursday, 8 December 2011

The Central Bank of Cyprus (CBC) notes the announcements made today by the European Banking Authority ("EBA") regarding the capital exercise which demonstrate the following result for the two Cypriot banks participating in the exercise.

The capital exercise proposed by the EBA and agreed by the Council on 26 October 2011 requires banks to strengthen their capital positions by building up a temporary capital buffer against sovereign debt exposures to reflect current market prices. In addition, it requires them to establish a buffer such that the Core Tier 1 capital ratio reaches a level of 9% by the end of June 2012. The amount of any final capital shortfall identified is based on September 2011 figures. The amount of the sovereign capital buffer will not be revised.

A total of 71 banks across Europe, including Bank of Cyprus and Marfin Popular Bank, were subjected to the capital exercise whose objective is to create an exceptional and temporary capital buffer to address current market concerns over sovereign risk and other residual credit risk related to the current difficult market environment. Explicitly, this buffer would not be designed to cover losses in sovereigns but to provide a reassurance to markets about banks' ability to withstand a range of shocks and still maintain adequate capital.

Following completion of the capital exercise conducted by the EBA, in close cooperation with the Central Bank of Cyprus, the exercise has determined that the two Cypriot banks have a capital shortfall of €3,531 mn which must be addressed by end June 2012. This shortfall was calculated without taking into account the existing contingent convertible hybrid instruments amounting to €1bn that can be used to cover part of the shortfall.

Both banks are required to ensure that by the end of June 2012 they will adhere to the 9% core tier ratio. In this regard, they are requested to submit to the CBC, by 20 January 2012, a plan setting out the proposed mix of actions so as to meet the required 9% target, thereby bringing the shortfall to zero by June 2012. The CBC will assess the banks' plans in consultation with relevant host supervisors and the EBA.

The capital to be raised and measures to be taken by the banks are designed to restore confidence in market participants, to facilitate banks' access to the funding markets as well as to put them in the condition to continue providing financial support to the real economy.

The methodology underlying the capital exercise was outlined by the EBA prior to its announcement to ensure consistency across all banks in the EU banking system involved in the exercise.