



Press release of Banco de Portugal on the results of Novo Banco in the stress test of the comprehensive assessment conducted by the Single Supervisory Mechanism/European Central Bank

- Novo Banco successfully completes the ECB Banking Supervision stress test in the baseline scenario. A shortfall of EUR 1,398 million was identified in the adverse stress test scenario, which is in line with expectations.
- Shortfall in the adverse stress test scenario will be covered by measures to be specified in the bank's strategic plan, which is under preparation and will be submitted in the coming weeks, as well as by the outcome of the sale process of Novo Banco.
- Announcement by the ECB provides clarification on the capital needs of Novo Banco and allows that preparation for the new stage of the sale process is launched immediately.
- With the support of Banco de Portugal and Fundo de Resolução, Novo Banco will pursue the efforts to strengthen the bank's soundness and business will carry on normally.

The European Central Bank (ECB) announced today the results of the comprehensive assessment of a set of nine euro area banks, including Novo Banco.

The comprehensive assessment comprises two components: an Asset Quality Review (AQR) and a stress test. Based on the special audits performed in 2014, the ECB had considered that Novo Banco had already successfully completed the asset quality review.

According to the results released today, Novo Banco has successfully passed the stress test conducted by the ECB under the most likely (baseline) scenario (CET1 ratio of 8.24%, above the 8.0% threshold), but fell short under the more adverse scenario (CET1 ratio of 2.43%, compared with a 5.5% threshold), corresponding to a shortfall of EUR 1,398 million, estimated for end-2017 (Chart 1).



The comprehensive assessment of Novo Banco therefore results in a shortfall only occurring in 2017 under the more adverse stress scenario which refers to a hypothetical scenario, by nature reflecting a pessimistic outlook.

The shortfall recorded by Novo Banco under the more adverse stress test scenario is broadly in line with expectations and reflects the bank's specific nature as the bridge bank that resulted from the resolution measure applied to Banco Espírito Santo, S.A. This shortfall must nevertheless be addressed.

As announced **by Banco de Portugal on 15 September, the Board of Directors of Novo Banco has already been empowered to present a plan to strengthen its solvency and implement strategic reorganisation.** This process has already started, in anticipation of the existence of a shortfall, and is expected to be submitted in the coming weeks. It shall be subsequently debated in the scope of the existing dialogue and co-operation with the ECB and the European Commission. The plan will include measures to address the shortfall within an appropriate time frame, to be planned and executed in cooperation and with the support of Banco de Portugal, in its capacity as resolution authority, and Fundo de Resolução, as the single shareholder.

Amongst others, those measures included the following, to be implemented in the short term with the support of Banco de Portugal and Fundo de Resolução:

- Sale of Novo Banco's shareholding in GNB Vida - Companhia de Seguros, S.A.;
- Sale of other shareholdings which are perceived to be non-core for the bank's business.

The measures to be set out in the strategic plan will complement the reinforcement of Novo Banco's solvency that will come from the sale process of the Resolution Fund's shareholding. Preparation of the new stage of the sale process will start immediately, now that one of the main elements of uncertainty affecting the previous procedure has been removed.

Strategic reorganisation and strengthening the solvency of Novo Banco do not of course compromise the normal business of the bank. Banco de Portugal, in its capacity as resolution authority in control of Novo Banco, and the Resolution Fund, in its capacity still as Novo Banco's only shareholder, in close cooperation with Novo Banco, continue to be focused in guaranteeing that conditions are in place for consolidation of the progress made to date and for the sale of the shares held by the Resolution Fund.



The macroeconomic and financial scenarios for the stress tests on Novo Banco

The stress test was developed under two different scenarios for macroeconomic developments in the period from 2015 to 2017. The baseline (more likely) scenario was drawn up by the European Commission and reflected the official macroeconomic projections as of end-2014.

The adverse scenario was built by modelling deviations from the baseline scenario, resulting from negative shocks of low probability impacting on the macroeconomic and financial variables. Those shocks have been defined with reference to the main systemic risks identified for the European Union at the time of the 2014 comprehensive assessment, including:

- Significant increase in government debt yields in most economies;
- Further sharp deterioration in credit quality in economies with low domestic aggregate demand and with banking systems perceived as more vulnerable;
- Postponement of reform, raising doubts over the sustainability of the public finances in many economies;
- Insufficient adjustment of banks' balance sheets, restricting their ability to obtain market financing at a reasonable cost.

The adverse scenario assumed the same level of severity as the scenario calibrated in the 2014 stress test, assessed from the deviations from the baseline scenario.

The scenarios for Portugal

In the stress test's baseline scenario, economic activity recovers gradually in Portugal, with the respective growth rate at levels slightly below the European Union's average, throughout the projection horizon (2015-2017).

The adverse scenario is characterised by the following main projections for the same projection horizon (2015-2017):

- Cumulative reduction in economic activity of 2.8 percentage points;
- Unemployment rate above 14% from 2016 onwards;



- Significant increase in long-term interest rates, which are expected to stand at around 3.5 to 4.0%, with an impact on the economy's financing and the valuation of banks' debt security portfolios;
- Cumulative reduction in residential property prices of around 13%.

It is worth mentioning that the latest projections are slightly more favourable for most variables, even when compared with projections underlying the baseline scenario of the stress test. In the light of these developments it is fair to conclude that the adverse scenario, which is designed by nature to be less likely than the baseline scenario, incorporates projections which, at this stage, are even less likely to materialise.

Main variables of the macroeconomic and financial scenarios

	Portugal		Portugal			European Union		
	2015 (projections / latest observed values)		2015	2016	2017	2015	2016	2017
	2015	2016	2015	2016	2017	2015	2016	2017
Baseline scenario								
GDP at constant prices (annual rate of change (%))	1,7*		1,6	1,7	1,9	1,7	2,1	2,0
Unemployment (as a % of labour force)	12,4**		13,4	12,6	11,8	9,8	9,3	8,6
Long-term interest rates (ten-year Treasury bonds (%))	2,39***		1,9	2,0	2,2	1,2	1,3	1,5
Residential property prices (annual rate of change (%))	2,9****		-1,0	-1,3	-0,5	2,1	3,5	4,5
Adverse scenario								
GDP at constant prices (annual rate of change (%))			0,1	-2,1	-0,8	-0,5	-1,3	0,3
Unemployment (as a % of labour force)			13,8	14,3	14,6	10,4	11,2	11,5
Long-term interest rates (ten-year Treasury bonds (%))			4,2	3,7	3,9	2,7	2,4	2,7
Residential property prices (annual rate of change (%))			-4,7	-4,9	-3,8	-6,6	-5,4	-1,3

* Banco de Portugal projections - June 2015 ** Value 2nd quarter of 2015; Source : INE.

*** Data at September 30, 2015 ; Source : Bloomberg. **** Chain rate of change 2nd quarter of 2015; Source : INE.

Methodology

The starting point for the exercise was 31 December 2014, with the financial and prudential results projected over a three-year period (i.e. 2015-2017). The relevant variable for the analysis is the CET1 ratio and the threshold set for this indicator is 8% for the baseline scenario and 5.5% for the adverse scenario, as in the 2014 stress test.

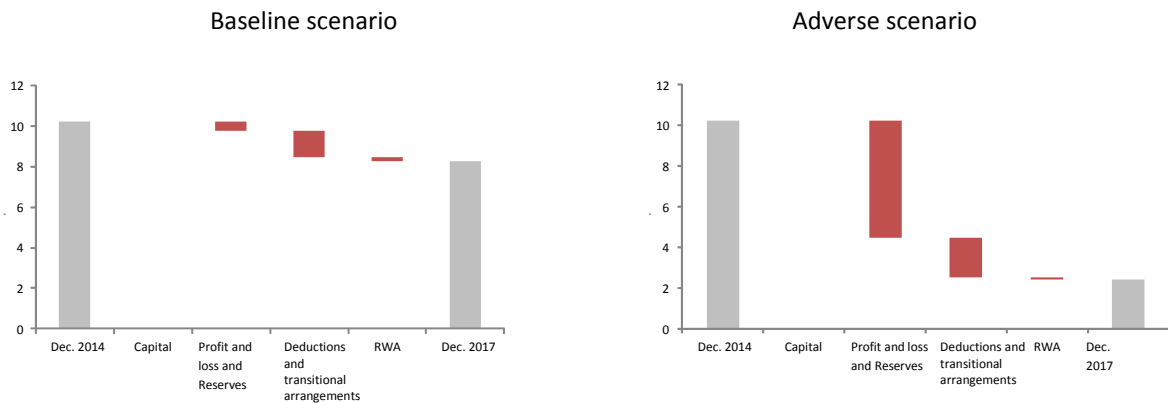
The stress test was performed under a general static balance sheet assumption, under which balance sheet items remain constant (as at December 2014) and the financial instruments are replaced at maturity, keeping the same characteristics. Management measures that may be



adopted by institutions in order to improve their performance are therefore not taken into account.

Due to the static balance sheet methodology, the projections are particularly restricted by the values recorded at the exercise's starting point. The result of Novo Banco's stress test was therefore affected by the difficulties faced by this bank during its first months of activity, following the resolution of BES.

Chart 1 – Developments in the CET1 ratio - Novo Banco



Notes: Columns in grey correspond to the CET1 ratio as at December 2014 and December 2017. Reported data corresponds to Novo Banco, on a consolidated basis, excluding BES1.

Negative contributions to developments in the ratio are shown in red. The column "Capital" refers to capital increases and/or reimbursement of hybrid instruments; the column "Profit and loss and Reserves" refers to cumulative profit and loss and changes in reserves; the column "Deductions and transitional arrangements" refers to deductions from own funds in accordance with the CRR/CRD IV and respective transitional arrangements; the column "RWA" shows the impact on the ratio of changes in capital requirements.

Lisbon, 14 November 2015



Annex – Main results - Novo Banco, SA

31 December 2014	EUR million, %
Common Equity Tier 1 (1)	4,490
Risk weighted assets (1)	43,954
CET 1 ratio, %	10.2

Results in the baseline scenario for December 2017	EUR million, %
Common Equity Tier 1 (1)	3,713
Risk weighted assets	45,097
CET 1 ratio, %	8.2

Results in the adverse scenario for December 2017	EUR million, %
Common Equity Tier 1 (1)	1,103
Risk weighted assets	45,478
CET 1 ratio, %	2.4

Shortfall (2)	Basis points	EUR million
To the 8% threshold in the baseline scenario	0	0
To the 5,5% threshold in the adverse scenario	307	1,398

(1) Phasing-in provisions in accordance with CRR/CRD4 as of the reporting date. Data as of 31/12/2014 calculated in accordance with the rules in force at 01/01/2015.

(2) The value for RWA's refers to the worst year of the relevant scenario.