

Convergence Romania Financial Sector Modernization Special Projects Public-Private Initiative Steering Committee



Credit Exposure Stress Testing Techniques

<http://www.spi-romania.eu/program-2007/methodological-aspects-of-stress-test-for-banks/>

SPI Committee Meeting July 25, 2007

Project Objective:

Improve the NBR methodology for stress testing for companies and households and create a framework for the NBR to share its knowledge in the area of stress testing for banks with credit institutions.

Project Working Group Activities

PWG members: 4

PWG meetings: 1

Public stakeholders

- National Bank of Romania.

Private stakeholders

- Banking sector (2 banks).

Project Main Steps

Nov. 2006: Convergence appoints the project technical anchor
Dec. 7, 2006: Project strategy meeting clarifying the specific technical needs of NBR in the area of stress testing for households and corporate and the banks' involvement in the project
Dec. 15, 2006: NBR expresses its view according to which banks should not be involved in the project regarding the stress testing for households and companies
Jan., 2007: SPI Secretariat prepares a proposal for a project split into two parts (NBR technical assistance and stress testing for banks) and a project revival strategy
Jan.-Mar. 2007: SPI Secretariat, with the support of Convergence, mobilizes Bank of Italy to provide technical assistance to NBR
June 2007: SPI Secretariat prepares a background paper on the role, formulation and international experience of stress testing in banks and asks NBR to provide its input on the central bank experience in banks' stress testing and the recommended guidelines for banks.

Summary of Impact Assessment:

Government: RON 38 mil (5 year net present value) as tax revenues
Banks: RON 162 mil. (5 year net present value) in savings from stress testing adoption in reducing annual LLPs for lending activity

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SPI Project on Credit Exposure Stress Testing Techniques

Project Team

Project Working Group

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SPI Project on Credit Exposure Stress Testing Techniques

Project Status Report

I. Actions undertaken in April-June 2007

The actions undertaken have followed the project strategy endorsed by the project management group, respectively to split the project into two parts:

1. addressing the specific technical needs of the NBR in the area of stress testing for households and firms get solved with the support of international experts / central banks with extensive relevant knowledge (contacts facilitated by SPI Secretariat and Convergence);
2. developing a knowledge transfer component where the central bank could support the banking community in improving its knowledge of stress testing.

A. Technical assistance for NBR

The SPI Secretariat, with the support of Convergence, continued the discussions with Bank of Italy, which confirmed its availability to provide the necessary technical assistance to the NBR for improving its stress testing methodology for households and firms. The cooperation between the two central banks will have to be framed by the European System of Central Banks rules.

B. Knowledge transfer between the NBR and banks

The SPI Secretariat prepared a background paper on the role, formulation and international experience of stress testing in banks and requested NBR to provide its input on:

- the central bank experience in banks' stress testing and
- the recommended guidelines for stress tests performed by banks.

II. Project next steps

In order to achieve the new SPI Project objective – that is, to develop a knowledge transfer component where the central bank could support the banking community in improving its knowledge of stress testing, the PWG agreed to follow the following steps:

- **July 2007** – NBR will finalize its contribution to the background paper on the central bank experience in banks' stress testing, which will outline the main methodological aspects as well as scenario formulation issues and the guidelines for stress testing by banks;
- **September 2007** - A round table will be organized with banks in order to share the central bank knowledge and guidance on stress testing with banks. The minutes of the discussions and the stress testing guidelines for banks will be shared with the banking community.

III. Proposed SPI Committee decision

It is proposed that the SPI Committee takes note on the latest developments and encourages the NBR to pursue the objective of strengthening the awareness and knowledge of banks in the area of stress testing.