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Standard & Poor's Publishes Its Additional Loss-Absorbing Capacity Methodology; Teleconference Wed. April 29, 10 AM ET

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TORONTO (Standard & Poor's) April 27, 2015--Standard & Poor's Ratings Services today said it published its new methodology addressing additional loss-absorbing capacity (ALAC), titled "Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity," which represents a form of potential external support that can be incorporated in bank issuer credit ratings (ICRs). These new criteria address regulatory policy initiatives in different jurisdictions to implement bail-in regulatory mechanisms (where certain creditors are first to take losses rather than taxpayers). These mechanisms aim to improve a bank's capacity to survive extreme stresses without necessarily relying on government bailouts by a recapitalization on the back of the write-down or conversion into common equity of various obligations. The "Principles Of Credit Ratings," published Feb. 16, 2011, on RatingsDirect, form the basis of these criteria.

We have also published "How The Potential Bail-In Of Additional Loss-Absorbing Capacity (ALAC) Instruments Affects Bank Ratings Under Our New Criteria," which provides background on the criteria changes, and discusses certain features of the criteria including questions regarding their implementation in various regions.

The ALAC criteria recognize that new regulations requiring banks to hold material amounts of "bail-inable" liabilities (that is, those that can be written down or converted to common equity in a resolution without triggering a legal default or entry into liquidation of the bank), can reduce the default likelihood of a bank's senior unsecured obligations.

"The costs of bank bailouts in the global financial crisis have spurred ongoing changes to bank prudential regulations," said Standard & Poor's credit analyst Thomas Connell. These regulations aim at effective bank supervision, preservation of financial system stability, and an end to an expectation of taxpayer-funded bailouts that can lead to excessive bank risk-taking. "We have already reflected these regulatory priorities in changes to our criteria for assigning issue credit ratings to bank hybrid capital instruments, based on an expectation of increased bail-in risks for these instruments," Mr. Connell added. (See "Standard & Poor's Finalizes The Rating Approach For Bank And Prudentially Regulated Finance Company Hybrid Capital Instruments," Sept. 18, 2014.) Similarly, declining expectations for potential extraordinary government support for banks have been a prominent theme of our bank rating surveillance, looking at policy priorities in the wake of the financial crisis.

SCOPE OF THE CRITERIA

These criteria have the same scope as the bank criteria--i.e., they apply to ratings on retail, commercial, and corporate and investment banks. The definition of a bank is broad and includes the larger broker-dealers, mortgage lenders, trust banks, credit unions, building societies, and custody banks. These criteria are applicable to banking groups that are headed either by an operating company or by a nonoperating holding company (NOHC). These criteria do not apply to ratings on finance companies, asset managers, financial market infrastructure entities, and regional securities brokers.

SUMMARY OF THE CRITERIA

ALAC consists of certain bank hybrid capital instruments and, in specified circumstances, other liabilities (such as NOHC debt in some jurisdictions) that can absorb losses of a bank at or near nonviability--for example, in the event of a bank resolution, in a way that reduces the risk of the bank defaulting, according to our definitions, on its senior unsecured obligations. In certain circumstances, instruments issued by an NOHC are eligible for inclusion in ALAC alongside qualifying instruments issued by the operating bank.

This methodology is a framework for determining the uplift we incorporate into a bank ICR--relative to its stand-alone credit profile--for ALAC. The criteria address features of a resolution policy framework that could provide a basis for ALAC uplift; what instruments constitute eligible ALAC; and factors governing the amount of ALAC (and related qualitative considerations) necessary for one or two notches of ALAC-related uplift.

The methodology also describes how this uplift interacts with uplift for government and group support, the criteria for which remain otherwise

unchanged, as outlined in "Banks: Rating Methodology And Assumptions," Nov. 9, 2011 and "Group Rating Methodology," Nov. 19, 2013.

IMPACT ON OUTSTANDING RATINGS

We expect these criteria to result in limited rating changes upon becoming effective. As of this date, in our view, only four jurisdictions (all in Europe) have resolution regimes in place that may meet the conditions for an effective resolution regime. In our preliminary estimate, we expect that just less than half of the eligible institutions have sufficient ALAC (based on our current projections) for one or two notches of ALAC uplift; such uplift may partially or fully offset the reduction or elimination of ICR uplift, if any, due to a weakening of our expectations of extraordinary government support. We expect that there could be an associated ratings impact on the ICRs on about 40 other financial services entities globally because of their belonging to these groups (and on some of their issue credit ratings, including those on several insurance company hybrids.) Over time, we expect these ALAC criteria to apply to more jurisdictions as resolution policy frameworks are being defined and implemented, including the role of bail-in instruments that would generally constitute a bank's ALAC.

EFFECTIVE DATE AND TRANSITION

The revised criteria are effective immediately. We intend to complete our review of issuer and issue credit ratings that have been put under criteria observation (UCO) in late May or early June. See "Ratings On 57 Issuers Placed Under Criteria Observation After Bank Additional Loss Absorption (ALAC) Criteria Publication," published April 27, 2015.

CHANGES FROM THE REQUEST FOR COMMENT

Today, we also published "RFC Process Summary: Standard & Poor's Summarizes The Request For Comment Process For Additional Loss-Absorbing Capacity Methodology for Banks," which provides an overview of the main changes between the "Request for Comment: Incorporating Additional Loss-Absorbing Capacity Into Bank Rating Methodology," published Nov. 24, 2014, and the final criteria, as well as the rationale behind those changes.

TELECONFERENCE DETAILS

New Bank Additional Loss Absorbing Capacity (ALAC) Criteria Webcasts
Standard & Poor's will host two complimentary Webcasts to discuss the criteria on the following dates:

EMEA and North America: Wed., April 29, 2015

3:00 p.m. British Summer Time, 4:00 p.m. Central European Summer Time, and
10:00 a.m. Eastern Daylight Time

Registration Link:

<http://w.on24.com/r.htm?e=986734&s=1&k=BF6B5D414ECBBE75095FFF3BB09AC17B>

APAC: Thursday, April 30, 2015

2:00 p.m. Australian Eastern Standard Time, 12:00 p.m. Singapore Time, Hong
Kong/China Standard Time, 11:00 a.m. Indochina Time, 1:00 p.m. Japan/Korea

Standard Time, 9:30 p.m. India Standard Time

Registration Link:

<http://w.on24.com/r.htm?e=987165&s=1&k=0EC3F57C6C35FDD283D8261BEDF84A26>

Standard & Poor's Webcasts deliver audio in a streamlined console. You will need computer speakers or headphones to listen to the audio stream. You may submit your questions for the presenters in real-time via the red Q&A icon located at the bottom of the screen.

Replays of both webcasts will be made available shortly afterwards and will be accessible for 90 days. The link is the same as the registration link.

Please feel free to forward this invitation to any interested colleagues.

All the articles are published under our topic page including regional CreditMatters TV interviews:

https://www.spratings.com/financial-institutions/banks/Global-Banking.html?sp_m_id=51809&sp_rid=1367094

RELATED CRITERIA AND RESEARCH

Related Criteria

- Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Group Rating Methodology, Nov. 19, 2013

Related Research

- RFC Process Summary: Standard & Poor's Summarizes The Request For Comment Process For Additional Loss-Absorbing Capacity Methodology for Banks, April 27, 2015
- How The Potential Bail-In Of Additional Loss-Absorbing Capacity (ALAC) Instruments Affects Bank Ratings Under Our New Criteria, April 27, 2015

The report is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. If you are not a RatingsDirect subscriber, you may purchase a copy of the report by calling (1) 212-438-7280 or sending an e-mail to research_request@standardandpoors.com. Ratings information can also be found on Standard & Poor's public Web site by using the Ratings search box located in the left column at www.standardandpoors.com. Members of the media may request a copy of this report by contacting the media representative provided.

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