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The Danish Financial Supervisory Authority

30 July 2021

Results for the Danish participants in the EU-wide stress test 2021

Danske Bank, Nykredit, Jyske Bank, and Sydbank have participated in the EU-wide stress test 2021. This is a very severe stress test, which leads to significant decreases in the capital ratios of the institutions. For Danske Bank the decrease is of a magnitude that the institution has to make use of the capital conservation buffer over the three-year projection. Jyske Bank fulfils its capital requirements, but with modest excess capital. All institutions fulfil their solvency need with a comfortable margin.

”The new results show that the capitalisation of some of the largest Danish institutions come under pressure in the EU-wide stress test. However, all Danish institutions retain capital that is comfortably above their solvency need. The results reflect a very severe adverse scenario, which is assumed to build on an already stressed macroeconomic starting point as a result of the COVID-19 crisis. Although this is a very severe stress test, the results underline the need for institutions to maintain a robust capitalization going forward", says Director General Jesper Berg.

Background
The purpose of the EU-wide stress test is to assess the robustness of the European banking sector in the face of a severe economic downturn. In order to ensure level playing field across the participating institutions, the European Banking Authority (EBA) has established adverse scenarios and a common methodology for calculating the consequences. This approach has contributed to transparency on the exposures and risks of the European banking sector on a harmonised basis.

The stress test includes 50 banks in 15 countries, equivalent to around 70 per cent of the European banking sector’s total assets. In addition to this sample, there are other banks that national regulatory authorities have chosen to stress.

Danske Bank, Nykredit, and Jyske Bank are participating from Denmark in the EBA sample of banks. As has also been the case in the past, the Danish Financial Supervisory Authority (DFSA) has chosen to request Sydbank to run a similar stress test in order to achieve greater coverage of the Danish banking sector. The four Danish participants have all been subject to the same macroeconomic scenarios, methodology, reporting requirements and quality assurance.

Overall, the stress test covers around 90 percent of the Danish banking sectors total assets. All institutions participate at Group level. The results are based on the banks' financial accounts and capital position 2020 and are calculated on the assumption of a static (unchanged) balance sheet and without allowing for management interventions.

The EU-wide stress test 2021 is coordinated by the EBA in cooperation with the National Supervisory Authorities (in Denmark DFSA), the European Systemic Risk Board (ESRB), and the European Central Bank (ECB).

Scenarios and assumptions
The EU-wide stress test sets out a macroeconomic adverse scenario for each country.

The adverse scenario for Denmark describes a severe economic downturn with negative GDP growth, large drops in residential and especially commercial property prices, and sharply rising unemployment. The adverse scenario builds on an already stressed macroeconomic starting point at the end of 2020, as a result of the COVID-19 pandemic, making it a very severe adverse scenario.

The adverse scenario for Denmark (and the other Nordic countries) is also more severe than for the EU as a whole, see table 1. This is partly explained by the fact that the Danish and Nordic economies were not as severely hit by the COVID-19 pandemic as other European countries.

Table 1: Adverse scenarios for Denmark, Sweden, Norway and the EU

Scenario variables	EBA 2021 stress scenarios			
	Denmark	Sweden	Norway	EU
Accumulated growth in per cent				
Real GDP	-4.3	-4.7	-4.3	-3.6
Memo: Real GDP growth in 2020	*-3.6*	*-3.6*	*-2.8*	*-6.9*
Residential property prices	-21.9	-27.6	-27.3	-16.1
Commercial property prices	-36.6	-40.5	-41.3	-31.2
Per cent / percentage points				
Unemployment - level EoY	11.4	14.3	6.6	12.1
Unemployment - change (2020-2023)	6.5	5.6	2.1	4.7

Note: The adverse scenario covers a three-year horizon (2021-23). The table shows the development of the variables over the 3-year scenario, with the exception of GDP, where growth is shown for the year with the accumulated largest decline. For Denmark, Norway and Sweden it is 2022. For the EU it is 2023. Eurostat's unemployment rate statement. "Memo: Real GDP growth in 2020" reflects estimates as of the preparation of the scenario.

Source: ESRB and own calculations.

The stress test also includes an adverse market risk scenario that describes negative developments in the financial markets with, among other things, sharply falling stock prices and rising credit spreads.

The stress test is based on the banks' own calculations. Banks shall recognise credit losses due to the macroeconomic deterioration in the adverse scenario as well as losses on their market positions due to negative developments in financial markets. In addition, earnings decrease as a result of lower net interest margins.

However, banks' calculations are subject to a number of methodological restrictions. The EBA's common methodology thus lays down a number of restrictions on the development of, among other things, banks' earnings, risk exposure amount, and balance sheet, which all result in more conservative outcomes. The restrictive method, along with the very severe adverse scenario, means that the stress test is very severe in its design.

The results do not take into account changes in financial regulation, which are expected to be implemented during the stress test horizon (2021-23). These include new EBA guidelines for IRB models and the finalisation of Basel-III ("Basel IV"). Effects from new EU regulations introducing a minimum loss coverage of non-performing exposures ("NPL calendar") are included. In addition, banks may take into account the transitional arrangement of IFRS 9, which allow the banks, who make use of these arrangements, to add back to their capital a transitional amount.

The DFSA has carried out a quality assurance of the results in order to ensure compliance with the methodology and sufficiently prudent results in the adverse scenario. By a varying degree, the quality assurance has changed results in a more prudent direction. The quality assurance takes into account differences in business models, including the volume of mortgage lending and the volume of foreign exposures.

The Danish results

The capital situation in the Danish institutions is significantly affected by the severe economic downturn in the adverse scenario. The common equity tier 1 (CET1) ratio thus falls in the range of 6-7 percentage points compared to the starting point end-2020, see figure 1.

The capital effects for all the institutions are significantly higher than in the latest EU-wide stress test from 2018. This can be explained, among other things, by the very severe adverse scenario in this year's stress test (e.g. given the already stressed macroeconomic starting point) and the current low interest rate environment, which has led to a downward pressure on the banks' earnings.

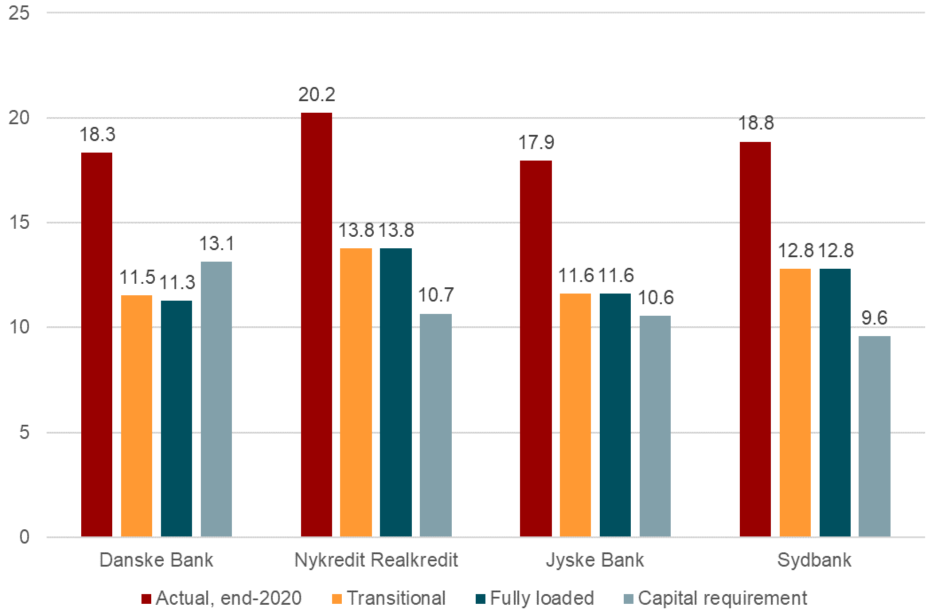
Excess capital to the capital requirements can be calculated on a transitional and fully loaded basis. The transitional calculation allows, among others the aforementioned transitional arrangements associated with IFRS 9. Danske Bank and Sydbank make use of the transitional arrangement, but the effect is modest.

The Danish institutions have under the adverse scenario, *on a transitional basis*, a CET1 ratio in the range of 11.5-13.9 per cent by end-2023. Danske Bank does not fulfil the CET1 capital requirement in the stress test (shortfall of 1.6 per cent of risk exposure amount), see figure 1 (yellow vs. grey bar). However, Danske Bank fulfils the solvency need and the SIFI buffer with a comfortable margin. The other institutions all maintain excess capital to the CET1 requirement. This reflects, among other things, that the other institutions have higher excess capital at the starting point (end-2020). [1]

Danske Bank's shortfall is slightly higher (1.8 per cent of risk exposure amount) on a *fully loaded basis*.

[1] For a more detailed overview of the institutions' capital position, etc. see the attached annex.

Figure 1: Common Equity Tier 1 capital (CET1) and the associated capital requirement end-2020 and in the adverse scenario (worst year), per cent of risk exposure amount



Note: The capital requirement in the stress scenario is calculated as the minimum requirement (4.5%) + CET1 amount of the Pillar II requirement (by end-2020) + capital conservation buffer (2.5%).) + SIFI buffer (institution specific). The worst year refers to the year in the stress scenario where excess capital is lowest. For Nykredit Realkredit it is end-2022. For the other institutions, it is end-2023. "Fully loaded" shows the capital ratio calculated without IFRS 9 transitional arrangements for the institutions using it (Danske Bank and Sydbank).

When looking at total capital on a transitional basis, Danske Bank has a capital shortfall of 2.5 per cent of risk exposure amount (=15.6-18.1), see figure 2, and will thus make use of the entire capital conservation buffer. Danske Bank will however, fulfil the SIFI buffer (3 per cent in the case of Danske Bank) in the worst year in the stress scenario. Danske Bank will have a comfortable excess capital to the solvency need in all three years.

Jyske Bank is very close to the total capital requirement in the last year of the stress test with a modest excess capital of 0.1 per cent of risk exposure amount (=15.7-15.6).

Nykredit Realkredit and Sydbank fulfil the capital requirement by a large margin.

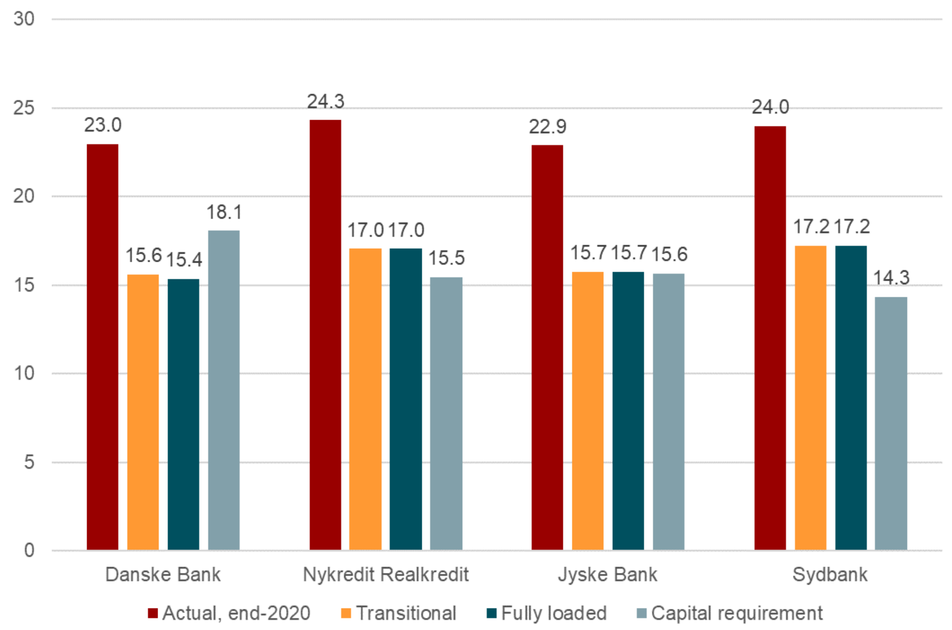
For all institutions, the excess capital is lower for the total capital requirement than for the CET1 requirement. The requirement for total capital is therefore the binding capital requirement for the institutions.[2]

[2] For Sydbank the Tier 1 capital requirement is the binding capital requirement, see annex.

The transitional arrangement in IFRS 9 improve Danske Bank's capitalization in the stress scenario by 0.2 per cent of risk exposure amount. In the calculation assuming fully loaded effects in 2023, the banks' capital shortfall would thus increase to 2.7 per cent of risk exposure amount.

In this case, Danske Bank will not fulfil the SIFI buffer but will continue to fulfil the solvency need by a significant margin. The transitional arrangement will apply at the end of 2023.

Figure 2: Total capital and the associated capital requirement at end-2020 and in the adverse scenario (worst year), percentage of risk exposure amount

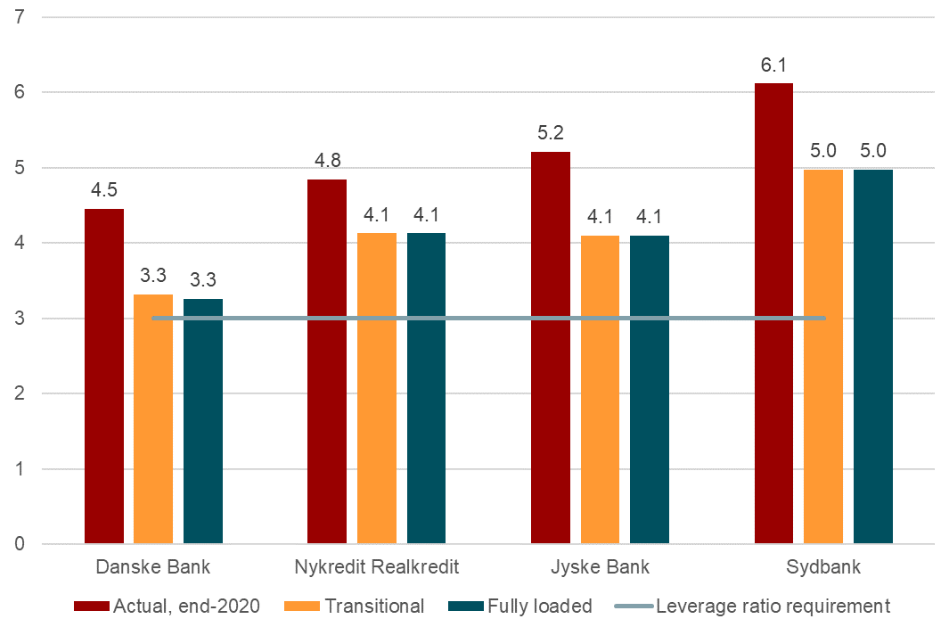


Note: The capital requirement in the stress scenario is calculated as the minimum requirement (8%) + Pillar II requirement (by end-2020) + capital conservation buffer (2.5%).) + SIFI buffer (institution specific). The worst year refers to the year in the stress scenario where excess capital is lowest. For Nykredit Realkredit it is end-2022. For the other institutions, it is end-2023. "Fully loaded" shows the capital ratio calculated without IFRS 9 transitional arrangements for the institutions using it (Danske Bank and Sydbank).

Breach of the capital buffer requirement generally limits an institution's ability to pay dividends, coupons on AT1 capital, and variable remuneration. The effects are included in the stress test for Danske Bank, where applicable.

In the worst year of the stress test, the institutions have a leverage ratio in the range of 3.3-5.0 per cent of total levereage ratio exposure, see figure 3.

Figure 3: Leverage ratio and leverage ratio requirement, end-2020 and in the stress scenario (worst year), percentage of total leverage ratio exposure



Note: The worst year refers to the year in the stress scenario where excess capital is lowest. For Nykredit Realkredit, this is the end of 2022. For the other institutions, it is the end of 2023. "Fully loaded"' shows the leverage ratio calculated without transitional arrangements.

All institutions thus fulfil the leverage ratio requirement of 3 per cent.

Capital issues and redemptions by end-June 2021

As mentioned, the stress test takes the institutions' capital position at the end of 2020 as a starting point. During the first half of 2021, several institutions have made changes to their capital position, see annex table A.

The biggest effects are for Danske Bank and Jyske Bank, which have increased their total capital through capital issues (net) during the first six months of 2021.

If this is taken into account, all other things equal, the capital shortfall to the total capital requirement will be smaller for Danske Bank (by 0.7 per cent of risk exposure amount), while the capital shortfall compared to the CET1 requirement is unaffected. It is the total capital requirement that is binding for Danske Bank. Danske Bank will continue to breach the capital requirements in the stress test, both in relation to CET1 and the total capital, but to a lesser extent.

For Jyske Bank, is the distance to the capital requirement for total capital increased (to 1.1 per cent of risk exposure amount) when capital issues during the first half of 2021 are included. The bank will thus fufill the total capital requirement with a larger margin.

Application of the results
The result of the stress test shall according to EBA's instructions, inform the supervisory review and evaluation process (SREP) for each institution.

The Danish results will thus be included in the DFSA's considerations regarding the setting of a so-called ”Pillar II Guidance” (P2G) for the participating Danish institutions.[3] P2G can be interpreted as a prudential add-on to the solvency need, which aims to ensure that an institution at all times has a sufficiently robust capitalisation to be able to fulfil the solvency need in an adverse scenario. A P2G is determined for an institution if the supervisory authorities assess that the institution cannot fulfil the solvency need in an adverse scenario.

The DFSA's ongoing dialogue with the institutions on capital targets, capital redemptions, and distribution policy will continue to be based on stress tests based on scenarios and assumptions laid down by the DFSA. The DFSA expects the Danish institutions to have a sufficiently robust capitalisation such that they at all time are able to fulfil the total capital requirement including capital buffer requirements (i.e. solvency need + SIFI buffer + capital conservation buffer) in an adverse scenario. This approach usually leads to expectations of a higher capital target than under P2G.

For the expectations of the DFSA regarding the institutions capital targets, see the following note (in Danish): https://www.finanstilsynet.dk/Nyheder-og-Presse/Pressemeddelelser/2018/kapitalplaner_og_kapitalmaalsetninger071118

[3] See the Danish Financial Business Act § 124a

Annexed tables (percentage of total risk exposure amount, unless otherwise stated)

Danske Bank	Actual	Transitional						Memo: Fully loaded
		Base			Stress			Stress
1. Capital	**2020**	**2021**	**2022**	**2023**	**2021**	**2022**	**2023**	**Worst year (2023)**
Common Equity Tier 1	18.3%	18.5%	18.9%	18.9%	13.8%	12.4%	11.5%	11.3%
Tier 1 capital	20.5%	20.7%	21.1%	21.1%	15.8%	14.4%	13.5%	13.2%
Total capital	23.0%	23.2%	23.5%	23.5%	18.1%	16.5%	15.6%	15.4%
2. Capital requirements								
Common Equity Tier 1	13.2%	13.2%	13.2%	13.2%	13.1%	13.1%	13.1%	13.1%
Tier 1 capital	15.4%	15.4%	15.4%	15.4%	15.2%	15.2%	15.2%	15.2%
Total capital	18.2%	18.2%	18.2%	18.2%	18.1%	18.1%	18.1%	18.1%
...of which solvency need	*12.6%*	*12.6%*	*12.6%*	*12.6%*	*12.6%*	*12.6%*	*12.6%*	*12.6%*
3. Excess capital								
Common Equity Tier 1	5.1%	5.3%	5.6%	5.6%	0.6%	**-0.7%**	**-1.6%**	**-1.8%**
Tier 1 capital	5.2%	5.4%	5.7%	5.7%	0.6%	**-0.9%**	**-1.8%**	**-2.0%**
Total capital	4.8%	5.0%	5.3%	5.3%	**0.1%**	**-1.5%**	**-2.5%**	**-2.7%**
Memo: Lowest excess capital	4.8%	5.0%	5.3%	5.3%	**0.1%**	**-1.5%**	**-2.5%**	**-2.7%**
Memo: Leverage ratio [1)]	4.5%	4.5%	4.6%	4.6%	3.6%	3.5%	3.3%	3.3%

[1)] Percent of total leverage ratio exposure

Nykredit Realkredit	Actual	Transitional						Memo: Fully loaded
		Base			Stress			Stress
1. Capital	**2020**	**2021**	**2022**	**2023**	**2021**	**2022**	**2023**	**Worst year (2022)**
Common Equity Tier 1	20.2%	20.7%	21.1%	21.4%	16.0%	13.8%	13.9%	13.8%
Tier 1 capital	21.1%	21.6%	22.1%	22.3%	16.8%	14.5%	14.6%	14.5%
Total capital	24.3%	24.8%	25.2%	25.5%	19.7%	17.0%	17.2%	17.0%
2. Capital requirements								
Common Equity Tier 1	10.7%	10.7%	10.7%	10.7%	10.7%	10.7%	10.7%	10.7%
Tier 1 capital	12.7%	12.7%	12.7%	12.7%	12.7%	12.7%	12.7%	12.7%
Total capital	15.5%	15.5%	15.5%	15.5%	15.5%	15.5%	15.5%	15.5%
...of which solvency need	*11.0%*	*11.0%*	*11.0%*	*11.0%*	*11.0%*	*11.0%*	*11.0%*	*11.0%*
3. Excess capital								
Common Equity Tier 1	9.6%	10.0%	10.5%	10.7%	5.3%	3.1%	3.3%	3.1%
Tier 1 capital	8.4%	8.9%	9.3%	9.6%	4.1%	1.8%	1.9%	1.8%
Total capital	8.9%	9.3%	9.8%	10.0%	4.3%	1.6%	1.7%	1.6%
Memo: Lowest excess capital	8.4%	8.9%	9.3%	9.6%	4.1%	1.6%	1.7%	1.6%
Memo: Leverage ratio [1)]	4.8%	5.0%	5.1%	5.1%	4.2%	4.1%	4.2%	4.1%

[1)] Percent of total leverage ratio exposure

Excess capital less than 0.5%
Capital shortfall

Jyske Bank	Actual	Transitional						Memo: Fully loaded
		Base			Stress			Stress
1. Capital	2020	2021	2022	2023	2021	2022	2023	Worst year (2023)
Common Equity Tier 1	17.9%	18.5%	18.7%	18.7%	12.9%	12.1%	11.6%	11.6%
Tier 1 capital	19.9%	20.4%	20.5%	20.5%	14.5%	13.6%	13.1%	13.1%
Total capital	22.9%	23.4%	23.6%	23.6%	17.1%	16.2%	15.7%	15.7%
2. Capital requirements								
Common Equity Tier 1	10.6%	10.6%	10.6%	10.6%	10.6%	10.6%	10.6%	10.6%
Tier 1 capital	12.7%	12.7%	12.7%	12.7%	12.7%	12.7%	12.7%	12.7%
Total capital	15.6%	15.6%	15.6%	15.6%	15.6%	15.6%	15.6%	15.6%
...of which solvency need	*11.6%*	*11.6%*	*11.6%*	*11.6%*	*11.6%*	*11.6%*	*11.6%*	*11.6%*
3. Excess capital								
Common Equity Tier 1	7.4%	7.9%	8.1%	8.2%	2.3%	1.5%	1.1%	1.1%
Tier 1 capital	7.2%	7.6%	7.8%	7.8%	1.8%	0.9%	**0.4%**	**0.4%**
Total capital	7.2%	7.8%	7.9%	7.9%	1.5%	0.5%	**0.1%**	**0.1%**
Memo: Lowest excess capital	7.2%	7.6%	7.8%	7.8%	1.5%	0.5%	**0.1%**	**0.1%**
Memo: Leverage ratio [1)]	5.2%	5.3%	5.4%	5.5%	4.4%	4.3%	4.1%	4.1%

[1)] Percent of total leverage ratio exposure

Sydbank	Actual	Transitional						Memo: Fully loaded
		Base			Stress			Stress
1. Capital	2020	2021	2022	2023	2021	2022	2023	Worst year (2023)
Common Equity Tier 1	18.8%	19.4%	20.0%	20.5%	14.5%	13.4%	12.8%	12.8%
Tier 1 capital	20.4%	20.9%	21.4%	21.9%	15.7%	14.5%	14.0%	14.0%
Total capital	24.0%	24.5%	25.1%	25.6%	18.9%	17.8%	17.2%	17.2%
2. Capital requirements								
Common Equity Tier 1	9.6%	9.6%	9.6%	9.6%	9.6%	9.6%	9.6%	9.6%
Tier 1 capital	11.6%	11.6%	11.6%	11.6%	11.6%	11.6%	11.6%	11.6%
Total capital	14.3%	14.3%	14.3%	14.3%	14.3%	14.3%	14.3%	14.3%
...of which solvency need	*10.8%*	*10.8%*	*10.8%*	*10.8%*	*10.8%*	*10.8%*	*10.8%*	*10.8%*
3. Excess capital								
Common Equity Tier 1	9.3%	9.8%	10.5%	10.9%	4.9%	3.8%	3.2%	3.2%
Tier 1 capital	8.8%	9.3%	9.8%	10.2%	4.1%	2.9%	2.3%	2.3%
Total capital	9.6%	10.2%	10.8%	11.2%	4.6%	3.4%	2.9%	2.9%
Memo: Lowest excess capital	8.8%	9.3%	9.8%	10.2%	4.1%	2.9%	2.3%	2.3%
Memo: Leverage ratio [1)]	6.1%	6.3%	6.4%	6.6%	5.6%	5.2%	5.0%	5.0%

Note: Alm. Brand Bank is fully included in the results for the Sydbank Group at the end of 2020 and in the projection period.

[1)] Percent of total leverage ratio exposure

Excess capital less than 0.5%

Capital shortfall

Table A: Capital issues (net) in the period 1 January 2021 - 30 June 2021, bn. DKK and percentage of total risk exposure amount

Institution	Q1 2021		Q2 2021		Total		
	CET1	AT1/T2	CET1	AT1/T2	CET1	AT1/T2	Percent of total risk exposure amount (worst year)
Danske Bank	0.0	5.6	0.0	1.0	0.0	6.5	0.7
Nykredit Realkredit	0.0	0.7	0.0	-0.7	0.0	0.0	0.0
Jyske Bank	0.0	1.5	0.0	0.7	0.0	2.2	1.0
Sydbank	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Note: Capital issues (net) equals capital issues less capital redemptions carried out during the period.

The worst year refers to the year in the adverse scenario where excess capital is the lowest. For Nykredit Realkredit, this is the end of 2022. For the other institutions, it is the end of 2023.