

Top 100 Banks: Capital Ratios Show Resilience To The Pandemic

September 28, 2021

S&P Global Ratings expects risk-adjusted capital (RAC) ratios for the top 100 banks to remain resilient in the next two years, with some variation across countries. Bank capital around the world held up well during COVID-19, demonstrating the effectiveness of Basel rules for capital and strengthening of bank supervision in the past 10 years. Some banks were able to recognize the bulk of the credit losses last year, lessening the need to continue raising provisions, while others will take longer to do so. As such, pressures on earnings will persist on the latter set of banks, but the impact should be gradual allowing them to recognize losses as revenues recover, supporting their capital ratios. In countries, such as Australia, banks have announced the returning of surplus capital, which has been accumulated during the pandemic, through the sale of non-core businesses.

The RAC ratios of the top 100 rated banks remained broadly stable in 2020 compared with 2019, despite the earnings deterioration due to the rise in loan-loss provisions last year. The average RAC ratio was 9.1% in 2020, equal to the one in the prior year. We believe this is mainly due to the following factors:

- Banks desire to maintain prudent capital buffers to contend with the pandemic;
- Lower dividend payouts, given restrictions put in place by regulators during the pandemic;
- The rise of government-guaranteed loans in banks' portfolios, which require less capital; and
- Credit losses will be spread over a longer time frame in some jurisdictions.

The Basel Committee is now focusing on completing what's already been agreed upon. However, we believe uniform implementation of the rules will be difficult to achieve. The decision to delay their implementation by a year to January 2023, due to the pandemic, was fully justified. But the risk of uneven application of the standards is one of several reasons why we believe investors will have to live with partial comparability of regulatory metrics (see "The Basel Capital Compromise For Banks: Better Buffers, Elusive Comparability," published June 3, 2021).

Nevertheless, the consistency of regulatory capital ratios has improved among banks in Basel III jurisdictions. Still, various levels of national discretion and differences in banks' internal models continue to influence regulatory capital ratios. As a result, our RAC ratios remain the cornerstone of our capital analysis in our bank ratings framework. In our view, our RAC ratios continue to provide a more comparable view of bank capital and stronger risk differentiation, particularly in the current operating environment.

Our list of the top 100 global rated banks is based on their regulatory Tier 1 capital. Starting in 2016, the RAC ratios reflect our revised methodology for assessing the capital adequacy of banks.

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Table 1

Rank		Long-term ICR	SACP	Capital and earnings position	Risk position	Combined impact (capital and earnings and risk position)	2020 actual RAC ratio before diversification	2021 forecasted RAC ratio before diversification	2022 forecasted RAC ratio before diversification
1	Industrial and Commercial Bank of China Ltd.	A	bbb+	Adequate	Adequate	0	8.2%	[7.8%-8.3%]	[7.8%-8.3%]
2	China Construction Bank Corp.	А	bbb+	Adequate	Adequate	0	7.9%	[7.6%-8.1%]	[7.6%-8.1%]
3	Agricultural Bank of China Ltd.	А	bbb+	Adequate	Adequate	0	8.0%	[7.5%-8.0%]	[7.3%-7.8%]
4	Bank of China Ltd.	А	a-	Adequate	Adequate	0	7.7%	[7.4%-7.9%]	[7.3%-7.8%]
5	JPMorgan Chase & Co.*	A+	а	Adequate	Adequate	0	8.6%	[8.5%-9.0%]	[8.5%-9.0%]
6	Bank of America Corp.*	A+	а	Adequate	Strong	+1	10.5%	[10.0%-10.5%]	[10.0%-10.5%]
7	Citigroup Inc.*	A+	a-	Adequate	Adequate	0	8.4%	[8.5%-9.0%]	[8.5%-9.0%]
8	HSBC Holdings PLC*	A+	а	Adequate	Strong	+1	9.8%	[9.5%-10.0%]	[9.5%-10.0%]
9	Wells Fargo & Co.*	A+	a-	Adequate	Adequate	0	8.7%	[8.0%-8.5%]	[8.0%-8.5%]
10	Mitsubishi UFJ Financial Group, Inc.*†	A	а	Adequate	Adequate	0	7.3%	[7.25%-7.75%]	[7.25%-7.75%]
11	Bank of Communications Co. Ltd.	A-	bbb-	Adequate	Adequate	0	7.3%	[7.1%-7.6%]	[7.0%-7.5%]
12	Credit Agricole Group	A+	а	Adequate	Strong	+1	8.9%	[9.0%-9.5%]	[9.0%-9.5%]
13	BNP Paribas	A+	а	Adequate	Adequate	0	7.4%	[7.0%-7.5%]	[7.25%-7.75%]
14	China Merchants Bank Co. Ltd.	BBB+	bbb	Moderate	Strong	+1	6.2%	[5.9%-6.4%]	[5.5%-6.0%]
15	Postal Savings Bank of China Co. Ltd.	A	bbb	Moderate	Adequate	0	6.8%	[6.2%-6.7%]	[6.0%-6.5%]
16	Sumitomo Mitsui Financial Group Inc.*†	A	а	Adequate	Adequate	0	7.6%	[7.3%-7.8%]	[7.3%-7.8%]
17	Shanghai Pudong Development Bank Co. Ltd.	BBB	bb	Weak	Adequate	-1	4.6%	[4.0%-4.5%]	[4.0%-4.5%]
18	Banco Santander S.A.	А	а	Adequate	Strong	+1	7.7%	[7.7%-8.1%]	[7.9%-8.3%]

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19	The Goldman Sachs Group Inc.*	A+	bbb+	Adequate	Moderate	-1	10.6%	[10.0%-10.5%]	[10.0%-10.5%]
20	Morgan Stanley*	A+	a-	Strong	Moderate	0	13.0%	[11.0%-11.5%]	[11.0%-11.5%]
21	Mizuho Financial Group Inc.*†	А	а	Adequate	Adequate	0	6.6%	[6.75%-7.25%]	[7.0%-7.5%]
22	BPCE	А	a-	Strong	Adequate	+1	9.8%	[9.5%-10.0%]	[9.75%-10.25%]
23	China CITIC Bank Corp. Ltd.	BBB+	bb	Weak	Adequate	-1	4.9%	[5.0%-5.5%]	[4.5%-5.0%]
24	Norinchukin Bank†	Α	bbb+	Adequate	Moderate	-1	11.3%	[10.5%-11.0%]	[9.5%-10.0%]
25	China Minsheng Banking Corp. Ltd.	BBB-	bb	Weak	Adequate	-1	5.6%	[5.2%-5.7%]	[4.5%-5.0%]
26	Japan Post Bank Co., Ltd.†	А	bbb+	Adequate	Moderate	-1	9.6%	[8.5%-9.0%]	[8.2%-8.7%]
27	Barclays PLC*	А	bbb+	Strong	Moderate	0	11.0%	[10.75%-11.25%]	[10.75%-11.25%]
28	UniCredit SpA‡	BBB	bbb	Adequate	Moderate	-1	8.3%	[7.9%-8.4%]	[7.9%-8.4%]
29	China Everbright Bank Co. Ltd.	BBB+	bb+	Moderate	Adequate	0	5.2%	[5.0%-5.5%]	[5.0%-5.5%]
30	Intesa Sanpaolo SpA	BBB	bbb	Moderate	Strong	0	6.1%	[5.9%-6.4%]	[5.9%-6.4%]
31	Credit Mutuel Group	А	а	Strong	Adequate	+1	10.1%	[9.75%-10.25%]	[10.0%-10,5%]
32	ING Groep N.V.*	A+	а	Strong	Adequate	+1	10.8%	[10.3%-10.8%]	[10.5%-11.0%]
33	Deutsche Bank AG	BBB+	bbb	Adequate	Moderate	-1	9.4%	[8.8%-9.3%]	[8.9%-9.4%]
34	Banco Bilbao Vizcaya Argentaria S.A.	A-	a-	Adequate	Strong	+1	8.2%	[8.9%-9.4%]	[8.9%-9.4%]
35	Credit Suisse Group AG*	A+	a+	Strong	Moderate	0	12.4%	[12.4%-12.9%]	[12.6%-13.1%]
36	Societe Generale	А	bbb+	Adequate	Adequate	0	9.0%	[9.0%-9.5%]	[9.0%-9.5%]
37	UBS Group AG*	A+	а	Strong	Moderate	0	14.1%	[13.5%-14.0%]	[13.0%-13.5%]
38	Royal Bank of Canada†	AA-	a+	Adequate	Strong	+1	9.2%	[9.0%-9.5%]	[9.0%-9.5%]
39	Lloyds Banking Group PLC*	A+	a-	Adequate	Adequate	0	8.7%	[8.75%-9.25%]	[8.5%-9.0%]
40	Ping An Bank Co. Ltd.	BBB+	bb	Weak	Adequate	-1	5.5%	[5.0%-5.5%]	[5.0%-5.5%]

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41	Toronto-Dominion Bank†	AA-	a+	Adequate	Strong	+1	8.8%	[8.5%-9.0%]	[8.5%-9.0%]
42	NatWest Group plc*	А	bbb+	Adequate	Adequate	0	10.7%	[10.0%-10.5%]	[9.5%-10.0%]
43	Cooperatieve Rabobank U.A.	A+	а	Strong	Adequate	+1	10.4%	[10.5%-11.0%]	[10.55%-11.05%]
44	Truist Financial Corp*	А	а	Adequate	Strong	+1	8.8%	[7.9%-8.4%]	[8.5%-9.0%]
45	Capital One Financial Corp.*	BBB+	bbb+	Adequate	Adequate	0	9.3%	[9.0%-9.5%]	[9.5%-10.0%]
46	U.S. Bancorp*	AA-	a+	Adequate	Strong	+1	8.8%	[8.5%-9.0%]	[9.5%-10.0%]
47	Standard Chartered PLC*	А	A-	Adequate	Adequate	0	9.3%	[9.0%-9.5%]	[9.0%-9.5%]
48	Commonwealth Bank of Australia†	AA-	а	Strong	Adequate	+1	12.8%	[13.15%-13.65%]	[11.65%-12.15%]
49	Hua Xia Bank Co. Ltd.	BBB-	bb	Moderate	Moderate	-1	5.3%	[5.4%-5.9%]	[5.0%-5.5%]
50	PNC Financial Services Group*	А	а	Adequate	Strong	+1	10.4%	[8.5%-9.0%]	[8.5%-9.0%]
51	Westpac Banking Corp.†	AA-	а	Strong	Adequate	+1	12.6%	[12.55%-13.05%]	[11.35%-11.85%]
52	Bank of Nova Scotia†	A+	а	Adequate	Strong	+1	7.9%	[8.0%-8.5%]	[8.0%-8.5%]
53	Australia and New Zealand Banking Group Ltd.†	AA-	а	Strong	Adequate	+1	11.4%	[10.8%-11.3%]	[10.6%-11.1%]
54	National Australia Bank Ltd.†	AA-	а	Strong	Adequate	+1	11.2%	[10.8%-11.3%]	[10.6%-11.1%]
55	State Bank of India†	BBB-	bbb-	Moderate	Moderate	-1	5.0%	[5.0%-5.5%]	[5.0%-5.5%]
56	DBS Bank Ltd.	AA-	а	Adequate	Adequate	0	8.5%	[8.0%-8.5%]	[8.0%-8.5%]
57	Bank of Montreal†	A+	а	Adequate	Strong	+1	8.4%	[8.5%-9.0%]	[8.5%-9.0%]
58	Shinhan Bank	A+	a-	Adequate	Adeqaute	0	7.9%	[7.9%-8.4%]	[7.9%-8.4%]
59	Korea Development Bank	AA	bb-	Moderate	Weak	-3	4.9%	[5.2%-5.7%]	[5.2%-5.7%]
60	China Guangfa Bank Co. Ltd.	BBB-	bb	Moderate	Moderate	-1	5.4%	[5.0%-5.5%]	[5.0%-5.5%]

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61	Commerzbank AG	BBB+	bbb	Adequate	Adequate	0	9.6%	[9.0%-9.5%]	[9.2%-9.7%]
62	Development Bank of Japan Inc.†	А	bbb	Strong	Moderate	0	11.3%	[10.5%-11.0%]	[10.25%-10.75%]
63	Nordea Bank Abp	AA-	a+	Strong	Adequate	+1	12.8%	[12.75%-13.25%]	[12.0%-12.6%]
64	HDFC Bank Ltd.†	BBB-	bbb+	Adequate	Strong	+1	9.5%	[9.0%-9.5%]	[9.0%-9.5%]
65	Banco Nacional de Desenvolvimento Economico e Social	BB-	bbb-	Adequate	Strong	+1	7.4%	[8.0%-8.5%]	[8.0%-8.5%]
66	CaixaBank S.A.	BBB+	bbb+	Adequate	Adequate	0	7.6%	[7.0%-7.5%]	[7.25%-7.75%]
67	United Overseas Bank Ltd.	AA-	а	Adequate	Adequate	0	7.9%	[7.5%-8.0%]	[7.5%-8.0%]
68	Itau Unibanco Holding S.A.	BB-	bbb	Moderate	Adequate	0	5.6%	[5.5%-6.0%]	[5.5%-6.0%]
69	Danske Bank A/S	А	a-	Strong	Moderate	0	11.9%	[11.6%-12.2%]	[11.6%-12.2%]
70	ABN AMRO Bank N.V.	А	bbb+	Strong	Adequate	+1	13.6%	[14.0%-14.5%]	[14.2%-14.7%]
71	Bank of New York Mellon Corp.*	AA-	a+	Adequate	Strong	+1	9.8%	[8.0%-8.5%]	[9.0%-9.5%]
72	Canadian Imperial Bank of Commerce†	A+	a-	Adequate	Adequate	0	8.5%	[8.5%-9.0%]	[8.5%-9.0%]
73	Oversea-Chinese Banking Corp. Ltd.	AA-	а	Adequate	Adequate	0	8.6%	[8.0%-8.5%]	[8.0%-8.5%]
74	Nomura Holdings Inc.*†	Α-	bbb	Strong	Moderate	0	14.3%	[13.5%-14.5%]	[13.5%-14.5%]
75	Banco do Brasil S.A.	BB-	bbb	Moderate	Adequate	0	6.0%	[5.7%-6.3%]	[5.7%-6.3%]
76	Kookmin Bank	A+	a-	Adequate	Adequate	0	8.2%	[8.3%-8.8%]	[8.3%-8.8%]
77	Sumitomo Mitsui Trust Holdings*†	А	a-	Adequate	Adequate	0	6.7%	[7.0%-7.5%]	[7.25%-7.75%]
78	Qatar National Bank (Q.P.S.C.)	А	bbb	Adequate	Adequate	0	9.3%	[9.5%-9.7%]	[9.5%-9.7%]
79	Erste Group Bank AG	Α	а	Adequate	Adequate	0	10.2%	[9.8%-10.3%]	[9.6%-10.1%]
80	KBC Group N.V.*	A+	а	Strong	Adequate	+1	12.1%	[11.6%-12.1%]	[11.5%-12.0%]
81	KEB Hana Bank	A+	a-	Adequate	Adequate	0	8.3%	[8.0%-8.5%]	[8.0%-8.5%]

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82	Banco Bradesco S.A.	BB-	bbb-	Weak	Adequate	-1	4.0%	[4.0%-4.5%]	[4.5%-5.0%]
83	DNB Bank ASA	AA-	a+	Strong	Adequate	+1	14.2%	[13.9%-14.6%]	[14.0%-14.7%]
84	Industrial Bank of Korea	AA-	bbb+	Adequate	Adequate	0	9.6%	[9.4%-9.9%]	[9.4%-9.9%]
85	Saudi National Bank	A-	a-	Strong	Adequate	+1	10.6%	[11.0%-11.5%]	[11.25%-11.75%]
86	VTB Bank JSC	BBB-	bb-	Weak	Adeqaute	-1	4.1%	[4.1%-4.6%]	[4.2%-4.7%]
87	Raiffeisen Schweiz Genossenschaft	A+	a+	Very Strong	Adequate	+2	22.3%	[23.0%-23.5%]	[23.5%-24.0%]
88	First Abu Dhabi Bank¶	AA-	a-	Strong	Strong	+2	12.1%	[11.5%-12.0%]	[11.5%-12.0%]
89	ICICI Bank Ltd.†	BBB-	bbb-	Strong	Moderate	0	10.1%	[10.0%-10.5%]	[10.0%-10.5%]
90	Federation des caisses Desjardins du Quebec†	A+	а	Strong	Adequate	+1	14.2%	[14.5%-15.0%]	[14.5%-15.0%]
91	American Express Co.*	Α-	a-	Adequate	Strong	+1	6.6%	[6.5%-7.0%]	[6.5%-7.0%]
92	China Zheshang Bank Co. Ltd.	BBB-	bb	Weak	Adequate	-1	3.8%	[3.6%-4.1%]	[3.7%-4.2%]
93	Skandinaviska Enskilda Banken AB (publ)	A+	а	Strong	Adequate	+1	11.5%	[11.2%-11.7%]	[11.0%-11.5%]
94	Svenska Handelsbanken AB	AA-	a+	Strong	Adequate	+1	12.5%	[12.25%-12.75%]	[12.0%-12.5%]
95	Nationwide Building Society	А	a-	Strong	Adequate	+1	11.8%	[12.0%-12.5%]	[12.25%-12.75%]
96	La Banque Postale	А	bbb+	Adequate	Moderate	-1	7.5%	[7.5%-8.0%]	[7.5%-8.0%]
97	Resona Bank Ltd.†	А	a-	Adequate	Adequate	0	8.0%	[7.25%-7.75%]	[7.25%-7.75%]
98	Woori Bank	A+	a-	Adequate	Adequate	0	7.7%	[7.7%-8.2%]	[7.7%-8.2%]
99	Ally Financial Inc.	BBB-	bbb	Adequate	Adequate	0	8.8%	[8.5%-9.0%]	[8.5%-9.0%]
100	State Street Corp.*	AA-	a+	Adequate	Strong	+1	9.2%	[8.0%-8.5%]	[8.0%-8.5%]

Table 1

					Combined			
					impact			
					(capital			
		Group	Capital		and	2020 actual		
		SACP	and		earnings	RAC ratio	2021 forecasted	2022 forecasted
	Long-term	or	earnings	Risk	and risk	before	RAC ratio before	RAC ratio before
Rank	ICR	SACP	position	position	position)	diversification	diversification	diversification

Note: The ranking is based on Tier 1 Capital as of December 2020. All RAC ratios are calculated at the group level. The RAC forecasts for Chinese banks incorporate loan-like off B/S wealth management products. *Holding company; the rating reflects that of the main operating company. † RAC ratio for the Indian banks (March 2021), Japanese banks (September 2020), Australian banks (March 2021 except for Commonwealth Bank of Australia and National Australia Bank Ltd, for which we are using the December 2020 and September 2020 data respectively), Canadian banks (October 2020), Nationwide Building Society (RAC ratio as of April 2021), ‡ Estimate, ¶First Abu Dhabi Bank, RAC is based on the merged entity.

Key Takeaways

- We expect RAC ratios to remain relatively stable, reflecting a gradual recognition of credit losses globally, except in some regions such as North America and Brazil, where the bulk of credit losses have already been recognized and Australia where banks are returning excess capital. Among European banks, RAC ratios may fall moderately this year, not at least as banks restart distributions to shareholders, but even then RAC ratios may well remain above the end of 2019 levels for many banks.
- As the economic recovery gains momentum, government support is starting to unwind, so far in an orderly manner. Banks remain in a broadly comfortable position to absorb future losses through earnings, rather than capital.
- The RAC ratios for 69 of the top 100 banks have remained stable or shifted less than 5 basis points (bps) as of the end of 2020 compared with 2019. For 18 banks, the RAC improved by more than 5 bps, while the ratio for 13 others has weakened by more than 5 bps.
- The gap between our RAC ratios and regulatory Tier 1 ratios persists, mainly reflecting the various levels of national regulatory discretion, the use of internal models, and the sensitivity of RAC ratios to weaker economies.

S&P's RAC Ratios Continue To Provide Strong Risk Differentiation

Regional differences in the RAC ratios among the world's top 100 rated banks persist (see chart 1). Banks in Switzerland, the Nordic countries, and Australia have the strongest capital ratios; while the weakest ratios among the top 100 banks remain in Brazil, China, and Spain. This is mostly due to these countries' weaker economies, resulting in higher risk weights on domestic banks' assets than those of their peers in the sample. Although Spain's economic growth had been improving until the pandemic-related shock, the country's economy was severely damaged during the 2008 financial crisis and has yet to fully recover from it.

We base the risk weights we apply to banks' exposures on our assessment of each country's economic risk, a component of our Banking Industry Country Risk Assessment (BICRA), and on the

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risk weights applied to sovereign exposures, which are based on the sovereign ratings. The higher the risk, the higher the risk weights, which result in weaker ratios, while all other credit fundamental remain unchanged. Consequently, changes in our view of a country's economic conditions result in changes in the domestic banks' RAC ratios.

We saw the rise in economic risk in France, Germany, and United Arab Emirates in the past 12 months, which partly explains the erosion in respective banks' 2021 forecasts.

We see significant variations in RAC ratios in some regions, which is why we present a range of minimum and maximum ratios across regions in chart 1. Those among Japanese and North American banks were the widest.

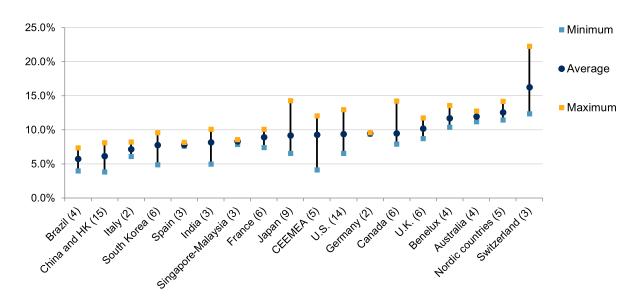
Rating Methodology

In this article, we include the world's top 100 rated banks ranked based on their regulatory Tier 1 capital. We're mindful, however, that the top 100 banks in this survey--across 26 countries--may not always be fully representative of the jurisdictions where these banks are domiciled, given that other banks in those countries aren't within the top 100, and some banking sectors are more concentrated than others. Within the sample, banks in some regions account for a more significant portion of domestic financial systems' assets than in others.

Some large players also have geographically diversified profiles, and their RAC ratios incorporate wider risk diversity than purely domestic-focused institutions.

Chart 1

The 2020 RAC Ratios For The World's Top 100 Rated Banks, By Country



Note: Numbers in brackets represent the number of banks in that country/region in the sample. Copyright © 2021 by Standard & Poor's Financial Services LLC. All rights reserved.

We Expect RAC Ratios To Broadly Stabilize After Years Of Buildup

Our survey indicates that the RAC ratios for 69 of the top 100 banks have remained stable or shifted less than 5 bps as of the end of 2020 compared with 2019. For 18 banks, the RAC improved by more than 5 bps, while the ratio for 13 others has weakened by more than 5 bps.

We expect RAC ratios to remain relatively stable for the next two years, because we expect lending growth to be relatively modest over the same period, while provisioning needs moderate from their peak last year, allowing profitability to gradually recover. We expect the economic recovery on the back of unprecedented government support, less need for restrictions to control the virus while the vaccination pace ramps up to help limit the residual risk inflicted by the pandemic on banks' asset quality.

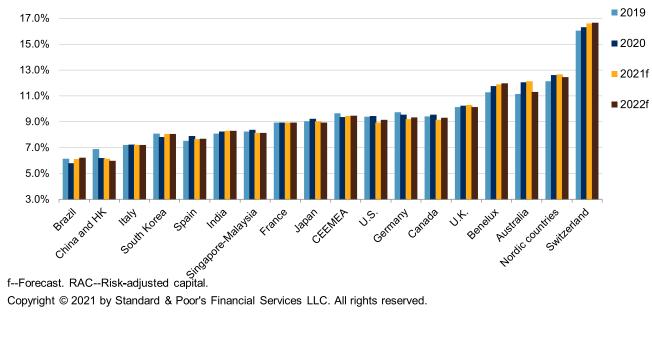
Given the pandemic's harsh economic impact, NPAs could still increase in the coming months in some jurisdictions, particularly in sectors most affected by lockdowns and the changes in customer consumption patterns, but the extraordinary loan-loss provisions that banks raised in 2020 should contain future credit losses.

Nevertheless, we forecast the RAC ratios for Australia's four major banks to be lower in 2022. The lower RAC ratios reflect the Australian major banks returning excess capital to shareholders. Already three of the four major banks have announced buybacks. These buybacks reflect the sale of non-core businesses, a buildup of capital during the pandemic followed by the relaxation of pandemic-related regulatory restrictions, and greater clarity in the Australian Prudential Regulation Authority's new capital framework.

Chart 2

RAC Ratios For The World's Top 100 Rated Banks

Trend by country or region



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Capital Strength Impact

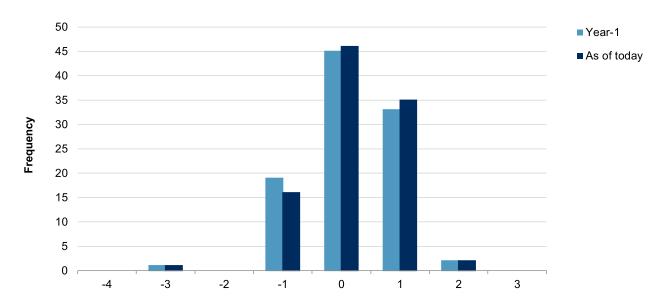
Similar to what we saw in our previous surveys, the capital strength impact on stand-alone credit profiles (SACPs) of the world's top 100 rated banks ranges from minus 3 notches to plus 2 notches (see chart 3 and refer to appendix for further clarification). The capital strength impact is neutral or positive to the SACPs of 80 banks in our current review, the same trend as in our last survey.

The current distribution of the combined impact remains significantly stronger than six years ago, when only 67 banks had a neutral or positive impact, and reflects the capital buildup among the top 100 banks during that period.

Additionally, we now consider capital adequacy (capital combined with risk position) a ratings strength for 37 of the top 100 banks, up from 35 last year and 21 six years ago. Any expected improvements or deteriorations in RAC ratios are already captured in this combined assessment because we base the capital assessment on our capital projections, rather than actual values, and we have incorporated the expected improvements for the next two years.

Chart 3

Capital Strength Impact On SACP For The World's Top 100 Rated Banks



Notching impact combining capital and risk positions. SACP--Stand-alone credit profile. Copyright © 2021 by Standard & Poor's Financial Services LLC. All rights reserved.

Our RAC Ratios Provide Stronger Risk Differentiation Than Regulatory **Tier 1 Ratios**

Our RAC ratios continue to be typically lower than regulatory Tier 1 ratios, reflecting the various levels of national discretion on regulatory ratios and differences in banks' internal models that still influence regulatory ratios to a large extent. However, some of the features in the Basel III framework, which regulators around the world are currently implementing, help diminish the gap, given that these features were already part of our capital methodology. For example, we've deducted tax loss carry forward and goodwill from our measure of TAC since we introduced our RAC framework in 2010.

We continue to observe the widest difference between the RAC and regulatory ratios for banks in countries whose sovereign ratings and economic risk scores are lower, reflecting the higher charges we apply to their exposures versus regulatory risk weights (see chart 4). That includes the risk weights we apply to sovereign exposures, which we base on our sovereign ratings, versus the risk weights applied by the regulators, which are subject to national discretion and usually very low or nonexistent. The biggest gap between the two metrics remains among banks in Brazil, the U.K., and Italy, as we observed in our previous surveys. The large gap among Brazilian and Italian banks is mainly due to both countries' weaker economic risk score; the higher risk weights we apply to deferred tax assets (DTAs) because of temporary differences from what the regulator applies; and the relatively higher risk weights we apply to the sovereign exposures based on our sovereign rating, while the regulator applies no risk weight. Moreover, Brazil's average Tier 1 capital ratio is relatively high due to BNDES that as of December 2020 had a Tier 1 ratio of 31.2%.

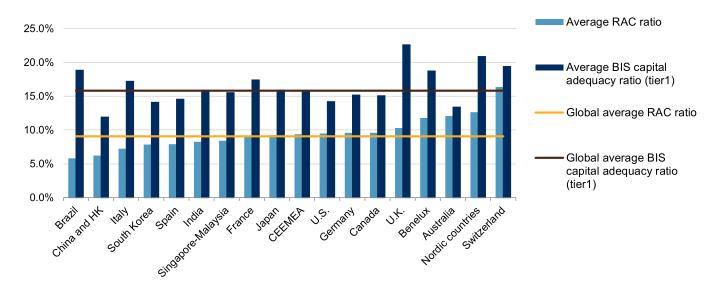
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Under our RAC methodology, the bank's large equity and investment portfolio in government-owned and private companies have significantly higher risk weights, which weakens BNDES' RAC ratio. In contrast, the gap in some other countries results from the extensive use of internal models. Internal models tend to produce lower risk weights than the standardized approach and what our core RAC assumptions indicate. For example, this is the case for banks in the U.K., France, and the Benelux and Nordic countries that have large gaps, because although their economic risk is stronger, the banks have insurance operations and use internal models.

The gap between our RAC ratio and regulatory ratios is the smallest in Australia. This reflects the domestic regulator's conservative settings in its prudential capital framework and include higher loss given default floors for residential mortgages floors, a more punitive approach towards equity investments, capital requirements for interest rate risk in the banking book, etc.

Chart 4

The 2020 RAC Ratio And BIS Capital Adequacy Ratio (Tier 1) For The World's Top 100 Rated Banks



RAC--Risk-adjusted capital. BIS--Bank for international settlements.

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Appendix: The Capital Strength Impact On Banks' SACPs

To evaluate a bank's capital strength, we primarily look at capital and earnings and the risk position. These two factors are part of the four components of our rating analysis of banks. We assess these factors on a six-point scale: very weak, weak, moderate, adequate, strong, and very strong. The assessment of the risk position incorporates other factors not captured in our RAC ratios, such as differences in underwriting standards across banks and their credit losses.

In general, as long as the banks' anchor SACP--derived from our BICRA methodology--is investment-grade, an adequate assessment is neutral to a bank's SACP. All else being equal, a moderate assessment would lower the SACP by one notch, a weak assessment by two or three

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notches, and a very weak one by five notches. On the other hand, a strong assessment would raise the SACP by one notch, and the very strong one by two notches.

Related Criteria

- Guidance: Applying The Risk-Adjusted Capital Framework Methodology, Sept. 13, 2018
- General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011

Related Research

- Banking Country Outlook Midyear 2021: Tantalizing Signs Of Stability, July 22, 2021
- Global Banks Outlook Midyear 2021: Clawing Back To Normalcy, July 22, 2021
- Updated Bank Credit Loss Forecasts Show A Little More Clarity, A Little Less Gloom Global, July
- The Basel Capital Compromise For Banks: Better Buffers, Elusive Comparability, June 3, 2021
- Bank Regulatory Buffers Face Their First Usability Test, June 11, 2020

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