FINANSTILSYNET

MEMORANDUM

Finanstilsynet
(The Danish Financial Supervisory Authority)

2 March 2015

Report on review of new loans, etc. at Jyske Bank A/S

Introduction

The Danish Financial Supervisory Authority conducted a review of new loans, etc. at Jyske Bank A/S. The objective was to assess the bank's risk tolerance in connection with new loans, etc. and assess the basis on which the bank authorised new loans. The inspection took place in the fourth quarter of 2014.

The review formed part of a general inspection reviewing the same theme in 13 other financial institutions. The background is that the FSA has established that the low demand on the part of trade and industry as well as households for loans has, in combination with the financial institutions' improved capital structure and funding conditions, increased competition. Basically, this is a positive situation, but it may also entail a risk that credit standards in connection with new loans will be lowered, for instance in such a way that clients' own financing, pledges, mortgages and guarantees are reduced to such an extent that will materially increase the risk assumed by financial institutions.

Summary and risk assessment

The FSA had selected 125 of the bank's authorisations of loans over the period July 2013 to June 2014. These included loans to large, medium-sized and small business enterprises as well as the financing of rental properties and the financing of acquisitions. Moreover, the FSA reviewed the bank's credit policy and selected business procedures.

Before loans are authorised, the bank prepares a recommendation describing the purpose of the loan, the client's financial situation, the collateral provided and the risks associated with the client. The FSA assessed that generally the quality of the bank's recommendations was satisfactory. However, in some areas, other major banks conduct more comprehensive analyses of risks. This is for instance the case in connection with loan applications relating to rental properties, where in some instances Jyske Bank had not adjusted the value of properties to realistic market values.

Moreover, the FSA found that the bank's risk tolerance was generally in line with that of other major banks and hence also affected by increasing competition, particularly for financially strong corporate clients. Hence there were some examples that competition with other banks had caused Jyske Bank to ease its terms and conditions, for instance, by lowering the interest rate that the client paid and in a few cases by not demanding guarantees.

The bank's pricing of loans, except for loans to large corporate clients, seems to be at the low end relative to other major banks. The difference between the prices the bank charged clients' with a good financial situation and those the bank charged clients with a less favourable or poor financial situation was smaller than the difference seen at other major banks. Generally the bank's requirements as to collateral, guarantees, etc. were in line with those of other major banks.

The bank's activities in respect of financing of acquisitions are still limited, even though the level of activity has increased in recent years. The FSA has informed Jyske Bank that if the bank intends to increase its financing of acquisitions to any considerable extent or if it increases the risk profile in such cases, the bank must be aware that competences and resources must be adjusted to this.

Especially in connection with major banks' financing of acquisitions, the FSA has generally seen increasing growth, risk tolerance and competition, which development has resulted in more relaxed credit terms and conditions.

Therefore Jyske Bank must be aware of the risk of financing acquisitions at too high prices and with too high debt ratios.

The supervisory board of a financial institution must adopt a credit policy, from which the financial institution's credit risk profile must appear. Authorisation of loans must take place according to the credit policy. The FSA established that in various areas Jyske Bank's credit policy was too vague or inadequate, for instance in regard to risk classification of clients, concentration risk and reporting to the supervisory board. The supervisory board had therefore not considered the desired credit risk profile. Hence there was a risk that in some areas the bank would authorise loans involving a risk that was not wanted by the supervisory board. Therefore the bank was ordered to make the necessary changes to its credit policy.

As at 30 September 2014, the Jyske Bank Group stated its solvency requirement at 10.7 per cent. The actual solvency ratio as at 30 September 2014 was 16.7 per cent. The inspection did not give rise to any changes in the FSA’s assessment of the group’s solvency requirement.