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Recommendation of the Bank of Italy on dividend distribution and variable remuneration policies of banks, which repeals the Recommendation of 16 December 2020

In 2020, the Bank of Italy issued three Recommendations ([1]) addressed to the less significant banks subject to its supervision, which recommended to adopt restrictive policies on dividend distribution and variable remuneration. Their objectives were to strengthen banks' own funds through internal capital generation and to better prepare the financial system to absorb losses that might arise as a result of the health emergency associated with the pandemic, thereby enabling it to continue to support the economy. The banks were therefore invited not to pay dividends and to refrain from carrying out share buy-backs. The importance of adopting a prudent and farsighted approach in their variable remuneration policies was also underlined.

The policies were in line with the recommendations of the European Systemic Risk Board (ESRB) to the competent authorities and those of the European Central Bank to significant banks under the Single Supervisory Mechanism.

Specifically, in its Recommendation of December 2020, the Bank of Italy continued to ask banks to maintain a prudent approach, although it allowed less significant banks to make a limited distribution of dividends. This recommendation also stressed that, in the absence of a substantial worsening of the macroeconomic situation, as of 30 September 2021, the Bank of Italy would return to assessing dividend distribution and variable remuneration policies based on the regular supervisory review and evaluation process (SREP) for banks.

The most recent macroeconomic projections point to an improvement in the economy. This will make it possible, in line with the ECB's decision for significant banks, to return to using the ordinary SREP criteria for assessing banks' capital and their dividend distribution and share buy-back plans. Less significant banks must therefore continue to take a prudent approach in deciding on their dividend distribution and share buy-back policies, carefully considering the sustainability of their business models. They should also not underestimate the risk that, once the support measures introduced to address the COVID-19 pandemic are expired, additional losses may have an impact on their capital trajectories.

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[1] Issued respectively on 27 March 2020 (which expired on 1 October 2020) (https://www.bancaditalia.it/media/comunicati/documenti/2020-01/cs-dividend-policy-reccomendation.pdf?language_id=1), 28 July (which expired on 1 January 2021) (https://www.bancaditalia.it/media/comunicati/documenti/2020-02/CS_Raccomandazione_politiche_dividendi_ENG.pdf?language_id=1) and 16 December 2020 (expiring on 30 September 2021) (https://www.bancaditalia.it/media/comunicati/documenti/2020-02/Recommendation-of-the-Bank-of-Italy-on-the-dividend-distribution-and-variable-remuneration-policies-of-banks-16122020.pdf?language_id=1).

In performing its assessments, the Bank of Italy will take a forward-looking approach, also taking into consideration whether the banks' provisioning policies to address credit risk are suitable, as they may impact the banks' capital generation capacity. These elements will be the subject of discussion with the banks as part of regular supervisory dialogue.

The Bank of Italy also recommends less significant banks to continue to adopt a prudent and farsighted approach when deciding on remuneration policies, which will be evaluated as part of the SREP and will take into account the possible impact on the banks' ability to maintain a sound capital base.

The previous Recommendation on dividends and remuneration policies remains applicable until 30 September 2021, meaning the next decisions to pay dividends should take place in the fourth quarter of 2021.

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