Some banks have strengthened their links to domestic sovereigns ... ... which together could create losses for banks.

Higher buffers have left most banks better prepared for shocks ... ... but in an adverse downside scenario, capital ratios would come under more pressure.

Sources: Banca IFIS; Bloomberg Finance L.P.; European Banking Authority; Haver Analytics; national central banks; PriceWaterhouseCoopers; SNL Financial; and IMF staff analysis.

Note: Panel 1 is based on banking system data, while panels 2–6 are based on the sample of banks in the European Banking Authority transparency exercise (EBA banks). Panel 5 (6) shows the impact of the mild (severe) downside scenario for changes in government bond yields and the moderate (adverse) scenario for the loan loss adjustment. Positive values for the loan loss adjustment and mark-to-market impact in panels 5 and 6 represent a fall in the capital ratio; negative values represent an increase in the capital ratio. The capital ratios include the impact of reductions in risk-weighted assets related to the disposal of unsecured nonperforming loans, which can in some cases result in a negative number (an improvement in the capital ratio) for the impact of the loan loss adjustment; see Online Annex 1.1 for more details. Data labels in the figure use International Organization for Standardization (ISO) country codes.