SYSTEMATIC AND SYSTEMIC STRESS TESTS

Martin Summer
Head of Economic Studies Division, Oesterreichische Nationalbank

Abstract
For a given bank portfolio, which economic and financial scenarios will lead to big losses? How big can losses in such scenarios possibly get? These are the two central questions of a stress test. We believe that most current stress testing models have problems in answering these questions. They select stress scenarios in a way which might leave aside many dangerous scenarios and thus create an illusion of safety; and which might consider highly implausible scenarios and thus trigger a false alarm. With respect to loss evaluation most stress tests do not include tools to analyze systemic risk. We make a conceptual proposal how these shortcomings may be addressed and how stress tests could be made both systematic and systemic. We demonstrate the application of our concepts using publicly available data on European banks and capital markets.