

---

## Commentary

# European Banks' AT1 Instruments at a Crossroads: Regulatory Reassessment and Market Implications

---

Morningstar DBRS

11 March 2026

### Key Highlights

- One of the ECB's recommendations reopens the debate about the effectiveness of AT1 instruments as going concern capital, with options ranging from redesign to full removal.
- We do not expect an immediate credit rating impact, as policy direction and implementation remain uncertain and will unfold over several years.
- AT1 demand remains solid; however, market conditions have become more challenging amid the escalation of geopolitical tensions in the Middle East.

Nicola De Caro  
Senior Vice President, Sector Lead  
European Financial Institution Ratings  
+49 69 8088 3505  
nicola.decaro@morningstar.com

Marcos Alvarez  
Managing Director  
Global Financial Institution Ratings  
+34 919 036 529  
marcos.alvarez@morningstar.com

### Overview

This commentary assesses the ECB's December 2025 recommendations within the broader policy debate on the effectiveness of Additional Tier 1 (AT1) instruments as going-concern capital. While the ECB's recommendation provides limited details, its stance points to two potential pathways: a structural redesign of AT1 instruments or complete removal from the going-concern capital stack. At this stage, we do not anticipate immediate implications for our AT1 credit ratings or for our rating approach to AT1, Tier 2, or senior instruments. The impact remains uncertain and will depend on the final policy design and its implementation. The approval process and implementation may take several years, potentially with grandfathering for outstanding instruments, and could face political resistance; meanwhile, other jurisdictions—such as Australia—have already opted to eliminate AT1 instruments.

The EU AT1 market has remained stable since the ECB's announcement, and early-year issuances have attracted strong investor demand. This resilience may reflect the long-term nature of the policy process, as well as continued investor appetite for bank capital instruments—particularly from large, well-capitalised institutions that have strengthened their profitability, risk profile, and capital position in recent years. However, in recent days the escalation of the Iran conflict has increased cross-asset volatility, widening European bank credit spreads, AT1s included, as investors reassessed geopolitical and inflation risks, and the implications for central banks' policy paths.

Overall, we view regulatory efforts to simplify the prudential framework positively, insofar as they enhance transparency, efficiency, and market functioning while supporting investor confidence and financial stability. We will continue to monitor developments closely, given the material size of the AT1 market in the EU and the potentially significant implications of any structural changes to the regime.

### The ECB Recommendations: AT1s and Beyond

The ECB's High-Level Task Force on Simplification noted in Recommendation #2 published in December 2025 that the going-concern loss-absorbing capacity of the capital stack could be strengthened by reassessing the design and role of AT1 and Tier 2 instruments. The recommendation outlines two strategic pathways: either enhancing AT1 instruments' features to ensure more reliable and transparent loss absorption in going-concern conditions or removing non-CET1 instruments altogether—whether by replacing them with CET1 or eliminating them without substitution.

More broadly, this recommendation sits within a wider simplification agenda that seeks to streamline the EU's prudential framework by reducing capital-stack and leverage-ratio complexity, expanding proportional regimes, harmonising macroprudential tools, aligning minimum requirements for own funds and eligible liabilities and total loss-absorbing capacity, and simplifying stress testing and reporting requirements across authorities. Importantly, these EU efforts unfold at a time when other jurisdictions—most notably the U.S.—are also moving towards simpler or lighter regulatory frameworks. This shift has direct implications for the relative competitiveness of EU banks, as regulatory complexity and compliance costs can widen structural divergences between EU and U.S. institutions in terms of capital efficiency, profitability, and market positioning.

### **AT1 as a Going Concern Capital Instrument: Operational Challenges**

AT1 instruments, while designed to be going-concern capital capable of absorbing losses through conversion or write-down, have shown certain functional and operational limitations. The 2023 Credit Suisse AG case—occurring outside the EU—represents the only major instance where AT1 instruments absorbed losses ahead of CET1 and outside a formal resolution process. This case created uncertainties, triggered legal challenges, and underscored doubts about the instrument's effectiveness as a going-concern buffer. By contrast, past cases such as Banco Popular Español S.A. in 2017 show that AT1 triggers typically activate only at the point of non-viability, effectively functioning as gone-concern tools rather than early-stage stabilisers.

Structural features, including quantitative contractual triggers, further constrain the usability of AT1 instruments in going-concern situations. Most EU instruments feature a 5.125% CET1 trigger (with higher thresholds in the UK and Switzerland and none in Canada). Yet experience shows that authorities tend to intervene before quantitative triggers are breached, particularly when crises are liquidity-confidence driven despite capital ratios remaining above thresholds.

Market behaviour has also raised issues related to AT1s: coupons, though discretionary and non-cumulative, are rarely cancelled; issuers routinely call instruments at the first call date (typically after five to seven years), subject to regulatory approval. This is because the coupon reset mechanism often makes the post-reset cost unattractive, and failing to call could be perceived by investors as a sign of weakness. If the issuer does not call, the bond rolls into a reset period with a new coupon based on a five-year swap rate plus the original spread (typically in the range of 350 basis points (bps) to 450 bps).

### **Potential Policy Scenarios**

In our view, regulators will likely review some of the following options: (1) raise quantitative triggers (potentially credit negative for AT1s); (2) remove contractual triggers and treat AT1 more like equity (as in Canada); (3) tighten call and coupon conditions to reduce adverse signalling and improve going-concern credibility; or, in the most radical scenario (4) eliminate AT1 instruments, replacing them with CET1 and/or Tier 2 capital. A CET1-only replacement would increase capital costs and effectively raise capital requirements, while removal without a substitute would diminish systemwide loss-absorbing capacity, underscoring the policy trade-off between simplicity, cost, and resilience.

### Australia Backs Out

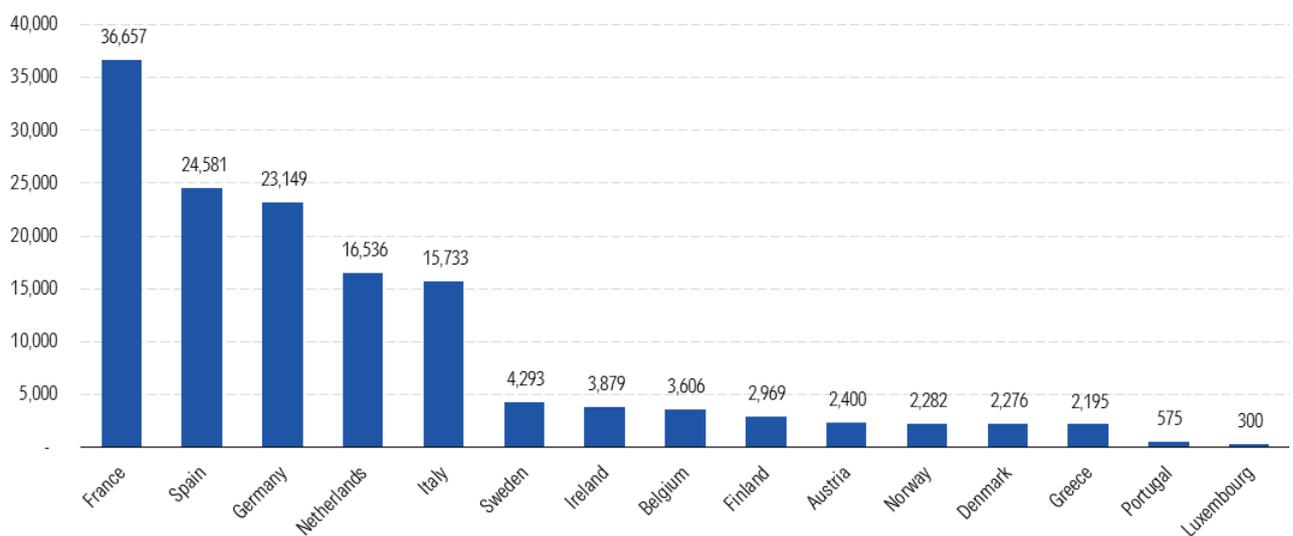
In December 2024, the Australian Prudential Authority (APRA) announced its decision to eliminate AT1 instruments from the prudential capital stack, reflecting the regulator's assessment that AT1 has not operated as a dependable going-concern buffer and instead introduces contagion and legal-execution risk. Moreover, the Australian AT1 market differs from other jurisdictions because a significant share of banks' AT1 instruments is held by retail investors—primarily high-net-worth individuals—adding further complexity and making loss absorption potentially more challenging than if these instruments were predominantly held by institutional investors.

Under the revised framework, which is effective from 1 January 2027, Australian banks will replace AT1 instruments with CET1 and Tier 2 capital. All outstanding AT1 instruments will be fully phased out by 2032 by gradually removing regulatory recognition and making no changes to the existing legal terms, including subordination, of these outstanding instruments. APRA also recalibrated the minimum leverage ratio to 3.25% of CET1, from 3.50%, preventing unintended tightening linked to the withdrawal of AT1 capacity.

### The EU AT1 Market

The EU AT1 market is sizeable, with data from the latest EU transparency exercise (covering 119 banks across 25 countries) showing EUR 142 billion of AT1 instruments outstanding at the end of H1 2025, equivalent to roughly 8.8% of total CET1 capital, compared with EUR 260 billion in Tier 2 instruments. The five largest EU jurisdictions account for around 83% of the AT1 market, with France as the largest issuer, followed by Spain and Germany (Exhibit 1). Across a sample of major EU banks, AT1 instruments represent, on average, around 2.1% of risk-weighted assets (Exhibit 2), underscoring their modest—though not negligible—role within banks' capital stacks.

**Exhibit 1** Total AT1 Capital by Country (EUR Millions)\* as of H1 2025

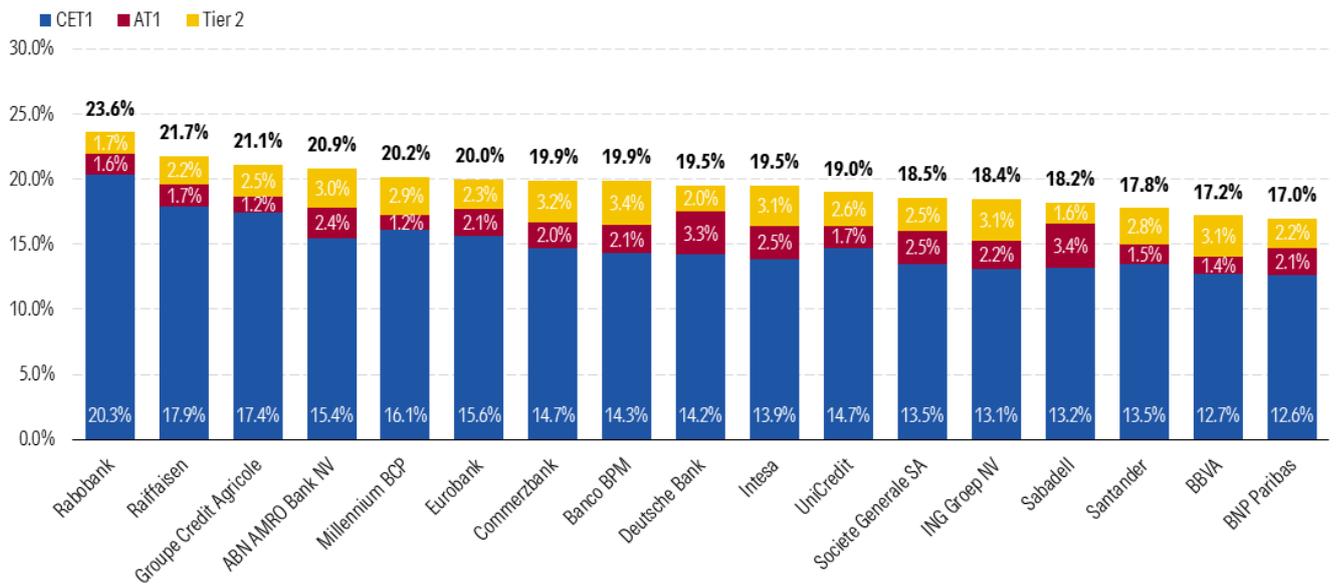


Source: Morningstar Inc, European Banking Authority (EBA). \*Exhibit includes top 15 countries by total issuance.

Market conditions have remained orderly following the ECB's December recommendation. Recent transactions, including AT1 issuances from UniCredit S.p.A. and Intesa Sanpaolo S.p.A., priced with

record-low coupons and reset margins, have signalled robust investor demand and favourable funding conditions for high-quality issuers. Despite regulatory uncertainty, we expect issuance activity to remain measured, with investors likely to maintain a preference for strong credit profiles and well-capitalised banks. Periods of elevated market volatility, such as those seen in recent weeks, can magnify call-refinancing risks, as higher swap rates and spread widening may temporarily make refinancing more expensive or less predictable.

**Exhibit 2** Total Capital Ratios Breakdown - EU Banks\* as of YE 2025



Source: Morningstar Inc., company data. \*Based on a sample of large banks. Note: Capital ratios may not be fully comparable due to different reporting across banks.

**Credit Considerations**

Overall, we assign greater value to common equity, given its immediate availability to absorb losses on a going-concern basis. In our *Global Methodology for Rating Banks and Banking Organisations*, AT1 instruments are typically positioned three to six notches below a bank's Intrinsic Assessment (IA) to reflect their heightened loss-absorbing risk and structural subordination.

Our credit rating drivers for AT1 instruments focus primarily on:

1. Probability of Tripping the Trigger: this includes the buffer between the bank's current capital ratios and the trigger level, the issuer's flexibility to take mitigating actions (e.g., raise capital), the potential behaviour of regulators in determining non-viability or directing conversions/write-downs, and the overall capital structure.
2. Recovery Prospects After a Conversion or Write-down: we assess the expected economic value following loss absorption.

Within Europe, we currently rate select Italian and Portuguese AT1 instruments, which are four notches below the banks' IAs. We will continue to monitor the ECB's recommendation and its potential implications, which may extend beyond the treatment of AT1 instruments alone. We view regulatory simplification positively where it enhances transparency, efficiency and market effectiveness. At this stage, we do not anticipate immediate credit rating actions on AT1

instruments, nor changes to our notching approach for AT1, Tier 2, or senior instruments. While some reform options could ultimately prove credit-negative for AT1 instruments, the impact remains uncertain and will depend on the final policy design and its implementation timetable. In the near term, we expect market volatility linked to ongoing geopolitical developments to remain an important driver of AT1 risk premia. These events also underscore the importance of robust capital buffers and strong liquidity profiles to navigate periods of stress.

#### **Related Research**

- [Middle East Conflict: Direct and Indirect Impact Manageable for Global Banks and Asset Managers](#), 3 March 2026
- [Bank of England's Lowering of Capital Requirements Highlights UK Banking System Resilience](#), 5 December 2025
- [2026 European Banking Sector Outlook Neutral: A Goldilocks Year Ahead?](#), 24 November 2025
- [Morningstar DBRS' Revised AT1 Ratings for European Banks](#), 10 November 2025
- [Credit Suisse's AT1 Controversy Unlikely Outside Switzerland](#), 22 March 2023

Notes: All figures in euros unless otherwise noted.

Source: Morningstar Inc, ECB, EBA, APRA, Bank of International Settlements, banks' prospectus.

### About Morningstar DBRS

Morningstar DBRS is a full-service global credit ratings business with approximately 700 employees around the world. We're a market leader in Canada, and in multiple asset classes across the U.S. and Europe.

We rate more than 4,000 issuers and nearly 60,000 securities worldwide, providing independent credit ratings for financial institutions, corporate and sovereign entities, and structured finance products and instruments. Market innovators choose to work with us because of our agility, transparency, and tech-forward approach.

Morningstar DBRS is empowering investor success as the go-to source for independent credit ratings. And we are bringing transparency, responsiveness, and leading-edge technology to the industry.

That's why Morningstar DBRS is the next generation of credit ratings.

Learn more at [dbrs.morningstar.com](https://dbrs.morningstar.com).



The Morningstar DBRS group of companies consists of DBRS, Inc. (Delaware, U.S.)(NRSRO, DRO affiliate); DBRS Limited (Ontario, Canada)(DRO, NRSRO affiliate); DBRS Ratings GmbH (Frankfurt, Germany)(EU CRA, NRSRO affiliate, DRO affiliate); DBRS Ratings Limited (England and Wales)(UK CRA, NRSRO affiliate, DRO affiliate); and DBRS Ratings Pty Limited (Australia)(AFSL No. 569400). DBRS Ratings Pty Limited holds an Australian financial services license under the Australian Corporations Act 2001 to only provide credit ratings to "wholesale clients" within the meaning of section 761G of the Act. For more information on regulatory registrations, recognitions, and approvals of the Morningstar DBRS group of companies, please see: <https://dbrs.morningstar.com/research/225752/highlights.pdf>.

For persons in Australia: By continuing to access Morningstar DBRS credit ratings and other types of credit opinions and related research (collectively, Relevant Documents), you represent to Morningstar DBRS that you are, or are accessing the Relevant Documents as a representative of, a "wholesale client" and that neither you nor any entity you represent will directly or indirectly disseminate the Relevant Documents or their contents to "retail clients" within the meaning of section 761G of the Australian Corporations Act 2001. Morningstar DBRS does not authorize distribution of the Relevant Documents to any person in Australia other than a "wholesale client" and accepts no responsibility or liability whatsoever for the actions of third parties in this respect.

The Morningstar DBRS group of companies are wholly owned subsidiaries of Morningstar, Inc.

© 2026 Morningstar DBRS. All Rights Reserved. The information upon which Morningstar DBRS credit ratings and other types of credit opinions and reports are based is obtained by Morningstar DBRS from sources Morningstar DBRS believes to be reliable. Morningstar DBRS does not audit the information it receives in connection with the analytical process, and it does not and cannot independently verify that information in every instance. The extent of any factual investigation or independent verification depends on facts and circumstances. Morningstar DBRS credit ratings, other types of credit opinions, reports, and any other information provided by Morningstar DBRS are provided "as is" and without representation or warranty of any kind and Morningstar DBRS assumes no obligation to update any such credit ratings, opinions, reports, or other information. Morningstar DBRS hereby disclaims any representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability, fitness for any particular purpose, or non-infringement of any of such information. In no event shall Morningstar DBRS or its directors, officers, employees, independent contractors, agents, affiliates, and representatives (collectively, Morningstar DBRS Representatives) be liable for (1) any inaccuracy, delay, loss of data, interruption in service, error, or omission or for any damages resulting therefrom; or (2) any direct, indirect, incidental, special, compensatory, or consequential damages arising from any use of credit ratings, other types of credit opinions, and reports or arising from any error (negligent or otherwise) or other circumstance or contingency within or outside the control of Morningstar DBRS or any Morningstar DBRS Representative in connection with or related to obtaining, collecting, compiling, analyzing, interpreting, communicating, publishing, or delivering any such information. IN ANY EVENT, TO THE EXTENT PERMITTED BY LAW, THE AGGREGATE LIABILITY OF MORNINGSTAR DBRS AND MORNINGSTAR DBRS REPRESENTATIVES FOR ANY REASON WHATSOEVER SHALL NOT EXCEED THE GREATER OF (A) THE TOTAL AMOUNT PAID BY THE USER FOR SERVICES PROVIDED BY MORNINGSTAR DBRS DURING THE TWELVE (12) MONTHS IMMEDIATELY PRECEDING THE EVENT GIVING RISE TO LIABILITY, AND (B) USD 100. Morningstar DBRS does not act as a fiduciary or an investment advisor. Morningstar DBRS does not provide investment, financial, or other advice. Credit ratings, other types of credit opinions, and other analysis and research issued by Morningstar DBRS (a) are, and must be construed solely as, statements of opinion and not statements of fact as to creditworthiness, investment, financial, or other advice or recommendations to purchase, sell, or hold any securities; (b) do not take into account your personal objectives, financial situations, or needs and do not comment on the suitability of any investment, loan, or security; (c) should be weighed, if at all, solely as one factor in any investment or credit decision; (d) are not intended for use by retail investors; and (e) address only credit risk and do not address other investment risks, such as liquidity risk or market volatility risk. Accordingly, credit ratings, other types of credit opinions, and other analysis and research issued by Morningstar DBRS are not a substitute for due care and the study and evaluation of each investment decision, security, or credit that one may consider making, purchasing, holding, selling, or providing, as applicable. A report with respect to a Morningstar DBRS credit rating or other credit opinion is neither a prospectus nor a substitute for the information assembled, verified, and presented to investors by the issuer and its agents in connection with the sale of the securities. Users should obtain appropriate advice from a financial or other professional advisor prior to making any financial decisions. Users should also consider the definitions, limitations, policies, criteria, and methodology used by Morningstar DBRS to arrive at the credit ratings, opinions, research, or other analysis provided by Morningstar DBRS. Morningstar DBRS may receive compensation for its credit ratings and other credit opinions from, among others, issuers, insurers, guarantors, and/or underwriters of debt securities. This publication may not be reproduced, retransmitted, or distributed in any form without the prior written consent of Morningstar DBRS. ALL MORNINGSTAR DBRS CREDIT RATINGS AND OTHER TYPES OF CREDIT OPINIONS ARE SUBJECT TO DEFINITIONS, LIMITATIONS, POLICIES, AND METHODOLOGIES THAT ARE AVAILABLE ON <https://dbrs.morningstar.com>. Morningstar DBRS may use artificial intelligence ("AI") tools to assist with certain research, drafting, and internal processes. Any content supported by AI is subject to human review and approval. Users may, through hypertext or other computer links, gain access to or from websites operated by persons other than Morningstar DBRS. Such hyperlinks or other computer links are provided for convenience only. Morningstar DBRS does not endorse the content, the operator, or operations of third-party websites. Morningstar DBRS is not responsible for the content or operation of such third-party websites and Morningstar DBRS shall have no liability to you or any other person or entity for the use of third-party websites.