



Valley National Bancorp

2015 Annual Dodd-Frank Act Stress Test Disclosure

June 2015

2015 Annual Dodd-Frank Act Company-Run Stress Test Disclosure for Valley National Bancorp and Valley National Bank

Introduction

Section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) and related regulations requires national banks and federal savings associations with consolidated assets of more than \$10 billion, including Valley National Bancorp (referred to herein as “Valley”, “we”, “us”, “our” or “the Bank”), to conduct annual stress tests. In the Dodd-Frank Act stress test (“DFAST”) conducted annually and completed in March of this year, we are required to perform stress tests using a set of macroeconomic scenarios (supervisory baseline, supervisory adverse and supervisory severely adverse) developed by the Board of Governors of the Federal Reserve System (“Federal Reserve Board”). The results of the stress tests are submitted to the Office of the Comptroller of the Currency (“OCC”) and the Federal Reserve Board.

Stress testing is an integral component of our internal capital adequacy assessment and we incorporate DFAST into our internal processes to assess our capital adequacy and to ensure that the Bank holds an appropriate amount of capital relative to the risks of our businesses and consistent with Valley’s Board of Director’s Risk Appetite Statement.

The DFAST rules require us to publish a summary of the stress test results based on the Federal Reserve Board’s severely adverse scenario in June of this year. Our planning horizon for the 2015 stress test is the first quarter of 2015 through the fourth quarter of 2016.

We were instructed by the OCC to utilize our projections beginning in the first quarter of 2015 due to an acquisition that closed in the fourth quarter of 2014.

Basel III-Based Capital Rules (“Basel III”)

The Bank is required to compute its capital ratios for each quarter of the planning horizon. The Common Equity Tier I, Tier I, Total Capital and Leverage ratios are calculated utilizing the Basel III-based capital rules.

Standardized Capital Rules

We are also required to calculate capital ratios under the Standardized Capital Rules. Effective in the first quarter of 2015, risk weighted assets (“RWAs”) and capital are calculated under the Standardized Capital Rules that utilize the Revised Capital Framework definition of capital. The new definitions of capital include changes to certain limitations on the instruments that can be included in regulatory capital and the items that must be deducted. The revised capital framework also introduces a new regulatory capital ratio, Common Equity Tier I which is calculated for all quarters over the planning horizon.

Severely Adverse Scenario

The severely adverse scenario is developed and prescribed by the Federal Reserve Board. For the 2015 DFAST, the scenarios include 28 variables, 16 domestic and 12 international. This included six measures of economic activity and prices; four aggregate measures of asset prices or financial conditions; six measures of interest rates; and twelve measures of international conditions.

GDP and Unemployment

The severely adverse scenario for the United States is characterized by a deep and prolonged recession in which the unemployment rate increases by 4 percentage points from its level in the third quarter of 2014, peaking at 10 percent in the middle of 2016. In terms of both the peak level reached by the unemployment rate and its total increase, this shock is of a similar magnitude to those experienced in severe U.S. contractions during the past half century. By the end of 2015, the level of real GDP is approximately 4½ percent lower than its level in the third quarter of 2014; it begins to recover thereafter.

U.S. Interest Rates and Credit Spreads

In response to this economic contraction—and despite the higher near-term path of CPI inflation—Treasury yields of all maturities are significantly lower throughout the scenario. Short-term interest rates remain near zero through 2017; long-term Treasury yields drop to 1 percent in the fourth quarter of 2014 and then edge up slowly over the remainder of the scenario period. Driven by the assumed decline in corporate credit quality, spreads on investment-grade corporate bonds jump from about 170 basis points to 500 basis points at their peak. As a result, despite lower long-term Treasury yields, corporate financial conditions tighten significantly in 2015 and the yield on investment-grade corporate bonds is higher than the baseline until the fourth quarter of 2016. Mortgage rates also increase over the course of 2015, driven by some widening in spreads.

Equity Markets & Other Prices

Consistent with these developments, asset prices contract sharply in the scenario. Equity prices fall by approximately 60 percent from the third quarter of 2014 through the fourth quarter of 2015, and equity market volatility increases sharply. House prices decline by approximately 25 percent during the scenario period relative to their level in the third quarter of 2014, while commercial real estate prices are more than 30 percent lower at their trough.

Summary of Results

The following table summarizes the results of the Bank's calculations under the Federal Reserve Board's severely adverse scenario over the planning horizon. The results incorporate the following capital action assumptions as prescribed by the Federal Reserve Board's DFAST rules for each of the quarters in the planning horizon:

- common stock dividends equal to the quarterly average dollar amount of common stock dividends that were paid in the first quarter of 2014 through the fourth quarter of 2014;
- payments on any other instrument eligible for inclusion in the numerator of a regulatory capital ratio equal to the stated dividend, interest or principal due on such instrument; and
- no redemption or repurchase of any capital instrument eligible for inclusion in the numerator of a regulatory capital ratio.

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Projected Capital Ratios, Risk Weighted Assets (“RWAs”), Pre-Provision Net Revenues (“PPNR”), Aggregate Losses and Net Income
Valley National Bancorp Projections Under the Federal Reserve Board’s Severely Adverse Scenario

These results are calculated using capital action assumptions required by the DFAST rules. All projections represent hypothetical estimates that involve an economic outcome that is more adverse than expected. These estimates are not forecasts.

Actual and Projected Capital Ratios through Q4 2016 under the Federal Reserve Board's Severely Adverse Scenario				
	Actual		Stressed Capital Ratios	
	Q3 2014	Q4 2014	Ending	Lowest
Common equity tier 1 ratio (%) ¹	-	-	9.04%	9.04%
Tier 1 capital ratio (%) ¹	9.58%	9.73%	9.04%	9.04%
Total capital ratio (%) ¹	11.44%	11.42%	11.18%	11.18%
Tier 1 leverage ratio (%) ¹	7.39%	7.46%	6.81%	6.81%
¹ Projected capital ratios are presented under Basel III				

Projected Loan Losses by Type of Loan from Q1 2015 through Q4 2016 under the Federal Reserve Board's Severely Adverse Scenario			
	in millions	Portfolio Loss Rates ¹	
Total Loan and Lease Losses	82.2	0.60%	
First Lien Mortgages	6.0	0.24%	
Junior Liens and HELOCs	2.7	1.04%	
Commercial and Industrial	27.7	1.26%	
Commercial Real Estate	24.1	1.78%	
Credit Cards	0.9	11.84%	
Other Consumer	15.6	2.30%	
Other Loans	5.2	1.69%	
¹ Loss rates are calculated based on the average asset size of the respective category			

Projected PPNR, Losses and Net(Loss)/Income After Taxes from Q1 2015 through Q4 2016 under the Federal Reserve Board's Severely Adverse Scenario		
	in millions	Percentage of Average Assets
PPNR	328.0	1.74%
Other Revenue	-	-
Less		
Provision for Loan Losses	112.3	0.60%
Realized Losses/(Gains) on Securities	-	-
Equals		
Net (Loss)/Income Before Taxes	215.7	1.15%

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**Projected Capital Ratios, Risk Weighted Assets (“RWAs”), Pre-Provision Net Revenues (“PPNR”), Aggregate Losses and Net Income
Valley National Bank Projections Under the Federal Reserve Board’s Severely Adverse Scenario**

These results are calculated using capital action assumptions required by the DFAST rules. All projections represent hypothetical estimates that involve an economic outcome that is more adverse than expected. These estimates are not forecasts.

Actual and Projected Capital Ratios through Q4 2016 under the Federal Reserve Board's Severely Adverse Scenario				
	Actual		Stressed Capital Ratios	
	Q3 2014	Q4 2014	Ending	Lowest
Common equity tier 1 ratio (%) ¹	-	-	9.63%	9.63%
Tier 1 capital ratio (%) ¹	10.24%	10.17%	9.63%	9.63%
Total capital ratio (%) ¹	11.09%	10.94%	10.56%	10.56%
Tier 1 leverage ratio (%) ¹	7.90%	7.79%	7.25%	7.25%
¹ Projected capital ratios are presented under Basel III				

Projected Loan Losses by Type of Loan from Q1 2015 through Q4 2016 under the Federal Reserve Board's Severely Adverse Scenario			
	in millions		Portfolio Loss Rates ¹
Total Loan and Lease Losses	82.2		0.60%
First Lien Mortgages	6.0		0.24%
Junior Liens and HELOCs	2.7		1.04%
Commercial and Industrial	27.7		1.26%
Commercial Real Estate	24.1		1.78%
Credit Cards	0.9		11.84%
Other Consumer	15.6		2.30%
Other Loans	5.2		1.69%
¹ Loss rates are calculated based on the average asset size of the respective category			

Projected PPNR, Losses and Net(Loss)/Income After Taxes from Q1 2015 through Q4 2016 under the Federal Reserve Board's Severely Adverse Scenario		
	in millions	Percentage of Average Assets
PPNR	348.5	1.85%
Other Revenue	-	-
Less		
Provision for Loan Losses	112.3	0.60%
Realized Losses/(Gains) on Securities	-	-
Equals		
Net (Loss)/Income Before Taxes	184.3	0.98%

Based on the Federal Reserve Board's severely adverse scenario, the most significant drivers of the changes in the Bank's regulatory capital ratios over the planning horizon when compared with actual regulatory capital ratios as of the fourth quarter of 2014 are:

- increased RWAs resulting from modest loan growth over the planning horizon and the requirement to project RWAs based on the revised capital framework;
- loan losses which are included in our net (loss)/income projections and increased allowance for loans and lease losses; and
- lower Pre-Provision Net Revenue ("PPNR") over the planning horizon resulting in decreased net (loss)/income.

Material Risk Captured in the Stress Test

Credit Risk

Credit risk is the risk to earnings or capital arising from an obligor's failure to meet the terms of any contract with the bank or otherwise to perform as agreed. Credit risk is found in all activities where success depends on counterparty, issuer, or borrower performance. It arises any time bank funds are extended, committed, invested, or otherwise exposed through actual or implied contractual agreements.

Credit risk is incorporated into our 2015 DFAST results via the severely adverse macroeconomic scenario. The significant drop in economic output, home prices and equity prices as well as a rise in the unemployment rate resulted in increased credit risk which is also reflected into our provision for loan and lease losses.

Liquidity Risk

Liquidity risk is the risk to earnings or capital arising from a bank's inability to meet its obligations when they come due without incurring unacceptable losses. Liquidity risk includes the inability to manage unplanned decreases or changes in funding sources. Liquidity risk also arises from the failure to recognize or address changes in market conditions that affect the ability to liquidate assets quickly and with minimal loss in value.

Our 2015 DFAST results account for liquidity risk by projecting funding balances based on the severely adverse scenario and assessing the impact of the outflows on our balance sheet.

Interest Rate Risk

Interest rate risk is the risk to earnings or capital arising from movements in market interest rates. Interest rate risk arises from the impact of movements in interest rates and the timing of cash flows (repricing risk), from changing rate relationships among different yield curves affecting bank activities (basis risk), from changing rate relationships across the spectrum of maturities (yield curve risk), and from interest-related options embedded in bank products (options risk).

Interest rate risk is incorporated into our 2015 DFAST results via the severely adverse macroeconomic scenario. The compression experienced in the yield curve is evidenced by the narrowing of the 3-month and 10-year Treasury Rate spread. This dynamic sufficiently captures interest rate risk over the course of the planning horizon.

Operational Risk

Operational risk is the risk to earnings or capital arising from inadequate or failed internal processes or systems, the misconduct or errors of people, and adverse external events. Operational losses result from internal fraud; external fraud; employment practices and workplace safety; clients, products, and business practices; damage to physical assets; business disruption and systems failures; and execution, delivery, and process management. For capital stress testing purposes, compliance risk has been considered as part of operational risk.

Operational risk losses are assessed based on the assumed conditions of the severely adverse scenario. The estimates may include judgements based on the Bank's historical operational risk experience, internal factors and industry trends. The 2015 DFAST results incorporate operational risk losses within the non-interest expense projections over the planning horizon.

Acquisition Risk

Acquisition risk can potentially impact enterprise-wide risk indicators. Risk exposures arise from expanding the geographic reach of the combined entity and broadening of the customer base potentially through new products or services. An acquisition may result in greater concentration of counterparty credit risk or exposure to financial instruments. Identifying potential changes in enterprise risks, creating an action plan to address them, and assessing changes to risk management strategies post-acquisition are critical to managing acquisition risk.

Description of Our Stress Testing Methodologies

Our stress testing projections are primarily estimated using quantitative methodologies. Management judgement is also a critical component of the process and therefore some estimates are conveyed based on a qualitative approach. We use econometric models to estimate pre-provision net revenue and credit losses to assess our capital levels for each quarter over the planning horizon.

On whole, line items determined to be material to the balance sheet or income statements are projected using quantitative models. However, in certain situations where statistical correlations to macroeconomic variables are weak or in cases where sufficient historical data are not available, we use qualitative estimations to determine the projections over the planning horizon. Typically, qualitative estimations are more conservative in nature in that the results are more adverse to capital.

We largely utilize the variables developed and prescribed by the Federal Reserve Board in our econometric models. In certain circumstances we may utilize variables that are extrapolated based on what was provided by the Federal Reserve Board.

Valley National Bancorp's wholly owned subsidiary, Valley National Bank represents 99.9 percent of the consolidated Company's assets; therefore, we apply the same methodologies when conducting stress tests at the bank level.

Supplementary Information

Additional information on DFAST is available on the Federal Reserve Board's website at <http://www.federalreserveboard.gov>.