



Dodd-Frank Act Stress Test 2016 Public Disclosure

October 27, 2016

About MB Financial

MB Financial, Inc., headquartered in Chicago, Illinois, is a financial holding company with retail banking offices located primarily in the Chicago area.

The words “MB Financial,” “the Company,” “we,” and “our” refer to MB Financial, Inc. and its consolidated subsidiaries, unless the context indicates otherwise. Our primary market is the Chicago metropolitan area, in which we operate 80 banking offices through our bank subsidiary, MB Financial Bank, N.A. the words “the Bank” refer to MB Financial Bank, N.A. Through MB Financial Bank, we offer a broad range of financial services primarily to small and middle market businesses and individuals in the markets that we serve. Our primary business segments include banking, leasing, and mortgage banking. As of December 31, 2015, on a consolidated basis, we had total assets of \$15.6 billion, deposits of \$11.5 billion, stockholders’ equity of \$2.1 billion, and client assets under management of \$3.8 billion in our Wealth Management Group (including \$2.7 billion in our trust department and \$1.1 billion in our majority-owned asset management firm, Cedar Hill Associates LLC).

On August 24, 2016, the Company acquired American Chartered Bancorp, Inc. (“American Chartered” or “ACB”), which was the holding company for American Chartered Bank. American Chartered Bank operated 15 banking offices in the Chicago area and, as of June 30, 2016, had approximately \$2.8 billion in total assets, \$2.0 billion in loans, and \$2.4 billion in deposits. American Chartered Bank was merged into MB Financial Bank on August 24, 2016.

Overview

As required under the Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA), banks and bank holding companies with total assets greater than \$10 billion are required to meet the stress testing requirements described in the DFA on an annual basis.

Bank holding companies and national banks subject to the DFA stress test (DFAST) requirements must assess the potential impact of a minimum of three macroeconomic scenarios provided by the Board of Governors of the Federal Reserve System and the Office of Comptroller of the Currency (OCC) - baseline, adverse, and severely adverse - on their consolidated earnings, pre-provision net revenue (PPNR), loan loss provision, net income, balance sheet (including risk-weighted assets), and capital over a nine quarter projection period.

The three macroeconomic scenarios provided by the Federal Reserve and the OCC are not a forecast of expected macroeconomic and financial conditions, but are hypothetical scenarios designed to assess the strength of banking organizations and their resilience to adverse economic and financial conditions. Results of the three scenarios for the Company and the Bank are sent to the Federal Reserve and the OCC, respectively.

Description of the Types of Risk Included

Outside of the capital stress test process, MB Financial has a system in place to set risk appetites and measure risks against those appetites. The risk appetite framework is expressed both in qualitative and quantitative terms. The areas of risk appetite that are measured on a regular basis are: capital, compliance, credit, interest rate, liquidity, and operational. Capital, credit, liquidity, interest rate, operational, and reputational risks are most closely tied to the capital stress test process.

- **Capital Risk** – the risk that the Company will not maintain capital levels above “well capitalized” for the Holding Company and Bank per regulatory requirements. The overarching goal of the stress test is to evaluate the impact of a stressed economic environment on our capital ratios.
- **Credit Risk** – the risk of unexpected losses due to borrower default. This risk is reflected in our charge-off and non-accrual models, as well as in the calculation of the Allowance for Loan and Lease Losses (ALLL) and the provision expense.
- **Liquidity Risk** – our liquidity risk appetite states that we will ensure that the company meets its cash and collateral obligations so that we can meet both expected and unexpected cash flows, as well as collateral needs. The Asset Liability Management (ALM) system used to project the DFAST income statement and balance sheet explicitly models the Company’s and the Bank’s cash flows.

Types of Risks Included (continued)

- **Interest Rate Risk** – the risk to earnings or capital arising from movement of interest rates. It arises from differences between the timing of rate changes and the timing of cash flows (repricing risk); from changing rate relationships among yield curves that affect bank activities (basis risk); from changing rate relationships across the spectrum of maturities (yield curve risk); and from interest-rate-related options embedded in bank products (option risk). The interest rate environment is an input into, and interest rate risk is captured within the ALM system used to project the DFAST income statement and balance sheet.
- **Operational Risk** – the risk of loss resulting from the inadequate or failed internal processes, people and systems or from external events. We incorporated operational losses in estimating non-interest expense under the baseline, adverse and severely adverse scenarios. Operational risk is also reflected in the models developed by our mortgage division to forecast income related items.
- **Reputational Risk** – can result in losses, lost revenues, higher regulatory and capital costs as well as reduced shareholder value as a result of damages to a firm's reputation in the context of soundness and safety and/or potential criminal events.

Summary of Methodologies Used in the Stress Test

Credit-loss related models were developed through regression analysis by identifying statistical relationships between our historical loan losses and macro-economic variables (including regional variables).

Allowance for Loan and Lease Losses (ALLL) – similar to our loss estimation approach, we determined ALLL levels for each scenario through regression analysis. Provision amounts were calculated from the projected ALLL levels and loss estimates.

Mortgage Models – we forecasted originations, gain-on-sale amounts, net servicing income, and the fair-market-value of mortgage servicing rights. Both analytical based approaches and assumption based approaches were used in the development of these forecasts.

The **Income Statement** and **Balance Sheet** were modeled within the Company's ALM system. This system modeled the cash flows and financial statement impacts that resulted from the following inputs:

- Regulatory agency prescribed interest rate environments
- Projected loan growth assumptions
- Projected deposit growth assumptions
- Loan & deposit pricing assumptions
- Other income and expense assumptions
- Model projected charge offs, ALLL, and non-accrual rates

Regulatory Agency Prescribed Scenarios

To meet the stress testing requirements, we must project the impact of three regulator-prescribed scenarios on our financial statements.

1. **Baseline Scenario** – moderate economic expansion.
2. **Adverse Scenario** – weakening economic activity across all countries included in the scenario. The economic downturn is accompanied by a period of deflation in the United States and in the other countries. Reflecting weak economic conditions and deflationary pressures, short-term interest rates in the United States remain near zero over the projection period. Financial conditions tighten for corporations and households during the recession and asset prices decline in the adverse scenario.
3. **Severely Adverse Scenario** – characterized by a severe global recession, accompanied by a heightened period of corporate financial stress and negative yields for short-term U.S. Treasury securities. Corporate financial conditions are severely stressed, reflecting mounting credit losses, heightened investor risk aversion, and strained market liquidity conditions.

These are hypothetical scenarios. The scenarios considered do not represent forecasts of economic activity made by the Federal Reserve , the OCC, or MB.

Summary of Results in the Severely Adverse Scenario

The intent of the stress test is to determine whether the Company would remain solvent under severely adverse economic conditions. For this reason, we discuss in detail only the results of the severely adverse scenario in this disclosure.

As would be expected, credit losses have a significant impact on the Company's performance. Losses increase significantly, with cumulative charge-offs over the projection period of \$633 million, representing 6.01% of balances at the start of the scenario. For the nine-quarter horizon, total provision expense was \$787 million, resulting in a net loss of \$66 million.

MB Financial, Inc.
Summary Results - Severely Adverse Scenario
Q1 2016 to Q1 2018
(Dollars in Thousands)

	<u>MB Financial, Inc.</u>	<u>MB Financial Bank, NA</u>
Aggregate Loan & Lease Losses	\$ 633,412	\$ 633,412
Pre-Provision Net Revenue (PPNR)	612,446	637,785
Provision for Loan and Lease Losses	787,027	787,027
Net Income (Loss)	(66,084)	(50,881)

Projected Capital Ratios

For all of the capital stress testing scenarios, our capital ratios are above the “well capitalized” threshold as shown below, and therefore remain within our risk appetite.

MB Financial, Inc.
Severely Adverse Scenario
Q1 2016 to Q1 2018

MB Financial, Inc.	12/31/2015	3/31/2018	Minimum (A)	Capital Adequacy (B)
Common equity tier 1 risk-based capital ratio	9.27	8.01	8.01	4.50
Tier 1 risk-based capital ratio	11.54	8.95	8.95	6.00
Tier 1 leverage ratio	10.40	7.12	7.12	4.00
Total risk-based capital ratio	12.54	11.86	11.86	8.00

MB Financial Bank, NA	12/31/2015	3/31/2018	Minimum (A)	"Well-Capitalized" (C)
Common equity tier 1 risk-based capital ratio	10.61	10.93	10.93	6.50
Tier 1 risk-based capital ratio	10.61	10.94	10.93	8.00
Tier 1 leverage ratio	9.54	8.72	8.72	5.00
Total risk-based capital ratio	11.62	12.19	12.18	10.00

(A) "Minimum" represents the lowest projected capital ratio in the nine-quarter planning horizon.

(B) Effective January 1, 2015, we became subject to new capital regulations adopted by the Federal Reserve and the OCC. These regulations implement the regulatory capital reforms required by the Dodd Frank Act and the Basel Committee on Banking Supervision.

(C) "Well-Capitalized" refers to capital requirements under the Federal Deposit Insurance Corporation Improvement Act of 1991 for the Bank.

Explanation of Changes in Capital Ratios

Capital decreases in this scenario due to the decline in loans, margin compression, and significantly higher credit costs.

Loans decline by 17% over the nine quarter period (excluding loans acquired on June 30, 2016) as we expect our credit appetite would diminish as credit deteriorates. Although interest rates are decreasing, we expect loan credit spreads to widen, consistent with the increase in BBB corporate yields relative to increase in treasury yields.

While elevated non-accruing loans (reaching 4.42% of loans in 2017) compress our net interest margin, the impact is partially offset by wider credit spreads. Cumulative charge-offs over the projection period are \$633 million, or 6.01% of the balances at the start of the scenario. The scenario results in a cumulative net loss of \$66 million over the nine quarter projection period.

Explanation of Changes in Capital Ratios (continued)

Other contributing factors to changes in the capital ratios include:

- In Q2 2016, the quarter in which the ACB merger was originally expected to be completed (it was ultimately completed in Q3 2016), the Company passed the \$15 billion threshold for including trust preferred securities (TRUPS) in Tier 1 Capital. Trust preferred securities are only held at the holding company level, so this accounting change only affected holding company capital ratios.
- Risk Weighted Assets (RWA) decreased due to balance sheet reduction and loan decreases that were partially offset by investment security purchases. The decreased RWA partially offset the effect of the TRUPS accounting change for the holding company, but improved capital ratios for MB Financial Bank.
- Beginning in Q1 2018, ratios decreased due to an increase in risk-weighted assets primarily due to the change in the risk weighting of the mortgage servicing asset to 250%.
- As a result of the severe economic conditions, discretionary dividend payments to the holding company's common shareholders were suspended.

Conclusion

Uses of Stress Test Results:

The stress test results are an important factor considered by the Federal Reserve and the OCC in evaluating, among other matters, the capital adequacy of the Company and whether any proposed payments of dividends or stock repurchases may be an unsafe or unsound practice. We must consider the results of stress tests in the normal course of business, including consideration of capital planning, assessment of capital adequacy and risk management practices.

Forward-Looking Statements

This document contains a summary of the results of a forward-looking, Company-run stress test exercise that regulations of the Federal Reserve and the OCC require us to perform and publicly disclose. Accordingly, this document contains statements that we believe constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, including estimates of financial condition, results of operations, and capital ratios under a hypothetical supervisory severely adverse scenario that incorporates a set of assumed economic and financial conditions prescribed by the bank regulatory agencies. Forward-looking statements represent management's current projections regarding future events based on certain estimates and assumptions made by management or mandated by the bank regulatory agencies that are inherently uncertain. Actual results may differ materially from those set forth in the forward-looking statements. Factors that could cause our actual results to differ materially from those described in the forward-looking statements include actual economic and financial conditions (as opposed to the hypothetical economic and financial conditions required to be used in the stress test) and various other factors that can be found in MB Financial, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2015 and Quarterly Reports on Form 10-Q for the quarters ended March 31, 2016 and June 30, 2016, which have been filed with the Securities and Exchange Commission (the "SEC") and are available on the SEC's website at www.sec.gov, and on MB Financial's website, at www.mbfinancial.com, as well as any additional factors set forth in subsequent periodic and current reports filed or furnished by MB Financial, Inc. with the SEC. Such forward-looking statements speak only as of the date of this document, and we assume no obligation to update any of these statements in light of new information, future events or otherwise following the date of this document.