UniCredit

European Parliament Financial Service Forum (EPFSF)
Breakfast Seminar on Non Performing Loans
MAENA FERRERO Speach

(1) Looking at the second progress report that shows a clear trend of decreasing NPLs stock in Europe, are policy initiatives needed to continue this trend? (priority question)

- **Reducing NPLs to pre-crisis level and restoring profitability is the leading concern of Banks** (**and UniCredit in particular**) **not because of Regulatory Provisions** but because is the right thing to do and the way to bring value to investors. This is what is required first of all by the market (investors, analysts, rating agencies, banks' clients)

- **Banks have worked hard in this directions even if with differences among the countries.** UniCredit has been taking proactive management actions in tackling the issue – **the reduction of €35 billion of gross NPEs since 2015 is a tangible sign of such actions**

- **In this contest, the effort of the European Institutions to establish a comprehensive EU strategy** to address the high level of NPLs **within the eurozone banking sector is more than welcome and supported by UniCredit** because it ensure
    - a level playing field by setting common minimum rules
    - major transparency of the market
    - fostering of best practices in management

- **On the other hand** we think that **is of the utmost importance to calibrate the incentives to NPLs decrease in order to avoid improper value destruction for banks**

- For these reasons **we do not think that a pillar 1 measure is needed, especially as it can produce as final result a reduction in bank lending. We would suggest, therefore, caution against an unduly rushed process to agree a Pillar 1 prudential backstop** as many aspects of the Regulation need to be further analyzed and fine-tuned. **A Pillar 2 measure is the best incentive scheme for the bank in our opinion**

- On the other hand we think that **other measures, such as the draft rules to promote a secondary market for NPLs and the recovery of collateral, should be first adopted**. With respect to these files, we are particularly disappointed that they have been relegated, as we deem that they represent an effective solution in reducing the current stockpile of bad debt on bank balance sheets

- Also in light of the fact that **after bad loans now the big chunk are UTP**, it is of the utmost importance
    - on the one side to harmonize the pre-insolvency laws ensuring the converge to best practices of the single jurisdictions
    - on the other side avoid perverse incentive towards liquidating approaches instead of restructuring approach aimed at regularizing the clients (reference to calendar provisioning current rules)

- Finally **we advise to be careful in being too prescriptive on matters that the market is probably best suited to regulate.** With particular reference to data tapes (500 fields have never been requested by any UniCredit NPL or Performing loans purchaser) and platforms

(2) Does the statutory backstop overlap with existing accounting rules, Pillar 2 supervisory powers, and greater transparency and disclosure requirements? Why do we need a statutory prudential backstop in addition? (priority question)

- With regard to the prudential backstop, our view is that **Pillar 1 measures are not necessary.** There are a lot of aspects in the application of the rules that need to be carefully analysed and modelled in order to avoid unduly distortive effects (among the most important
    - **eligible collateral:** enlarge the scope of eligible collateral without differentiation btwn standard and advanced, considering all immovable properties (like ECB Addendum) if valuation of the property is aligned to criteria set in Chapter 7 of NPE Guidelines
    - **partial write-offs:** consider as other accounting provisions in calculating the backstop
    - **forbearance treatment:** allow the possibility to freeze the backstop for 3 years since FB concession as long as the transaction is not overdue (like ECB Addendum)
    - **changing the date of application** of the regulation **to the date of publication**, avoiding a retroactive application of the backstop
- **20 pages for such a prescriptive regulation are not enough**

- **On the other hands a Pillar 2 measure would be the best incentive scheme for the banks** because
    - it would be applied in the **context of individual supervision**
    - **better taking into account the individual institutions' specificities** on different products / guarantees as well as the **local peculiarities of the legal-judicial environment**

- **Furthermore it has to be clearly said that, if both Pillar 1 and Pillar 2 measures were kept, the interplay between the two will be particularly critical in terms of implementation and ongoing management** when both measures will entry into force as they address the same NPLs issue with different approaches, perimeter, calibration and timing of implementation

- We deem that **the accounting standards developed in IFRS 9 already ensure a sufficient level of provisioning based on internal models that have been extensively audited and challenged by the Regulator**
    - it would be much better **to keep on challenging the soundness of these models and the quality of credit processes and information feeding them** (NPE Guidelines issued in November 2016 goes in this right direction) even considering the huge amount of investments in this direction
    - **Pillar 1 Calendar Provisioning would disregard all this framework after 2 / 7 years** from NPE classification implicitly assuming a priori for all banks' NPE transactions that processes and models have failed

  We ask for a strict but more tailor maid approach

- **Furthermore, the calendar provisioning doesn't create the right incentives for a proactive bank approach in managing NPLs.** Since the recovery period is mainly driven by the effectiveness of the legal-judicial environment, the proposed measure will **push banks towards a liquidating approach rather than offering restructuring alternatives** with respect to debtors that are in temporary difficulty so as to release the collateral and minimize short-term costs
- Finally, we are concerned that **a prescriptive backstop might turn out to be excessively restrictive**, leading to a **severe reduction in bank lending especially towards SME clients (usually unsecured and lower credit quality)**, with important negative spill-over effects on investments, growth and the real economy as a whole, amplifying the pro-cyclical effects during the downturn phases

(3) Will the new out-of-court enforcement improve the balance between creditors and borrower and the efficiency of traditional court procedures? (priority question)

- **UniCredit welcomes the Commission's intention to increase the protection of secured creditors** from business borrower's default by introducing a new instrument labelled **Accelerated Extrajudicial Collateral Enforcement** (AECE) – allowing for the automatic transfer of the business debtor property to the creditor so enabling the bank to recover quicker the value through a private sale or a public auction

- We consider that **greater protection of secured creditors and their collateral will have a positive impact on borrowers** and grant them an easier and cheaper access to credit.

- However **a new form of collateral enforcement would be really effective only if it can be used also in the insolvency / pre-insolvency processes**. If it is not enforceable in restructuring / insolvency at the request of the creditor, we risk creating a tool which becomes irrelevant when it is most needed

- In general, we deem that the **policy makers should focus more on harmonizing the insolvency and pre-insolvency framework at the European level**. Pushing local Regulators to shortening the length of judicial procedures and facilitating early restructuring , thus giving a second chance to the entrepreneurs and consequently enhancing occupation and growth

- **With respect to this, it is worrisome that the Council has activated the fast track procedure on the Backstop part of the NPLs package, without prioritizing the others NPL package's files,** and especially the ones promoting a secondary market and the recovery of collateral

- Finally, it has to be said that **in some jurisdiction like Italy, in the short term the Regulators should push more for an efficient and effective use of current laws.** Statistics shows clearly that the performances of insolvency procedures for the different courts is extremely volatile depending by the managerial capability of the Head of Court. More transparency on these performances and push for benchmarking towards the bests would help

- **A very last remark** is based **on the experience done in Italy with the so called Patto Marciano**, introduced in 2016
  The benefits of this early enforcement tool **are largely still to be felt**
  - because it applies only to new loans
  - it has not been taken up as expected

(4) Why introduce onerous disclosure and reporting requirements for loan transactions in well-functioning markets such as performing loans, securitizations, or syndicated loans? (back-up question)

- With reference to **data disclosure requirements** for loan sale transaction (public or private) with professional investors **our view is to let the market do its work as it is generally efficient in these cases**

- It is the primary interest of a professional investor receive the right and complete information needed to assess the asset on sale. If they are not satisfied either they skip the deal or they adjust downward the price.

- **For what concern EBA NPL Templates published on 14th December 2017**, not binding for the moment, we can only observe that in UniCredit experience of loans' sales (both performing and non performing, secured and unsecured) a maximum of 150 / 200 fields have been requested by investors, not 500. Such a request would only put useless burden and unnecessary costs on banks, with the risk of reducing liquidity and increase transactions costs in market segments with strong transaction volumes and robust investor appetite

- **For what concern the Directive issued by the Commission on the 14th March 2018 on credit servicers and credit purchaser for the Part I concerning Development of Secondary Markets for NPLs**, the introduction of onerous disclosure and reporting requirements for well-functioning markets such as performing loan transactions, large corporate NPLs, private deals is again not necessary and useless burdensome

- **Also to be considered the interplay with the regulatory provisions on similar topics on behalf of other Authorities such as ESMA** (European Security and Market Authority) which on August 2018 issued Technical Standards on disclosure requirements for Securitizations, envisaging also templates for NPL transactions disclosure (→ entry into force 1 Jan 2019)

- **To conclude, we deem that the way in which Regulator may be most effective on data disclosure is in fostering effective internal data governance of the Banks**
  - **either via regulation:** in this respect BSBS 239 issued in January 2013 setting principles for Risk Data Aggregation and Reporting Processes for Global Systemically important Banks with compliance due by January 1st 2016 according to UniCredit has been a strong boost to data governance improvement
  - **and via SREP process:** where ECB is always extremely demanding on data quality and data completeness within analyzed processes