NPL SUMMIT 2019

Divani Apollon Palace & Thalasso

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NPLs

Basic Legal Frame, Developments & Trends

* Status as of 8.11.2019

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I. INTRODUCTION

Word of the Year 2018

Oxford Dictionaries

TOXIC !

1664 – first appearance in English

1911 – first appearance as an entry

1980 – widespread figurative use

2018 – interest in the word surges in various contexts: politics, the environment, society, social media and …

…TOXIC LOANS – NPLs !

II. BASIC BACKGROUND

1. Basel III – July 2013

Background: The International Financial Crisis

Legal Framework as of 1.1.2014

Regulation (EE) 575/2013

Directive 2013/36/EE - Law 4261/2014

The international financial crisis has led to the introduction of new banking rules.

Capital adequacy and bank liquidity:

- banks are required to maintain more capital in order to ensure smooth operation

- the minimum capital requirement ratio is increased

In order to deal with issues related to:

- funding
- reduced capital adequacy
- bank credit risk management

Various financial instruments were established

2. BASEL IV - 2016-2017

Changes to international banking standards

Regulation 2019 /630 of 17.4.2019

amending Reg. 575/2013 re minimum loss coverage for NPEs

resulting to increased minimum capital requirements

III. SECURITIZATION – GENERAL

“Red” – “Toxic” loans

They must be addressed – How?

Securitization of claims:

One of the most effective financial instruments

Main Law: 3156/2003

"On Bond Loans, Securitization of Claims and of Claims from Real Estate and other provisions", as in force.

Securitization of claims:

The transfer of trade receivables, due to sale,

from a “transferor” company (Originator) to a “transferee” company (Issuer),

combined with the issuance by the transferee and offer of bonds.

Bonds repayment is achieved:

a) with the income collected from the transferred trade receivables, and/or

b) with loans, credit agreements or financial derivatives.

More specifically, securitization is:

The transfer, by way of sale, of a company's trade receivables, whereby that company assigns assets to a special purpose vehicle (SPV)

The SPV then, on the basis of the securitized assets, issues marketable asset-backed bonds which are offered to investors…

… and through the offering of those notes, the financing is secured for

a) the SPV and

b) the Originator, receiving the consideration of the transferred claims

While the notes offered by the SPV are redeemed when the claims are settled.

IV. SECURITIZATION ESPECIALLY FOR BANKS

Securitization involves significant advantages

particularly for banks

since it leads to:

1. Increased capital adequacy:

Saving capital by way of reducing credit risk-weighted assets,

as the securitized loan portfolio is transferred to the SPV in exchange for liquid assets

2. Increased degree of asset liquidity:

Exchanging low liquidity assets (securitized NPLs) for cash,

which the bank can then use as it wishes to achieve additional returns

3. Increased return on equity:

achieving a higher turnover (more liquid assets, i.e. increased lending capacity),

therefore increased commission revenues and

keeping the interest margin as profit instead of using it to cover the credit risks

4. Effective risk management:

through the transfer of part of the lending portfolios to

investors and specialized servicing companies for loans and credits

Overall:

The banks improve their operation since they

- increase their capital adequacy
- draw liquidity
- pass the credit risk to third parties - investors

V. SECURITIZATION

2 CASE STUDIES – ATTICA BANK

Special features:

innovative operations given that they contributed both

- to the injection of capital to the bank and

- to the drastic reduction of non-performing loans

* Model structure followed thereafter

1. Orphan SPV

An SPV, based on the principles of exclusivity of purpose and independence, where:

- securitization is the exclusive purpose and

- there is legal and financial autonomy**:**

Independence of the securitized assets and

Protection from the bank lenders /

separation from the rest of the bank assets

“Orphan” SPV:

It belongs to an independent operator and is entirely separate from the other parties to the procedure (originator, servicer, trustee)

Key characteristics:

- separate accounting treatment and separate bank accounts

- the bank does not secure the obligations of the SPV

2. Sale and purchase of a junior note with immediate payment of price

Combination of orphan SPV model,
with the sale by the bank of a junior note for a price that is paid upon sale and treated as net TIER I profit

3. Passing the non-recovery risk to the investor

Uncollected loans are not returned to the bank as bad debts,

due to the true sale and de-recognition model

1. SECURITIZATION of €1,331.2m

June-July 2017:

Attica Bank securitized a non-performing loan portfolio

by transferring it to the Luxembourg SPV

ARTEMIS SECURITISATION S.A. (ASSA).

ASSA issued and transferred to the bank:

- A €525m A-Note (Senior Note) and

- A €806.2m B-Note (Junior Note),

which were secured by a legal pledge on the portfolio

ASSA assigned the management of the securitized portfolio

to the company

THEA ARTEMIS – SOCIETE ANONYME FOR MANAGEMENT OF LOANS AND APPROPRIATIONS,

which was set up by the bank (under Law 4354/2015)

The bank agreed to transfer to a company belonging to the preferred investor selected through an open tender (Aldridge EDC Specialty Finance):

a) 80% of the shares of the management company at their nominal value, and

b) the Junior Note issued, for an amount of €70m

Upon complection of the transaction which, based on its model, constituted a *true sale* of a non-performing loans portfolio and

after complying with the statutory formalities (approval by the Bank of Greece),

the bank was able to:

- de-recognize the portfolio and

- recognize a €70m profit, counted as TIER 1 in its capital

2. SECURITIZATION OF €700.5m

December 2017:

Attica Bank securitized a non-performing loan portfolio of approximately €700.5m to the Luxembourg SPV ABS METEXELIXIS S.A.

The SPV issued a €343,250,000 Class A note and a €357,250,000 Class B note, maturing in 2027

October 2018: 95% of the Junior Note was transferred to an investor (TOCU Europe II, S.a.r.l.).

Upon complection of the transaction which, based on its model, constituted a true sale of a non-performing loans portfolio and

after complying with the statutory formalities (approval by the Bank of Greece),

the bank was able to:

- de-recognize this portfolio and

- recognize a €47m profit, counted as TIER 1 in its capital

VI. SERVICING & SELLING NPLs

Law 4354/2015
imposed by the Third Program/Law 4336/2015
NPLs Servicing Cos

Basic Legal Frame:
Law 4354, BoG 118/2017 Act,
Legislation on lending, etc., Banks Code of Ethics,
Laws on SAs & Consumers

Servicing Companies:

special purpose companies

BoG licensed & supervised

No of Servicers:

21 [by 4 November 2019]

10 pending to be licensed by BoG

[Capital.gr 19.10.2019]

Total NPLs amount served:

17.448b /June 2019 &

31.8b approx. to be sold or securitized by 2021

[Bank of Greece & Capital.gr 19.10.2019]

VII. REAL ESTATE AS SECURITY

& ITS PROTECTION

1. The real estate security:

-Due diligence peculiarities

-Legal & land-planning discrepancies / cumbersome legal and land-planning actions

-Value assessment problems

-Time & cost issues

2. Liquidation:

11,999 successful auctions between Jan. & Sept. 2019

25,000 – 30,000 est. auctions by the end of 2019

[Capital.gr 11.10.2019]

3. Banks’ plans

Asset backed NPLs of approx. 11.2b
are in place to be sold /securitized by the end of 2019

[Kathimerini: 15.10.2019]

4. The protection legal regimes

4.1. Law 4605/2019

The new legal frame as from 30.4.2019

E-platform launched on 1.7.2019

[Special Secretariat for Private Debt Management]

Est. covering 180,000 debtors with 11b debt approx.

Est. half of the pending Katselis law petitions could fall within

[Kathimerini: 5.7.2019]

Scope:

Natural persons with debts to banks & the Depositories & Loans Fund

in default (90 days+) by 31.12.2018

Protection of main residence in Greece

Securitization, etc. does <u>not</u> affect process

<u>Not</u>, if Greek State guarantee or any previous restructuring, incl. a definite decision under the Katselis regime

Eligibility criteria:

Property value - up to 250,000 [or 175,000 if business loans incl.]
Annual family income - 12,500-36,000 depending on family status
Total debt: - up to 130,000 [or 100,000 if business loans incl.]
Total (immovables/cars) assets - up to 80,000 [if the debt above 20,000]
Total deposits, etc. - up to 15,000

Basic Formalities – Outcome:

Deadline: 31.12.2019 […extension open…]
E-application /platform [www.keyd.gov.gr] – automated checking
Temporary protection = no auction [from creditors' notification until court petition /2.5 months]

Monthly installments up to 120% of property's commercial value,
3m euribor + 2%
25 years (or 80-years of debtor's age)
Greek State's contribution 20%-50% reviewed annually
[cost 150-200m p.a. – Kathimerini, 25.6.2019**]**
Protection lost: if 3m in default

E-platform: Data of 1.7.2019 - 3.11.2019 [4m]:

- 29,895 users have initiated drafting the application
- 267 applications have been submitted & notified to the banks
- 56 proposals have been made by the banks
- [just] 10 proposals have been concluded

[Special Secretariat for Private Debt Management & Naftemporiki 7.11.2019]

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Pending changes to Law 4605/2019 [Draft bill filed on 4.11.2019]

- Extended coverage

- Procedural facilities

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4.2. Law 3869/2010
The "Katselis" law

Deadline for petitions expired: 28.2.2019

Ordinary hearings fixed many years after the submission of the petition to the court (ranging from 7 months to 6 years)

220,000 petitions valued 17b approx.

89,500 petitions pending - Q1 2019

[FPRESS: 12.6.2019 & The Management of natural persons' over-indebtedness - Report on statistical results, March 2019]

Decisions issued:

- 45% for the banks
- 55% for the debtors

[Data by June 2019]

Trend: Increased decisions for the banks

Problem: The strategic non-payers

A platform was launched on 1.11.2019
for the cross-checking
of all Katselis Law pending petitions

Heads of the 4 systemic banks panel 19.6.2019:

The Katselis law "cost" around 20% of the banks' NPLs

[Newsit 20.6.2019]

VIII. NPLs GENERAL SCHEME

HFSF [Hellenic Financial Stability Fund] - Ministry of Finance Proposal of 2018 – 2019:

“Hercules Project”
Asset Protection Scheme /APS

Status [6.11.2019]:

- Cleared by DG Comp [10.10.2019]

- Under review by SSM

Basics:

-securitization via

-transfer of 30b NPLs to an SPV

-with a Greek State guarantee of up to 9b

Hercules’ six steps plan:

**Step 1: Bad loans will be securitized in three tranches:
senior, mezzanine, if necessary, and junior.
The state guarantee will only apply to the senior part.**

**Step 2: The senior and the mezzanine will have a floating coupon and a flexible redemption structure to pass on cash flows from the securitized NPL portfolio.
Coupons will be paid quarterly or annually and will be based on the remaining notional value of the notes.**

Step 3: The guarantee can be activated only if the rating of the senior tranche is not lower than a “BB-” and

it will become effective only after the bank has sold at least 50% plus one share of the junior tranche.

The junior and the mezzanine notes can’t be bought by the state or state-related bodies or companies.

Step 4: Upon securitization, the bank will appoint an independent servicer to work-out the underlying NPLs of the securitization structure.

Step 5: To manage potential liquidity mismatches between cash flows from the underlying NPL portfolio and contractually obligatory coupon payments on the senior and the mezzanine notes, the securitization structure will have a liquidity buffer sufficient to achieve the minimum required rating.

Step 6: The initial appointed NPL servicer can be replaced if the state guarantee is called upon or if, after two consecutive interest payment dates, it has recovered less than initial projections.

[Bloomberg /Euro2day: 15.10.2019]

The law on Hercules is expected to introduce:

- A monitoring trustee;

- A Collecting Transactions Data authority;

- Mechanisms for the servicers' operation, incl. incentives / "penalties" for not meeting targets & a "Credit Registry";

- Probably, tax incentives for investors.

[Capital.gr 5.11.2019; Kathimerini 24.10.2019]

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Pending Approval:

European Central Bank's (ECB's) Single Supervisory Mechanism (SSM)

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Basic pending Issues:

- Zero-risk weighting on a securitization backed by a state that does not have an investment grade
Without a zero-risk weighting, too costly for banks

- Banks' participation

[businessdaily.gr 25.10.2019 & 4.11.2019; naftemporiki 7.11.2019]

Time frame:

Efforts for a law by end of November 2019

but currently uncertain

VIX. BANKS OWN ACTIONS ON NPLs

Overall:
Planned NPLs decrease by 53b
to a 13% NPE ratio
in 2019 – 2021

[Capital.gr 19.10.2019]

Heads of the 4 systemic banks panel 19.6.2019:

Banks' prime scope:
a) speed up sale /assignment of NPLs
b) esp. NBG: NPLs rescheduling

[Newsit 20.6.2019]

Piraeus Bank [ongoing transactions]:

- Sale of

Iris - 0.7b unsecured business & consumer loans &

Trinity - 0.3b secured business loans

- Securitization of

Phoenix - 2b residential loans &

Galaway – 1b secured business loans

Eurobank [ongoing transactions]:

- Securitization of
Cairo – 7.5b residential & business loans secured by 73,000 properties

Alpha Bank [ongoing transactions]:

- Securitization of
Orion 1.9b /36,000 residential loans

- Sale of
Neptune – 1.8b secured business loans

NBG [ongoing transactions]:
- Sale of
Leo – 0.3b secured maritime loans &
Icon – 0.9b secured business loans

- Securitization of
3b approx. residential loans

[mononews.gr 5.11.2019, Kathimerini 15.10.2019]

X. LATEST REPORTS ON NPLs STATUS

1. European Banking Authority's (EBA)
2nd thematic Report on NPLs (8.11.2019)

- Total NPLs decrease to EUR 636b /NPL ratio 3% (June 2019)

- Greece the highest NPL ratio = 39.2%
Cyprus follows = 21.5% & 5 other countries above 5%

Note: Less efficient legal frameworks &
Thin secondary NPL markets

2. The 4th EU Commission Report of 12.6.2019 re status by 30.9.2018

GR 43.5% NPLs of the total (down 3% approx. from 2017)

-13 times the EU average of 3.3% and

-2 times above the 2nd/Cyprus=21.8%

3. IMF First Post-Program Report of 12.3.2019

Among the major risks of GR economy, the high NPLs

Concerns & urgent need for reduction by private-sector instruments

4.1. BoG - Monetary Policy Report 2018-2019 (July 2019) [Status end of March 2019]

- NPLs amounted to €80 billion, down by about €1.8 billion from end-December 2018. Reduction mainly driven by write-offs (€0.9 billion) & loan sales (€0.8 billion).

- The ratio of NPLs to total loans remained elevated at 45.2%.

- Overall, the recoveries from active NPL management remain limited.

4.2. of the Greek Financial System Report (June 201BoG: - Overview 9)

- End of 2018: NPLs 81.8b = 45.4% of the total (down by 12.6b vis-à-vis 2017)

- End of 2021: Banks plan to reduce NPLs below 20% to be 6 times the EU average

5. EU Commission
3rd Enhanced Surveillance Report
(5 June 2019)

Very slow improvement /delays re NPLs:

E-auctions slowed down

Settlement of pending cases under the Katselis Law

Operation of the new e-platform re main residence protection petitions enacted in April 2019

[Note: End of law by 31.12.2019]

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Personal insolvency regime restructuring

Speed up BoG & HFSF proposed general schemes

Greek NPLs as of end of 2019 = est. 41.2%, above 12 times the EU average of 3.2%

[euro2day 5.6.2019, insider.gr 5.6.2019]

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6. ASHURST /London - A Global NPL Perspective Report of March 2019

- Possibility to invest in Greek NPLs within the next 2 years: 46% of investors, second after Italy (51%)

- Already invested in Greek NPLs in the last 2 years: 39% of investors, second after Italy (43%)

7. MORGAN STANLEY Report of 4.11.2019

Hercules' plan is expected to help clear the banks from NPLs amounting to 22b in 2020 &
reducing the NPE ration to 23% (from 36% in 2019).

[Kathimerini: 5.11.2019]

XI. RECENT LEGISLATIVE ACTIONS

1. EU Council Position on Secondary Markets for NPLs (of 27.3.2019)

Proposed Directive to harmonize rules on how non-credit institutions can buy credit agreements from banks

-to remove obstacles to such transfer

-to simplify & harmonize authorization requirements for credit services across the EU

-to maintain the protection of borrowers /consumers rights

2. EU Directive 2019/1023 of 20 June 2019

-preventive restructuring
-discharge of debt
-increased efficiency of procedures
-amending Directive (EU) 2017/1132

3. New legislation expected - 1 /2

- The APS Scheme - Hercules Law

- Tax incentives for investing to the Hercules scheme

- Amendments to Law 4605/2019
  Expansion of coverage and procedural improvements

3. New legislation expected - 2 /2

- NPLs Secondary Market

- Insolvency /Bankruptcy changes re individuals & businesses

NOTE: World Bank "Doing Business 2020" Report
Greece 79 out of 190 countries
Esp. poor performance in:
real estate transfer - judicial proceedings - bankruptcy law

XII. GENERAL CONCLUSIONS

Great challenges - High prospects
Huge demand for reformation within a short time
Complex legal regime - further developments to come
Flexibility & clever planning needed

THE MOTTO

Live your NPL Myth in Greece, today!

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Many thanks

for your attention

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