



Ms Danièle Nouy

Chair of the Supervisory Board of the
Single Supervisory Mechanism
European Central Bank
60640 Frankfurt am Main
Germany

28 November 2017

Dear Chair,

Non-performing loans – Addendum to the ECB Guidance

I write to you regarding the proposed “Addendum to the ECB Guidance to banks on non-performing loans: Prudential provisioning backstop for non-performing exposures” (hereinafter referred to as “the Addendum”), which specifies quantitative supervisory expectations for minimum levels of prudential provisions for new non-performing loans (NPLs).

BusinessEurope has supported reinforced prudential rules as financial market stability is fundamental for the economy. The new rules have restored confidence in financial institutions and made them more resilient. At the same time, bank lending came under pressure and there is a risk that as economic growth picks up banks will be unable to meet companies’ funding requirements on the necessary scale.

In this context, we are concerned about the potential impact of the Addendum and the fact that it, if confirmed, would lead to higher capital requirements than those set by EU law and major changes in the way banks finance businesses. Apart from the fact that this raises questions about the legality of such action, it would also further increase financing problems. The Addendum – which is not supported by any previous impact analysis – proposes changes that may have different negative effects, such as shifting banks’ businesses and their medium and long-term industrial plans; and curbing financing channels for enterprises, particularly small and medium-sized ones, which still rely heavily on bank lending.

In particular, we are worried about the impact of the provision of the Addendum according to which banks should reach a coverage rate of 100% of the value of NPL in 2 years for unsecured loans and 7 years for secured ones. This increase of coverage ratio (which appears to be in conflict with IFRS9) is regardless of the value of collateral and will make both secured and unsecured credit more expensive.

Even though the Addendum specifies that these measures should be applied after a case-by-case assessment (which would increase uncertainty), we believe, similar to



the European Parliament, that they will be interpreted as mandatory. As such, it will penalise the banking sector as a whole and, by extension, all bank financing for businesses.

Moreover, one of the major effects of this Addendum will be the profound change in the banks' approach to risk management. Especially for SMEs and corporates, banks will systematically ask for collateral in order to avoid the 2-year spectrum of 100% prudential provisioning. The release of the Addendum at the beginning of a recovery phase would represent a restrictive measure conflicting with the expansive monetary policy by the ECB itself.

This could also have a relevant impact on the secondary market of NPLs whose performance – also thanks to the ECB action and to measures introduced by several European Governments – has started to function more satisfactory in the last months. The European Banking Federation notes that the non-performing loans ratio of the EU banking system has been significantly reduced via banks' internal efforts, from 7.3% in 2015 to 4.5% in June 2017 also thanks to the sale of NPLs to third parties. BusinessEurope is concerned that the introduction of new and severe provisions could negatively affect the market price of NPLs thus creating unintended impediments to the development of a secondary markets for NPLs or resulting in significant reductions in banks' capital.

Whilst we appreciate that all comments received will be carefully considered before the draft Addendum will be finalised, we believe that the deadline proposed for the introduction of such fundamental changes is too early. It is necessary not only to change the timing of the new NPL guidance, but also to avoid the introduction of standardised restrictive and potential retroactive rules. In order to sterilise risks in the European banking sector, the differences between EU countries' banking systems should be considered to ensure balanced actions that pursue financial stability whilst encouraging growth.

Risk reduction measures can also lead to adverse effects and increase systemic risk. It is therefore essential that a comprehensive impact assessment of the proposed changes is carried out before validating and finalising new rules to ensure that they function effectively, encourage growth and prevent damage to businesses in the wider economy.

Yours sincerely,



Markus J. Beyrer