



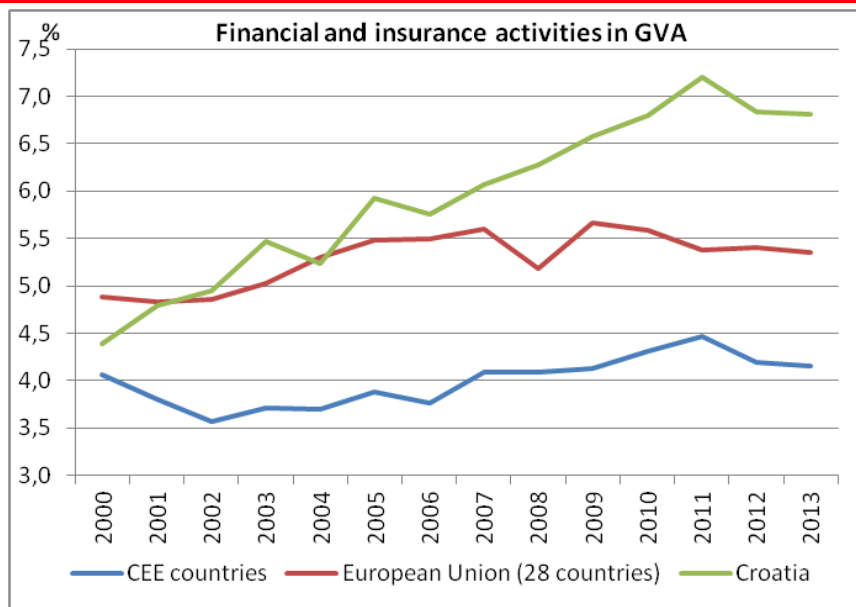
CROATIAN NATIONAL BANK

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# NPL recovery and resolution

February 2015

# Croatian banking in the last six years

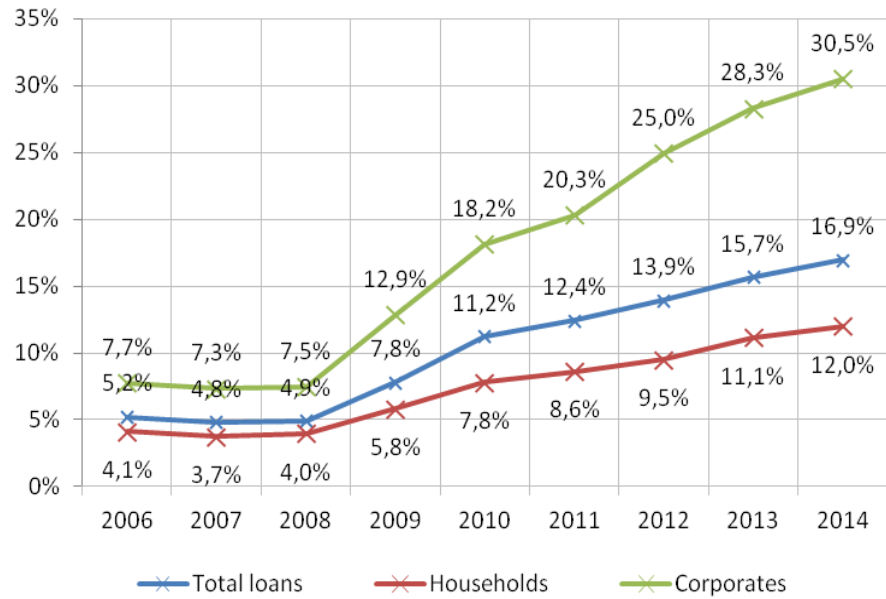


- banking in Croatia in the last 6 years – summary:
  - maintaining profitability
  - strong capital position
  - moderate deleveraging

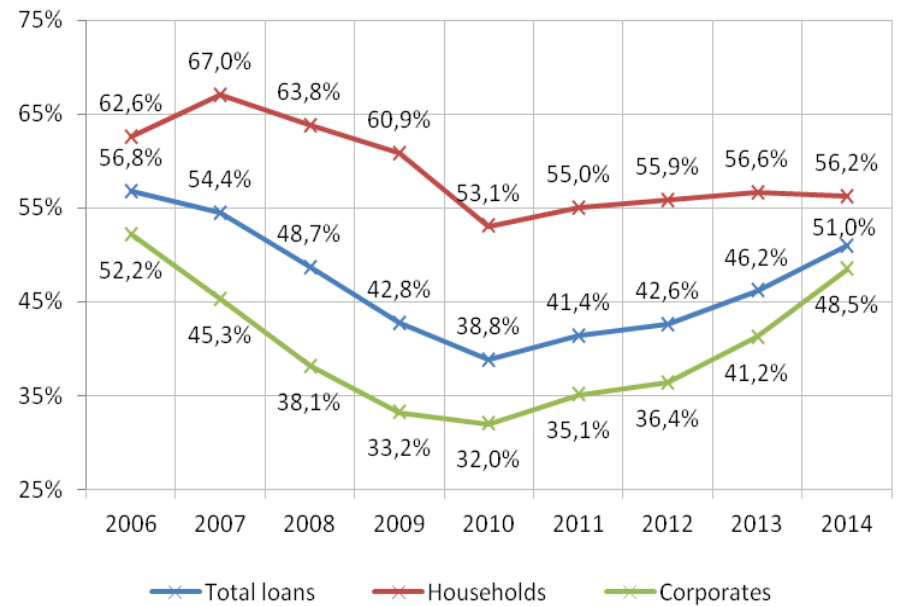
- no new loans
- lack of active strategy in dealing with NPLs
- banks create 6% of GDP, but recently have a very limited influence on real sector
- banking avoided crisis, but could not avoid consequences of depression

# NPL development

## NPL Ratio

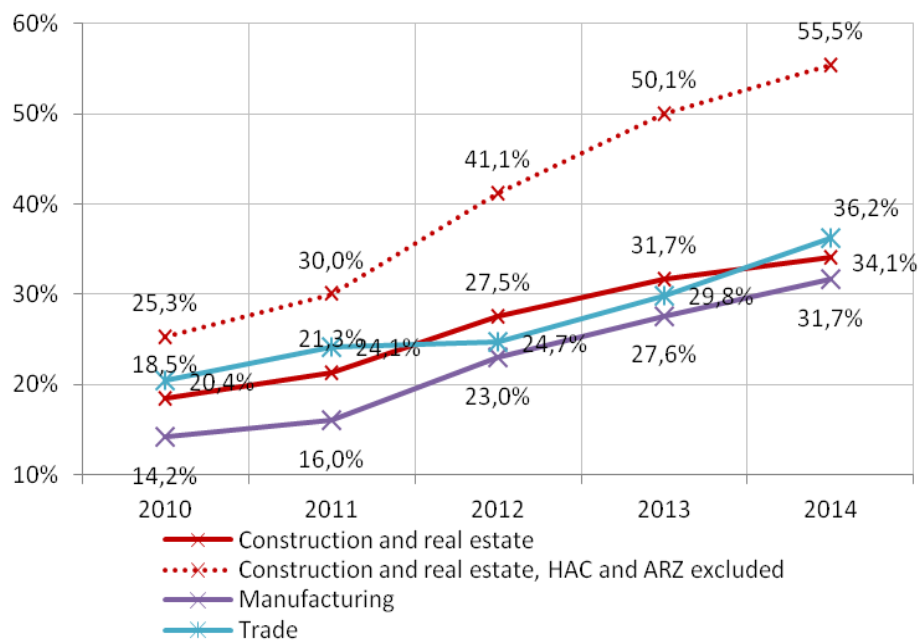


## NPL Coverage

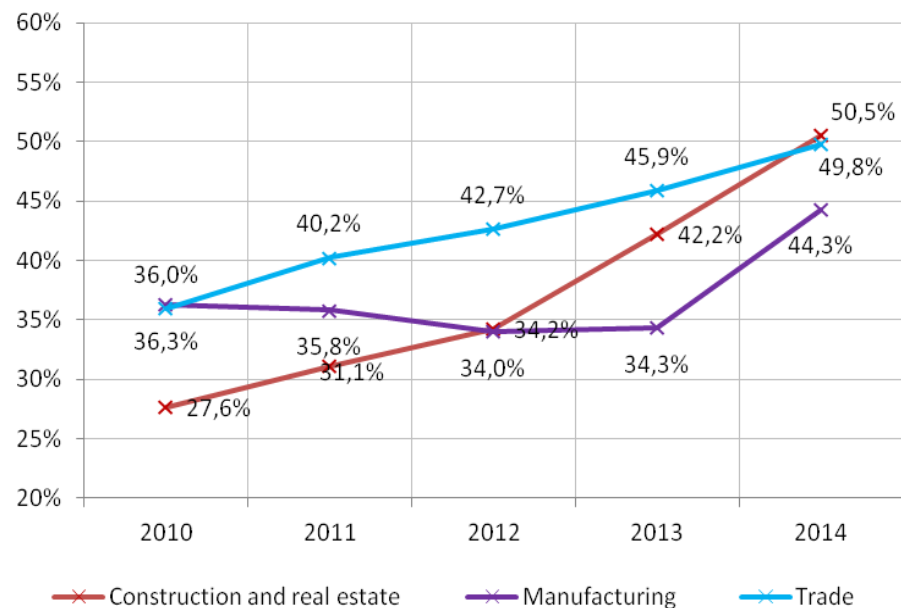


# Most critical segments (1): corporate sectors

NPL Ratio, corporates

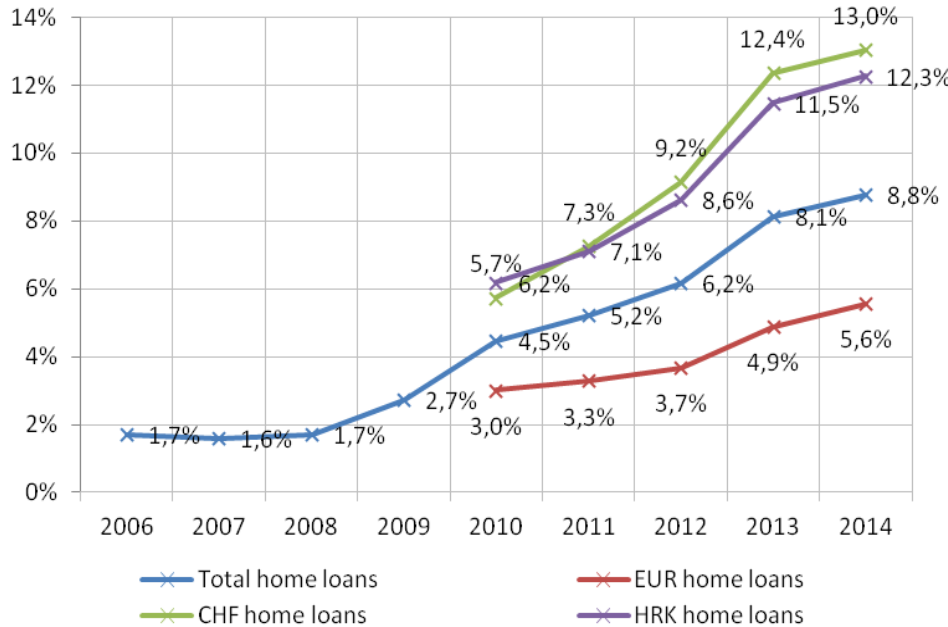


NPL Coverage, corporates

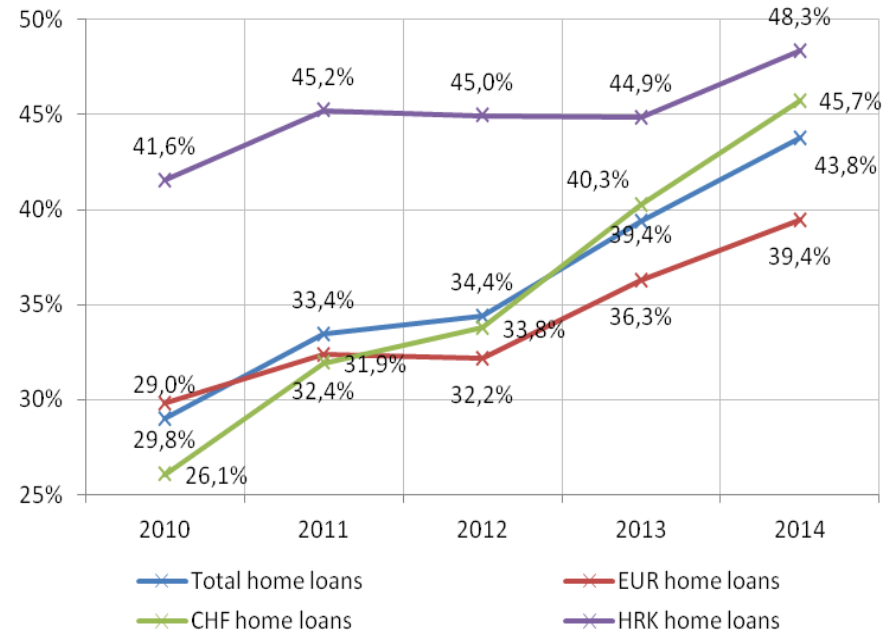


# Most critical segments (2): home loans

NPL Ratio, home loans



NPL Coverage, home loans



# Risks created by NPLs

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- ❑ carrying value of NPLs presents danger to the capital position and P&L of banks
- ❑ far predominant part of NPL value is accounted by the application of **IAS 39** on **pledged/mortgaged real estate units**
- ❑ the risk present in the NPL portfolio is therefore (apart from the credit risk) the sum of **legal risk** and **real estate market risk**
- ❑ effective **resolution** or full provisioning of NPLs removes risk
- ❑ repossession of real estate without selling it to a third party isn't an effective resolution
- ❑ "waiting it out" is not an effective solution

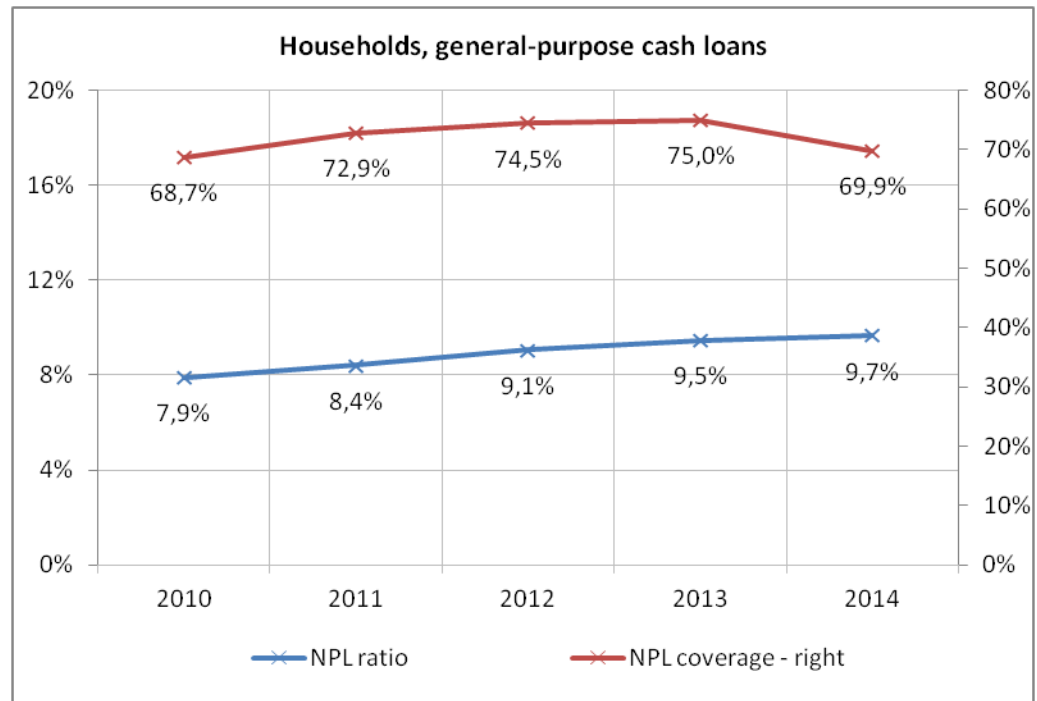
# NPL resolution – corporate – experience

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- ❑ 2H2014, CNB's **bank survey** regarding exposures that were or still are covered with a mortgage on a commercial real estate – data on legal actions taken in order to collect a claim by activating the collateral, 01/2008 – 08/2014
- ❑ repossession is initiated on 3.579 commercial properties
- ❑ on 618 properties (**17%**) repossession is realized, with a collectability ratio (buying price/evaluated price when granting a loan) at 55%
- ❑ 52% of realized properties taken over in the lenders' balance sheet → can't be considered real collection
- ❑ 48% of realized properties (8% of initiated foreclosures) sold for cash (real collection)
- ❑ collection by foreclosing on commercial properties: slow, uncertain, low liquidity, low collectability
- ❑ IAS 39 forecasts based on very different assumptions

# NPL resolution – consumer loans

- consumer loans are "resolved" by provisioning





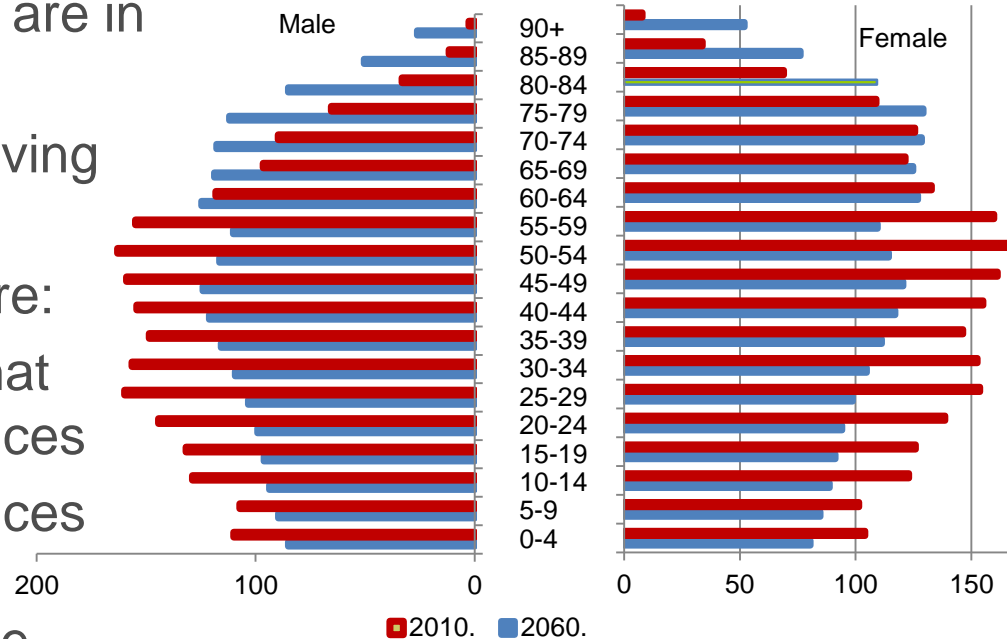
# NPL resolution – housing – experience

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- ❑ housing NPLs could be attributed to loans nominated in CHF and to vintages created in 2007 and 2008
- ❑ too optimistic credit approval policies were present across the market and final pre-crisis vintages incorporate: *high L/V* and *annuity/income ratio*, together with significant part of portfolio approved in a *non-correlated currency*
- ❑ debtor having his housing unit repossessed by a bank generally has no means to acquire a new one and repay the loan "with recourse"; if collection is attempted, costs of such proceedings could likely exceed the collected amount
- ❑ banks are competent institutions and if they had consistently used proper professional standards, the problem would be much smaller

# NPL resolution – housing – macro-overview

- certainty about **commercial viability** of a flat is high – as long as tenants are in it
- completing repossession and moving tenants out creates uncertainty!
- census 2011 – in Croatia there are:
  - 2.246.910 housing units, of that 1.912.901 permanent residences
  - 1.496.558 permanent residences are inhabited by 1.517.249 households, while 342.349 are temporarily uninhabited and 73.994 are abandoned
  - only in Zagreb there are 69.870 temporarily uninhabited flats & houses



In future, without significant immigration, demand for housing should decrease

# Conclusion

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- ❑ the major issue concerning resolution is the corporate loans resolution; they are by amount and macro-economic impact a dominant problem
- ❑ consumer loans are "resolved through provisioning" and they represent no risk
- ❑ CHF-denominated housing loans require alleviation of financial pressure on debtors
- ❑ EUR-denominated housing loans are performing and have no acute resolution issue
- ❑ problems facing effective resolution:
  - low liquidity of real estate
  - high legal cost/uncertainty connected with foreclosure
  - PR aspect of repossession
  - "underwater" position of significant part of clients with CHF-denominated loans
  - regulatory & tax obstacles for application of haircuts