EBCI Vienna Initiative

Debt Restructuring and NPL Resolution

The private banks´ restructuring initiative

Workshop convened under the Vienna Initiative 2.0

Vienna, 23 September 2014

ERSTE Raiffeisen Bank International UniCredit

Perspectives from Erste Group in Croatia

Macroeconomic Framework Croatia

	2010	2011	2012	2013	2014f	2015f	2016f
Real GDP growth in %	-2.3	-0.2	-2.2	-0.9	-0.5	0.0	0.8
Private consumption growth in %	-1.3	0.3	-3.0	-1.3	-1.0	-0.2	0.5
Fixed capital formation in %	-15.0	-3.4	-3.1	-1.3	-2.4	1.3	2.5
Nominal GDP in HRK bn	323.8	328.7	327.0	326.8	325.5	327.5	335.0
GDP per capita (EUR)	10,101	10,289	10,117	10,037	9,916	9,913	10,128
Unemployment rate in % -ILO, average	11.8	13.5	15.8	17.3	18.0	18.5	18.8
CPI inflation, average in %	1.2	2.3	3.4	2.3	0.2	1.2	2.0
Current account balance as % of GDP	-1.1	-0.9	-0.1	0.9	1.0	1.4	1.0
Net FDI as % of GDP	1.1	2.4	2.5	1.6	1.4	1.9	2.8
Foreign debt / GDP in %	104.6	104.2	103.5	105.7	107.1	108.5	109.3
Budget balance (% of GDP)*	-6.4	-7.8	-5.0	-4.9	-5.5	-4.5	-4.0
Public debt (% of GDP)	44.9	51.9	56.0	67.4	73.4	77.4	80.3
HRK/EUR, average	7.29	7.43	7.52	7.57	7.64	7.68	7.69

*ESA95

Source: MoF, CNB, CBS, ESB

- Economic outlook remains challenging as GDP is expected to stagnate also in 2015 owing to the weak investments prospects, deteriorating external demand prospects with EU growth outlook taking a geopolitical hit. Prolonged austerity efforts would remain a drag to consumption performance.
- Labor market trends remain adverse with no meaningful improvement in 2015-16 expected. Inflation is seen accelerating from low levels in the mid-run.
- External position remains boosted by the current account surplus, while refinancing operations are seen remaining fairly smooth. Accommodative ECB stance supports public financing prospects, while private sector continues to gradually deleverage.
- Fiscal risks remain pronounced given the divergence from EDP set consolidation path – consolidation efforts remain yet largely inadequate and translating into public debt further trending up.

Pre-bankruptcy settlement - concept

Restructure or “go bust” – how do Pre-bankruptcy settlements work:

- safeguard procedure for debtor, process of 120 days (prolongation +90 days added in July ‘13)
- administrator – examines claims and follows up payments through accounts
- settlement in front of a council of Ministry of Finance, courts only confirm later
- pre-bankruptcy creditor – unsecured or waiving collateral, voting rights
- separate rights creditor – secured, waiving cash flows, no voting rights
- 70% haircuts allowed, 2/3 majority creditor votes needed for acceptance (1/2 in all creditor groups)
- If not accepted – immediate filing for bankruptcy

Problems:

- Currently V 4.0 (four) of the Pre-bankruptcy Act since 2013
- Process mainly controlled by Debtors
- Limited (quality) advisor resources → DO IT ON YOUR OWN AND OPTIMISE
- Best practice? BE CREATIVE, QUICK, NEGOTIATE, ALLY (case by case approach)

Pre-bankruptcy settlement - results

Restructuring with a new legal instrument – Pre-bankruptcy settlement

- Corporate illiquidity within Croatian economy – 71.874* entities with blocked accounts in the amount of HRK 56,1 bn (EUR 7,4 bn) in 2012

- Pre-insolvency numbers October 2012 – February 2014

    - 6.105 companies already went into the process

        - 46.614 employees, HRK 54,9 bn debt (EUR 7,2 bn)

        - 652 large companies, HRK 49,8 bn debt (EUR 6,6 bn)

    - 4.831 completed – out of that 1.550 accepted (HRK 26,4 bn debt), 795 confirmed by courts (HRK 15,8 bn debt), 1.274 still in progress

Basically: If you are dealing with restructuring in Croatia, you are usually dealing with pre-bankruptcy settlement

* as of 31/12/2013

Key challenges in managing Workout in Croatia

- ❑ Frequent changes of legislation (e.g. Pre-bankruptcy legislation introduced in 2013 – 4 alterations up to now; enforcement law – 2 alterations in 2 years; bankruptcy law amendments)
- ❑ Court system still slow and inefficient (esp. bankruptcy law)
- ❑ Slowdown of liquidation process by liquidators and ex-owners of bankrupt companies
- ❑ Lack of Equity: Restructured companies often lack fresh capital for stable going-concern. Private equity funds not eager to invest; restructured companies are mostly SME
- ❑ Write-offs are generally taxed: although Ministry of Finance introduced some changes in order to improve tax deductibility of write-offs and thus speed up workout strategies, many limiting issues remain: as a result NPL sales remain difficult compared to many other countries esp. in retail segment - lower level of activities of collection agencies like in CEE; Retail NPL level in Croatian FIs remains higher than in comparable CEE countries mainly due to unsold NPL stock.
- ❑ No existing cooperation framework between creditors (although attempts made) – a lot depends on individual good contacts between financial institutions

Perspectives from Raiffeisen in Serbia

Roland Wass, Deputy Chairman of the Managing Board/CRO/CFO

Raiffeisen banka a.d. Belgrade

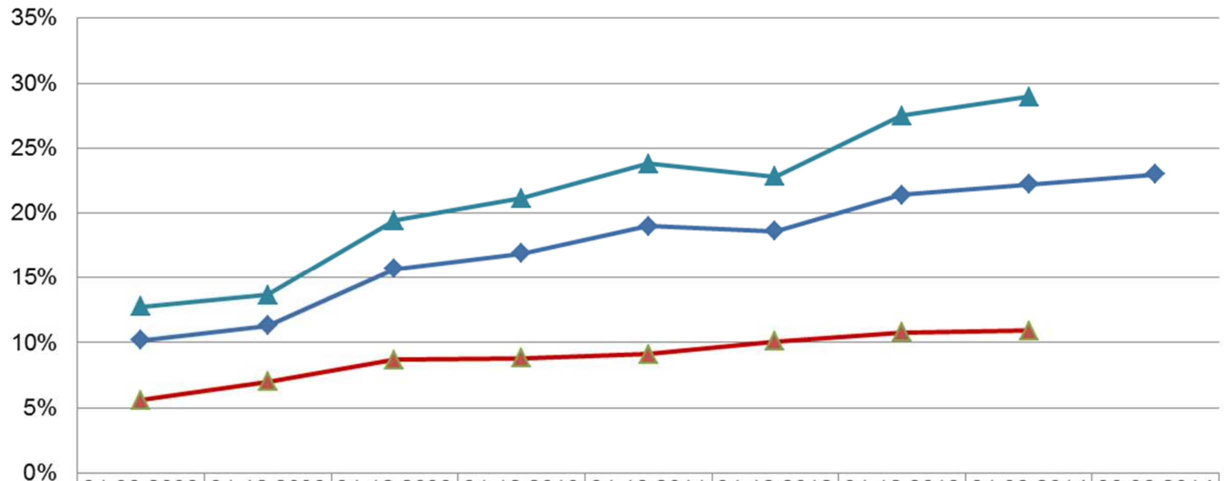
Raiffeisen Bank International

Situation with regards to NPLs in Serbia

NPL development last 5 years (by NBS standard)

Is this the whole picture?

NPL Ratio - Banking Sector



	31.09.2008	31.12.2008	31.12.2009	31.12.2010	31.12.2011	31.12.2012	31.12.2013	31.03.2014	30.06.2014
Retail, Banking Sector	5.6%	7.0%	8.7%	8.8%	9.1%	10.1%	10.8%	10.9%	
Non Retail, Banking Sector	12.8%	13.7%	19.4%	21.1%	23.8%	22.8%	27.5%	28.9%	
Total, Banking Sector	10.2%	11.3%	15.7%	16.9%	19.0%	18.6%	21.4%	22.2%	23.0%

Situation with regards to NPLs in Serbia

- What this situation means for Serbia:
  - banks have less appetite for new financing → impact on growth in Serbia
  - financings are more expensive as costs for NPLs have to be covered
  - slow NPL resolution means "dead assets"
  - bad overall view on country, potential impact on Foreign Investments

Why did it come that far?

- ❑ Overall bad economic environment - deep crisis (which hit a country in transition)

- ❑ Wrong investment and financing decisions both from client and bank

- ❑ Why wrong decisions?

    - lack of better knowledge both banks and clients
    - too big growth and market share expectations before the crisis

- ❑ Special Serbian topic: blocking of accounts

What has been done in the near past in order to tackle the situation?

- Regulatory support:

  - NBS allowed recovery from NPL not only for 1. restructuring (as it was previously), but also for Voluntary Financial Restructuring and Pre-packed reorganization plans
  - non-financial institutions became eligible buyers of financial debts

- Legal changes:

  - abolished tax on write-off
  - new Bankruptcy Law (banks were involved in the creation of this Law)

What can we do to solve the situation quicker?

- Behavioral changes - guidelines for better cooperation between banks with regards to problem solving

- Legal changes
  - Change of Mortgage Law (after sale of assets all encumbrances to be deleted)
  - Change of Law on Pledges (to have possibility to sell under estimated market value by prescribing additional discounts for first and second sale)

- Administrative changes
  - To accelerate the work of the Court and Cadastre

- Private market for distressed assets has to be developed

- Alignment NBS/IFRS rules for provisions and NPL definition

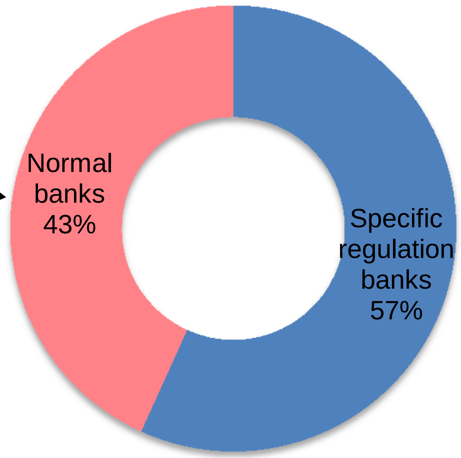
Perspectives from UniCredit in Slovenia

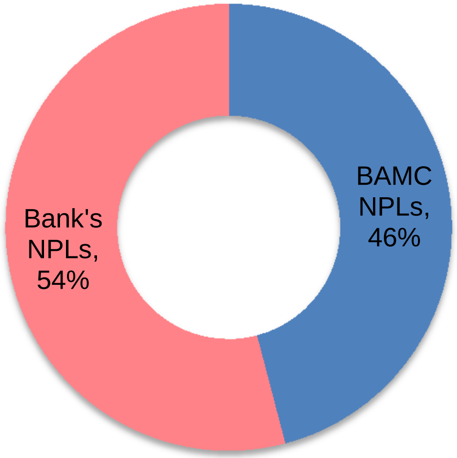
Damijan Dolinar, CRO, Unicredit Banka Slovenija d.d.

Some figures

Banking sector, 30.6.2014	
Total Assets	EUR 39,0 bn
Loans to customers	EUR 23,3 bn
Equity	EUR 3,9 bn
Impaired loans ratio	**15,3%**
Impaired loans ratio corporates	**23,3%**
BAMC gross loans	EUR 3,3 bn

Source: Bank of Slovenia, BAMC





GDP level (2013) and growth rates (2014-16)

	2013	2014	2015	2016
GDP	EUR 35,3 Bn	0,5%	0,7%	1,3%

Source: UMAR

Toolkit has been renewed recently

Tool	Update
Bank principles on restructuring NEW (Good old out of court agreement)	▪ Slovene version of London rules and Vienna rules ▪ Defines principles and process ▪ Absolute priority rule ▪ Equal treatment
Preventive restructuring/pre-insolvency proceeding NEW	▪ Intended for borrowers not yet insolvent, but likely to become so in a year ▪ Runs outside of compulsory settlement procedure. ▪ Carve out of non-financial debt ▪ Cram down of dissenting creditors
Compulsory settelement RENEWED	▪ Special rules for systemically important companies ▪ Enhanced rule of absolute priority ▪ Increased flexibility in starting it ▪ New restructuring measures added (e.g. restructuring of collateralized exposure)

Obstacles to more effective restructurings

REGULATORS, STATE

- Difficulties in including tax authority exposure
- Limitations of banks under "specific regulation"
- BAMC and its workload
- Skills and incentives of bankruptcy managers
- Regulatory reporting pack of limited use

BANKS

- Limited technical competence
- Limited people and negotiation skills by restructuring managers
- Obsession with rules rather than content
- Limited evidence of new money and guarantees
- Principles don't stick yet entirely

But some cases worked. How did they look like?

1. Awareness, skills and readiness to cooperate by borrower's top management.
2. Proper financial, legal and other advisors to the retructuring.
3. Bank coordination done by a reputable bank with skilled and senior staff.
4. Participating banks represented by senior staff.
5. Patience, knowledge, skill, and empathy among players.
6. Some source of fresh money from somewhere.
7. There was TRUST!