Block 2A
Focus on Greece and Cyprus
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NPEs – Hot Topics /Greece:

- Securitization (review)

- The example of Attica Bank (special features: orphan SPV, true sale, de-recognition)

- The BoG proposal for NPEs (November 2018)

- Developments

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I. INTRODUCTION

An extremely hot issue!

Why ?

Word of the Year 2018

Oxford Dictionaries

TOXIC !

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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 – NPEs !

II. BACKGROUND IN BRIEF

Basel III – Regulatory Framework (July 3013)

Legal Framework as of 1.1.2014

Regulation (EE) 575/2013

Directive 2013/36/EE – Law 4261/2014

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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

“Red” – “Toxic” loans

They must be addressed – How?

Securitization of claims:

One of the most effective financial instruments

III. SECURITIZATION IN GENERAL

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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.

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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. MAIN SECURITIZATION ADVANTAGES 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. CASE STUDIES – ATTICA BANK

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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

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 - 2017

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 - 2017

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. THE BANK OF GREECE (BoG) REPORT-PROPOSAL OF 22.11.2018 FOR THE BANKS’ NON-PERFORMING EXPOSURES (NPEs)

Transfer to an SPV

- of significant part of the banks’ NPEs (€40 bil.),

- along with part (€7.4 bil.) of the deferred tax credit against the Greek State (the State) which are booked on systemic banks balance sheets,

at net book value (net of loan loss provisions).

The amount of the deferred tax credit to be transferred will match additional loss, so that the valuation of these loans approach market prices.

Legislation will be introduced enabling to transform the transferred deferred tax credit into an irrevocable claim of the SPV on the State, with a pre-determined repayment schedule.

To finance the transfer:

the SPV will proceed with a securitization,

and three classes of notes will be issued: senior, mezzanine, junior equity.

The lower class of notes (junior equity) will be subscribed by banks (each participating by no more than 20%) and by the State.

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Valuation of loans to be transferred by independent third parties

The final structure of the transaction

(including the tranches of the three classes of notes)

will be determined by the arrangers, subject to market conditions

It is anticipated that investors will absorb part of the upper class of securities (senior) and a large portion of the intermediate part (mezzanine).

The ability to absorb additional losses arising from the participation of the State (through the transformation of the deferred tax credit into an irrevocable claim of the SPV) is considered to significantly enhance the probability of repayment of the senior bond classes (senior, mezzanine).

Any excess value will be distributed to the State and to the banks through participation in the lower class of notes (junior).

The scheme will be managed exclusively by private investors, i.e. servicing companies for loans and credits,

with a separation of transactions and management per asset class

(business, mortgage, consumer loans, etc.)

Competitive process of manager appointment

Management framework in line with best international transparency and supervisory practices

Before completion of the transaction,

banks are expected to proceed, in consultation with the supervisory arm of the European Central Bank,

to a restatement of targets for NPE reduction, with the ultimate goal of achieving a single-digit ratio within three years.

Pending Issues - Approvals

Single Supervisory Mechanism– SSM

European Central Bank - ECB

D G Comp – state aid question

[also on the previous EFSF proposed scheme]

Objections - Comments

Morgan Stanley – transfer price

Goldman Sachs – impact on system

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Bloomberg – one-way the prompt solution

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UBS – completion S1 2019, implementation +9 months,

if it goes ahead, no new bank recapitalization will be required,

but there are various risks: political, international climate, regulatory framework, immediate liquidity needs, etc.

The participation of the four systemic banks is assumed

However, in the meantime, separate plans:

- Eurobank (Pillar – €2 bil., Grivalia Properties – €7bil.)

- Piraeus (Recoveries Business Unit/RBU to Cerberus Capital)

- Alpha Bank (2 portfolios of €1.5 bil. and €2 bil.)

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Many thanks

for your attention!