BANK GOSPODARSTWA KRAJOWEGO

European Association of Public Banks
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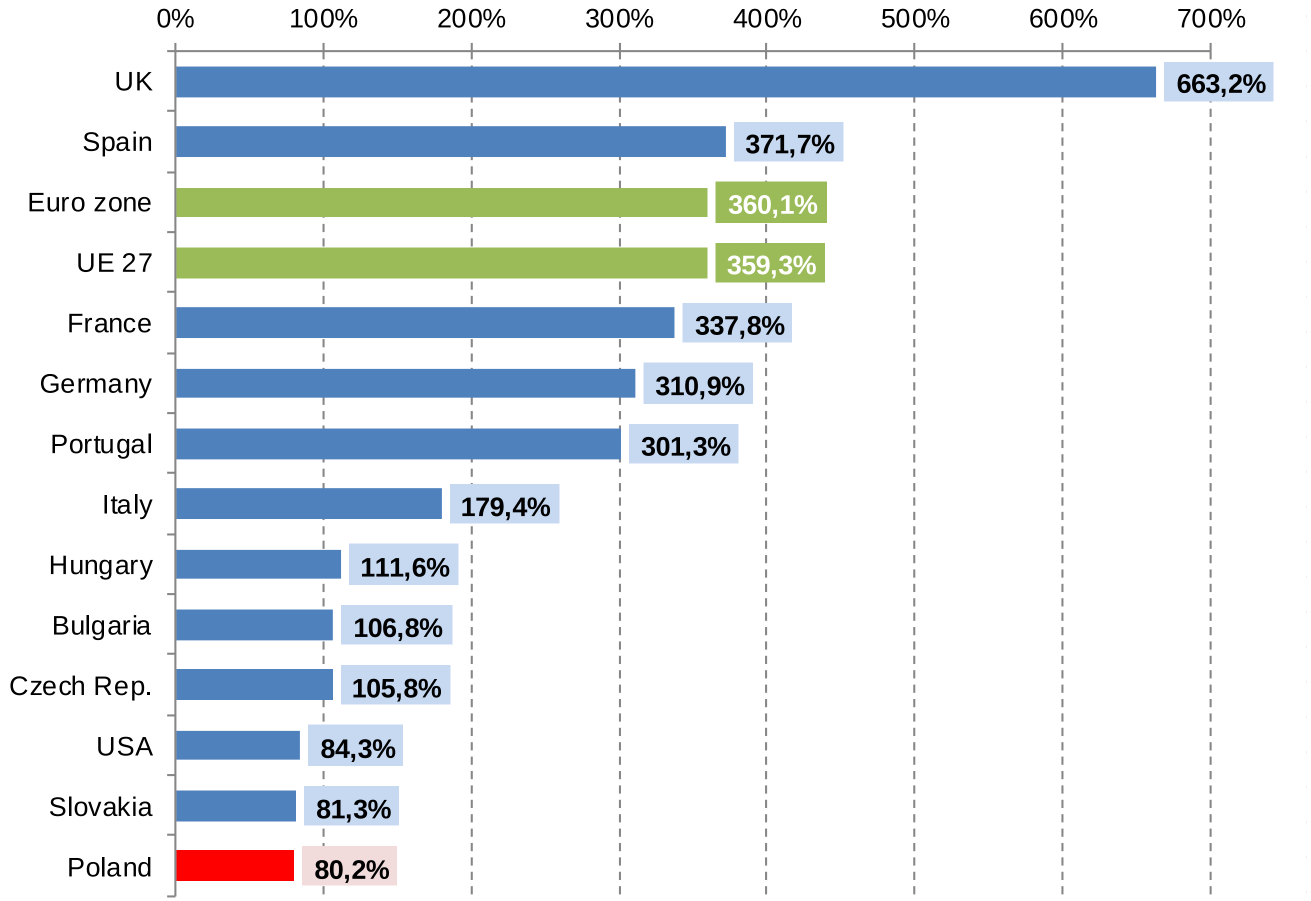
The Polish Banking Sector.
Selected European Regulatory Reforms

Jerzy Pruski

Warsaw, 11.06.2013

Banking sector size

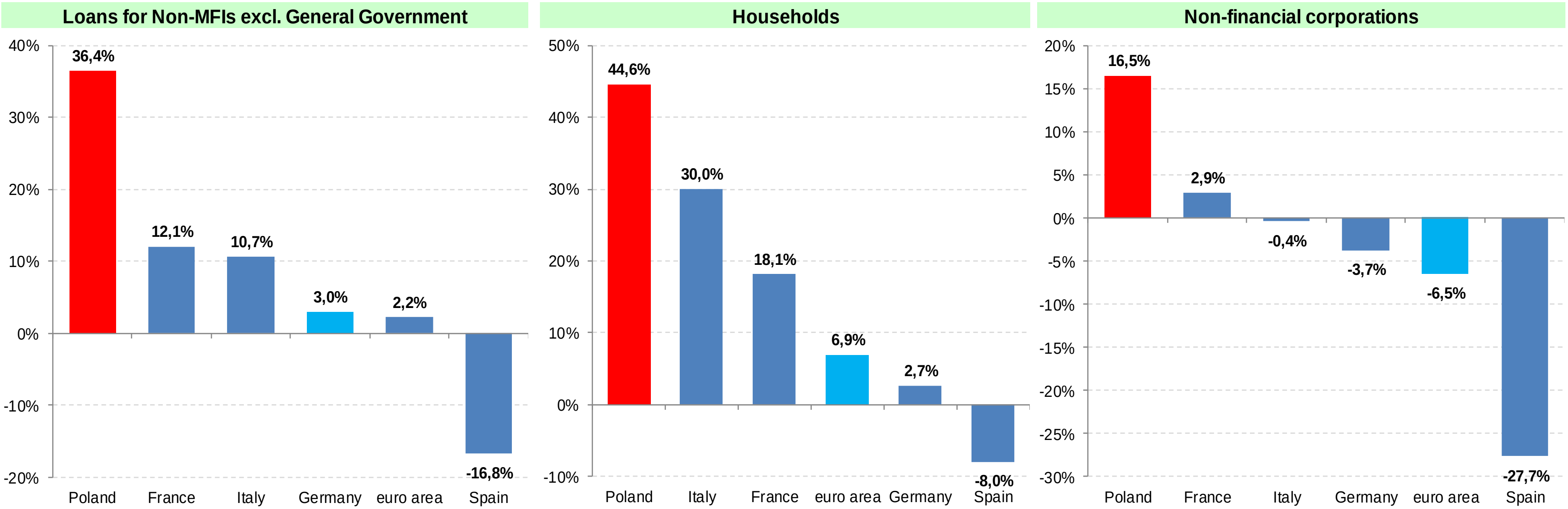
Banking sector size to GDP (2011)



Source: ECB, Eurostat, FED, OECD.

Credit growth during the economic crisis

Credit growth in Q4 2008 - Q1 2013 period

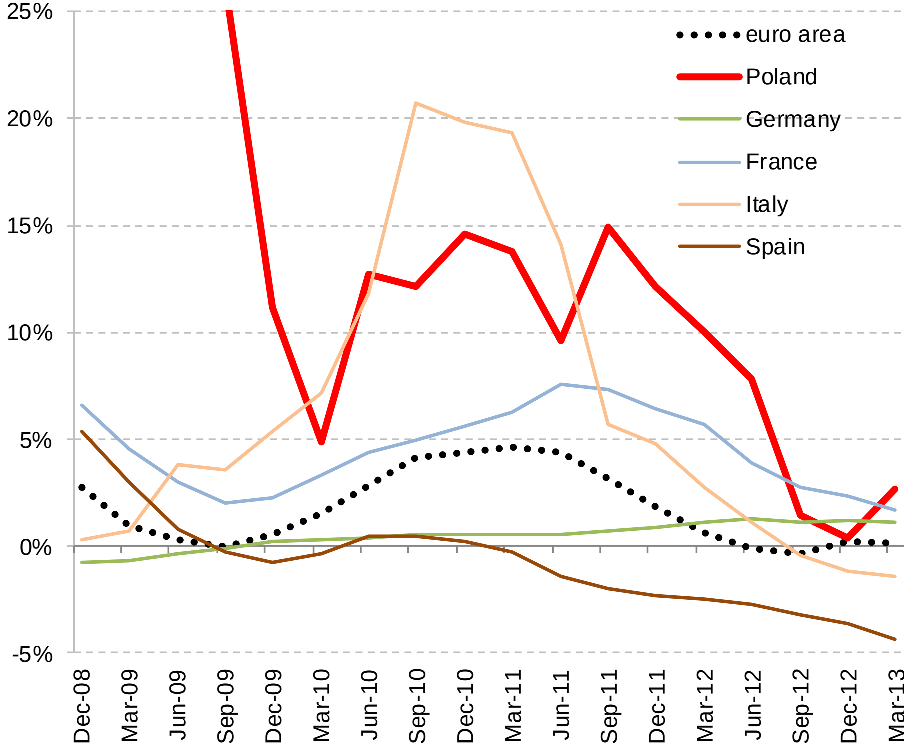


Source: ECB, SIS NBP.

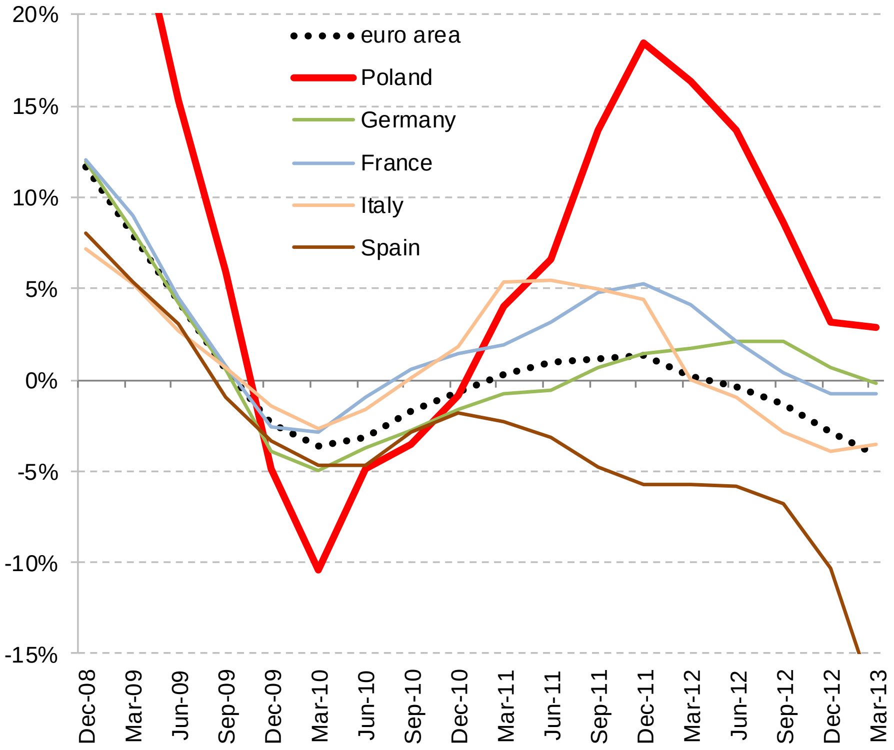
Credit growth in the Polish banking sector is much higher than in other EU countries

Loan portfolio increase

Credit for households (change y/y)



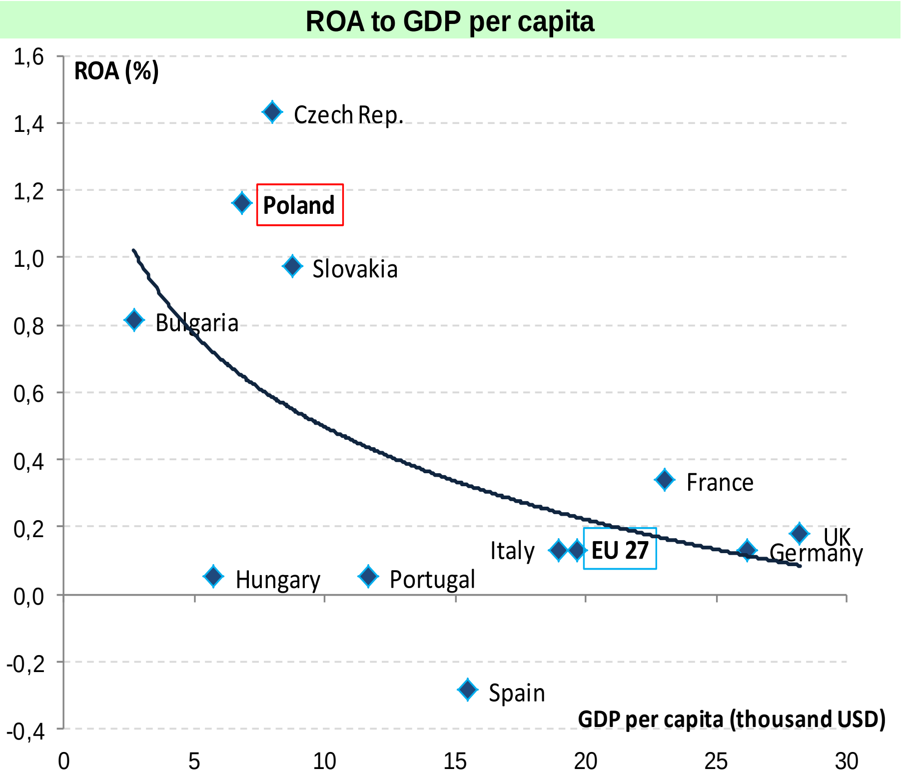
Credit for non-financial corporations (change y/y)

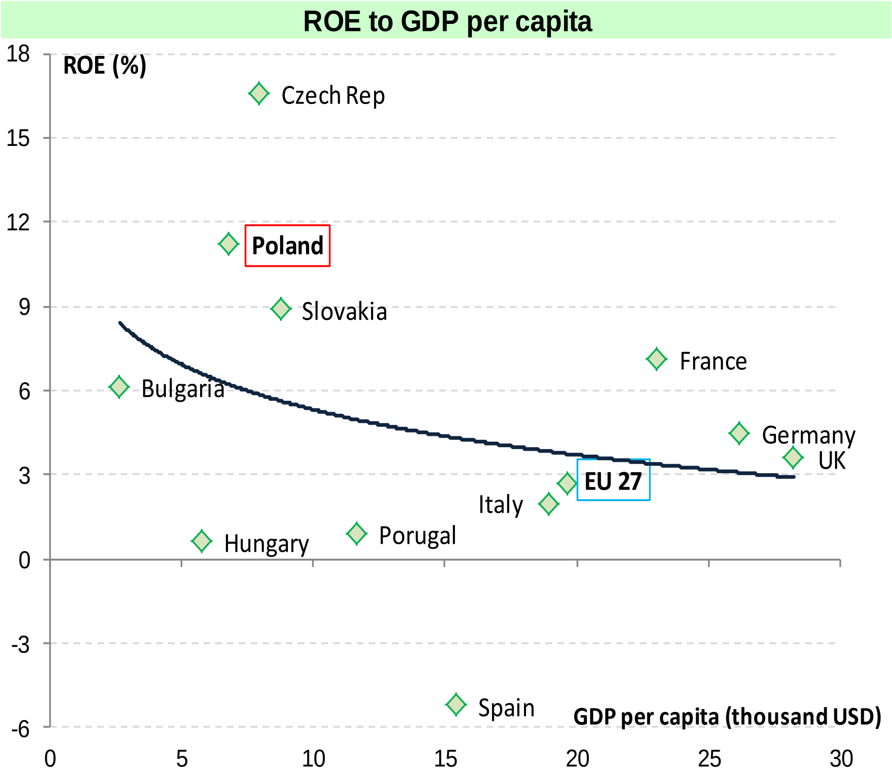


Source: ECB, SIS NBP.

Deeper contraction in lending in the euro area than in Poland

Banking sector effectiveness



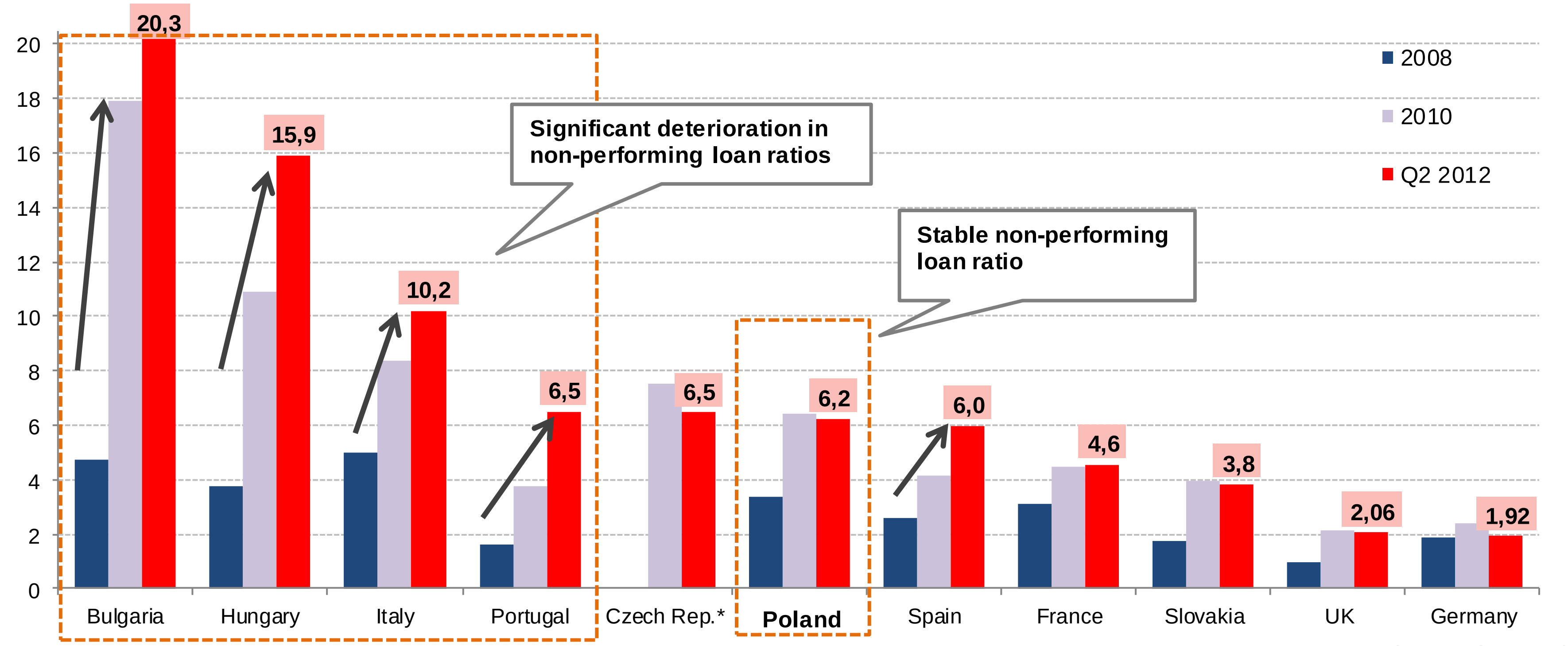


Source: ECB, data for H1 2012.

Effectiveness ratios are higher in the Polish banking sector in comparison with Western European countries

NPL ratio

Non-performing loan ratio (%)



Significant deterioration in non-performing loan ratios

Stable non-performing loan ratio

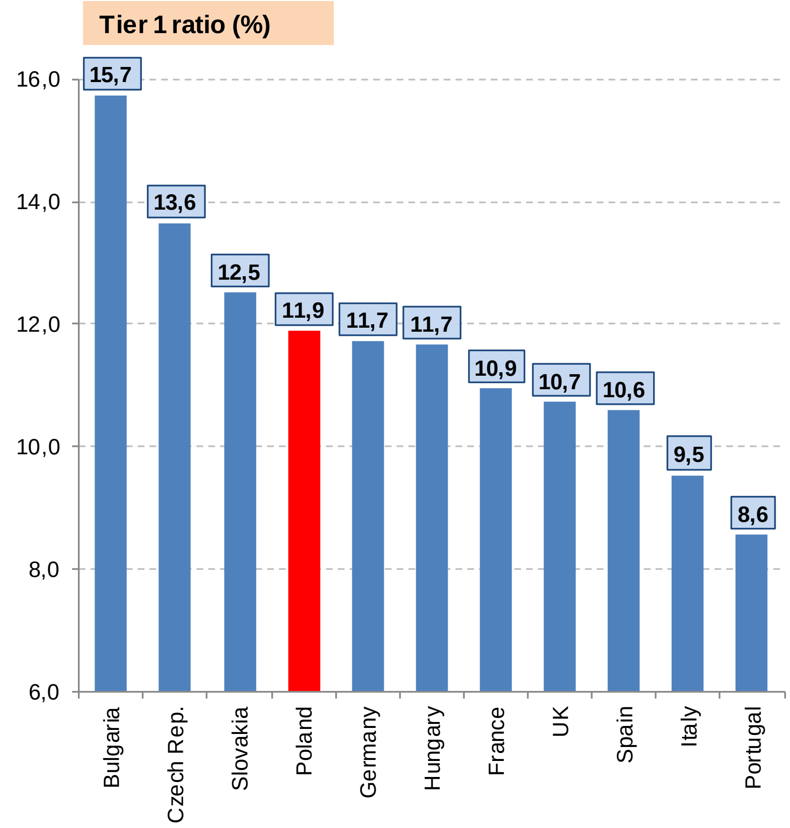
Source: ECB.

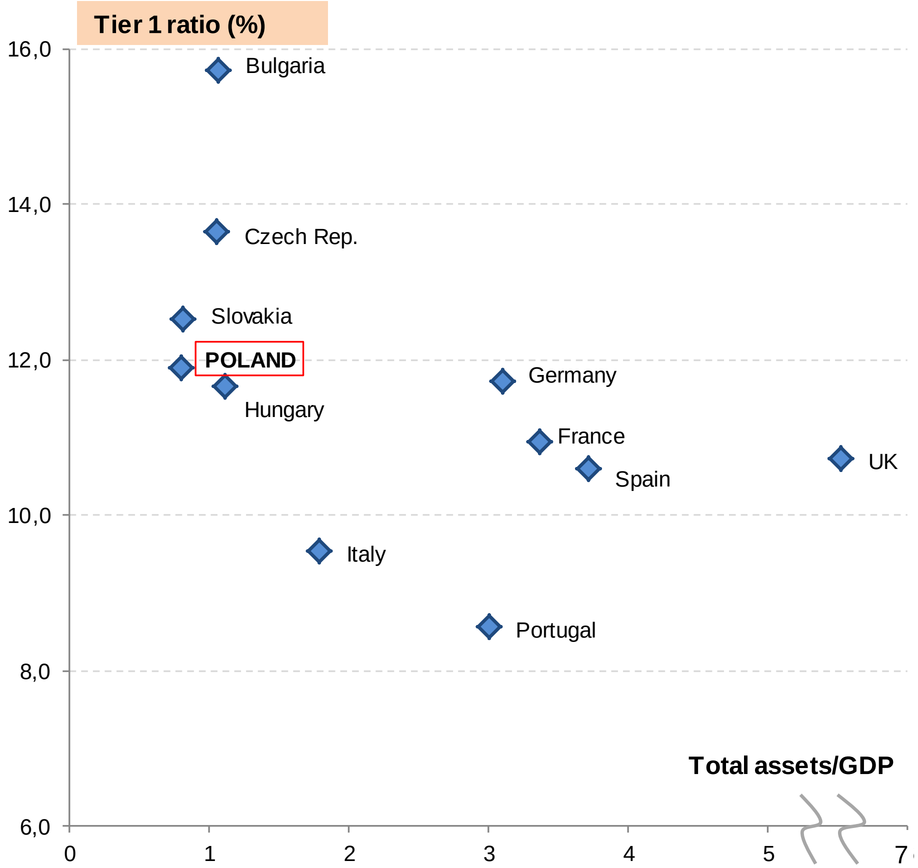
No systematic escalation of credit risk in the Polish banking sector

High level of profitability as an additional buffer

Capital adequacy

Tier 1 ratio (2011)





Source: ECB, Eurostat.

Solvency ratio in the Polish banking sector: 15.4% (Q1 2013) – satisfactory in comparison with Western European countries

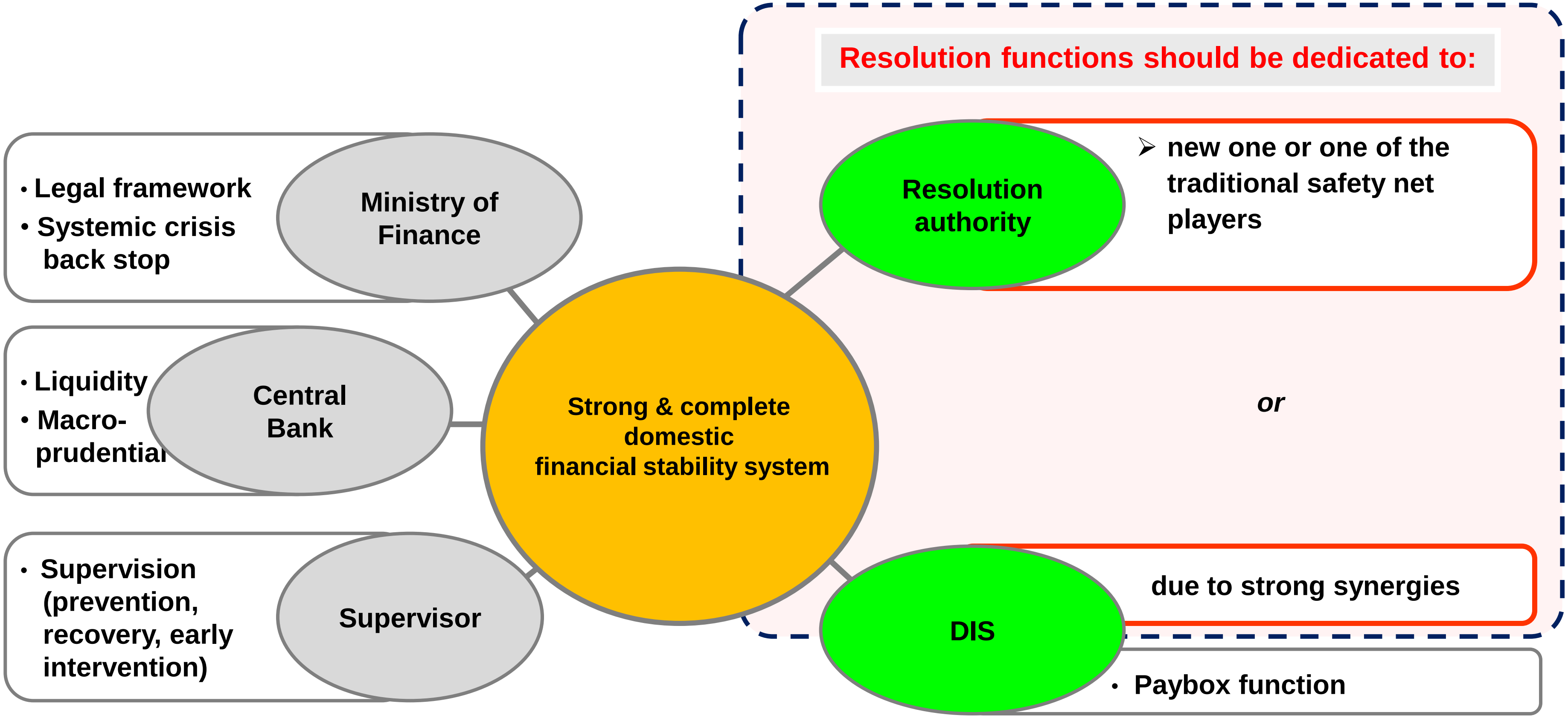
Protection of financial stability and safety net role

Protection and enhancement of financial stability are a complex exercise that consists of many functions and exceeds the possibilities of one institution and may create conflict of interest and forbearance risk

Special competences related to realisation of these functions are concentrated in a few institutions that constitute the financial safety net

Aiming at limiting the frequency and scale of malfunctions and disruptions in the financial system as well as buffering their adverse effects.

Robust financial stability net



Resolution functions should be dedicated to:

- Legal framework
- Systemic crisis back stop

Ministry of Finance

- Liquidity
- Macro-prudential

Central Bank

- Supervision (prevention, recovery, early intervention)

Supervisor

Strong & complete domestic financial stability system

Resolution authority

- new one or one of the traditional safety net players

or

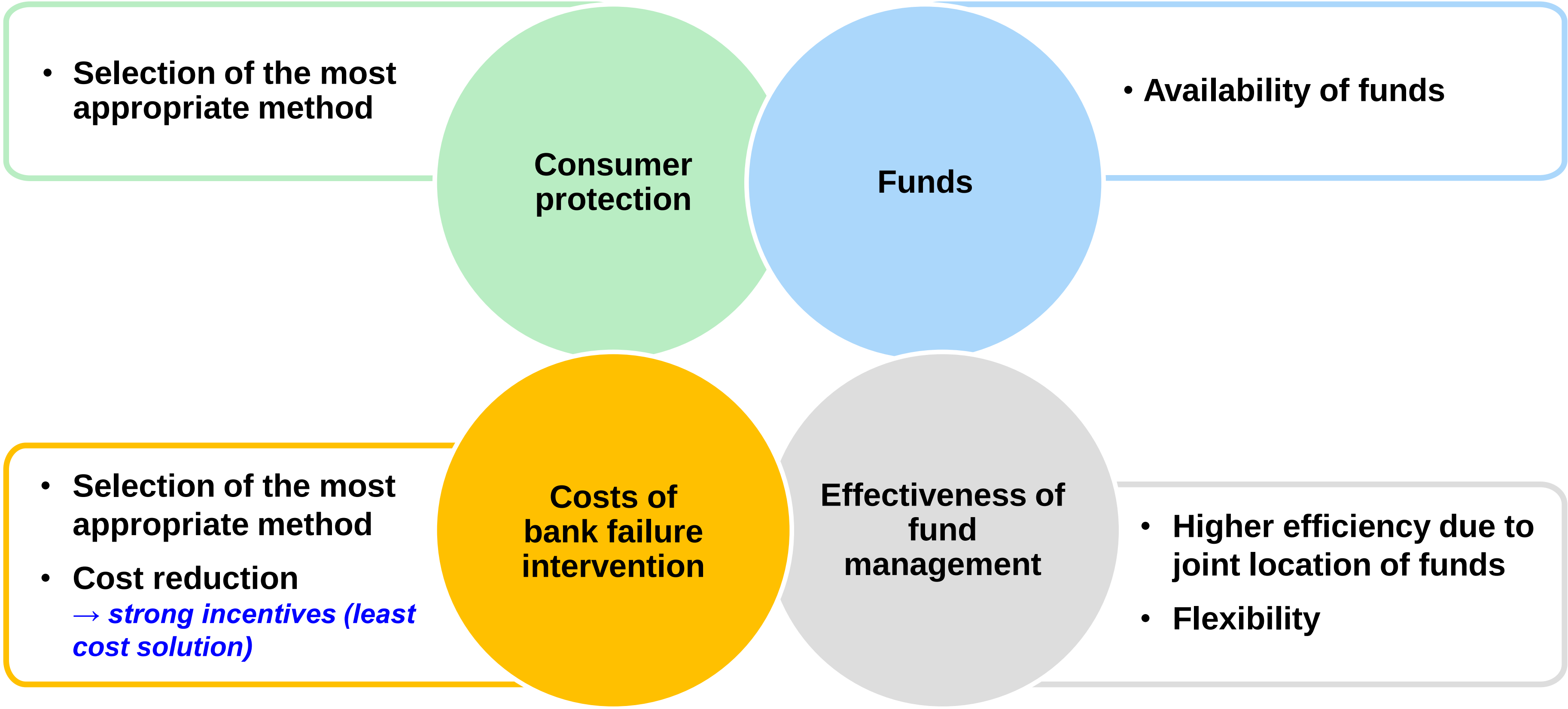
DIS

due to strong synergies

- Paybox function

Financial stability network widen with resolution function enable to affect the market and limit any disruptions more effectively

Strong arguments to attribute resolution tools to DIS's



- Selection of the most appropriate method

Consumer protection

Funds

- Availability of funds

- Selection of the most appropriate method
- Cost reduction
  → strong incentives (least cost solution)

Costs of bank failure intervention

Effectiveness of fund management

- Higher efficiency due to joint location of funds
- Flexibility

Resolution benefits

- **Minimization of public funds and deposit insurance funds through preservation of assets of failed bank & prompt transfer (deposits) to acquiring banks before full insolvency**

- **Stem financial system contagion or deposit runs by transferring working parts of balance sheet (or entire bank) to purchaser (another bank) or bridge bank.**

- **Protect economic stability as critical economic functions are kept going (funding and clearing)**

- **Even gap filling between transferred liabilities and assets by resolution authority is less costly than deposits pay out**

Resolution tools

There is a set of 4 restructuring tools recognized by global resolution standards (but only first three sufficiently tested in practice)

Purchase and assumption

- Sale of the institution or the whole or part of its business on commercial terms to a private sector purchaser
- Different forms of support to the acquirer available (e.g. loss sharing mechanism)

Bridge bank

- Transfer of all or part of the business of an institution to a bridge instiution owned and controlled by the resolution authority
- Temporary solution

Asset separation

- Transfer of impaired or toxic assets to an asset management vehicle to allow them to be managed and worked out over time
- Support efficiency of other tools by cleaning the balance sheet
- Only in conjunction with another tool (to avoid moral hazard)

Bail-in

- Write-down of capital instruments and conversion of liabilities to cover the losses and create robust capital base
- Only in conjunction with a business restoration plan to recover long-term viability

Resolution funding

- Shareholders and creditors of failing bank bear first losses
- Not covered losses are paid from sector funds (ex ante and ex post sourced resolution fund)
- Because of time pressure bridge funding can be necessary (resolution fund)

- Set up ex ante fund sourced by contribution of banking sector (annual fee)
- Possible additional ex post contribution
- Possible support from paybox ex ante funds (as resolution is to avoid paybox)
- Possibility to contract market financing allowances (repaid with sector contributions)

Resolution tools – Bail in

Definition

Recapitalization to reach prudential norms, condition for authorization and carry on operations and long term viability (market confidence):

- **Loss coverage and objective valuation with capital instruments (including convertible ones)**
- **Improvement of capital structure to convert liabilities into core Tier I**
- **Increase of capital as a result of conversion of liabilities**

Observing principles that shareholders bear first losses:

- **Write down of capital instruments,**
- **Conversion of liabilities into shares to substantially dilute existing shareholdings**

Recapitalization of failing bank or to capitalize bridge bank

- **Write down of eligible liabilities (to cover losses)**

or/and

- **Conversion of liabilities into shares (to recapitalize)**

Currently discussed issues

Taking into consideration efforts taken in European and global perspective the current discussion relating to resolution concentrates on these issues:

Funding of resolution process

- Use of DIS funds to support resolution measures
- Funding of group resolution

Bail-in mechanism

- Scope of bail-inable liabilities
- Statutory vs. discretionary exclusions
- Depositor preference
- MREL

Depositor preference in insolvency is of crucial meaning for deposit insurers and their position in the resolution framework as well as the future shape of the bail-in mechanism

Currently discussed issues – home-host

- Intra group support shall be recovery tools, it’s to late to use it in resolution (risk of reimbursement)
- At the time resolution triggers are met, focus shall be on execution not solution development

☐ Recovery plan

☐ Early intervention tools and special administration

☐ Resolution plan

☐ Resolvability assessment

☐ Recommendation on impediments removal

☐ Resolution financing (MREL, burden sharing)

☐ Resolution scheme

- MREL level (solo, consolidated) is base for resolution financing structure and depends on resolution strategy (SPE, MPE)
- Lack of reliance of resolution actions (resolution scheme) on resolution plan undermine resolution planning concept

Group recovery and resolution related issues shall be combined in the same process closed by a joint decision with appropriate safeguards for home and host contries (EBA mediation or own decision at relevant level)

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