Brussels, 18th March 2020

EACB call to regulators and supervisors to take further measures to ensure the banking sector can sustain the economy through the Covid19 emergency

The outbreak of the Covid19 as a pandemic event is likely to lead the global economy in a harsh recession. Europe, currently a center of the pandemic will be severely hit.

A dramatic contraction of the European economy is more than likely given measures such as the constraints imposed on cross-border travel and with retail, service and manufacturing activity reduced by isolation and social-distancing measures. This could lead to a dangerous demand and supply side shock.

At the same time cooperative banks' members and customers face ongoing payment obligations to providers, employees, tax authorities and banks. Many businesses, particularly SMEs, are already facing serious financial pressure which is only likely to increase.

Cooperative banks are committed by nature to fully support the local economy and can act as stabiliser in times like these. Public authorities also ask them to strongly support the economy and continue their financing.

We appreciate and welcome the decisions taken by the EBA[1] and the SSM[2] on 12th March to introduce a degree of flexibility in the framework, particularly postponing the 2020 stress test exercise and explicitly giving the possibility to use certain capital and liquidity buffers, and rearranging supervisory activities including on-site inspections, timing of remedial actions, submissions deadlines. In particular it is key to ensure that **banks' liquidity is available for supporting businesses, particularly for SMEs**, and using the LCR buffer should not lead to seeing institutions as less sound (e.g. for the purpose of the SREP).

In this vein, we believe that in order to preserve trust and ensure that banks can fully support the business eco-system further action is needed, and clarifications are required. Coordination among public authorities and between those and the banking sector is essential. We are collectively facing an extraordinary situation which requires agility, swift and bold reactions: when the house is burning, one should not count the litres of water to put out the fire.

Among the members of the EACB different measures are discussed:

In the first place, we believe that action is needed in the area of the **definition of default and the consequences for forbearance and restructuring measures**, and ultimately on NPL generation.

➢ We believe that a moratorium tool for sound borrowers facing liquidity challenges related to Covid19 effects would be a needed tool. Our members report that an increasing number of customers is requiring forbearance measures. Para. 18 of the EBA Guideline on definition of default (DoD) stipulates that "Where the repayment of the obligation is suspended because of a law allowing this option or other legal restrictions, the counting of days past due should also be suspended during that period". This should be clearly reflected in supervisory/regulatory action. We propose that such treatment for exposures affected by the consequences of the Coronavirus is applied consistently and across the board in the EU. This should be the case both where such measures have been fixed at national level via public authority

[1] https://eba.europa.eu/eba-statement-actions-mitigate-impact-covid-19-eu-banking-sector
[2] https://www.bankingsupervision.europa.eu/press/pr/date/2020/html/ssm.pr200312~43351ac3ac.en.html

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decision/legislation and where they are measures undertaken by individual banks. This would allow to avoid any contagion effect rippling through different regions.

- The framework for the definition of default would need fine tuning particularly with regard to default triggers (DPD and unlikeliness-to-pay indicators), curing periods and rules out of default status and on forbearance measures for customers performing before the COVID-19 crises.
- A comprehensive list of measures should be envisaged to allow banks renegotiating loans without facing uncertainties with regard to default and forbearance measures. Such list would provide level playing field and confirmation that such measures are not identified later on by the supervisors as forbearance or defaults and lead to corrections and severe consequences on the banks side. Once again, a European approach is much needed.
- It is our understanding, that we can provide restructuring to our clients that are not reaching the criteria of 1 % NPV reduction (para. 51 on EBA GL DoD) to performing customers that were fulfilling their financial commitments before the COVID-19 crises and the new terms reflecting the temporary difficulties of the customers do not met the other indicators listed in point 53 of EBA GL on DoD. The bank is allowed to use such restructuring measures to unlimited number of customers with the constraint that it is offered to clients performing before the COVID-19 crises. We believe this should be clearly stated by EBA/SSM, otherwise it would be unclear how restructuring can be used on large number of customers without recognizing them as defaulted.
- It is our understanding that the definition of 'financial difficulties' in relevant regulatory pieces[3] does not apply for customers that were performing and fulfilling their financial commitments before the COVID-19 crises. These customers are in temporary liquidity difficulties and if the bank manages to agree on new contract terms reflecting the temporary liquidity difficulties and without value loss towards the bank, then these agreements count as 'renegotiations' and 'roll-overs' in the meaning of above regulations. We believe that supervisors should make this explicit in order to allow banks to support clients to overcome temporary liquidity difficulties.
- Guidance may be necessary on how to assess moving exposures to stage 2 or stage 3 of IFRS 9 in order to fine tune the necessary accounting provisioning rules with the prudential ones. In this context in fact IFRS 9 if too rigidly applied may reveal strongly procyclical.
- As far as stress testing methodology is concerned, some relaxation of the criteria should be envisaged in the 2021 exercise, given that the negative impact of Covid19 on the EU economy and banking sector may be in action beyond the short term.
- Finally, it is necessary to neutralise at this stage the inevitable capital increases associated with the changes in technical criteria of definition of default and of the Targeted Review of Internal Models.

Secondly, we see the need for more punctual **clarifications in the area of usability of capital buffers**:

- We believe that freeing capital resources to sustain lending capacity by easing the Combined Buffer Requirement is necessary and should be a coordinated effort as certain buffers are set at national level (e.g. countercyclical capital buffer or other domestic buffers).
- Releasing the buffers would be a better solution than temporarily allowing banks to bite into them, indeed it is not clear from the SSM statement whether touching upon the buffer requirements would trigger restrictions to dividends' distribution (MDA trigger). Restricting

[3] E.g. see ECB Guidance on NPL chapter 5.3.1., EBA GL on forbearance and non-performing loans, Para. 151 (minimum requirements), Annex V to ITS on supervisory reporting, Chapter 18, para. 240 onwards

distributions at this moment of time risks having even worse consequences on the confidence in banks' solvency, despite the good capital standing.

- In order to ensure a level-playing field in the EU, we would suggest to the EBA to issue guidelines on how the SREP should be adjusted, especially with regard to two aspects: (i) supervisory expectation on the NPLs portfolio, (ii) the treatment of sovereign exposures and concentration on that asset class. We expect no change on the current rules.

We hope that our suggestions will be taken on board and we remain available for exchanging on these matters with a view to fine tune a coordinated action that can ensure the flow of credit and avoid long lasting detrimental consequences on the economy and ultimately on financial stability.

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