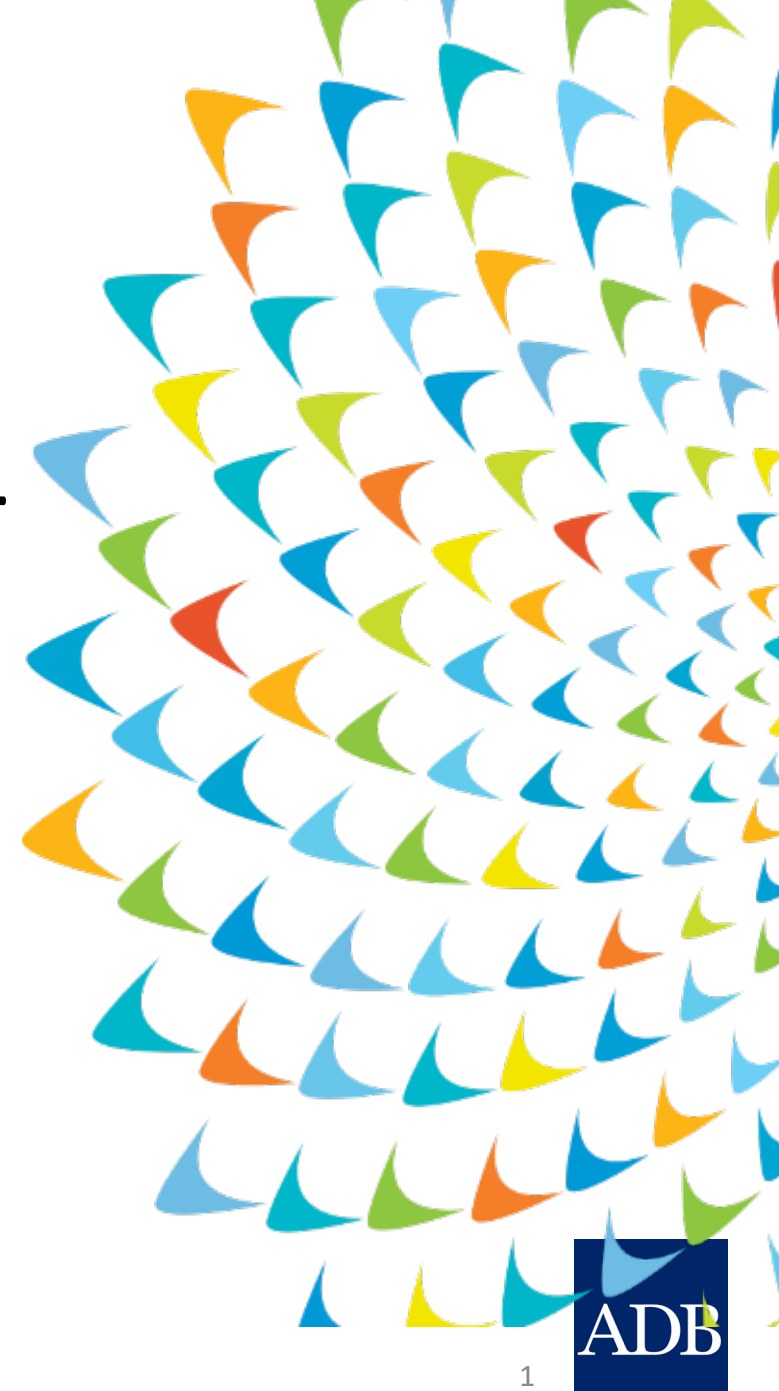


# Current challenges to NPL resolution in Asia

9 June 2021





# NPL Source-Cause Assessment

- Crisis periods of rising non-performing loan levels can generally be linked to prior actions/conditions or lack of actions
  - Regulatory side:
    - Inadequate legal and regulatory framework for financial institution supervision
    - Lack of consistent actions
    - Waivers and forbearance
  - Market:
    - Rapid growth
    - Chasing market share
    - New, untested areas
    - Changes in U/W and downstreaming
    - Ownership and governance
  - Economy and Cycles:
    - Not controllable - cyclical
    - Impaired risk assessment and risk management
    - Economic volatility and diversification
    - External shocks
    - COVID related



# NPL Lifecycle - “Stages of NPL Grief”

- Deny, Delay, Defer, Detriment
- Exponential concerns:
  - Lack of action - augments concerns
    - Impairs financial intermediation (explicit or implicit) – direct cut to lending, change in U/W practices, risk tolerance and rejections, focus on preservation (capital)
    - Subsequent resolution - more burden on safety frameworks like deposit insurance
  - Raised complexity – SIBs and regulatory measures
  - Potential economic crisis – economic restructures need financial systems
  - Dealing with mixed ownership - government owed, controlled or linked
    - Beyond simply a systemically important bank (SIB) issue
  - Political factors
    - Ownership and interests direct or indirect, old state links,
    - Typical looking bad
    - All blame the Central Bank or supervisory agency – hold on!



## NPL Lifecycle - “Stages of NPL Grief”

- Consider (hope) it is transient - “grow out of it”
- Don’t count on this – some research
  - Not all institutions survive or if can avoid systemic crisis
  - No specific number on NPLs
  - Interlinked with proper recognition, timing, actions, legal framework, etc.
  - Mix of the financial system – affecting all financing institutions, just banks (are they dominate?)
  - NPL % or % or recap to GDP



# NPL Actions

Case for:

- Early-warning systems
- Forward looking analysis (NPLs are backward looking)
- Systemic risk assessments
- Regulatory mechanisms – i.e. Prompt Corrective Actions
- Cross-supervisory entity coordination
- Action, Action, Action



# NPL Transparency

- Forebearance and waivers
- Real-estate owned as settlement of obligations
- Restructuring & re-ageings
- Non-accrual timing
- Evergreen lending
- Write-offs without collection
- NPL definitions & risk definitions
- Concept that provisioning solve NPLs – NOT – Underwriting and forensic assessment about how the condition arose



# NPL Impact

- Drag on a bank's performance:
  - Reduction in net interest income;
  - Increase in impairments costs;
  - Additional capital requirement;
  - Lower ratings and increased cost of funding, adversely affecting equity valuations;
  - Reduced risk appetite;
  - Alternative focus - additional management time and servicing costs.
- Financial intermediation impacted
  - Needed for wholistic fix
  - Financial systems dominated by banks, lack of a well-developed capital markets, a small nonbank sector, etc.
  - NPLs constrain the supply of credit to the private sector and hinder economic activity
- Investor interest - domestic and foreign – credibility and transparency of the fix
  - NPLs increase vulnerability to further shocks
  - Systemic crisis and financial stability



# NPL Actions

- Clarity on the issues and source/cause
  - Clear and holistic analysis
  - Setting sound goals, mapping plans and acting upon the plans
  - Trailing data - vintage analysis
- Need proper legal and supervisory authority
  - Including resolution powers (Basel Core Principles for Banking Supervision)
  - Willingness to enforce
  - Corporate legal reform – collateral laws, appraising (challenges in illiquid markets, independence)
  - If resolution – who leads – administrative law?
- Risk assessment, risk recognition, accounting
- Early recognition and resolution
  - Links to capital and prompt corrective actions
  - Authority to review and make changes to ratings and subsequent provisioning
- Financial stability framework
- Potential out-of-court methods - corp debt restructuring committees or mechanisms
- Special courts
- NPL sales, AMCs

Thank You