NATIONAL BANK OF ROMANIA

Financial stability department

Nr.IV/1/3382 / 22.12.2016

To: Francesco Mazzaferro
Head of the Secretariat
European Systemic Risk Board
Sonnemannstrasse 22
60314 Frankfurt am Main, Germany

Subject: Notification of Systemic Risk Buffer according to article 133 of Directive 2013/36/EU

As you have been informed, following the identification in December 2015 of a contagion risk using the instrument represented by the long-term sovereign debt ratings of banks' home countries, as reported by the credit rating agencies recognized as ECAIs, the National Committee for Financial Stability recommended to the National Bank of Romania to implement a Systemic Risk Buffer of 1% based on all exposures of banks having a parent bank registered in a country for which the credit rating for sovereign bonds issued by the central government is not "investment grade". The credit institutions in Romania which were eligible for additional capital requirements consisting in a systemic risk buffer of 1% for all exposures at the notification date are the following: Marfin Bank (Romania) S.A., Libra Internet Bank S.A., Alpha Bank Romania S.A., Bancpost S.A., Banca Românească S.A. - National Bank of Greece Group, Piraeus Bank Romania S.A. and OTP Bank Romania S.A. Given that (i) Alpha Bank Romania S.A. and Bancpost S.A. were systemically important as per the NBR assessment carried out in 2015 with an applicable O-SII buffer and (ii) the Systemic Risk Buffer was implemented based on all exposures of eligible banks, Alpha Bank Romania S.A. and Bancpost S.A were not subject to a cumulative obligation to maintain a Systemic Risk Buffer according to the CRD IV provisions regarding the combined buffer requirements.

In May 2016, the National Committee for Financial Stability analyzed the then recent national legislative developments regarding loan contracts that are likely to determine significant changes of the capital adequacy indicators of the Romanian banking system in the following period through increased capital requirements (the *Datio in Solutum* Law and *The program for household protection against the significant depreciation risk arising from exposure to foreign currency-denominated loans*) and issued *Recommendation No. 1/May 9, 2016 regarding the suspension of the Systemic Risk Buffer applicable to credit institutions in Romania.* Thus, the National Committee for Financial Stability has recommended to the National Bank of Romania, in its capacity as competent authority, to suspend the application of the Systemic Risk Buffer for the credit institutions during the period required for carrying out the study regarding the impact of the current legislative developments on the financial and prudential situation of the Romanian banking sector, respectively at least until December 31st, 2016. Considering the above mentioned, we communicate the following:

The National Bank of Romania has performed a preliminary assessment of the impact of the recent national legislative developments, considered to have a negative impact on the financial and prudential positions of credit institutions through the capital adequacy indicators channel.

Upon promulgation of Law 77/2006 *regarding the giving in payment of some immovable property for extinguishing the obligations undertaken by loans*, the Constitutional Court released a press statement on October 26th, 2016 admitting a series of exceptions of unconstitutionality. According to the release, the debtors' rights to give into payment immovable property can be applied only if a court verifies the conditions regarding the existence of the unpredictability principle. Unpredictability in the contract's execution occurs when an exceptional event which could not have been reasonably foreseen by any of the parties at the contract's inception takes place, making the debtor's obligation to execute the contract excessively burdensome. These conditions are verified by a court which can pronounce either on the contract's adjustments, either on its termination in a form decided by the court and which can lead up to the collateral's transfer towards the creditor, along with the discharge of all debts (principal and accessories). Also, the Constitutional Court mentioned that the unconstitutional naming of the phrase "*as well as from the immovable property devaluation*" from Law 77/2006 essentially took into account the fact that the object of loan contracts was represented by the loan amount itself and not immovable property. As such, the market devaluation of the property good used as collateral for the loan contract cannot constitute the basis for the giving in payment mechanism. According to the giving in payment notifications received by credit institutions until now, most of them refer to loans for which the remaining balance is higher than the property's market value; considering that the debtors' monthly installments are not considered to be excessively burdensome by the courts, it is expected that they do not benefit from the giving in payment option. Loss recognition by credit institutions will be gradually performed in time, starting with 2017, as courts will pronounce with regards to the conditions necessary to fulfill the unpredictability principle, for each loan contract. Consequently, we consider that the preliminary impact of Law 77/2006, as estimated by the Financial Stability Division, to be significantly lower following the Constitutional Court's decisions. The effects on banks will be distributed over a longer period of time, which will contribute to a reduction of consequences on financial stability.

The legislative initiative regarding foreign currency denominated loans' conversion conditions for consumer loans (Plx 345 – *draft law for the completion of Government Emergency Ordinance no. 50/2010 regarding consumer loan contracts*) was sent to the Constitutional Court on 25.10.2016, following an unconstitutionality notice by the Romanian Government. The draft law provides for the conversion of Swiss franc-denominated loans at the historical exchange rate and is applied both to ongoing contracts and to contracts which have been outsourced/sold/assigned, as well as in the case of contracts of consumers who have been subject to foreclosure. Also, at the request of consumers, the law can be applied even if the loan conversion was already finalized. Considering the Constitutional's Court recent decisions regarding the Datio in Solutum Law and should the draft law be promulgated, we consider that, in a similar manner, resolutions for the CHF debtors' requests will be dealt with on a case-by-case basis, using the historical exchange rate prevailing at the time of the contract's inception, following a court's decision regarding the aplicability of the unpredictability principle and the debtors' possibility to perform the conversion in terms as agreed by the draft law. As such, we consider the impact of the conversion of CHF-denominated loans at a historical exchange rate to be significantly lowered as compared to the preliminary estimations, both following the reduction of the number of potentially resolved situations in favor of debtors and the recognition of losses derived from applying the law gradually, giving banks the possibility to cover losses over a longer time span.

It is worth mentioning that, according to the analysis performed using data available at 30.06.2016, four of the eligible credit institutions for which the systemic risk buffer will be implemented, following the identification of a contagion risk using the instrument represented by the long-term sovereign debt ratings of banks' home countries were identified as systemic (Alpha Bank, Bancpost, Piraeus Bank and OTP Bank). In these conditions, considering that an O-SII buffer will be applied to the above mentioned institutions starting with 1.03.2017 (at a 1% level of the total risk-weighted assets), these will not be cumulatively obligated to maintain a systemic risk buffer, according to the combined buffer provisions established in CRD IV (in the context in which the systemic risk buffer is calculated using the total exposures). It is worth mentioning that Alpha Bank and Bancpost are already obliged to maintain the O-SII buffer, according to the provisions set in *NBR Order no. 1/December 2015*, issued on the basis of *NCFS Recommendation no. 1/2015 regarding the capital buffers implementation in Romania.*

NBR performed an analysis of external contagion risks. In November 2015, three of the home countries of Romanian bank branches had a speculative grade sovereign rating: Greece, Cyprus and Hungary. In 2016, Hungary migrated to investment grade, considering that *Standard&Poor's* and *Fitch* granted a BBB- rating (with stable and positive perspectives, respectively), and *Moody's* improved its rating to investment grade on November 4th, 2016. The contagion risk assessment for countries with a non-investment grade rating indicate that the banking crises episodes which Greece and Cyprus have experienced have been partially corrected through the implementation of financing programs with external creditors (ESM, IMF) with the main role of reestablishing confidence in the financial system. Even though some structural problems still persist, the better than expected macroeconomic outlook in Cyprus and the successful implementation of the program carried out with the ESM proves that, on the short term, the negative externalities from Cyprus' banking system are limited. Regarding the Greek economy, the 2015 banking crisis episode has been managed by the authorities, while at the same time the entering into a new accord with international creditors, as well as the continuation of structural reforms, have improved investors' perception on the short term. As such, considering the progress made by both countries in correcting fiscal imbalances, in implementing structural reforms and in reestablishing investors' confidence, short term risks have been significantly reduced.

Moreover, the NBR performed an analysis on the particularities of the current Romanian macro-financial framework, taking into account its development perspectives, as well as structural aspects regarding the real and financial sectors. The results of the analysis both on financial sector systemic risks and on macroeconomic equilibria, indicate that both favorable economic conditions (internal and external) and the relatively low level of potential risks toward the national banking system, not covered through other micro or macroprudential measures, do not indicate the need to maintain a systemic risk buffer at a level other than zero.

In this context, considering the reduction of the contagion risk and the low level of vulnerabilities of the domestic macroeconomic and financial outlook, the National Committee for Financial Stability issued a recommendation to the National Bank of Romania in order to deactivate the systemic risk buffer for the contagion risk identified using the instrument represented by the long-term sovereign debt ratings of banks' home countries, starting with 1.03.2017, the suspension period of the systemic risk buffer being extended until that date. Information regarding the systemic risk buffer deactivation has been posted on the NBR website (under Financial Stability / National Committee for Financial Stability / Press releases - http://www.bnr.ro/page.aspx?prid=12537).

Yours sincerely,

Eugen Rădulescu

Director