

Warsaw, 23 January 2017

Mr Francesco Mazzaferro
European Systemic Risk Board

Acting as the Chair of the Financial Stability Committee (Komitet Stabilności Finansowej, KSF), which is the macroprudential authority in Poland, I would like to kindly inform you that at its meeting on 13 January 2017 the KSF issued Resolution 14/2017 on the recommendation on the restructuring of the FX housing loans portfolio.

The resolution contains recommendations addressed to the Financial Supervision Authority, the Minister of Finance and the Bank Guarantee Fund on policy actions which will reduce risks stemming from the existing stock of FX mortgage loans. Committee's recommendations are aimed at a gradual restructuring of the banks' FX mortgage loan portfolio. The recommendations indicate desirable ways of restructuring FX loans, which in principle should be based on voluntary agreements between banks and their customers.

We assume the recommended solutions should aim at strengthening mutual trust between banks and customers and reduce uncertainty, while preserving financial stability. Due to the complexity of the process, recommendation refers to various available instruments (both micro- and macroprudential) impacting banks, being at the disposal of the safety net institutions represented in the Financial Stability Committee.

Please find enclosed recommendation of the KSF. I will inform you in due course on the next decisions in the respect of restructuration of FX mortgage loans in Poland.

Yours sincerely,

Resolution No 14/2017
of the Financial Stability Committee
of 13 January 2017

on the recommendation on the restructuring of the FX housing loans portfolio

Pursuant to Article 5 and Article 18 (1) of the Act of 5 August 2015 on macroprudential supervision over the financial system and crisis management (Journal of Laws, item 1513 and of 2016 item 996) the following shall be resolved:

In the years 2007-2008, in the period when the Polish zloty remained strong in relation to foreign currencies, there was a marked increase in foreign currency housing loans granted. This increase was a result of both demand and supply factors, including housing aspirations of the public, the differences in the interest rates and the expectations of Poland's imminent accession to the euro area. The sharp growth in FX housing loans coincided with the reorganisation of banking supervision and its separation from the structures of NBP at the beginning of 2008.

Since 2006 measures aimed at mitigating the threats arising from excessive growth of FX lending have been implemented. In particular, in 2006 the Polish Financial Supervision Authority issued Recommendation S requiring, among others, a more rigorous assessment of the borrower creditworthiness, and raised from 35% to 75% the risk weight applied to FX loans for the purpose of calculating capital requirements. In 2011 the risk weight was further raised to 100% and the amended Recommendation S introduced in 2013 actually prohibited FX lending.

Since the end of 2011, as a result of the changes in strategy of banks and the activities of the supervisory authority and NBP, lending in the housing loans segment has focused almost exclusively on loans in the Polish zloty. Nevertheless, the value of the FX housing loans portfolio is still high and represents a significant share of banks' balance sheets.

In economic terms, the FX loans portfolio does not generate significant risk to the stability of the financial system. The financial situation of the overwhelming majority of households that took out loans in foreign currency is good and their resilience to further exchange rate shocks remains high. This is attributed to the high initial income buffers, high growth in nominal wages since the loans were granted and the low level of interest rates in foreign currencies. As a result, FX housing loans have a good repayment rate and the NPL ratio is only slightly higher than for Polish zloty loans.

Liabilities resulting from FX housing loans can, however, constitute a significant burden for certain borrowers, in particular due to the increase in instalments and/or the loan principal in

relation to the value of the real estate, which makes the sale or exchange of the immovable property difficult.

The significant depreciation of the Polish zloty against the Swiss franc at the beginning of 2015 amplified negative social phenomena and resulted in the emergence of legislative initiatives aiming for intervention in relation to FX housing loans. In the case of the potential further depreciation of the Polish zloty, these developments may intensify.

In the Committee's opinion, potential invasive legal solutions leading to the statutory conversion of FX housing loans, regardless of their possible form, are not appropriate. The situation remains very complex and diverse, and in many cases the results of conversion could be contrary to the expectations of borrowers, while certain solutions would additionally lead to substantial differentiation between the situation of foreign currency borrowers and Polish zloty borrowers. Moreover, the statutory conversion of FX housing loans could cause very significant losses in certain banks, and in extreme cases even threaten the stability of the domestic financial system.

Given the above, in the view of the Committee, the FX housing loans portfolio generates systemic risk in the context of the potential consequences of the invasive legal solutions proposed in the public debate.

Therefore, the solutions for the restructuring of FX loans must be implemented on a voluntary basis. The role of the institutions exercising supervision over the financial system is to introduce solutions of a regulatory nature and deploy available supervisory instruments with the aim of supporting banks and borrowers in taking decisions on the FX loans restructuring, while securing an appropriate sequence of instrument application (in particular, Pillar II measures are applied to cover risk factors not covered or not sufficiently covered by Pillar I measures). The following recommendations are arranged according to the institutions to which they are addressed.

§ 1. Taking into account the results of the works of the Working Group on the Risk of FX Housing Loans and the opinions of the interested parties, the Financial Stability Committee recommends the competent entities:

1. the minister competent for financial institutions:
 - 1) to immediately complete work on the regulation on increasing the risk weight for exposures secured by mortgages on immovable property, referred to in Article 124 (2) of Regulation (EU) No 575/2013, in particular to increase the risk weight to 150% for exposures fully and completely secured by mortgages on residential property where the amount of principal or interest instalments depend on changes in the exchange rate of one or more foreign currencies different from the ones in which the borrower receives income;

- 2) to increase in accordance with Article 164 of Regulation (EU) No 575/2013 minimum LGD for exposures secured by mortgages on residential property, the purchase of which was financed by an FX loan. The implementation of the recommendation by the minister competent for financial institutions requires an amendment to the *Banking Act*, incorporating appropriate delegation for the minister to make use of the powers provided for in Article 164 of Regulation (EU) No 575/2013, and also an amendment to the *Act on supervision over the financial market* establishing the minister as the authority competent to issue regulations in accordance with Article 164 CRR;
- 3) to introduce changes to the operating design of the Borrowers' Support Fund. The changes should lead to greater use of the Fund's assets to provide assistance to borrowers (both FX and Polish zloty loans) in a difficult financial situation. Moreover, the Fund's assets could also be used for other forms of supporting the process of voluntary restructuring of the FX housing loans portfolio;
- 4) to work out, in justified cases, appropriate solutions mitigating potential excessive tax burden for borrowers and lenders, which might result from the restructuring of FX housing loans, taking into account justified social aspects and the impact on public finance;
- 5) to impose a systemic risk buffer of 3% applying to all exposures on the territory of the Republic of Poland.

2. the Polish Financial Supervision Authority:

- 1) to modify the Supervisory Review and Evaluation Process (BION Methodology) and supplement it with additional rules enabling the attribution of the appropriate capital add-ons with regard to additional risk factors related to FX housing loans (operational risk, market risk and borrowers' collective risk of default);
- 2) to supplement current Pillar II requirements with additional capital requirements related to operational risk, market risk and collective risk of default in the scope of risk factors related to FX housing loans, imposed under Article 138 (1)(2a) of the *Banking Act*;
- 3) to issue, under Article 137 (1)(5) of the *Banking Act*, a supervisory recommendation on good practices related to the restructuring of the FX housing loans portfolios. In particular, the recommendation should:
 - a) draw attention to the need to identify all types of risks and costs related to holding the FX housing loans portfolios, including the funding risk of the FX loans portfolio,
 - b) draw attention to the fact that excessive concentration of FX housing loans and the related risk of these loans can serve as a basis for assessment on not delivering a guarantee of safe and stable bank management,

- c) indicate that from the point of view of the stability of individual institutions and the sector as a whole, it is justified to actively carry out the restructuring of the FX housing loans portfolio by way of individual agreements with borrowers,
- d) outline good practices with regard to the conduct of common restructuring in the bank, so that it proceeds in an orderly manner, which does not endanger the maintenance of appropriate levels of regulatory capital in the bank, and ensures that restructuring measures proposed by the bank are met with due understanding by borrowers, whose loans are to be subject to restructuring,
- e) require banks to prepare plans for the restructuring process, in which the groups of loans intended for restructuring will be distinguished and which will include the proposed restructuring measures (instruments) and sequences of their application with regard to particular groups of loans,
- f) develop effective incentives for banks and borrowers aimed at facilitating the restructuring process, while mitigating moral hazard and allowing the waiver of future legal claims in exchange for more favourable restructuring conditions,
- g) outline the desirable framework for negotiations with borrowers regarding the terms and conditions of restructuring and for the process of loan restructuring as such,
- h) take into consideration the standpoint of the European Central Bank expressed in the opinions to the draft acts related to FX housing loans.

3. the Bank Guarantee Fund:

to include the risk related to FX housing loans in the method used for the purpose of calculating contributions to the deposit guarantee fund paid by banks. The size of FX housing loan portfolios should be taken into account in the assessment of the risk profile of the banks in the framework of the so-called Area IV "Business and management model".

§ 2. The resolution will be published on the website of NBP.

§ 3. The resolution enters into force on the date of adoption.

Chairperson
of the Financial Stability Committee

/-/ Adam Glapiński