European Parliament

Antonio Tajani

Chair of the Conference of Committee Chairs
Chair of the Committee on Constitutional Affairs

Bruxelles, 6th November 2020

To:
Ursula von der Leyen,
President European Commission

Valdis Dombrovskis,
Executive Vice-President European Commission for an Economy that works for people

Mairead McGuinness,
Commissioner for Financial services, financial stability
and Capital Markets Union

Paolo Gentiloni,
Commissioner for Economy

Thierry Breton,
Commissioner for Internal Market

Dear President, Dear Commissioners,

The Covid-19 pandemic has been having a deep economic downturn and an enormous social shock. Market failures are extensive and households and SMEs are facing a risk of discrimination in access to financial resources. For this reason, the European Union must provide financial help to enable countercyclical effects and avoid the so-called "cliff effects".

A key role in helping our economy to face this crisis is carried out by our banking system. Only a well-functioning banks could ensure a proper transmission of the ECB monetary policy towards the real economy as well as the appropriate support to households and enterprises, in particular SMEs, being the latter the backbone of our economy.
A few weeks ago, ECB President stated that: "*In this context, it is clear that both fiscal support and monetary policy support have to remain in place for as long as necessary and "cliff effects" must be avoided. Otherwise, we risk hysteresis in the labour market, an unnecessary loss of viable businesses and greater inequality. And the recovery in the euro area remains uncertain, uneven and incomplete,*

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while the new coronavirus-related restrictions currently being introduced across Europe will add to uncertainty for firms and households."[1]

Against this background, I would like to share with you some reflections on a number of urgent measures that I consider crucial to allow our banks to continue to play such a fundamental role.

Social effects of the COVID-19 pandemic

Many SMEs that were active before the crisis have been forced to shut down. In this regard, the overall framework for defaulted exposures could have unintended consequences, resulting in permanent damage to our society.

Credit volume and flexibility

The crisis related shock has significant implications for investment and working capital. Banks provide credit based on , evaluating the risk profile of the borrower according to market practices. Therefore, it is crucial to support bank-lending volumes and to ensure an appropriate level of credit flexibility since, under the current circumstances, the companies/SMEs financial flows/working capital is at serious risk..

Forecasting and planning challenges

The coronavirus pandemic has had an impact on the capacity in planning the future for all economic actors. Households, SMEs, large companies and even governments experience difficulty in elaborating reliable forecasts.

Civil courts and non-performing loans

Covid-19 has also affected civil court proceedings. In some areas, courts were closed during the lockdown, with all proceedings being rescheduled or postponed. Therefore, the usual internal recovery planning of banks was affected resulting. This may result in a temporary downturn in the market prices for non-performing loans (NPLs).

For these reasons, it is crucial for the EU to put in place every effort to facilitate investment in the real economy, foster the granting of loans to individuals and SMEs, encourage the recapitalisation of companies, and strengthen the role of securities markets.

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[1] Remarks at the G30 International Banking Seminar, Contribution by Christine Lagarde, President of the ECB, during the session "Rebuilding and Sustaining Growth", Frankfurt am Main, 18 October 2020

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To reach this goal, I think some useful tools should be introduced in the EU regulatory framework, underlining the pivotal need of simplify some burdens imposed by financial regulation, even if in temporary terms.

One crucial issue refers to the **potential increase in banks' Non Performing Loans- NPLs**.
While recently introduced in the EU regulatory framework, through Regulations and Guidance by the EU Authorities, several instruments to manage NPL were clearly designed to handle them in normal circumstances only.

For this reason, in the current crisis-scenario, the regulatory framework securing non-performing loans shows some rigidities that could have a negative impact on the real economy, and in particular on SMEs,.

In particular, the rigidities related to the so-called "calendar provisioning", must be carefully managed since:

- the devaluation of NPLs within a short timetable that fails to take into due account the real economic value of the related collateral, would generate counterproductive effects. Strict timetables in loan devaluations had already been causing difficulties in the management of NPLs on the secondary market before the outbreak of the pandemic and could be even more problematic in the post-pandemic economy.

- Moreover, we have to assure that the regulatory framework does not harm the banking system and, conversely, it unduly benefits other operators, such as speculative funds, which operate on the NPLs market without being submitted to the same banking regulatory/framework.

- Obviously, hese circumstance would put enterprises in even more difficulties if banks are persuaded to get rid of these loans within a too shorttimescale.

In light of the above, I would like to suggest some temporary modifications to be introduced in the regulatory framework.

In particular,

1. the provisioning curves (times and qualities) – the capital with which banks have to cover devaluations – foreseen by the "Backstop Regulation" must be suspended or recalibrated, at least temporarily, for the time necessary to restore confidence on economic recovery.

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2. Furthermore, SMEs could be negatively impacted by the 90-day "past due" rule, which triggers the classification of credit as "default". To help SMEs, this rule should be temporarily reconsidered, having in mind that even the most reliable debtor could be involved in the slowdown of the economy. Such temporary modification is crucial to benefit enterprises that otherwise could face enormous difficulties in finding financial resources and liquidity.

3. Some reflections are also needed on the rules concerning the treatment of defaulted exposures. In particular their treatment when sold on a secondary market, being this provision currently under revision but only where a securitisation is involved (Article 127 CRR).

Yours sincerely,

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