



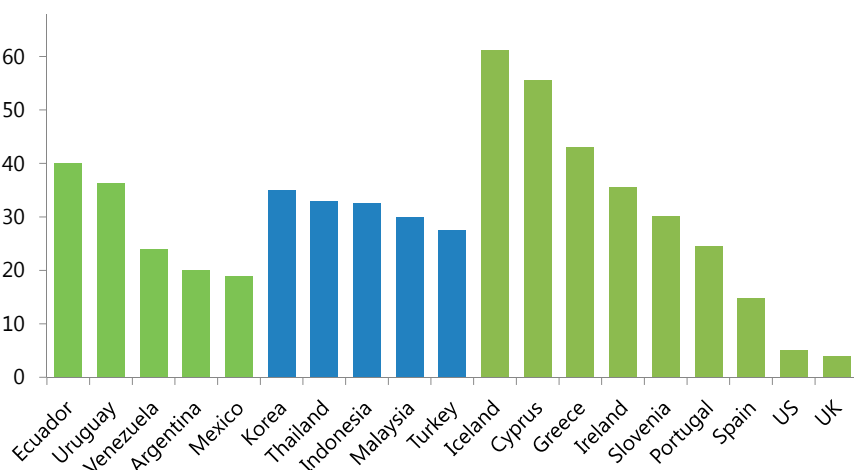
Solving NPLs through Innovative Solutions – Nicosia, 5 February 2016

Cyprus' NPL strategy in light of international experience

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The views presented in this presentation are exclusively those of the author and not necessarily those of the IMF.

High NPLs are a common feature of financial crises



Structural obstacles found in Cyprus back in 2013 common for countries with NPL challenges ...

- **Economic disincentives**
 - Inadequate capital buffers due to unrealistic collateral valuation and loan classification
 - Insufficient provisions due to incurred-loss approach and accrual of interest income from NPLs
 - Economic uncertainty impacts pricing and delays loan restructuring
 - Tax impediments
- **Information and resource challenges**
 - Lack bank-internal expertise and infrastructure to self-manage NPLs
 - Insufficient and outdated data for affordability assessments
- **Inefficient Insolvency regimes and institutions, debt enforcement rules**
 - Costly/protracted foreclosure procedures; limited out-of-court mechanisms, judges/insolvency administrators
- **Non-existent distressed debt market**
 - Discouraging foreign investment and attraction of specialist expertise

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... suggesting the need for a multi-faceted strategy for NPL resolution.

- **Require banks to recognize and act on NPLs**, reinforced by intense supervision
 - Int. experience: swift loss recognition (Sweden, Korea), supervisory engagement [strategy, targets] (Cyprus, Greece, Ireland, and Spain)
- **Reform debt enforcement and insolvency regimes** to facilitate asset recovery, debt restructuring, and liquidation
 - Int. experience: (i) *liquidation* of non-viable debtors (Ireland, Indonesia, Thailand, Turkey, Japan, and Korea); (ii) *rehabilitation* of viable debtors through insolvency procedures/out-of-court workout
- **Develop debt markets** to bridge “pricing gap” and leverage outside expertise
 - Int. experience: AMCs (private and public) used for NPL disposal/corporate restructuring (Sweden, Indonesia, Malaysia, Korea, and Thailand; Spain (SAREB) and Ireland (NAMA); loan servicing providers

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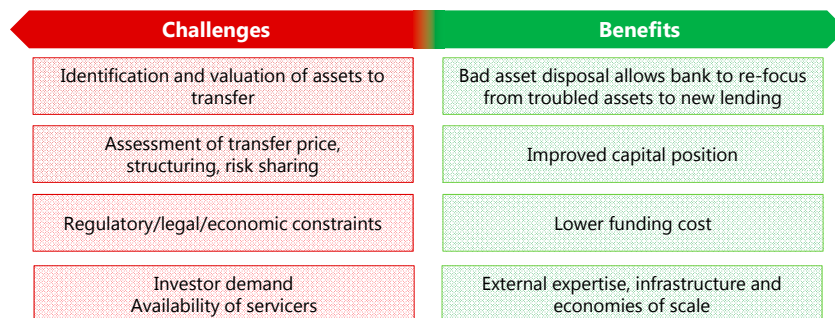
Legal framework: Tools and Institutions

- **Insolvency reform:** Enable permanent deleveraging
 - Pre-packs (minimal judicial intervention), Involvement of all creditors (including secured and public creditors), Priority for fresh financing
- **Out of court mechanisms:** 2nd avenue to manage case load
 - Enable consensual debt restructuring out of court pursuant to non-binding guidance
 - Hybrid features (stay; majority voting); Enhanced regimes (mediation; committee)
- **Institutions:** Enable application of legal framework
 - Specialized judges, Insolvency practitioners, ...
- **Tax:** Remove tax impediments
- **Country-specific issues:** Title deeds, public debt
- **Foreclosure regime:** Enable enforcement
 - Provide incentives, allow liquidation of non-viable borrowers
- **Communication:** Inform and educate borrowers

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Distressed Debt Markets and External NPL Resolution

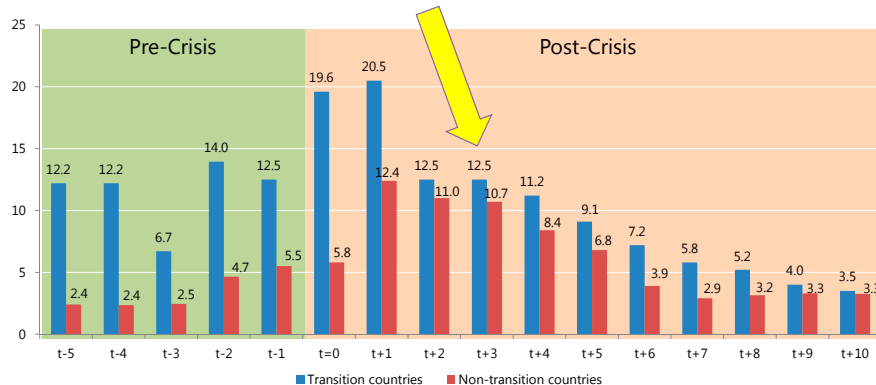
- Support the development of **distressed debt markets**
 - **Servicing:** leverages outside expertise, speeding up NPL resolution and increasing return; and/or
 - **Sale:** Removes NPLs from balance sheets, puts it into investment vehicles, taps outside financing.



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The Time Dimension of NPLs

Reverting to pre-crisis NPL levels takes years

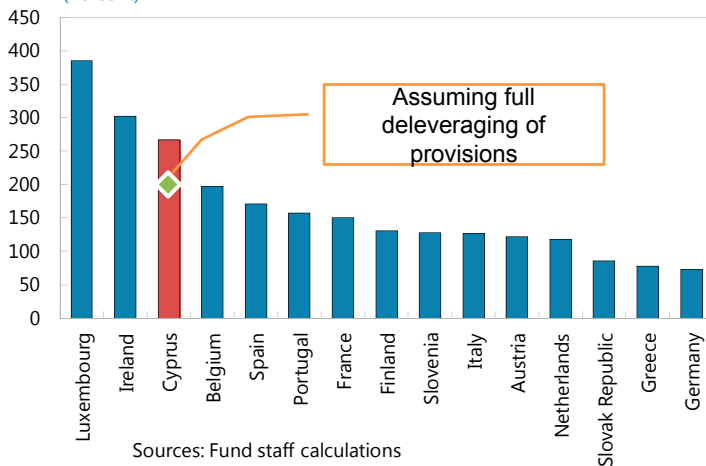


Source: EBRD, IMF. Note: t = 0 corresponds to the starting year of the crisis.
Transition countries (year of the crisis): Armenia (1994), Azerbaijan (1995), Belarus (1995), Bulgaria (1996), Croatia (1996), Czech Republic (1996), Georgia (1991), Kyrgyz Republic (1995), Latvia (1995), Lithuania (1995), Russian Federation (1998), Slovak Republic (1998), Ukraine (1998)
Non-transition countries (year of the crisis): Argentina (2001), Colombia (1998), Dominican Republic (2003), Ecuador (1998), Japan (1997), Korea (1997), Malaysia (1997), Nicaragua (2000), Philippines (1997), Turkey (2000), United Kingdom (2007), United States (2007), Uruguay (2002).

High indebtedness remains key impediment for NPL resolution and new lending

Corporate Debt Relative to GDP

(Percent)



Sources: Fund staff calculations

Thank you!

