NON-PERFORMING LOANS

CURRENT SITUATION

During the course of last year, the share of non-performing loans (hereinafter: NPL) in overall loans in the banking sector had been decreasing and reached its lowest level of 4.1% at the end of year.

The active involvement of the Serbian government and of the National Bank of Serbia (hereinafter: NBS) certainly contributed to this result because they adopted Action Plans as well as amendments and supplements to: the Decision on Reporting of Banks; Decision on Classification of Balance Sheet Assets and Office Balance Items of the Bank; Decision on Bank Risk Management; Decision on Bank Capital Adequacy; Decision on Management of Bank Liquidity Risk; Decision on Accounting Write-Off of Balance Assets of Banks, whereby the NBS as regulatory body undoubtedly influenced the heightened responsibility and caution in the activities of banks, as well as on good capitalization of the country's banking sector.

COVID-19

The outbreak of the COVID-19 pandemic triggered the enactment of a set of economic measures adopted by many EU members, upon reviewing the consequences which the pandemic might inflict, especially to small and medium-sized companies, entrepreneurs and citizens that may face lack of liquidity and difficulties in duly settling their financial and other obligations. In order to prevent the crisis, the European Banking Authorities – EBA enacted on April 2, 2020 Guideline EBA/GL/2020/02 ("Guidelines on legislative and non-legislative moratoria on loan repayments applied in the light of the COVID-19 crisis") which regulates the terms of application of the Moratorium with validity date until June 30, 2020, amended on June 25, 2020 by way of Guidelines amendment EBA/GL/2020/02 ("GUIDELINES AMENDING GUIDELINES EBA/GL/2020/02 on legislative and non-legislative moratoria on loan payments applied in the light of the COVID-19 crisis"), which extends the period of moratorium application until 30th of September this year.

Soon after the introduction of state of emergency (15.03.2020) due to COVID-19 pandemic, a set of regulations was adopted by the Government of the Republic of Serbia and National Bank of Serbia enacted a set of regulations which, in addition to the medical aspect, also deal with the economic aspects of the pandemic.

POSITIVE DEVELOPMENTS

The NBS enacted, among the others, the decisions that regulate standstill (a moratorium), in the repayment of obligations of borrowers or leasing clients, specifically the following:

- Decision on Temporary Measures for Preserving Financial System Stability
- Decision on Temporary Measures for Lessors aimed at Preserving Financial System Stability
- Decision on Temporary Measures for Banks aimed to reduce the impact of COVID-19 and preserve the Financial System Stability, that has been brought into force on 28.07.2020, and that has extended the moratorium validity period until 30th of September, 2020.

The Moratorium enables the borrowers not to settle their liabilities towards creditors on the basis of credit or leasing, including the payment of any costs, as well as the payment of default interest on the unsettled claim, and has suspended initiating enforcement proceedings, forced collection, etc., until the moratorium expiration date after which banks were to submit new repayment schedules to their borrowers.

In order to prevent possible deterioration of borrowers standing for certain loan categories (consumer, cash, except current account overdrafts and housing loans), the NBS has granted relief in the repayment terms to individuals with lower income and citizens wishing to extend their repayment period, specifically by means of:

- Decision on Supplement to Capital Adequacy Decision
- Decision on Amendments and Supplements to Decision on Managing Concentration Risk arising from Bank Exposure to Specific Products.

This foresees the possibility for refinancing i.e. to change the maturity date of the last loan instalment by an additional two years after present maturity term for the respective loan categories, provided that the borrower is creditworthy within a certain category type. This method of refinancing the obligations of debtors has a direct positive impact on reducing potential NPLs, given that all loans, which are subject to a moratorium (old and new) are not considered as restructured loans.

Having in mind abovementioned, in summary, the first wave of the epidemic was clearly well supported by bylaws passed on by the Government of the Republic of Serbia and NBS, however, it is also the fact that the decisions adopted by NBS in the previous period and executed by the banks enabled the financial sector to have enough funds and to sustain the state of emergency without any significant issues. However, as the situation with COVID-19 is still ongoing, nobody can accurately foresee the direction in which the global and local health situations are headed in, and by that, how it is going to impact the business environment. Hence, it is of crucial importance to monitor the situation in other to ensure the timely reaction by the both the state and NBS, followed by the adoption of necessary legislations enabling the control of NLP flows and their impact on the security of the financial sector as whole, especially having in mind that answer on question - how much will be increase of NPL percentage, we will be able to obtain at the end of Q1 of next year.

REMAINING ISSUES

Therefore, it is undeniable that because of COVID-19 on one hand and the set of measures on the other hand, and especially the measures referring to moratorium and guarantee scheme – there were no increase in NLPs, as there were no delays in payment, but generally speaking there was an increase in coast of provisions – because of which there is a room for action.

Last years' edition of the "White Book" on the topic of managing NPL portfolio has explained the necessity for the amendment of the regulations in detail, as well as its practical execution with the special regard to the Law on Consensual Financial Restructuring, Law on Enforcement and Security, Law on Tax Procedure and Tax Administration, as well as to the obstacles, such as the assigning of the regular loans outside of the banking sector. Having in mind the current COVID-19 situation, in this years' edition we haven't referred to the topic of NPL in the light of the existing regulations, however we still consider that these matters also require resolution, as stated below in the Recommendations section.

FIC RECOMMENDATIONS

These recommendations are in line with the White Book edition for 2019:

- Promoting out-of-court restructuring of debts in practice, in line with legal framework, in the process of out-of-court voluntary debt restructuring. (2)
- Enabling transfer of NPLs between resident bank and from resident to non-resident, regardless of whether it involves participants in syndication. (2)
- Removing obstacles for transfer of duly repaid receivables from legal entities from banks onto other legal entities, and not just onto other banks. (2)

Recommendations regarding mitigating the consequences of COVID-19

- To keep work on timely amendment of the regulations. (3)
- Consider possibilities for relief in provisions of banks. (3)
- Amendments to the Law on the Protection of Financial Service Consumers in order to enable that a bank may assign receivables from a natural person – financial services consumer to another legal entity. (3)