FX issues

Currency risk hindering Polish mortgage portfolio sales

Recent speculation that Deutsche Bank could be selling its Polish unit has highlighted the FX issues associated with shedding non-core mortgage assets in the country. Roughly a third of Deutsche Bank Polska's assets are said to be euro- and Swiss franc-denominated mortgages, the sale of which is likely to be challenged by the Polish regulator in an effort to maintain financial sector stability.

Poland has been grappling with Swiss franc- and euro-denominated mortgage loans since the financial crisis. More than half a million Poles took out Swiss franc mortgages before the crisis to benefit from lower Swiss interest rates.

The zloty, however, has declined in value against the franc over the past six years, leaving many borrowers struggling to repay their loans. Polish President Andrzej Duda promised during his election campaign last year to ease the burden on borrowers.

Stone Mountain Capital ceo Oliver Fochler notes that while the books are "highly distressed", based on the appreciation of the Swiss franc, the underlying credit quality "might be good".

According to Marek Chatrný, managing partner of Reform Capital, the Polish regulator's stance is not surprising. He attributes it to "the currency risk for the mortgage borrowers."

"If a third party purchases the portfolio, the regulator will be hard on them," he suggests.

As to how investors could overcome such a barrier, he says that there are two possibilities. "Either the bank could organise a securitisation fund itself or, even better, the bank keeps the assets on its books and agrees an income participation agreement where the bank doesn't sell anything, but it cannot undertake discounted settlements."

In terms of dealing with the foreign exchange risk of mortgage loans, Chatrný says that "investors will have a harder time collecting such an asset, since you have a better chance of collecting it if it's in zlotys." But he concedes that investors are interested in any NPLs, given the low yield environment.

Chatrný points out that most of the investors in Polish NPLs are local investors, including Polish pension funds and debt management firms, such as KRUK and Kredyt Inkaso. Some of them are foreign-owned, however. One example of the latter is Ultimo, which was acquired in 2014 by Norwegian debt management firm B2Holding.

Investors tend to be owners of a non-standardised securitisation fund - a "misnomer", as Chatrný calls it - funded by external investors from the UK or Scandinavia.

In April, GE Capital reduced its stake in Bank BPH in Poland by spinning off the non-mortgage banking assets to Alior Bank and retaining US$3.9bn of mortgages (FX and local currency). Other foreign lenders reportedly in the process of selling their Polish arms include Raiffeisen and UniCredit.

According to an April 2016 Vienna Initiative report, the NPL market in Poland and Eastern Europe began to gain momentum in 2015, with an increase in portfolio sales due to a growing number of lenders considering portfolio disposals and international distressed asset investors actively looking into the region in search of yield. The report notes that the improvement of economic conditions in 2015, coupled with an increase in provisioning following the AQR exercises in several of the CESEE countries, has served as a catalyst for NPL sales in the region.

In parallel, authorities and regulators across the region have prioritised the establishment of strategies towards NPL resolution. However, the report emphasises that of all the sub-categories of NPLs, residential loans/mortgages are less attractive to investors, due to stricter regulations associated with this asset class that render collection and enforcement more challenging.

In a follow-up report in October, the Vienna Initiative points out that on a year-on-year comparison, transaction volumes have been 30.1% higher in 2016 compared to 2015.

In Poland in particular, the gross value of NPL transactions increased by 55% between February 2015 and February 2016, according to KPMG's annual report on European debt sales. The report states that KRUK accounts for 21% of the purchased debt, making it the largest player in the Polish debt management market.

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