



**EUROPEAN CENTRAL BANK**  
BANKING SUPERVISION

**Andrea ENRIA**

Chair of the Supervisory Board

*COURTESY TRANSLATION*

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European Parliament  
60, rue Wiertz  
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Frankfurt am Main, 4 December 2020

**Re: Your letter (QZ-062)**

Honourable Members of the European Parliament,

Thank you for your letter on the temporary amendment of the provisioning calendar and the default criteria, which was passed on to me by Ms Irene Tinagli, Chair of the Committee on Economic and Monetary Affairs, accompanied by a cover letter dated 3 November 2020.

The coronavirus (COVID-19) pandemic has disrupted European economies and affected the risk environment in which Banks operate. Supervisors, regulators and governments have reacted swiftly to limit the procyclical impact of this crisis. As supervisors, we have ensured that banks can make use of capital and liquid resources to provide more financial support to borrowers and enable them to overcome temporary stress.<sup>1</sup>

Thanks in part to these extraordinary support measures, the crisis has so far not led to a noticeable tightening of lending standards. Also, so far banks have not experienced any material increase in non-performing loans (NPLs). In the second quarter of 2020, the NPL ratio for significant institutions stood at 2.94% compared with 3.22% in the fourth quarter of 2019.

However, we do expect non-performing loans (NPLs) to rise. To answer your first question, as I mentioned recently,<sup>2</sup> the ECB estimates that in a severe scenario with a much weaker and protracted recovery,<sup>3</sup> NPLs

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<sup>1</sup> See [press releases](#) dated 12 March, 20 March, 27 March, 16 April, 28 July, and 17 September 2020.

<sup>2</sup> See "[ECB: the EU needs a regional 'bad bank'](#)", [Financial Times](#), 26 October 2020.

at euro area banks could reach up to €1.4 trillion. Please note that it is still problematic to quantify the exact amount, mainly because of the current uncertainties in the macroeconomic outlook and the persistently high COVID-19 caseload in the euro area. The ECB is therefore monitoring the development of NPL ratios very closely.

Regarding your second question, I would first like to highlight that some adjustments have already been made in response to the pandemic. Notably, the ECB extended the preferential treatment foreseen for NPLs guaranteed or insured by official export credit agencies to NPLs that benefit from guarantees granted by national governments or other public entities.<sup>4</sup> Also, banks with high levels of NPLs have been allowed to postpone the submission of their plans to improve their asset quality. At the same time, in order to maintain a clear view on the risks in the banking sector, including in times of distress, it remains crucial to continue identifying and reporting asset quality deterioration and the build-up of NPLs in accordance with the existing rules. This is particularly necessary to encourage banks to engage with distressed debtors at an early stage and to provide them with appropriate solutions in a timely manner.

Moreover, I would like to reiterate that addressing NPLs has been one of the key priorities for ECB Banking Supervision since its inception. The overall objective of developing the supervisory approach was to avoid “wait and see” approaches, which lead to an excessive build-up of NPLs and impair the ability of banks to support the economic recovery. This was a key lesson learnt from the last crisis, as delaying the recognition and resolution of NPLs increases problems in the longer term and makes them harder to tackle. The NPL coverage expectations are a very important element of our framework that facilitates timely NPL resolution. First, they ensure that banks build up the provisioning buffers that are required to address NPLs. Second, they provide a strong incentive for banks to address NPLs in a timely manner.

Therefore, to answer your second question, we believe it is very important for the NPL coverage expectations not to be changed any further. As we already communicated in our FAQs on the ECB’s supervisory measures in response to the coronavirus,<sup>5</sup> our mitigation measures do not focus on the stock of NPLs accumulated prior to the outbreak. However, the ECB is fully aware that current market conditions may make the agreed reduction targets difficult to attain. In this vein, the Joint Supervisory Teams will show a large degree of flexibility when discussing the implementation of NPL strategies on a case-by-case basis.

In addition, the coverage expectations for loans originated as of 26 April 2019 have been included in the CRR,<sup>6</sup> and it is therefore outside the competence of the ECB to consider temporary adjustments to this rule.

To answer your third question, I would like to point out that the rule to classify loans 90 days past due as “in default” is set out in the CRR.<sup>7</sup> The ECB is therefore not competent to temporarily adjust this rule either. Still,

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<sup>3</sup> The vulnerability analysis performed by the ECB in July focused on two scenarios set out in the June 2020 Eurosystem staff macroeconomic projections for the euro area: the central scenario, the most likely to materialise according to Eurosystem staff; and the severe scenario, which represents a more adverse, but still plausible development of the crisis. The figure mentioned relates to the severe scenario.

<sup>4</sup> See [press release dated 20 March 2020](#).

<sup>5</sup> See [FAQs on ECB supervisory measures in reaction to the coronavirus](#).

<sup>6</sup> Article 47c of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms.

<sup>7</sup> Article 178.1 of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms.

from a supervisory perspective it would be disappointing to depart from a common rule that has been introduced after lengthy and laborious discussions, achieving for the first time a harmonised definition of default at the European level, in line with best international practices.

Yours sincerely,

[signed]

Andrea Enria