European NPLs: Smaller deals and a slower pace

The European non-performing loan landscape looks very different in 2022, with large deals driven by urgent government regulation supplanted by small but steady opportunities.

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Foreword

The market for non-performing and non-core loan deals remains in business—but not in the way that many expected after COVID-19 shut down vast swathes of the European economy.

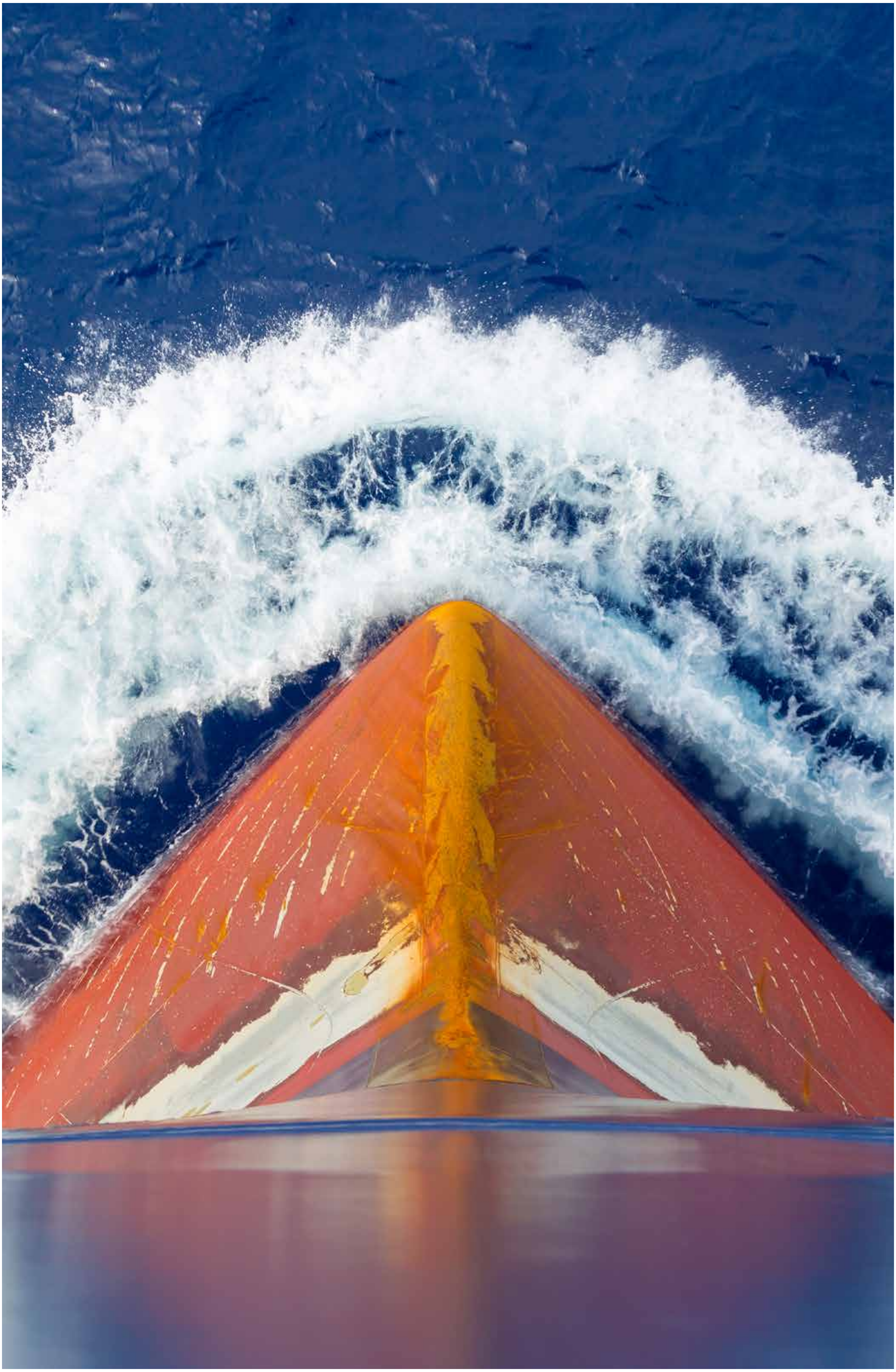
The banking sector's sale of legacy loans revived in 2021 following a marked slowdown in 2020, though the market did not return to the large-scale stocks of non-performing loans (NPLs) that were seen before the pandemic.

This may change if more distressed debt begins to emerge, having been protected by state interventions intended to support businesses affected by COVID-19. The events in Ukraine may also drive an increase in bad debt provisions and NPL volumes. For now, though, sellers, buyers and NPL market participants, such as servicers, are operating in a very different environment.

In this report, we take the temperature of that environment. The first section considers the changing dynamic of the marketplace, covering the outlook for NPLs, the rise of the secondary market transactions and the emergence of new types of NPL investors.

In section two, we take a deep dive into key markets across Europe. As in previous years, the economies of Southern Europe, led by Greece, Italy and Spain, were hotspots for NPL transactions. But other areas—notably Ireland, where NPL numbers were already relatively low—continue to see activity. Even in countries where banks are making very few disposals, the secondary market provides opportunities.

With so many unknowns, including the outcome of the situation in Ukraine and its impact on economics, the future for NPLs remains uncertain. But clear trends are emerging, from the growth of new entrants to the growing importance of data and analytics tools in driving value.



European NPLs: The journey from COVID-19 to Ukraine

While the spike in bad debt and subsequent tsunami of NPL and non-core loan deals that was anticipated due to COVID-19 did not materialise, the increasingly volatile market trends may lead investors to discover new and unexpected opportunities.

European NPL volumes continued to decline in 2021, as unprecedented fiscal and monetary interventions gave many organisations room to breathe that otherwise might have collapsed in the face of pandemic-related disruption.

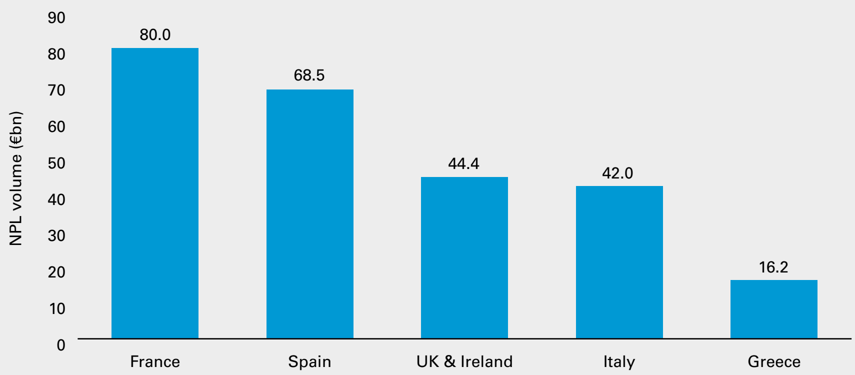
As the European Banking Authority (EBA) reported in its Q4 2021 Risk Dashboard: "The risk of significant economic disruption due to COVID-19 has continued to decline in the last two quarters."

Data from *Debtwire ABS Europe* shows that, at the end of the year, banks across Europe still had more than €300 billion in Stage 3 loans on their books. Looking at the largest banks in major jurisdictions, the bulk of these were in France, Spain, the UK and Ireland, Italy and Greece, with approximately €250 billion in NPLs between them and France leading the pack at €80 billion. While these numbers are still high, they are a far cry from the more than €1 trillion in European NPLs recorded back in 2014.

According to the EBA, countries with significant NPL ratios at the beginning of 2021 registered particularly impressive improvement. Moreover, asset quality increased throughout the banking sector, with a 7 per cent decrease in NPLs in 2021.

Policymakers are also relatively relaxed about the potential impact of the events in Ukraine on Europe's banks. Having said that, the situation is taking its toll—Cyprus-based RCB Bank has unveiled plans to close its banking operations in the face of geopolitical uncertainty, while banks across Europe have flagged write-downs totalling close to US$10 billion due to the conflict. Still, exposures to Russia and Ukraine account for just 0.3 per cent of banks' assets, the EBA points out, and loans to these countries are concentrated in a handful of lenders.

NPL volumes in Europe at end-2021 (€bn-equivalent)



Source: Debtwire ABS Europe, based on Stage 3 loans in financial reports from the largest banks in each jurisdiction

€300+ billion

Value of NPLs held by the largest banks in major jurisdictions across Europe at the end of 2021

For all that, however, it would be a mistake to grow complacent.

For one thing, the long-tail impact of COVID-19 remains unknown, particularly as governments have withdrawn pandemic-related support. Secondary effects of the crisis, such as supply chain disruption, inflationary pressure and rising interest rates, as well as the ongoing decline of the euro and various currency movements, continue to wash through Europe's economies and may tip some vulnerable businesses over the edge.

Notably, some governments are already considering further relief measures to insolvency laws to prevent a wave of real economy bankruptcies through uncertainties from the energy price shocks resulting from the Ukraine war.

Banks are already reporting evidence of potential stress. Volumes of Stage 2 loans—those in the early stages of underperformance—have begun to increase. So too have NPLs in sectors that have suffered disproportionately due to COVID-19.

Moreover, the events in Ukraine are casting a very long and dark shadow. The International Monetary Fund cut its global growth forecasts in April, citing "war-induced commodity price increases and broadening price pressures"— "Global growth is projected to slow from an estimated 6.1 per cent in 2021 to 3.6 per cent in 2022 and 2023. This is 0.8 and 0.2 percentage points lower for 2022 and 2023 than projected in January."

"EU/EEA banks also have indirect exposures [to the events in Ukraine] like those through businesses with trading links to these countries that could have a broader impact," warns the EBA's Dashboard.

For many market commentators, the potential for a recession in Europe in the next 12 months is becoming a real possibility.

Under the circumstances, it's entirely possible that we will see NPL volumes begin to climb once again.

NPL disposals slow

In the absence of a new stock of NPLs driven by the pandemic, however, the primary market for European banks disposing of toxic debt remains relatively flat. Disposals of legacy assets continue, particularly in markets such as Greece and Italy where state interventions underpinned such sales, but these have declined as banks worked through their backlogs.

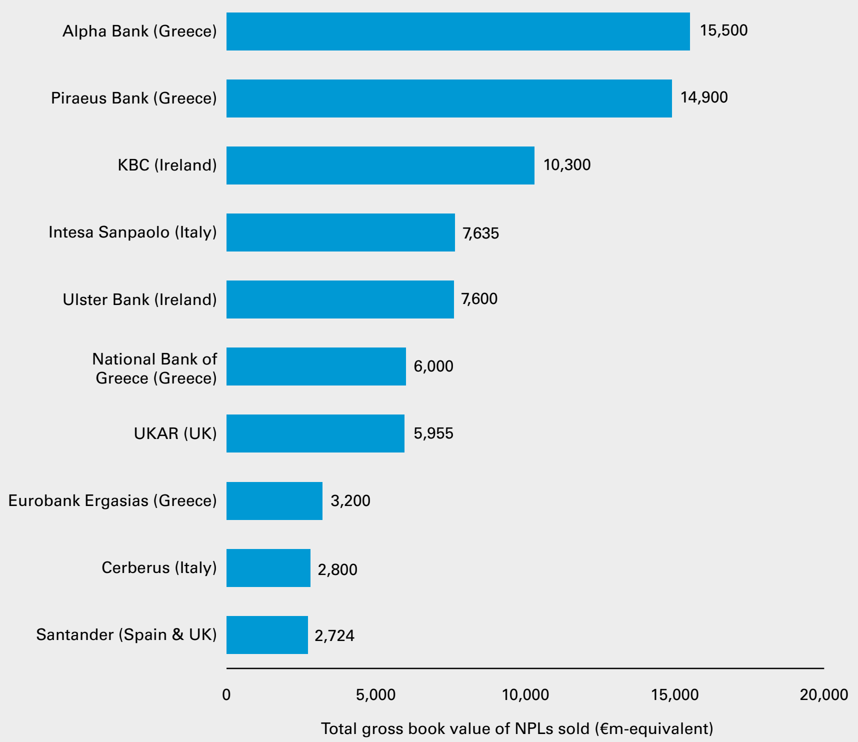
Analysis by *Debtwire ABS Europe* shows Europe's banks selling approximately €100 billion in NPLs and non-core loans in 2021. That is higher than 2020, when the pandemic caused extensive dislocation in the market for much of the year.

To put last year's figures into context, the latest analysis by *Debtwire ABS Europe* shows that European NPL sales were above €100 billion in four out of five years between 2015 and 2019. In 2018, the peak year for disposals, banks completed transactions worth more than €200 billion.

The stock of NPLs still on the balance sheets means there is scope for further deleveraging, but much of the legacy work has now been completed. In the absence of new stock, a return to earlier volumes is simply not possible. Smaller deal sizes are likely to be the norm for the foreseeable future. These will often be follow-on deals that mirror the structure of disposals already completed.

The other reason to expect the pace of disposals to be limited is that state guarantee schemes operating in Italy and Greece are coming to the end of their

European NPL top sellers in 2021 (€m equivalent)



Source: Debtwire ABS Europe's European NPLs database

Top European NPL deals signed in 2021 by volume

Seller	Country	Project name	Gross book value (m)	Buyer	Date
Alpha Bank	Greece	Galaxy	€10,800	Davidson Kempner	February
KBC	Ireland	-	€9,200	Bank of Ireland	October
Ulster Bank	Ireland	-	€7,600	Permanent TSB	December
Piraeus Bank	Greece	Sunrise I	€7,200	Intrum, Serengeti	June
National Bank of Greece	Greece	Frontier	€6,000	Bain, Fortress, doValue	October
Piraeus Bank	Greece	Vega	€5,000	Intrum	March
UKAR	UK	Jupiter	£5,000	Davidson Kempner and PIMCO	March
Alpha Bank	Greece	Cosmos	€3,400	Davidson Kempner	October
Eurobank Ergasias	Greece	Mexico	€3,200	doValue, Waterwheel	October
Intesa Sanpaolo, BPER	Italy	Grogu SPV	€3,100	N/A	December

Source: Debtwire ABS Europe's European NPLs database

lifetimes, due to end in 2022 and 2023 respectively.

Even if Italy extends its scheme, as the government hopes the European Commission will allow, structuring further disposals under these arrangements is becoming more challenging now that larger portfolios have been offloaded. The schemes require transactions to be of a certain size and structure to work effectively—because senior debt is guaranteed, but junior and mezzanine debt is not. Unless there is sufficient guaranteed senior debt to provide capital savings to offset any write-downs on the remainder of the debt, purchasers may struggle to achieve their targeted discounts.

There may not be enough NPLs left to create many more such arrangements.

The changing buyer pool

The changing profile of the primary NPL market is leading to shifts in the buyer pool, with two clear and distinct groups of potential acquirers for portfolios coming up for sale.

The first of these groups consists of traditional investors, including private equity (PE) firms, hedge funds and credit funds. This group continues to feature the large investors that have been the mainstay of the buyer pool in recent years—for example, large and experienced PE acquirers of NPLs last year included KKR and Apollo—but smaller players are also entering the market. These are often focused on more digestible portfolio sizes or a specific niche in the market such as a certain sector.

In many cases, these investors are focused on securing a return via a sale on the secondary market. They invest to drive up value in the portfolios through rehabilitation or asset recovery, for example, before parcelling up tranches of their NPLs to sell.

In the opposite corner of the market, specialist servicing firms that helped banks and investors manage their NPL portfolios in the past are now emerging as prominent acquirers of loan books. Armed with expertise and experience in NPL management built up through servicing contracts, firms such as Intrum and Hoist have become active participants in the primary NPL market, securing value by driving improved recoveries from loan books acquired at substantial discounts.

“The stock of NPLs still on the balance sheets means there is scope for further deleveraging, but much of the legacy work has now been completed.

In Greece, for example, Intrum took part in three separate deals in 2021 and five further transactions in Italy. Hoist was also active in both countries.

Consolidation to come?

One question is whether these market shifts presage a wave of broader consolidatory M&A activity. Managing NPL portfolios is capital- and people-intensive and does not necessarily generate the kind of returns being pursued by banks, particularly in an ongoing environment of low margins and reduced profitability.

For that reason, while banks will often see the value of retaining relationships with certain clients—even though their loans have slipped into non-performing territory—the case for offloading work-out units may be alluring. Carving out and selling such units to third-party servicers would reduce banks' cost bases, even if the underlying NPLs remain on their books, with a servicing contract agreed with the acquirer. In other cases, banks might look to offload the NPLs as well, taking further volumes off their balance sheets.

For acquirers of such units, long-term servicing contracts offer the prospect of stable revenue flows and rapid growth. Accepting the underlying exposure of the NPLs as a route to these benefits may be a risk worth taking, particularly for servicers with the analytical expertise to quantify such dangers more accurately.

The search for scale will be an important part of this story for servicers. For example, in April 2022, Hoist Finance announced the divestment of its UK credit management subsidiary, including its unsecured NPL portfolios. As CEO Lars Wollung said at the time, this reflected the organisation's desire "to grow and invest in portfolios where [Hoist] can generate higher returns".

Servicer consolidation has already accelerated in other markets, with three or four large servicers now often dominating where a dozen firms were active five years or so ago.

Growth in the secondary market

One impact of declining NPL disposals by banks will inevitably be that the secondary market for NPLs is set to become proportionately more significant, at least in the short to medium term. The secondary market may also be boosted by EBA proposals to standardise the requirements for the information that NPL sellers must provide to prospective buyers. The EBA hopes its plans will improve transparency in the secondary market, enable cross-country comparisons and reduce information asymmetries between sellers and buyers.

The appetite of investors to offload some, if not all, of their NPL investments will be an important driver of the trend to increased secondary market activity. As funds seek to repay their own investors, they must either flip their NPLs into new funds or sell the assets. This is putting additional pressure on funds, since returns on loan books acquired prior to the pandemic are likely to have been hindered by the various disruptions experienced in the past two years. Court processes, for example, were postponed, and specialists with the skill to drive rehabilitation of loans were in short supply.

Market consolidation has similar implications. Where banks decide to carve out NPL servicing units, or specialist servicers look to restructure, the secondary market will also come into play.

Still, managing these portfolios well will be as crucial as ever to achieve hoped-for returns. In fact, the performance of European NPL securitisations was mixed in the second half of 2021, according to reporting by *Debtwire ABS Europe*, with gross collections ratios improving and deteriorating in roughly equal numbers. Italian and Spanish transactions were particularly likely to underperform

relative to initial expectations.

The events in Ukraine could further muddy the waters in the secondary market. Loans that may look saleable at a certain price today may feel very different six months from now.

Dividends from data

Improvements in data and analytics will play an important role here. Specialist investors are using more sophisticated tools to secure an increasingly granular understanding of portfolio performance. New entrants from the fintech industry are already raising the standard in this regard, creating new opportunities to generate value or offload underperforming assets. The dividing up of larger portfolios for smaller sales will accelerate as a result.

Consolidation plays into this theme. Resources for investment are concentrated in the hands of larger servicers and these businesses are growing their analytics competencies. As the volume of data on NPLs increases—not least with securitisations required to report key information regularly to drive transparency—this trend will no doubt pick up the pace.

Given the chance to pursue a data-driven strategy to secure higher returns from NPLs and drive price discovery, new investors may be encouraged to enter the market.

PE funds and other investors with significant amounts of capital to deploy, coupled with the ability to leverage new data analytics tools, will become more active participants.

Dealing with reperforming loans

In an improving post-pandemic economic environment, some NPLs will have an opportunity to become performing loans once again. Banks that have disposed of such loans may wish to buy them back and rebuild a potentially profitable relationship with the customer. Equally, the acquirer may be keen to sell, hoping to realise a return on their original investment.

In practice, however, banking regulators can make such transactions difficult, even limiting a bank's ability to forge new relationships with such customers. Anxiety about arrangements that could increase the risk of further spikes in NPLs—for example, if loans slip once more—has led to restrictions on resales and arrangements of this kind.

The regulatory hazard is not to be overlooked. The need to enable banks to do business with customers that have recovered from difficulty is likely to become more pressing in the coming years. In some sectors, the outlook has improved very quickly in the wake of the pandemic. For example, the food and beverage industry has bounced back faster than expected, as has the tourism and hospitality industry. If banks and regulators can come to an agreement, NPLs in these areas may have a future.

Equally, as European countries seek to rebuild their economies, businesses will need access to new funding. Preventing them from working with banks they once knew well could inhibit growth.

“

Given the chance to pursue a data-driven strategy to secure higher returns from NPLs and drive price discovery, new investors may be encouraged to enter the market.

Regional spotlight on NPLs: Greece, Italy, Spain and beyond

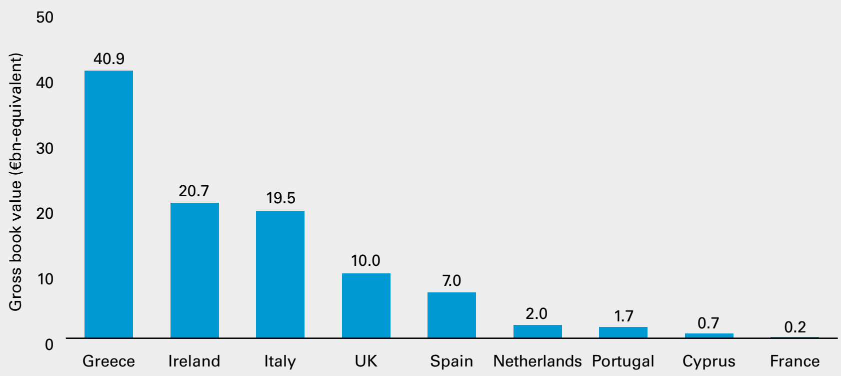
Europe's banks continue to defy expectations that the pandemic would drive a significant increase in NPLs—in fact, according to the EBA, not a single country saw its banking sector's NPL ratio increase in 2021, with the vast majority reporting an improvement.

While the pandemic failed to produce heightened levels of toxic debt, the European banking sector also continued its efforts to reduce existing NPL volumes. The trend was particularly strong in Greece and Italy, with banks making good use of the state-backed schemes offering generous guarantees on large tranches of NPL debt.

Elsewhere, however, disposals were more limited, with activity shifting into the secondary market. This may prove to be temporary, with some banks reporting increased provisions in 2021. The longer-term impact of the pandemic is still far from clear and a rise in bad debt is possible in the most exposed sectors of the economy, including retail, leisure and tourism. And while European banks have limited direct exposure to events in Ukraine and Russia, the broader impacts of the situation will begin to bite.

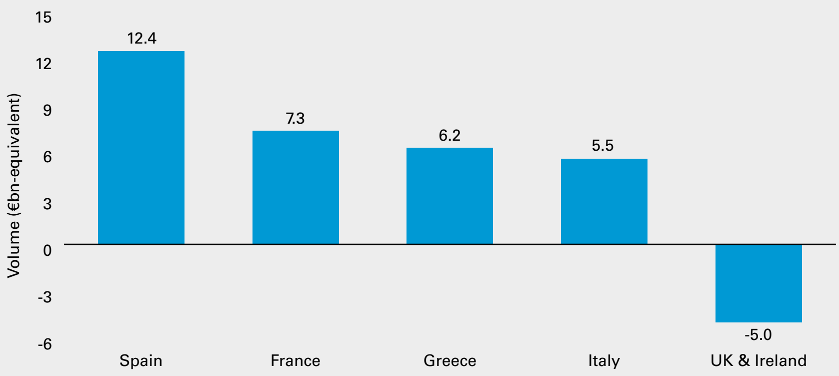
In the meantime, however, the average bank's NPL ratio across the European Economic Area fell from 2.5 per cent to 2 per cent in 2021, according to the EBA.

European NPLs: Total deals signed in 2021 by country



Source: Debtwire ABS Europe's European NPLs database

Provisions taken by top European banks by country in 2021



Source: Debtwire ABS Europe, based on provisions outlined in financial reports

GREECE: Rapid progress
Greece's banking sector continues to make strides towards normalcy, boosted by the government's Hercules Asset Protection Scheme (HAPS), which was modelled on the Italian Garanzia Cartolarizzazione Sofferenze (GACS) scheme. Through HAPS, the state guarantees securitised senior notes on loans while investors buy mezzanine and junior bonds.

The success of the HAPS programme has seen the proportion of Greek bank loans classified as NPLs fall from a high of close to 50 per cent in 2016 to 25.5 per cent at the start of 2021 and just 7 per cent by the end of the year.

In total, Greek lenders shed apprixmately €41 billion in NPLs last year, according to *Debtwire ABS Europe*. Of the deals contributing to that total, seven involved securitisations that took place through HAPS.

Those included Alpha Bank's €10.8 billion Project Galaxy NPL, with Davidson Kempner buying 51 per cent of the mezzanine and junior notes, Piraeus Bank's €7.2 billion Sunrise I deal with Intrum and Serengeti, and National Bank of Greece's €6 billion Project Frontier transaction with Bain Capital Credit, Fortress Investment Group and doValue.

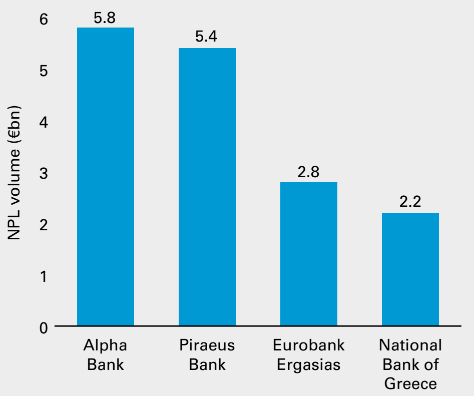
Outside of HAPS, deals in 2021 tended to be smaller, even as both Alpha Bank and Attica Bank completed €1.3 billion transactions.

Much of the hard work has now been completed for banks in Greece. By the end of 2021, the country's four largest lenders reported NPLs of approximately €16 billion on their balance sheets—significantly less than a year earlier.

The outlook also remains relatively benign, with little evidence of any post-pandemic surge in NPLs. Greek banks did take net provisions of €6.2 billion in 2021 just in case, but look set to avoid major setbacks.

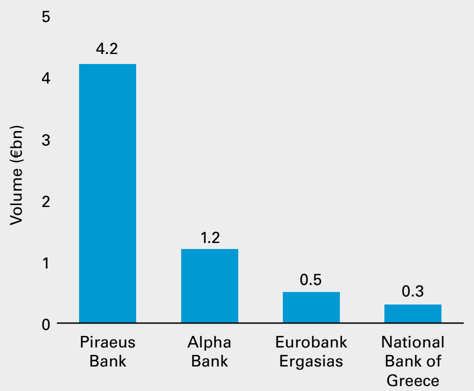
"By the end of 2021, the country's four largest lenders in Greece reported NPLs of approximately €16 billion on their balance sheets.

NPL volume in top Greek banks at end-2021 (€bn)



Source: Debtwire ABS Europe, based on Stage 3 loans in financial reports

Provisions taken by top Greek banks in 2021 (€bn)



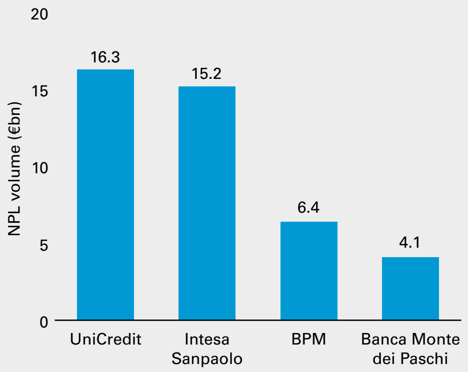
Source: Debtwire ABS Europe, based on provisions outlined in financial reports

Top NPL deals signed in Greece in 2021 by volume

Seller	Project name	Gross book value (€m)	Buyer	Type	Date
Alpha Bank	Galaxy	€10,800	Davidson Kempner	HAPS securitisation	February
Piraeus Bank	Sunrise I	€7,200	Intrum, Serengeti	HAPS securitisation	June
National Bank of Greece	Frontier	€6,000	Bain, Fortress, doValue	HAPS securitisation	October
Piraeus Bank	Vega	€5,000	Intrum	HAPS securitisation	March
Alpha Bank	Cosmos	€3,400	Davidson Kempner	HAPS securitisation	October

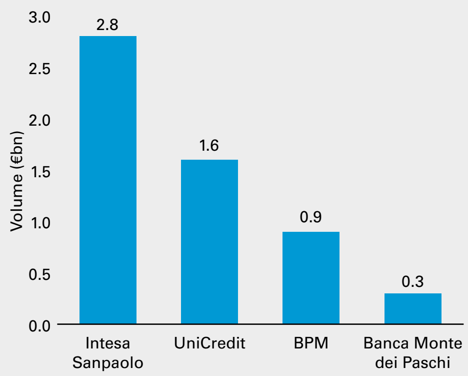
Source: Debtwire ABS Europe's European NPLs database

NPL volume in top Italian banks at end-2021 (€bn)



Source: Debtwire ABS Europe, based on Stage 3 loans in financial reports

Provisions taken by top Italian banks in 2021 (€bn)



Source: Debtwire ABS Europe, based on provisions outlined in financial reports

ITALY: Cautious optimism

Italian banks have further reduced their stock of NPLs in the past 12 months, helped by a one-year extension of the state-backed Garanzia Cartolarizzazione Sofferenze (GACS). The scheme, which works in similar fashion to the Greek HAPS programme, had been due to end in June 2021, but the European Commission backed an extension until June 2022.

The extension of GACS allowed Italian banks to reduce their NPL load from 4 per cent to 3.1 per cent of their loan books over the course of the year. The sector offloaded NPLs worth a total of €19.5 billion in 2021, including sales of unlikely-to-pay (UTP) portfolios valued at approximately €600 million, according to *Debtwire ABS Europe*. Almost half that total was accounted for by disposals made under GACS.

Those included Intesa Sanpaolo and BPER's €3.1 billion NPL securitisation, as well as the €1.3 billion Iccrea Banca NPL securitisation of a real estate lease portfolio, which took the total number of deals completed through GACS in the past five years to more than 40—collectively worth close to €100 billion.

Italy's secondary market also continues to be active, with leading transactions last year including Cerberus's €2.8 billion portfolio sale to Banca Ifis.

However, anxiety may be creeping into the market about the performance of Italian transactions. Underperforming deals such as 4Mori Sardegna, Leviticus SPV, Maggese, Belvedere SPV and Popolare Bari NPLs 2016 all reported decreases in collections ratios of low to mid-single digit percentage points, as did Monte Paschi di Siena's giant Siena NPL 2018.

Some analysts are growing nervous. Scope, for example, has recently downgraded the senior notes of 17 out of 26 NPL transactions, with an average downgrade of two notches. That said, several outperforming deals have increased their collections ratios, according to *Debtwire ABS Europe*. Diana SPV went from 41.15 per cent above business plan to 58.1 per cent and Futura 2019 improved from 21.38 per cent to 37.67 per cent. In the middle, big swings were seen for Yoda SPV, which improved 10 percentage points to 9 per cent above business plan, and Juno 1, which swung from 10.1 per cent above business plan to 6.33 per cent below.

In one bright spot, UBI's Sirio NPL has consistently outperformed its initial business plan, and extended that as of March 2022 with gross collections 110.43 per cent above business plan and a profitability ratio of 145.83 per cent.

Looking forward, activity levels in Italy are difficult to predict. Italy's government is reportedly lobbying the European Commission for a further extension of GACS, possibly for up to two years. And while Italy's banks disposed of €19.5 billion worth of NPLs in 2021, these institutions still have almost €42 billion in bad debt on their balance sheets and took net provisions of €5.5 billion in 2021.

Top NPL deals signed in Italy in 2021 by volume

Seller	Project name	Gross book value (€m)	Buyer	Type	Date
Intesa Sanpaolo, BPER	Grogu SPV	€3,100	N/A	GACS securitisation	December
Cerberus	Adige	€2,800	Banca Ifis	Unsecured	November
Intesa Sanpaolo	-	€2,600	MBCredit Solutions	Unsecured	September
Crédit Agricole Italia	Ortles 21	€1,800	N/A	GACS securitisation	December
Banco BPM	Aurelia SPV	€1,500	Elliott	GACS securitisation	June

Source: Debtwire ABS Europe's European NPLs database

SPAIN: Slower sales…for now

Most Spanish banks now have their NPL ratios under control and the flow of primary transactions has slowed, but secondary transactions by early-stage buyers are increasing, as are sales and securitisations of reperforming mortgage portfolios and giant servicing contracts are up for grabs.

The EBA reports that NPL ratios in the country's banking sector remained consistent in 2021, with 3 per cent of debt classified as non-performing by the end of the year, compared to 3.1 per cent 12 months earlier.

NPL disposals totalled nearly €7 billion in 2021. Notable deals included Sareb's offloading of a €1.6 billion portfolio of developer loans to Procobro and CaixaBank's sale of its €578 million residential NPL portfolio to KKR.

Banco Santander completed five disposals, including the sale of the €650 million Project Talos NPL portfolio to Marathon Asset Management, and the disposal of two Spanish hotel portfolios.

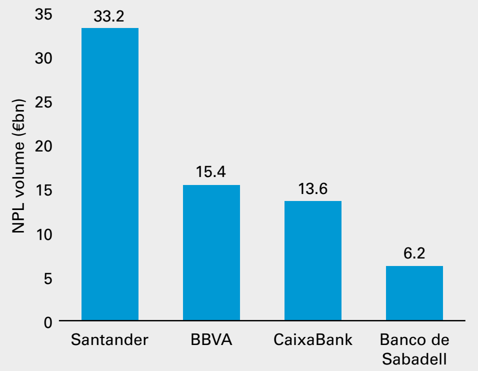
In the secondary market, *Debtwire ABS Europe* reports that some Spanish securitisations continue to disappoint, although last year did see a modest improvement for Prosil Acquisition (Salduero), whose collections increased a point to 50.5 per cent below business plan at the end of December. Retiro Mortgage Securities, however, deteriorated from 13.3 per cent below to 27.1 per cent below at the end of January.

Despite the progress made in recent years, Spain still has one of the largest stockpiles of NPLs in Europe. The country's four largest banks have €68.5 billion in bad debt on their balance sheets, despite disposals totalling €6.9 billion last year.

Moreover, provisions have risen sharply over the past 12 months, with the four largest banks earmarking a net €12.4 billion in 2021 for NPLs. Banco Santander took net provisions of €7.4 billion, while BBVA took €3 billion. That could swell the pipeline of deal activity in the months and years to come.

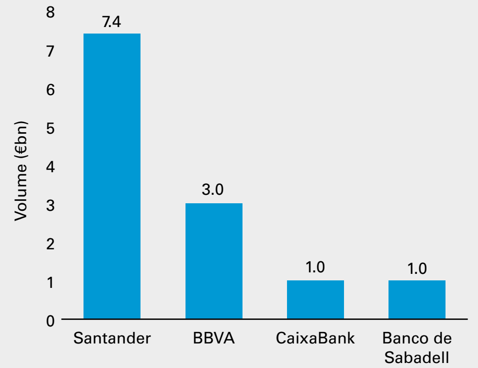
> **"Despite the progress made in recent years, Spain still has one of the largest stockpiles of NPLs in Europe. The country's four largest banks have €68.5 billion in bad debt on their balance sheets.**

NPL volume in top Spanish banks at end-2021 (€bn)



Source: Debtwire ABS Europe, based on Stage 3 loans in financial reports

Provisions taken by top Spanish banks in 2021 (€bn)



Source: Debtwire ABS Europe, based on provisions outlined in financial reports

Top NPL deals signed in Spain in 2021 by volume

Seller	Project name	Gross book value (€m)	Buyer	Type	Date
Sareb	-	€1,600	Procobro	Developer loans	July
Chenavari	Wave and Zenith	€700	Metric Capital with Albatris	Secured and REO–Residential, Commercial and Development (Secondary)	January
BBVA	Dakar	€700	KKR	Mixed secured and unsecured	January
Santander	Talos	€650	Marathon	Secured	August
Santander	Titan	€600	Tilden Park	Secured	December

Source: Debtwire ABS Europe's European NPLs database

REST OF EUROPE:

More modest activity

France, one of the European Union's largest economies, continues to report a benign NPL environment, with no sign of any imminent increase in impairments, and limited deal activity in the private market.

The French banking sector's NPL ratio was 1.9 per cent at the end of 2021, down from 2.1 per cent a year previously. Still, the country's four largest banks hold almost €80 billion in NPLs on their balance sheets, so more disposals can be expected in the years to come. That figure shrank by only €4.3 billion in 2021, and the four banks increased their provisions by a net €7.3 billion over the year.

France saw just a single NPL transaction in 2021, the €200 million disposal of small and medium-enterprise NPLs by Société Générale, picked up by iQera.

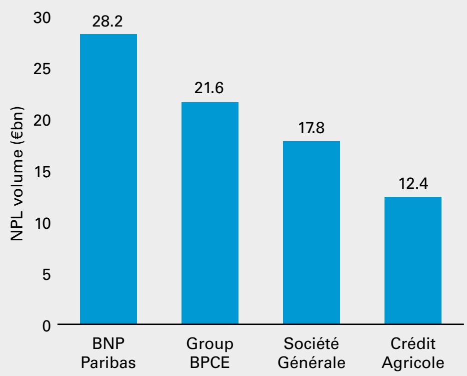
In the UK, the primary market for NPL disposals also remains muted, with just one significant transaction last year, NatWest Bank's £400 million Project Mercatus shopping centre NPL sale to a consortium of investors, which included Attestor, Octane Capital Partners and Ellandi.

Deal flows look unlikely to pick up in the immediate future, with the UK's four biggest banks reducing their NPL provisions by more than €4.5 billion last year. As a result, their NPL ratios averaged only 1.7 per cent by the end of the year.

Ireland continues to see heightened levels of activity, with €20.7 billion in NPLs and non-core loans sold in 2021, though the focus has shifted to disposals of performing loans by overseas lenders exiting the jurisdiction, such as KBC and NatWest. Ireland's three largest banks still hold NPLs and non-core loans with a gross book value of €7.9 billion on their balance sheets, though this was reduced by almost €1.7 billion last year. The sector's NPL ratio also decreased from 3.7 per cent to 2.8 per cent in 2021.

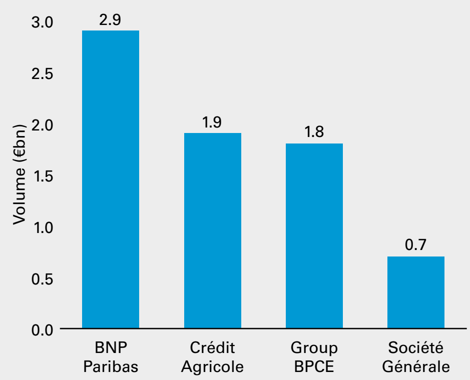
The German banking sector, meanwhile, continues to boast one of the lowest NPL ratios in Europe, with the EBA reporting a figure of 1.1 per cent at the end of 2021, slightly down on the 1.2 per cent at the start of the year. The country's

NPL volume in top French banks at end-2021 (€bn)



Source: Debtwire ABS Europe, based on Stage 3 loans in financial reports

Provisions taken by top French banks in 2021 (€bn)



Source: Debtwire ABS Europe, based on provisions outlined in financial reports

Top NPL deal signed in France in 2021 by volume*

Seller	Project name	Gross book value (€m)	Buyer	Type	Date
Société Générale	Orsay	€200	iQera	Secured – CRE	May

**There was only one NPL deal signed in France in 2021*

Source: Debtwire ABS Europe's European NPLs database

Top NPL deals signed in the UK and Ireland in 2021 by volume

Seller	Project name	Gross book value (€m)	Buyer	Type	Date
KBC (Ireland)	-	€9,200	Bank of Ireland	Mortgages	September
Ulster Bank (Ireland)	-	€7,600	Permanent TSB	Non-tracker mortgages and some SME loans	December
UKAR (UK)	Jupiter	£5,000	Davidson Kempner and PIMCO	Secured–Residential	March
Barclays (UK)	Barclays Asset Finance	£1,150	Pan European Asset Co and HPS Investment Partners	Secured	April
KBC (Ireland)	-	€1,100	CarVal	PDH and BTL mortgages	August

Source: Debtwire ABS Europe's European NPLs database

two largest banks were carrying €14.7 billion in NPLs on their balance sheets at the end of the year, down €329 million year-on-year. Provisions increased by a net €395 million over 2021, but German banks announced zero sales of NPL portfolios last year.

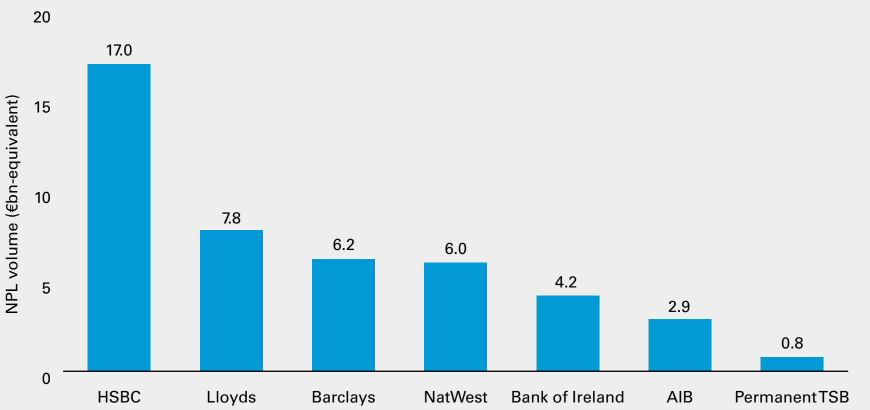
One other country worth mentioning is Cyprus, where the Bank of Cyprus announced the Helix 3 sale of €698 million in NPLs to Pimco in November 2021. The disposal of this portfolio of 20,000 loans enabled the bank to bring its NPL ratio down to 8.6 per cent, taking the figure into single figures a year earlier than it had previously expected.

Indeed, while the banking sector in Cyprus is small in the context of Europe as a whole, it does have a significant NPL issue. Its NPL ratio has come down in the past year, but still stands at 4.1 per cent, one of the highest on the continent.

The country is also more exposed than most to Russia. RCB Bank, for example, has faced scrutiny from regulators given its links to Russian bank VTB, which owned a substantial stake in RCB until earlier this year. It recently sold a €556 million portfolio of NPLs to Hellenic Bank.

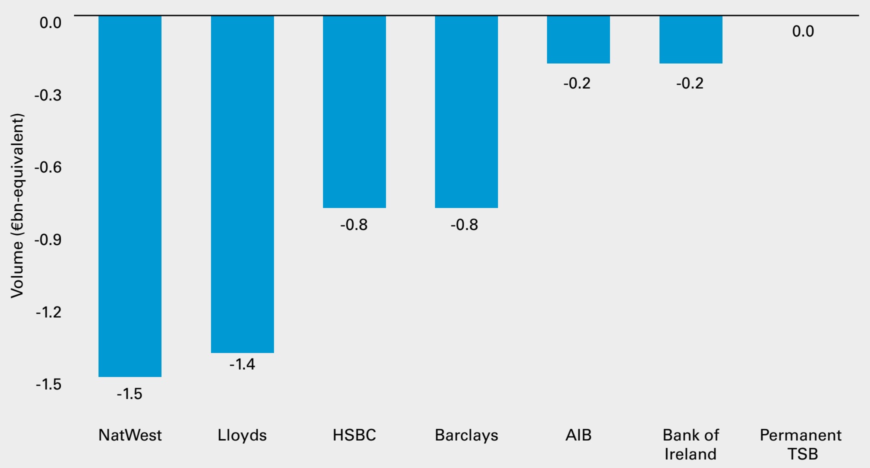
Moreover, Cypriot loan books loom large for banks in other jurisdictions. In February 2022, Greece's Alpha Bank announced the sale of a portfolio of Cypriot loans and real estate properties to Cerberus—the Project Sky portfolio was valued at €2.4 billion.

NPL volume in top UK and Irish banks at end-2021 (€bn-equivalent)



Source: Debtwire ABS Europe, based on Stage 3 loans in financial reports

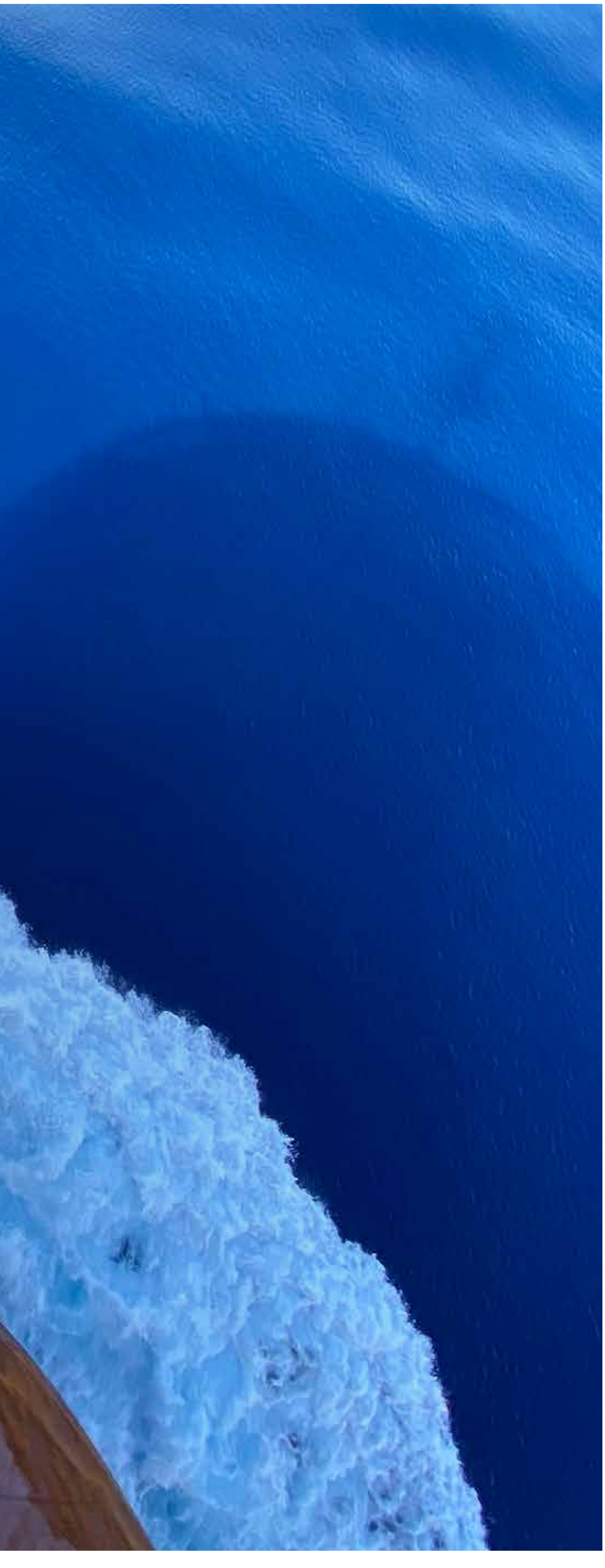
Provisions taken by top UK and Irish banks in 2021 (€bn-equivalent)



Source: Debtwire ABS Europe, based on provisions outlined in financial reports

NPL market dynamics are changing, possibly for good

What does the future hold for NPLs? There's still plenty of business to be done, but buyers and sellers alike will need to change tack to get the most from the available opportunities.



In our previous report, we pointed to a poll in which 70 per cent of respondents expected to see an increase in European NPL sales in 2021. The majority view would prove to be correct, but making forecasts for 2022 and beyond looks to be fraught with difficulties.

On the one hand, many European banks still hold significant stocks of NPLs, particularly in hotspots such as Spain and Italy, but also in France and in the UK and Ireland. Moreover, as the impact of COVID-19 continues to unwind and the economic fallout of the events in Ukraine grows, not to mention the potential for a recession on the horizon, there is scope for more loans to slip into non-performing territory.

It is possible that the year ahead will see banks under even greater pressure to make increased disposals—particularly while state-backed schemes in Italy and Greece continue to provide support in the process.

The counterargument is that, when it comes to legacy NPLs that banks were required to reduce in recent years, much of the heavy lifting has already been done. What remains is relatively modest by comparison. In 2015, for example, the EBA says the average bank in the European Union had an NPL ratio of 6.2 per cent. Today, the figure is down to 2 per cent.

In other words, even if current market volatility leads to a significant increase in NPL volumes, the need for large-scale disposals remains diminished, at least for the foreseeable future.

This is not to suggest that this is a market lacking in opportunity, just that the dynamics at play are changing. New entrants, including servicers with expertise and experience built on supporting investors, will introduce more competition, both for smaller disposals by banks and in the secondary market. Indeed, that secondary market is thriving.

Equally, growing sophistication in data and analytics technology is enabling buyers and sellers alike to pursue opportunities with greater clarity on price discovery and potential return. The regulatory backdrop is also changing, as we move towards the end of state-support schemes.

The bottom line is that, while the future direction of the NPL market is not set in stone, clear trends are emerging. Existing players and new entrants alike are beginning to position themselves accordingly.

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