UniCredit

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For publication

UniCredit response to the EBA consultation paper on "Draft Regulatory Technical Standards on the conditions that competent authorities shall take into account when determining higher risk-weights, in particular the term of "financial stability considerations" under Article 124(4)(b) CRR and the conditions that competent authorities shall take into account when determining higher minimum LGD values under Article 164(6) CRR"

UniCredit is a major international financial institution with strong roots in 17 European countries, active in approximately 50 markets, with more than 8,100 branches and over 146,600 employees at a Group level. UniCredit is among the top market players in Italy, Austria, Poland, CEE and Germany.

With reference to the exposures secured by either residential or commercial immovable properties, the CRR raises the issues that the risk weights resulting from the standardized approach and, likewise, the minimum LGD floors, in case of internal rating based (IRB) models, may be not enough conservative and may not embed relevant and updated information on forward-looking property market developments with the risk to underestimate the related risk weighted assets (RWA).

In this context, UniCredit welcomes the opportunity to reply to this EBA's discussion paper, which can be included in the EBA's broader scope of revision of the internal risk models. UniCredit indeed appreciates any regulatory effort as long as it is intended to preserve risk sensitivity and establish a level playing field, harmonizing rules across Europe. Notwithstanding, UniCredit has some concerns about the approach adopted by the EBA.

In fact, within the set of conditions identified to assess the appropriateness of the risk weights or LGD floors, UniCredit deems that the indicators chosen as predictors of future market developments are deeply affected by local market conditions and tend to vary even significantly across jurisdictions. When higher risk weights are set to one or more property segments, the competent authority should hence carefully consider those market-related peculiarities. Provided that market-related peculiarities should be duly taken into account, it is nevertheless important to have clearly defined reference criteria ensuring consistency of application across jurisdictions and preserving level playing field.

UniCredit would also challenge the choice of the factors made by the EBA, which represents a limit of the envisaged approach. As far as the Italian immovable property market is concerned, estimates based just on the immovable market prices and their volatility would not have been able to capture the rise in the losses observed in these years, which have been affected by several other non-macroeconomic indicators. For instance, an important source of information, during these stressed times, was the outcome of public auctions (due to the decrease in attendance and offers) and the very long-lasting recovery period. Since price and recovery trends of the more ordinary channels of sale and public auctions significantly diverge, this proved that a price indicator which mixes both is not reliable.

More importantly, to be effective a regulatory framework must be certain. Although it has been made clear that the proposed benchmarks are only indicative thresholds and do not automatically trigger any risk weight increase per se, their rationale has not been disclosed. UniCredit would appreciate a clarification on how already realized losses data are linked to their expected realization. Furthermore, with regard to "financial stability considerations", UniCredit deems that its definition is too vague and no benchmarks/early warnings are provided to assess the level of severity of the described phenomena which could jeopardize financial stability.

Another consideration that UniCredit wishes to point out is the importance of what referred to in art. 2(2)(f) of the consultation paper, namely to assess whether the increase of total risk-weighted amounts of exposures secured by immovable properties is already achieved by a reduction in the Loan-to-Value (LTV) ratio. This aspect seems to have been already addressed within the revision of the standardized approach for credit risk which is under finalization by the Basel Committee. Such a revised approach envisages the LTV as a risk driver that, together with the Debt Service Coverage Ratio (DSCR), would drive the identification of the risk weight linked to the underlying exposure. UniCredit is concerned that, being both the global as well as the European regulators committed on the revision of modelling methodologies of the same asset classes and with different timing of application, this might create overlaps and misalignments, forcing banks to operate in an uncertain regulatory environment.

Finally, since the EBA's declared goal is to harmonize practices across Europe, UniCredit deems relevant to highlight that in the standardized approach to assess the appropriateness of the risk weights the loss experience (taken from COREP, so an observed datum) is compared with the losses which are expected to be realized, while in the case of the IRB approach, banks will have to measure the discrepancy between the weighted average LGD for retail exposures secured by immovable property and the weighted average LGD they expect to be realized. Hence, UniCredit is wondering whether this difference in the approach could not generate unwarranted misalignments between standardized and IRB banks.

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Please find below the list of the key people involved in this work, whose contribution made possible to coordinate and provide UniCredit response to this Consultation. Some other experts have been involved in UniCredit, but are not listed below.

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