NPL ABS: Italian NPL sales to exceed €60bn in 2017 but investors warned of high portfolio sale failure rate

By Anna Carlisle, Jul-17

The Italian NPL market, which has approximately €324bn GBV of NPLs, is "the place to be," according to a new report from PwC. The firm cites the restructuring process of ailing banks, massive NPL deleverage plans at significant banks and a prominent overhaul of NPL management as a result of ECB guidelines. PwC predicts that transaction volume will easily reach and exceed €60bn in 2017. The €26.1bn Banca Monte dei Paschi di Siena (BMPS) securitisation - confirmed earlier this week - will account for a large portion of that amount. Banca Carige's Brisca Securitisation will also contribute.

Amendments to the Italian law on securitisation in June 2017, allowing the SPVs to purchase the asset securing securitised receivables (including assets subject to leasing agreements), will result in a higher number of transactions by encouraging more players, both originators and investors, to enter this market, PwC said.

Industry sources say that the number of parties looking at investing in Italian NPLs is already on the rise - with a particular uptick in the past six months. New investors from both sides of the Atlantic are currently assessing options - with varying amounts of cash to invest. According to Amelia Colvin, MD and global head of distressed and non-performing assets at Cadogan Securities, investors need to approach this market with caution.

"It is important to understand the ongoing political risk and failure rate of NPL portfolio sales," she said. "Many sellers (i.e. Tier 2 banks) lack experience in carrying through trades to the finish line. Some trades are failing to complete because the sellers add terms that were not in the original mandate, for example, or even change their mind before the deal is finished. It can be very unpredictable."

She said several investors have decided to seek opportunities in other markets once they understood those risks. "Small funds with €30m to €50m to deploy do not have a critical mass to be successful or make a significant impact in the Italian NPL market," she added. "Investing small sums carries significant risk." She suggested that deals are more likely to succeed when investors and counterparties partner together and find creative solutions to bring down the level of NPLs. "Having the capital is simply not enough," she added.

Kanav Kalia, director at Oxane Partners suggested that funds from the US in particular have been looking to get involved with European NPL opportunities in recent months. "Distressed funds set up in the wake of the 2007-2008 crisis are looking for fresh avenues and better returns and are therefore looking to NPL opportunities in Europe," he said. "Jurisdictions of interest are Spain, Italy and Portugal, while opportunities in the Greek market may emerge in the coming months."

According to Mr Kalia, those firms will purchase directly from the banks or via the secondary market, the former being the preferred option given the potential for higher IRR. The secondary market buys, he said, are more likely when funds are ramping-up their NPL book, thereby giving them a good exposure before going full steam. "The securitisation of NPL portfolios purchased by such US funds is one potential avenue to exit," Mr Kalia added.

The US funds purchasing portfolios of NPLs plan to ramp up their presence in Europe. This might be done by purchasing a majority stake in a servicer already active in the region. Alternatively, funds that are taking a longer-term view in a particular jurisdiction may set up a servicing arm from the ground up.

Recent activity

Atlante II, a fund set up in 2016 exclusively to purchase Italian banks' NPLs, confirmed earlier this week it will purchase 95% of the junior and mezzanine tranches issued by Banca Monte dei Paschi di Siena's (BMPS) €26.1bn NPL securitisation, according to Quaestio Capital Management, the firm that manages Atlante II. The senior tranche will be retained by MPS and sold once the rating and the GACS state guarantees have been obtained. The average purchase price is 21% of gross book value. In addition to the return of 12% for the fund, 50% of any additional returns will be distributed to BMPS.

Banca Carige has confirmed the structuring of its first NPL securitisation, called Brisca Securitisation Srl. The SPV has issued three classes of ABS: a €267.4m senior class, rated BBB(high) and A3 by DBRS and Moody's, respectively; a €30.5m mezzanine class, rated B(low) and B3 (DBRS and Moody's); and a €11.8m junior class of notes, which is not rated. The securities issued were fully underwritten by the Carige Group at their nominal value of approximately €309.7m, which is c.33% of the gross amount of transferred NPLs (c.€938m). The junior and mezzanine notes will be placed on the market for the purpose of deconsolidating the portfolio of transferred loans, according to a statement from Banca Carige, and the bank will apply for the Italian Government guarantee scheme (GACS).

Banca IMI (Gruppo Intesa SanPaolo) is arranger and placement agent in the transaction, while Prelios Credit Servicing is servicer. Studio Chiomenti, PwC Legal, Securitisation Services, BNP Paribas and Zenith Service took part in the deal. Earlier this year UniCredit sold a €17.7bn NPL portfolio to two separate securitisation vehicles built, respectively, by Fortress Investment Group and Pimco, with the seller retaining a minority stake in each vehicle. According to PwC, ISP has closed the largest Italian NPL deal not involving a securitisation this year, with Christofferson, Robb & Co. and Bayview buyers of c.€2.5bn (Project Beyond the Clouds).

Algebris Investments reached an agreement to buy €750m from Banco BPM (Project Rainbow). In May 2017 UBI acquired three regional lenders (Banca Marche, BPEL and CariChieti) and BPER acquired the regional bank CariFerrara, following their rescue in 2015 by Italian Authorities and the sale of their NPL to the bad bank "REV" (€10.3bn) in 2015 and to Atlante Fund (€2.2bn) in 2017.

PwC foresees that from 2017 onwards the transactions likely will include not only bad loans (NPLs), but also the other categories of non-performing exposures such as Unlikely to Pay (UTP) and Foreborne loans. "In other words, we expect new trends in the market as the sale of portfolios composed by mixed asset class as well as portfolios made by a limited number of borrowers specialised in real estate developments and sale of single names under restructuring," they added.

