BANKING & FINANCE

ANNUAL REVIEW **2015**

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Financier Worldwide canvasses the opinions of leading professionals around the world on the latest trends in banking & finance.

Contents


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Contents


01 0 1 0 1010101 10 101 0 1 0 1010101 10 101 0 1 0
1010101 10 101 0 1 0

INTRODUCTION

The financial crisis, which shook banking and financial markets to their core, is now a thing of the past. Yet across many jurisdictions, 2015 was still a mixed year for the banking and finance space.

Volatility has been felt across a number of important markets over the last 12 months. In the US, leveraged lending and high-yield issuance declined, whereas investment grade volume, mainly with regard to acquisition finance, was up.

Measures such as the US Leveraged Lending Guidelines have had an impact on borrowing. The guidelines follow other major regulatory developments in recent years, including Basel III, with its additional capital controls and requirements, and Dodd-Frank, which continues to pose new challenges to firms operating in the banking and finance space across Europe and the US.

Alternative forms of lending are also becoming more mainstream. Peer-to-peer and crowdfunding have become a more accepted form of financing, although there are calls for greater regulation in this area. In Spain, for example, crowdfunding platforms must now be registered with the National Securities Market Commission's registry and are subject to supervision by the Bank of Spain and to certain financial requirements.

The banking industry is a different animal compared to few years ago, as participants and lawmakers work to repair the reputational damage stemming from the financial crisis. Organisations continue to make significant changes to the way they conduct business. These changes are being felt at all levels.

Looking ahead, it seems unlikely that 2016 will be vastly different to 2015. In certain markets, lenders remain cautious, while in others, liquidity in the debt markets is set to increase.

UNITED STATES

LAUREN HANRAHAN
MILBANK, TWEED, HADLEY & MCCLOY

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN THE US? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

HANRAHAN: Banking and finance activity in the US in 2015 has been more volatile than in the prior year. By most accounts, leveraged lending and high-yield issuance in the US was down throughout 2015. Investment grade volume – particularly with regard to finance acquisitions – was up.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN THE US?

HANRAHAN: Unregulated financial institutions, business development companies and various types of funds have become more active presences in financing transactions recently, in particular in smaller and middle market transactions, due to the influence of the US Leveraged Lending Guidelines, among other factors. Borrowers continue to have access to a broad array of financing options, which seem to ebb and flow in popularity. For example, by many accounts there has been less second lien loan issuance this year.

Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

HANRAHAN: While the US Leveraged Lending Guidelines have sought to influence certain loan terms, borrowers have generally had the upper hand in negotiations recently and pushed for additional debt capacity – both in the form of future incremental debt capacity inside of the credit agreement and other pari passu, unsecured, junior lien and subordinated debt outside of the credit agreement – and additional acquisition, dividend and other covenant flexibility. Covenant-lite loans – credit facilities in which the financial maintenance covenant is only available for the benefit of the revolving credit facility and not the term loan facility – are available to many borrowers, although perhaps they have been less common than in prior years.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

HANRAHAN: In the US, it is relatively easy to grant and perfect a security interest in most types of assets under one pledge and security agreement and by making simple filings, called UCC financing statements. Real estate mortgages will need to be handled separately and other types of collateral will require additional perfection steps. There is typically an acknowledgment that the cost of perfecting certain types of collateral exceeds the benefits to the lenders of receiving such collateral, and guarantees from certain types of subsidiaries would not provide meaningful credit support. This acknowledgement often results in negotiating materiality thresholds or an agreed set of 'excluded assets'.

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN THE US OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

HANRAHAN: The regulatory changes, such as the Leveraged Lending Guidelines and Dodd-Frank, introduced over the last few years will continue to impact the banking industry. Additional capital requirements, such as Basel III, will continue to be phased-in in the short-term.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

HANRAHAN: The challenges will likely be the same as over the last few years. Implementation and compliance of the various applicable regulations and capital requirements will likely be at the forefront of the minds of senior banking and finance executives. There will likely be continued pressure on terms from borrowers and there will always be pressure to ensure discipline with respect to credit analysis and deal structuring.

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN THE US OVER THE NEXT 12-18 MONTHS?

HANRAHAN: The current trends will likely continue for the next 12-18 months.

"There will likely be continued pressure on terms from borrowers and there will always be pressure to ensure discipline with respect to credit analysis and deal structuring."

Milbank

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Lauren Hanrahan is a partner in the New York office of Milbank, Tweed, Hadley & McCloy and a member of the firm's Global Leveraged Finance Group. Ms Hanrahan's practice centres on representing banks and other financial institutions in senior lending transactions. She has significant experience in representing lenders in acquisition financings, including leveraged buyouts, tender offers and other going private transactions, recapitalisations, bridge and mezzanine financings, debtor-in-possession and exit facilities and special situation financings. She has a broad range of financing experience in both US and international transactions.

UNITED KINGDOM

NEIL CADDY
MILBANK, TWEED, HADLEY & MCCLOY

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN THE UK? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

CADDY: Banking and finance activity in the UK has been somewhat mixed this year. Earlier in the year the demand for paper from investors was extremely high. This meant that arrangers had little trouble in syndicating and indeed many larger deals undertook re-pricing transactions post closing. More recently, however, the buy-side seems to be much more selective as to which deals to invest in, meaning that re-pricing activity has dried up. This has also led to spreads widening when compared to earlier in the year and deal volumes have shrunk as compared to this time last year. That said, for the right credits, banks have in general been demonstrating that they are still very keen to lend to corporates.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN THE UK?

CADDY: I think this year in the UK can be characterised by the continued proliferation of the cov-lite loan product for big-ticket financings in particular and the increasing role of alternative capital providers in the small to mid-market. Neither of these trends are new for this year but activity levels in those areas suggest that both are here to stay. Cov-lite deals are now commonplace and are increasingly moving toward the terms available in the United States and are providing a good alternative to the high yield market for borrowers. The number of alternative capital providers which are active in the UK are increasing – many of which are able to write larger cheques than they could previously, thereby opening up the scope of transactions that they participate in.

Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

CADDY: Pricing does seem to have widened this year as compared to earlier in the year. The syndicated debt markets appear to be comfortable with the cov-lite product. The movement of the terms available in the loan market towards those in the US and the high yield product started with the top end of the market but it does appear, at least on certain terms, to be extending to the upper mid-market syndicated product as well. However, banks remain alive to jurisdictional specific issues that need to be kept in mind when doing deals in Europe. In alternative capital deals there is pressure to loosen terms but for the most part providers have been successful in maintaining reasonable covenant packages. In those deals, borrowers can of course take comfort from the fact that they will have a smaller lender group to deal with when it comes to waivers and amendments.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

CADDY: Lenders are taking precautions, however they recognise that there will always be a cost-benefit analysis to do when determining precise security packages. For instance, in pan-European deals being done out of the UK, real estate security will be very expensive to take in certain jurisdictions and may therefore fall outside of the security net. In the UK, this will not be an issue since all asset security can be taken under English law in a single debenture at minimal cost, but a proportionate approach will still be required in relation to perfection steps required in relation to certain assets. In most instances, debtors will need to accept a reasonable level of cover, in particular in relation to structurally important assets, such as shares and shareholder loans at the top of their group structure where possible.

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN THE UK OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

CADDY: There have been a number of regulatory changes introduced over the last few years that will continue to impact the banking industry as the effects of the changes are felt and the measures that they impose are phased in. Additional capital controls and requirements associated with Basel III and its implementation through the CRD IV Directive will continue to take effect in the UK and across Europe. Leveraged Lending Guidelines issued by the Federal Reserve in the United States will also continue to affect banks that operate in the US or are regulated there, even with respect to lending activities carried out in the UK.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

CADDY: I don't think the challenges will be that different to those encountered over the last few years. There will always be pressure on terms from debtors and there will always be pressure to ensure discipline with respect to credit analysis and deal structuring. That said, one area that may impact bankers on a day-to-day basis could be the introduction of a new individual accountability in banking and the senior managers regime by the FCA and PRA in the UK, which seeks to increase accountability for certain individuals at regulated entities. The regime is due to be implemented on 7 March 2016 and could see additional procedures imposed by those regulated entities in order to ensure and demonstrate compliance with the new regime.

“Alternative capital providers will continue to provide an alternative option for a wider array of debtors.”

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN THE UK OVER THE NEXT 12-18 MONTHS?

CADDY: In general terms, the banking and finance landscape should not change a great deal over the next 12 to 18 months. I would expect the trends we have seen over the last 12 to 18 months to continue. The UK market I expect will continue to track and converge with the market in the US and alternative capital providers will continue to provide an alternative option for a wider array of debtors. I would expect deal volumes to increase as compared to 2015.

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IRELAND

JOHN-HUGH COLLERAN
DILLON EUSTACE SOLICITORS

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN IRELAND? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

COLLERAN: Banks and financial institutions in the Irish market have continued to deleverage their balance sheets on a large scale by way of loan sales to international investors. However, after much loan sale activity by almost all of the traditional players in the market over the past two to three years, the end of this phase is now in sight. The National Asset Management Agency (NAMA), which initially assisted in deleveraging the five participating Irish financial institutions, is now well advanced in disposing of its acquired loan book and was the most active Irish seller so far in 2015. It is anticipated that NAMA will dispose of the bulk of its remaining assets during 2016. It has been evident during the year to date that the focus of the remaining traditional banks is now shifting from deleveraging and workout of their challenged loan books and they are increasingly willing to lend new monies, albeit still subject to relatively strict credit approvals.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN IRELAND?

COLLERAN: While the lending appetite of Irish banks has been increasing, there are still capital constraints and a greatly reduced number of players in the banking market. Accordingly, there is a strong demand for credit among Irish corporates and SMEs, and non-bank lending has been stepping in to fill this credit gap. For large corporates, the private placement bond market has been an increasingly popular source of finance. Institutional investors, encouraged by the Irish government, have also been moving into this space. In particular, US and UK investment companies have been entering into joint ventures with local partners to lend to Irish borrowers. Similarly, joint ventures have been formed between asset managers with dedicated lending funds and Irish state owned entities, such as the Ireland Strategic Investment Fund. With banks typically only willing to fund 60 to 65 percent LTV, mezzanine lenders have also been bridging the gap.

Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

COLLERAN: For large corporates with a strong credit proposition, access to finance is quite readily available and at competitive rates. This has been assisted by the growth in the economy, eurozone interest rates remaining at record lows and liquidity measures imposed by the ECB to boost supply. Furthermore, there is increased competition among banks, non-bank lenders and capital markets. Accordingly, some loosening of covenants is also evident at this end of the market. However, SMEs and smaller corporates are being subjected to much more robust credit analysis and, where lending is approved, it is subject to higher margins and to lower gearing levels. Banks are also applying a relatively conservative risk assessment approach and stringent stress testing, whereby, for instance, lending propositions are tested for a simultaneous drop in income and an increase in interest rates. Another feature of current lending to SMEs and mid-size corporates is shorter loan terms, with aggressive repayment schedules where there is proven capacity.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

COLLERAN: With the improved levels of liquidity, large corporates are in a better negotiating position than in recent years and will seek to avoid finance where lenders require significant over collateralisation. However, smaller corporates and SMEs, where they succeed in being credit approved, are generally still being subjected to quite onerous security requirements. Lenders are generally insisting on first fixed charges over as much of the undertaking of a borrower as practicable. Also, lenders are conducting a high level of due diligence on the assets of obligors, in particular insisting on full investigations of title. Many lenders are keen to take security over the shares in asset holding entities as well as over the assets themselves. Wherever possible, lenders are seeking guarantees in order to have recourse to as much of the borrower's group structure as possible. For SMEs, lenders are often requiring personal recourse to company directors and shareholders – but their credit analysis still remains focused on taking security over specific assets with ascertainable value.

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN IRELAND OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

COLLERAN: A number of 'core' supervisory responsibilities and decision making powers were moved from the Irish Central Bank to the ECB – in line with the Single Supervisory Mechanism – as of 4 November 2014, as part of the programme of advancing financial integration and stability across Europe. The Central Bank now retains responsibility for certain 'non-core' responsibilities, for example anti-money laundering and consumer protection. The Bank Recovery and Resolution Directive was implemented into Irish law on 15 July 2015 with the aim of eliminating – insofar as possible – the need for government-led bailouts by enabling authorities to intervene early to prevent failure of an institution and to take swift action where failure cannot be avoided. The Irish company law regime was consolidated and reformed by the Companies Act 2014, which came into effect on 1 June 2015. Among its welcome changes were a reduction in the scope of the prohibition on financial assistance and greater certainty on the charges registrable with the Companies Registration Office and how their priority is established.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

COLLERAN: The coming year will see a continued drive by the remaining large Irish domestic banks – AIB, Bank of Ireland and Permanent TSB – to reduce their level of state support or ownership and to return to a greater degree of commercial ownership and control. It is to be hoped that this will allow these pillar banks to respond in a more dynamic fashion to the renewed growth in the Irish economy and will thus boost competition and the availability of credit. With a large proportion of the credit that was extended between 2004 and 2007 due to be refinanced by 2017, and many of the markets which were the source of this finance now being either closed or operating at reduced capacity, a wide range of non-bank institutions have the potential to act as direct lenders to entities and individuals that are struggling to obtain financing by traditional means. This represents a significant competitive challenge for Irish banks and their senior executives.

“Continued growth in new lending by the banks can be anticipated as the banking sector further stabilises.”

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN IRELAND OVER THE NEXT 12-18 MONTHS?

COLLERAN: It can be expected that the process of normalisation of the Irish banking sector will continue, with the deleveraging process in its final stages and major loan portfolio sales by Irish institutions coming to an end. This period should also see the remaining domestic banks increasingly returning to a commercial funding structure. Accordingly, continued growth in new lending by the banks can be anticipated as the banking sector further stabilises and the Irish banks' focus continues to shift from management and work-out of impaired assets to lending opportunities in a growing economy. However, it would seem that the demand for credit will also continue to rise in view of the economic recovery and the need to refinance existing debt – particularly property-related debt. Accordingly, it will still be challenging for smaller borrowers to get credit approval and, while credit terms and covenants should ease further, they will remain relatively strict.

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NETHERLANDS

FERDINAND VEENMAN
KPMG ADVISORY N.V.

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN THE NETHERLANDS? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

VEENMAN: Compared to 2011 and based on 2014 year-end figures, the banking sector as a whole has shrunk by 11 percent. This has mostly been achieved by sales of non-core assets and has helped banks to comply with new regulatory capital requirements. In that same period, as a result of the bad economic situation, the demand for credit was very subdued. In 2015, on the back of an improving economy, we have seen an increase in demand for credit – both for retail and business clients. Retail lending, mostly residential mortgage lending, has re-priced to very healthy levels and we have also seen in increase in corporate lending margins, albeit more benign. We also observe that banks prefer lending to larger SMEs and corporate clients. We think the reason for this is that banks are increasingly looking to improve their financial performance and that this focus is part of that.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN THE NETHERLANDS?

VEENMAN: In the current market you can divide the way banks finance Dutch corporates along the axis of large corporates, mid-markets and SMEs. Between the three categories there are rather different appetites among banks to lend.

Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

VEENMAN: Large corporates are either stock listed, have issued rated debt or have conducted private placements in the US, Europe or specifically Germany. In general terms, the larger companies still have access to ample liquidity from third party investors and banks. As these corporates are accustomed to using the capital markets for their longer term financing needs, banks want to play a role in arranging such transactions. The best way to be selected by the company for these transactions is to provide the company with easy financing in the first place, which means covenant-lite, with limited restrictions, and cheap. Mid-markets, with EBITDA above €5m, already have a financing package with multiple banks or are using multiple bank financing products, and some of them are at the brink of becoming a large corporate. Banks consider them interesting because of the size of the so-called 'bankwallet', or the total amount a corporate pays to its bank per year in fees and interest. SMEs have EBITDA below €5m and are often 100 percent financed by one bank only. They are faced with retracting banks, not only in terms and conditions but mainly in credit appetite.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

VEENMAN: Besides discussions on being a core client or not, the house banks are more selective about which companies they finance and for how long. In general, the tenor of financing has been reduced in the last couple of years from seven or five years to five and three years, and sometimes even shorter. Dependent on the commercial position of the bank vis-à-vis the company, it may try to persuade the company to provide more 'real' security for the benefit of the bank, in financing that one might consider ABL-financing or, in certain cases, securitisation. On the other hand, third party investors, like pension funds and insurance companies, are also looking at the same companies and are willing to provide financing with longer tenors for the same risk. The coupon however is often 250bps higher than bank pricing for shorter tenors.

“All of these measures are impacting both balance sheet capacity and cost of capital in a negative manner.”

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN THE NETHERLANDS OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

VEENMAN: There is a wealth of new regulatory requirements that banks have to comply with. Many of these have already been implemented, some need to be implemented soon and some are still in the design phase. In recent years, most of the focus was on new capital and liquidity requirements and we see that banks have made major progress on these issues. There are, however, still regulatory topics that will likely affect banks’ balance sheet capacity, and therefore lending capacity, in the coming years. These include the continuing discussion on the final leverage ratio requirement. Each additional percentage point requirement may result in a 5 percent balance sheet capacity reduction in the Netherlands, the final details of the total loss absorbing capacity for TLACs, potentially setting a capital floor for the entire industry. IFRS9, a new accounting standard, is likely to result in significantly higher provisioning levels. Last but not least is the new proposed standardised approach under Basel IV. All of these measures are impacting both balance sheet capacity and cost of capital in a negative manner, so our expectation is that banks will have difficulty in meeting increasing demand for credit as the economic recovery continues.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

VEENMAN: Compliance with all regulations is a must for the licence to operate for banks, but so is having a sustainable business model where the return on capital exceeds the cost of capital. We have seen that this has not the been the case in recent years, and what banks require most is a ‘new’ business model whereby a better balance is found between use of their own balance sheet and use of the balance sheet of other participants in the economy, such as institutional investors. Using core and strategic competences of the bank, such as distribution, underwriting and administration for other investors who lack these competences, may provide the answer. Important to note is that competition for banks comes from non-traditional places such as FinTech.

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN THE NETHERLANDS OVER THE NEXT 12-18 MONTHS?

VEENMAN: We have seen a number of significant local institutional investors enter parts of the banking scene – mortgage lending and SME lending – through fund structures, and we expect this to continue next year. This is actually truer for mortgage lending than for SME lending because in that area there are still a few important hurdles to overcome. Firstly, the spread that Dutch SMEs have grown accustomed to is lower than what investors can get on risks of a similar rating category. Secondly, although new entrants embrace electronic data reporting – for instance, VAT and corporate tax reports – the quality of this information across SMEs is still very mixed. And thirdly, there is the challenge of efficient and effective origination to source clients, which is difficult to crack. But when we look at potential volumes they are likely to allocate to this asset class, and the loss of capacity in banking as a result of higher capital levels, it still leaves quite a significant gap to be filled. The same applies for the future of peer-to peer lending. This makes it very likely that banks will still be the dominant financier of consumer and business credit for some time to come.

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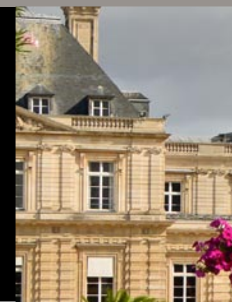
Ferdinand Veenman has over 20 years' experience as a banker at various financial institutions. Since 2009 he has been a partner in the Corporate Finance team of KPMG in the Netherlands and heads the Debt Advisory team. Over the last five years, Mr Veenman has helped a large number of national and international corporates and financial institutions to attract funding from banks, institutional investors and via capital markets transactions, including securitisation transactions. As Head of Banking in the Netherlands, Mr Veenman coordinates the activities of more than 200 professionals in audit and advisory serving KPMG's banking clients.

LUXEMBOURG

ALEXANDRINE ARMSTRONG-CERFONTAINE
KING & WOOD MALLESONS



Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN LUXEMBOURG? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

ARMSTRONG-CERFONTAINE: Banking activity in Luxembourg has a broad meaning. It includes retail services, funds administration, fiduciary and trustees services, financial engineering, as well as corporate finance services – with loans, structured products and capital markets issuances. Almost all of the 105 banks based in Luxembourg offer each of these services. Luxembourg corporates rely on banks to finance their activities and lending from Luxembourg banks continues to increase, as has been the case since the financial crisis in contrast to many European jurisdictions. It is well known that Luxembourg banks have been remarkably resilient and are a stable source of funding for corporates and foreign, mostly European, banks. Luxembourg banks are also present in cross-border financings and refinancings for corporates where the trends are equivalent to other European jurisdictions. High yield continues to be a key feature in European leveraged deals and is now also a financing product for European corporates. Therefore, financial market activities of Luxembourg banks have increased in recent years.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN LUXEMBOURG?

ARMSTRONG-CERFONTAINE: Debt volumes have increased in Europe and this is reflected in Luxembourg, which has seen, as other European countries, a trend for covenant-lite financings and term loans subject to bond-style undertakings only, from European and US banks. There is a strong US influence as European borrowers have turned to the US market, which has more liquidity. Bond issues are also an option, since parties enjoy a large degree of freedom in their terms and conditions. High yield issues have become very common for leveraged financings from €200m onwards, whether for add-ons or refinancings. Debt-to-EBITDA ratios have been, in most cases in 2013 and 2014, around 6 to 6.3 times EBITDA. A large number of debt funds have been set-up in Luxembourg and are very active in granting small to mid-market loans

in Europe. To some extent, the material increase in the requirements imposed on the banks' regulatory capital has generated opportunities for debt funds which are much less regulated than banks.

Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

ARMSTRONG-CERFONTAINE: The terms of lending vary greatly from one deal to another, but we are clearly in a borrower/issuer market, due to the low interest rates on the market. Covenant-lite loans are popular for larger leveraged financings and private equity sponsors tend to push very hard against the banks' controls. Financial covenants are also weak in investment grade and high-yield lite bonds are common. An equity cure is becoming a standard and sponsors push hard for more flexibility in guarantor coverage for bolt-on acquisitions. 'Yank-a-bank' provisions – with a consent threshold greater than two-thirds of the lenders' commitment – and 'snooze-you-lose' provisions are also typically included in loan agreements. Lastly, borrowers have a certain level of control over the syndication process as a white list of potential lenders is approved with the borrower.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

ARMSTRONG-CERFONTAINE: As a rule, there is no legal restriction imposed on lenders with respect to any security that is granted in their favour. However, the choice of security does take into consideration various factors, including the cost of security and the potential restrictions on guarantees and negative pledges, as tax issues that may arise when granting or enforcing the security.

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN LUXEMBOURG OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

ARMSTRONG-CERFONTAINE: Banks are affected by the increasing number of regulations focusing on compliance and transparency, of which FATCA and its successors, and EMIR have a large imprint. Most importantly, the strict regulatory environment on minimum capital and liquidity has impacted and will continue to impact on the banks' activities. Basel III, the Capital Requirement Directive IV and Capital Requirement Regulations are very complex regulations and their implementation will cost much to banks. In addition, the architecture of compliance has been strengthened and will require further investments from banks with the implementation of the new fourth AML Directive.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

ARMSTRONG-CERFONTAINE: Geopolitical risk is high up the agenda of many senior executives at the end of 2015. The implementation of the new regulations on capital and liquidity will be an operational challenge both because the tsunami of rules since the financial crisis may not provide a consistent framework for banks to work on and because, however they are implemented, they will impact on the bank's funding and liquidity. In other words, we are certain that there is much regulation but none of us can be certain that regulations are coordinated. The changes have and will also continue to increase operational costs for banks, which I would expect to impact on the type of activities they do and the location of their services. I would hope that the costs of too much regulation and the importance of banks are perceived by all who believe, seven years after the financial crisis, that banks must regain trust and repair their reputation.

"The strict regulatory environment on minimum capital and liquidity has impacted and will continue to impact on the banks' activities."

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN LUXEMBOURG OVER THE NEXT 12-18 MONTHS?

ARMSTRONG-CERFONTAINE: In addition to the above, the fight against money laundering and terrorist financing will become stricter. The CSSF recently announced additional restrictions, to be implemented in 2016-17. It is expected that the implementation of the fourth AML Directive will bring yet another cost to compliance teams. Furthermore, a new European General Data Protection Regulation, aimed to be adopted in 2015-16 and to supersede the Data Protection Directive (95/46/EC), brings a large number of amendments to the previous legislation, with data and reporting at the top of the agenda. It is also worth mentioning that a Brexit would cause an earthquake to all of us in Europe, perhaps a little more in Luxembourg, given that Luxembourg and Frankfurt are the two leading candidates to become the European financial centre.

KING & WOOD MALLESONS

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SWITZERLAND

JÜRG FRICK
DELOITTE AG

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN SWITZERLAND? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

FRICK: Banking and finance activity in Switzerland was recently influenced by a rather difficult economic, financial and regulatory environment. Negative interest rates introduced by the Swiss National Bank, negotiations with the US DoJ to solve tax issues and declining revenues combined with an unfavourable operating model absorbed our banking system. Risk considerations led to new capital allocations and subsequently to lower balance sheets. Although the appetite to lend to corporates remains and the availability of credit facilities, as shown in our CFO survey, is still high, margins began to rise and quality of assets became more important. Credit conditions – availability as well as costs – have been consistently rated as attractive over the last few years and they continue to be a strong advantage for Swiss companies.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN SWITZERLAND?

FRICK: Traditionally, bank credit facilities are focusing on corporate lending and financing as well as mortgages. Non-traditional debt sources are only playing a minor role in our region but are consistently watched by the banking industry. Mezzanine financing has never succeeded due to costs. Crowdfunding is still too small to be relevant.

Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

FRICK: Interest rates continue to be very low, even if the introduction of negative interest rates by the Swiss National Bank in January has caused credit interest rates to increase slightly from the record low before. While this may seem counterintuitive, negative interest rates have allowed banks to argue that higher rates are necessary because of higher refinancing costs. Capital requirements for mortgages have been increased by regulators, to avoid a real estate price bubble. Otherwise, covenants and other terms applied to debt offerings are standardised and largely unchanged.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

FRICK: Capital requirements have been increasing and credit risk management has seen further improvement. Companies generally rate credit conditions as attractive and bad debt losses continue to be low.

"Awareness and willingness to adapt to the necessary strategic realignment in general is high."

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN SWITZERLAND OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

RICK: There has been a multitude of regulatory changes recently in several areas. Regulation such as Basel III regulatory capital and liquidity requirements has strengthened financial institutions. Regulation has also enhanced market resilience and market infrastructure, not least in the area of OTC products. Increased capital requirements and additional regulation for mortgages are also aimed at increasing resilience of the mortgage and real estate markets. Consumer protection has been extended through introducing tests for investment suitability and increasing transparency requirements, for example MiFID II. Regulation has addressed tax transparency, especially for cross-border business, such as automatic exchange of information with the EU. Further pending regulation discussions include capital requirements and leveraged ratio, tax reform and market access for cross-border banking.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

FRICK: Regulation, as well as cost, revenue and margin pressure, strengthens the strategic realignment and the emphasis on innovation becomes a necessity, optimising structures and processes, decomposition of the value chain, moving toward value network instead of internal value chain. Digital innovation, using digital for process innovation, customer experience as well as new products and services such as crowd finance, while dealing with new, digital competitors, are also key challenges for Swiss banks. Both regulators as well as banks have worked diligently over the last few years to improve reputation and the resilience of Swiss banks in the event of another potential future financial crisis.

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN SWITZERLAND OVER THE NEXT 12-18 MONTHS?

FRICK: Consolidation of the banking sector is set to continue. While this process is challenging, it offers a lot of opportunities for the Swiss banking industry and will result in increased quality and greater efficiency. Technology and innovation will help increase the client service experience as well as provide a better focus in the form of clientele, products and business which will ultimately further strengthen Swiss banking. Increased capital requirements – even if they are higher than abroad – will make the banking system more independent and therefore more attractive for clients and shareholders. Awareness and willingness to adapt to the necessary strategic realignment in general is high, so progress here is likely and will further increase Swiss competitiveness. Switzerland has a big opportunity to realign business models today, repeat its continuing success in the coming years and decades, and will remain the number one finance place in the world.

Deloitte.

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SPAIN

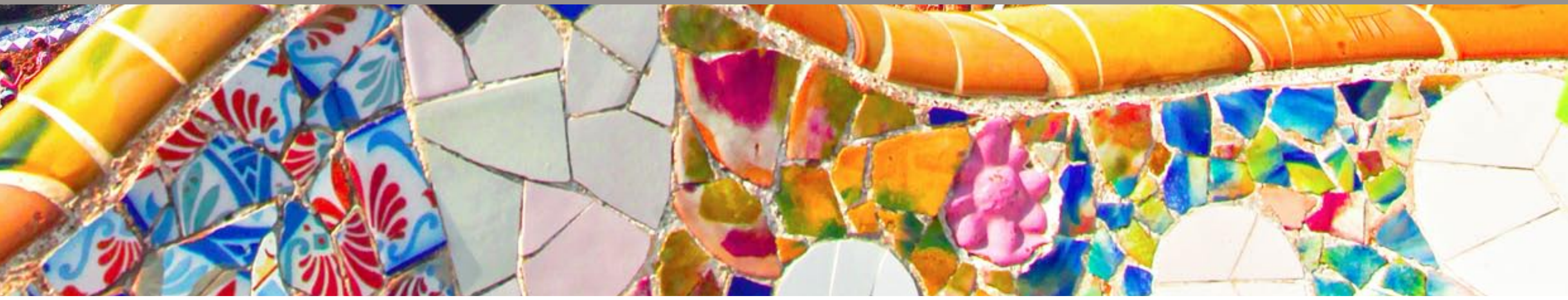
JOAQUÍN SALES
KING & WOOD MALLESONS

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN SPAIN? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

SALES: As in other European economies during the financial crisis, most Spanish companies have been forced to reduce production, which has in turn reduced their capital needs and subsequently their leverage levels, which otherwise would have been borrowed from banks. This has had an impact on lending levels in Spain, which have significantly declined. Spanish corporates have emerged from the crisis with a more international form and most of their new investments and financing needs are now located abroad. Fortunately, finance and banking activities in Spain are showing a positive balance compared to the same period in preceding years, which experts attribute to the overall growth shown by the main European economies, among which Spain is experiencing strong growth. The general drop in demand for external capital has forced banks and other financial institutions to reframe their operations in the Spanish market to overcome the final stages of the global crisis, and the European crisis in particular.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN SPAIN?

SALES: Non-traditional lenders, such as private equity and hedge funds, are taking their place alongside banks as a source of funding, either through direct lending or through secondary transactions, building up their portfolios to diversify risk. Following recent regulation, Law 5/2015 for the promotion of business financing, a new legal framework has been established in Spain with reference to both debt issuance and crowdfunding, so that access to debt capital markets is expected to improve. Due to the fast and easy way to obtain financing, crowdfunding has emerged as an alternative financing approach which is now in greater use than we've seen in previous years.



Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

SALES: Interest rates, covenants and other terms applied to debt offerings are typical in a post crisis scenario. Interest rates have been reduced in recent months and the financial covenants imposed on borrowers under financing agreement have been adjusted to the borrowers' current financial situation, which are now showing improvements in the balance sheet. Those lenders which have survived the crisis now find themselves with access to cheap liquidity in the current macroeconomic environment. This helps them offer attractive financing terms, although generally with lower gearing ratios. Now that all relevant EU public administrations have, or are in the process of, adopting measures and policies to adapt banking and finance markets to the new global scenario, it is the responsibility of financial institutions to review their policies on interest rates, covenants and other requirements in financing transactions to help create an environment of growth and prosperity.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

SALES: In the context of current financing transactions carried out in Spain, or in which a Spanish company is involved, regardless of the structure, lenders tend to cover any potential risk of non-payment by the borrower. This crystallises in lenders seeking to obtain a sound security package or sponsor before their risk department authorises the financing. For their part, the security provider and sponsor typically fight to limit their liability through agreed security principles – particularly if the security or guarantee to be provided involves high costs and expenses. Real estate mortgages remain rare outside of real estate financings, due to the exorbitant cost of the *ad valorem* stamp duty.

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN SPAIN OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

SALES: Law 5/2015 for the promotion of business financing has regulated crowdfunding for the first time in Spain and also implemented a new legal framework with reference to Spanish law governed debt issuance procedures. With reference to the latter, private limited liability companies, or *sociedades limitadas*, are now allowed to issue and guarantee the issuance of standard debt securities, although subject to certain quantitative limitations. Non-listed public limited liability companies, or *sociedades anónimas*, are now allowed to issue debt securities on an unlimited basis. The issuance procedure has been simplified both with reference to corporate requirements – for example, the management body of the issuer is now authorised to approve the issuance in most cases – as well as other formal requirements – for example, debt issuance may be effected prior to registering documentation with the competent public registry, with no requirement to publish notice in a public gazette. Crowdfunding activity is now reserved to authorised crowdfunding platforms, which must be registered with the National Securities Market Commission's registry and are subject to supervision by the Bank of Spain and to certain financial requirements. Specific restrictions apply to the ways in which the platforms can raise financing, use of the funds contributed and on the services the platforms can render for marketing and communication services.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

SALES: There needs to be a conscious effort to regain trust. Senior bankers acknowledge both in private and public that the reputation of the financial sector has been severely tarnished. Executives of financial institutions have to adapt their operations to the new market challenges and the new profile that customers present. Fortunately, the majority of banks that were suffering from hardship are now recovering. It is time to look ahead and focus on trying to adapt to the new times and needs of financial markets and consumers. Due to recent regulations and the policies that have been implemented by EU governments, banks and other financial institutions will be playing in a more controlled sector, where the protection of investors and the correct reallocation of

"Senior bankers acknowledge both in private and public that the reputation of the financial sector has been severely tarnished."

goods and resources have superseded the only goal that most financial institutions pursued in the past, which was maximising their benefits. Additionally, senior banking and finance executives will have to adapt to new ways of rendering the typical services offered by a financial institution, as every day more clients are demanding online services rather than using a branch, since it is cheaper, faster and safer.

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN SPAIN OVER THE NEXT 12-18 MONTHS?

SALES: We expect banks to become more aggressive and fight off new entrants in the market, to truly regain a more solid footing as they become familiar with new regulations and capital requirements. Funds and other investors will try to capitalise on their more flexible regulatory status and continue to grow their market share in both direct lending and capital market transactions.

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GERMANY

WERNER MEIER
KING & SPALDING LLP

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN GERMANY? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

MEIER: As elsewhere in Europe, limitations on bank's regulatory capital that were introduced after the financial crisis have caused banks in Germany to deleverage their capital. Also, concerns about emerging markets – including the Chinese economy in particular, the Greek debt crisis, and most recently the developments at Volkswagen and other corporates – have played a negative role. However, so far this has not had a substantial adverse impact on Germany's loan markets. There is abundant liquidity, and corporate borrowers have a wide variety of financing options available. This applies not only to investment grade or other large borrowers but also to mid-size companies. Increased M&A activity in Germany has resulted not only in an increase in the volume of acquisition financing, but also in a more competitive and more liquid market. At the same time, the high-yield bond market, which has always been smaller in Germany than elsewhere in Europe, is becoming increasingly weak.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN GERMANY?

MEIER: Traditional bilateral and syndicated bank loans, as well as *Schuldschein* loans – loans based on privately placed certificates of indebtedness – have seen a substantial increase over the last few years. Another basis for the robust German loan market is the market entry of alternative credit providers, particularly in the form of debt funds. As compared with other European countries, the market share of debt funds in Germany is still relatively low, but it has been increasing significantly of late. Furthermore, insurance companies and occupational pension funds – *Versorgungswerke* – have increasingly started to extend loans in Germany in order to generate higher interest returns on their investments. At the same time, in 2013 and early 2014, the share of bonds – both investment grade and high-yield – in German debt markets increased, in many situations replacing existing bank loans. However, in late summer 2014 the high-yield market froze due to the threat of higher interest rates and lack of secondary liquidity and subsequent re-pricing of risk in the

capital markets. Since then, financings via high-yield bonds have not been as frequent, due among other things to the ready availability of credit as a result of increased quantitative easing and the migration of covenant-lite financings from the US market.

Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

MEIER: The significantly increased liquidity in German debt markets has resulted in more favourable terms for borrowers, including less stringent covenants and lower margins. This applies both to loans and bonds. In real estate financings, lenders are careful to ensure that LTV requirements are observed, but otherwise the German debt markets today can be described as very borrower/issuer-friendly.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

MEIER: In traditional loan transactions with corporates, lenders generally seek to gain security over all significant assets of the borrower – typically over shares, receivables, bank accounts, inventory and equipment, real property and, more rarely, intellectual property. Also, the security taken typically includes upstream and cross-stream security given by other members of the borrower's group, although in this respect sharp restrictions apply on the basis of enforcement limitation language, which is generally agreed among the parties to take account of corporate law restrictions and avoid personal liability on the part of the borrower's management. In this connection, lenders often neglect applicable German law limits on over-collateralisation. Where over-collateralisation arises only after the drawing of the loan, the borrower is entitled to claim a partial release – a right which is generally not enforced except where the borrower falls into insolvency. However, where a significant degree of over-collateralisation exists from the outset of the transaction, lenders face the risk of having the complete security package declared null and void.

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN GERMANY OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

MEIER: Since the recent transfer of certain national bank supervisory authorities to the ECB, the latter has become increasingly active in this field. The European Bank Recovery and Resolution Directive (BRRD) of May 2014 provided, among others, for the bail-in of creditors of a distressed bank and introduced a new minimum requirement for eligible liabilities (MREL) to ensure the existence of sufficient bank debt that can be used for a bail-in measure. On the basis of the BRRD, in January 2015, a new German law on the recovery and resolution of German banks, containing among others specific rules for a bail-in of holders of bonds or *Schuldschein* loans of distressed German banks, became effective. This law was amended in November 2015, including by a provision which – not technically but effectively – subordinates holders of such instruments to any other unsecured, unsubordinated bank creditors. This change, which will take effect on 1 January 2017, could have a significant impact on the rating of bank bonds; this might particularly affect German savings banks as these hold a major portion of those instruments. Furthermore, in November 2015, the Financial Stability Board issued its total loss absorbing capacity (TLAC) standard for global systemically important banks; among German banks, these currently include only Deutsche Bank. The increasing market entry of debt funds in Germany was facilitated by a recent decision by the German bank regulator to treat both loan origination and loan restructuring as part of the collective asset management activities of alternative investment funds governed by the German Capital Investment Act – the KAGB – which implements the EU AIFM Directive. As a result, such debt funds do not require a banking licence.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

MEIER: Banks in Germany are currently implementing fundamental changes to the way they do business. There are significant layoffs on all levels, and senior bank executives face decreasing compensation, which is a reaction not only to reduced profitability levels but also to the significant deterioration of their reputation with the general public since the financial crisis.

"If, as expected, the European Central Bank further increases its quantitative easing programme, the liquidity in German debt markets will increase even further."

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN GERMANY OVER THE NEXT 12-18 MONTHS?

MEIER: If, as expected, the European Central Bank further increases its quantitative easing programme, the liquidity in German debt markets will increase even further. Debt funds and other alternative credit providers will play an increasingly important role. Bond markets are expected to continue to be volatile, due to significant uncertainty. This volatility is expected to increase on the basis of the imminent interest rate reversal in the US. In particular, the high-yield bond market is expected to remain weak. On the regulatory side, banks will continue to have to deal with ever increasing capital requirements and other regulatory limitations, both on a national and European level as well as globally on the basis of Basel III and the TLAC standard. All these developments will result in a substantial increase in costs for the affected banks. Also, important legislative changes relating to the insolvency of corporate groups and claw back rights in insolvency are currently pending. On the European level, in May 2015, amendments to the EU Insolvency Directive were passed. These aim to impede forum shopping and will apply to all insolvency proceedings from mid-2017.

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CHINA

SIMON GLEAVE
KPMG ASPAC

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN CHINA? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

GLEAVE: Despite the slower growth rate in the economy – a rate of around 7 percent – asset growth in China continues at around 10 percent. Loan growth, however, is slightly lower, at around 8 percent. Non-performing loans (NPLs) ratios have seen increases over the past year, averaging about 1.4 percent for the sector. Impaired loans disposals to asset management companies have, however, been high, reducing the increase in the NPL ratio.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN CHINA?

GLEAVE: Commercial bank lending remains the dominant form of credit in the economy but there is an emerging corporate debt market, and larger state owned corporates have continued to increase the amount of debt issues. Structured wealth management products issued by banks remain popular with investors and corporates, when access to bank lending is restricted.

Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

GLEAVE: Bank interest rates remain under government control but there is an expectation that interest rate deregulation will occur in the medium term. People's Bank of China (PBOC) base rates have been reduced over the last 12 months in order to help boost the economy, which has resulted in narrower margins for banks.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

GLEAVE: Corporate lending remains collateral-dependent in China. Given that there have been an increased number of bankruptcies, collateral, values and legal titles have been under scrutiny and loan to value ratios have been adjusted in general across the sector.

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN CHINA OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

GLEAVE: There have been a number of new regulations affecting sales of wealth management products, improving customer protection, as well as making changes to bank assurance agency sales. The four largest Chinese banks have all been designated as global systemically important financial institutions (G-SIFIs) with consequent increases in capital and oversight. Liquidity management has been a special area of focus following money market developments affecting certain smaller banks.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

GLEAVE: China has not been affected by the financial crisis in the same manner as international institutions, and in general reputations and trust with consumers remains strong. The key issue at present remains the management of credit portfolios with overdue loans increasingly showing the stress affecting all banks and the need for more active credit and recovery management.

"China has not been affected by the financial crisis in the same manner as international institutions, and in general reputations and trust with consumers remains strong."

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN CHINA OVER THE NEXT 12-18 MONTHS?

GLEAVE: There is rapidly growing competition from FinTech companies, several of which have received banking licences. Equally, direct banking models and mobile banking are moving forward rapidly. FinTech companies are being challenged by the banks which are adjusting their business models to compete. Additionally, as the RMB becomes a more international currency, major Chinese banks continue to expand overseas with both strategic acquisitions as well as organic growth of branch networks.

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SOUTH AFRICA

SIPHO MALABA
KPMG INC SOUTH AFRICA

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN SOUTH AFRICA? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

MALABA: In 2015, South African banks published increased headline earnings, despite having been faced with challenging operating conditions. Their strong performance is attributable to different operating and growth strategies implemented by the various banks. Sustained effort by all the banks to optimise channel choices and migrate customers to digital and mobile channels continues to positively impact electronic transactional volumes. The loans and advances books continued to grow in 2015, indicating that there still is an appetite to lend. Corporate lending has outstripped retail and personal lending. The slower increase in retail and personal lending is facilitated by the implementation of the Regulations for Affordability Assessment, as part of regulatory revisions related to the National Credit Act from March 2015. Most of the banks have reduced the value of non-performing loans and impairment cover has largely increased, indicative of more conservative provisioning for bad debt. This paints the picture of continuous efforts to manage credit risk more effectively, and improve the quality of credit books.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN SOUTH AFRICA?

MALABA: Loans common to the South African banking market are secured loans, unsecured loans and fixed rate loans. Unsecured loans are more commonly found in the retail sector. In South Africa, we have not seen a significant uptake in non-traditional debt finance such as convertible and venture debt.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

MALABA: Where possible, the banks do take precautions, in that they are taking security in the form of movable and immovable property. Nowadays, in the current economic environment, potential debtors will have to accept that a larger part of their assets will be held as security over the loans they require. There are two second-tier banks in the South African market that made significant inroads in the unsecured loans sector. In light of the recent collapse of one of these banks, the industry has tightened up on the requirements for unsecured loans.

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN SOUTH AFRICA OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

MALABA: The sector is experiencing significant regulatory change, which is becoming increasingly burdensome to financial institutions. The increase in capital adequacy requirements brought about by the gradual implementation of Basel III has resulted in the banks gradually scaling down their operations in all areas that require large capital commitments. We have seen a number of banks turn their attention to their wealth management operations. This area requires the banks to hold significantly less capital and produces annuity income streams. Looking specifically at the reforms in South Africa, there are a number of new, amended and proposed regulations, some of which are conduct risk, the Twin Peak model of financial regulation, the impact of Basel III and control deficiencies reported by the South African Reserve Bank with regards to the Anti-Money Laundering (AML) and Combating the Financing of Terrorism (CFT) Acts. A further, major regulatory change came in July 2015 when the National Credit Regulator (NCR) proposed limits on interest rates and fees. The proposal included a cut in the rates charged on short and unsecured loans, as well as credit cards – basically all the main channels of lending to the 'average' South African. This has been the first review of rates and fees since 2007 when the National Credit Act came into effect.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

MALABA: In terms of cyber crime, the IT systems of the banks are at risk and they need to implement the best software to protect themselves, as well as their customers' personal information. With regard to capital adequacy, executives must ensure they perform more stress testing on the amounts of capital that they have and be more aware of the regulations affecting them as the regulators have upped their own investigations and compliance reviews. More efforts must be made with regard to compliance with anti-money laundering regulations. Since the 2008 financial crisis, the Financial Services Board (FSB) in South Africa has focused on strengthening banks' capital and liquidity requirements, improving over the counter derivative markets, strengthening adherence to accounting and regulatory standards, and reforming compensation practices to support financial stability. As these are high focus areas for the FSB, this has been on top of most of the banks' agendas over the last few years.

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN SOUTH AFRICA OVER THE NEXT 12-18 MONTHS?

MALABA: At present, the South African economy is positioned precariously, with persistent structural issues such as an underwhelming GDP growth rate, trade and current account deficits, a steadily weakening rand and a heavily indebted consumer plaguing the business sector. The banking sector has, however, proven resilient in the face of the aforementioned challenges. Considering the recent volatility in global capital markets and sluggish growth, there is an expected boost to the banks as local rates would need to be raised to prevent even further currency weakness and to keep inflation within the 3 to 6 percent SARB target. While the major banks are not currently at risk of having their operations usurped, alternative banking channels such as peer-to-peer lending, which facilitate the provision of credit between two parties, thus eliminating the requirement for a traditional bank, are gaining traction. Banks will be forced to keep abreast of rapid shifts in technology. Advances in technology will not diminish the role of the banks, but rather alter it. With rapid changes and rises in new market entrants, the existing market leaders, the 'big four' and to some extent the second tier of banks, will need to innovate in order to stay

"Banks will be forced to keep abreast of rapid shifts in technology."

competitive. Through 2016, IFRS 9 is going to have a major impact on the banks as we are going to see depleted profits because of the impairments. They are going to have to hold a longer 'incurred but not yet reported' provision and take macroeconomic factors into account when calculating provisions. The effect will vary depending on whether it is a secured or unsecured portfolio with a greater impact being on the unsecured portfolio. Once adopted, IFRS 9 will give you a faster indication of the distress in your loan book. Because of the onerous disclosure requirements of IRFS 9, the majority of banks in South Africa have already started to collate all the relevant information required for the disclosure.

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UNITED ARAB EMIRATES

LUKE ELLYARD
KPMG LOWER GULF LIMITED

Q COULD YOU PROVIDE A BRIEF OVERVIEW OF RECENT BANKING AND FINANCE ACTIVITY IN THE UAE? ARE BANKS IN GENERAL DEMONSTRATING A STRONG APPETITE TO LEND TO CORPORATES?

ELLYARD: Generally, banks are always keen to lend to corporates – in the UAE as much as anywhere else. Following the global financial crisis across the MENA region, there was a general move away from unsecured 'name' lending and a tighter focus on quality of security or cash flow provided. This has been enhanced by the expected slowdown and liquidity tightening due to the prolonged oil price slump. Even large family groups, which traditionally have not needed to share much corporate information, are being more transparent about their balance sheets and are providing better collateral. We are also seeing a tendency – again perhaps overdue – of more professional relationship managers who are becoming more attuned to risk, and therefore opportunity, in their markets, industries and sectors.

Q WHAT TYPES OF FINANCING SEEM TO BE POPULAR? ARE NON-TRADITIONAL DEBT SOURCES PLAYING A NOTABLE ROLE IN SERVICING CORPORATE DEMAND FOR DEBT IN THE UAE?

ELLYARD: Banks make money by lending money. The UAE tends to be seen as an over-banked market so there is considerable competition between the banks to identify quality opportunities. The Central Bank of the UAE is keen to ensure that the banking sector has learnt the lessons of the downturn following the seizures in global financial markets following 2007 and has introduced limits on lending to certain sectors, related parties and large exposures, as well as tightening liquidity requirements. On the other hand, there are certain market sectors that are seen as riskier where the banks are reluctant to lend and non-traditional debt sources have filled the gap.

Q HOW WOULD YOU DESCRIBE INTEREST RATES, COVENANTS AND OTHER TERMS APPLIED TO DEBT OFFERINGS IN THE CURRENT MARKET?

ELLYARD: The short term interest rate, the Emirates Interbank Offer Rate (EIBOR), is calculated by the Central Bank based on submissions from a mixed panel of local and international banks so the system is comparable to mature financial markets and is considered transparent. The spread to the US dollar Libor three month has narrowed over the last four years and is currently approximately 50bps. Long term swap rates best reflects the hedging by corporates in the market of interest rate risk and spread between the US dollars and AED 10 year swaps are approximately 1.6 percent, so not too far out of alignment with global norms. In the real estate area, which is a significant proportion of lending in the market, pre-sales and pre-leases are increasingly critical for projects looking for funding. Sale and leaseback, REITs and sukuk financing are becoming increasingly popular options for funding as banks remain cautious.

Q ARE LENDERS TAKING ALL PRECAUTIONS TO ENSURE THEY GAIN SECURITY OVER ASSETS? WHAT CONCESSIONS MAY DEBTORS NEED TO ACCEPT IN ORDER TO OBTAIN A FINANCING PACKAGE?

ELLYARD: The UAE has plans to introduce a new bankruptcy law which is long awaited to bring much needed clarity on the legal proceedings in case of bankruptcy. There is, nonetheless, concern over proper due diligence. Relationship managers are driven by targets. They have to hit their targets and there has been a suggestion that some would rather arrange a loan and then wait for an issue. Syndicates with international deals carry a bigger stick, and are slowly establishing leading practice. On the real estate side, pre-sales and pre-leases are increasingly critical for projects looking for funding. Sale and leaseback, REITs and sukuk financing are becoming increasingly popular options for funding as banks remain cautious. Banks are looking to reduce their exposures to riskier unsecured segments, although there is continued interest in growing secured portfolios. Increasing competition among lenders for quality, secured assets should, interest rate rises withstanding, lead to continued competitive options. The most recent credit sentiment surveys from the

Central Bank of the UAE have commented on changes in credit standards, driven by the economic outlook, the quality of their institution's asset portfolio, the change in risk tolerance, and current and anticipated regulatory changes.

Q COULD YOU OUTLINE THE MAJOR REGULATORY CHANGES IN THE UAE? OVER THE PAST 12-18 MONTHS THAT WILL AFFECT THE BANKING INDUSTRY GOING FORWARD?

ELLYARD: On the regulatory side, Gulf central banks, and the financial institutions they regulate, have been busy digesting the package of reforms grouped together as Basel III to determine which elements are most relevant in their local market and how best to implement these into their existing regulatory frameworks. This is a delicate balance between continuing to adopt leading global practice while implementing reforms in a way that is sensitive to local market dynamics, and the objective of continued economic growth. Accounting reforms like IFRS 9 will run alongside the regulatory change programme, possibly increasing impairments and introducing additional volatility into CET1 ratios. New guidance around FinTech and cyber security is also expected to change the marketplace for the better.

Q IN YOUR OPINION, WHAT ARE THE KEY ISSUES AND CHALLENGES FACING SENIOR BANKING & FINANCE EXECUTIVES IN THE YEAR AHEAD? IS THERE A CONSCIOUS EFFORT TO REGAIN TRUST AND REPAIR REPUTATIONS FOLLOWING THE FINANCIAL CRISIS?

ELLYARD: The financial services sector is currently faced with a forced shift caused by a number of key mega trends. Globally, and in the UAE, institutions are focusing on enhancing their regulatory capital, while digital and broader technology advances are challenging the traditional ways of doing business. At the same time, there are new market participants – non-bank financial institutions are challenging incumbents, while a new generation of young customers without traditional customer loyalties have different expectations and are using social media to connect, communicate or complain. This is putting pressure on banks to find the right talent, entering the skills race to address regulatory and risk management pressures and technological advances. Today's leaders need to keep pace with a rapidly changing financial landscape, regionally and locally. Couple that with the some of the other external factors

"The UAE banking climate is expected to tighten as drawdowns continue while weaker oil prices filter through into the non-oil economy."

impacting the UAE and it's clear why these are interesting times facing senior executives who, in many of the large banks, are fairly new to the region and therefore do not come with any reputations to repair.

Q WHAT DEVELOPMENTS IN BANKING & FINANCE DO YOU EXPECT TO SEE IN THE UAE? OVER THE NEXT 12-18 MONTHS?

ELLYARD: A key source of GCC liquidity is either the government or government related entities (GREs). Governments are using excess cash to balance their books. The UAE banking climate is expected to tighten as drawdowns continue while weaker oil prices filter through into the non-oil economy. Add to this stock market volatility, pressures in the real estate market, changing tourist demographics, SME sector stresses and impending interest rate increases in the US, and it is clear that the next 12-18 months will be interesting for the financial sector.

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