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Weekly Briefing

Slovenia Economy briefing:

The negotiation between Slovenian government and EU representatives on New Bank of Ljubljana

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In the last few weeks, the major topic in the field of economy was the negotiation between Slovenian government and EU representatives on the selling-off of the biggest Slovenian bank, New Bank of Ljubljana (NLB).

History and background

New Bank of Ljubljana has been the main Slovenian bank for a great part of its history. It dates back to 1889, but it became the main bank in Slovenia by joining several banks in the federal republic' capital into the "Bank of Ljubljana" in the late 1960's, having branches all over the former Yugoslavia, but also abroad. The name was changed again in July 1994, 3 years after independence. New legal entity was then established, and with a changed name "New Bank of Ljubljana" it also cut the ties of post-Yugoslavia succession. This especially became an issue in the case of former Bank of Ljubljana clients in Croatia who after the re-constitution of the New Bank of Ljubljana lost their savings with Ljubljana-based NLB and had to claim them from Croatian banks (the sum being around 545 million in former German marks). The said Croatian banks then sued NLB in 27 separate lawsuits in Croatian courts – many of which are still not resolved.

The biggest change in the ownership structure was in 2002 when Belgian Bank KBC bought a 34% share, but a decade later they retreated from it completely selling off their share in 2013. In general 2013 was a very problematic year for the New Bank of Ljubljana. In the negative trend of falling credit rating of Slovenia (in 2013 it went from A- na BBB+ at Fitch, from Baa2 to Ba1 at Moody's and from A to A- at Standard & Poor's) especially the unstable status of big state owned banks was identified as one of the key weak points of Slovenian economy. A considerable injection of capital from the state budget was needed, the third and the biggest in three years (250 million € in 2011, 383 million € in 2012 and 1558 million € in 2013). After this measure, the European Commission decided to intervene by a direct intervention by the

»European Troika« (European Commission, European Central Bank and International Monetary Found). In negotiations between the Bratušek government with European Commission a certain compromise was achieved in order to ward off the intervention. The compromise mainly consisted in a promise made by the Slovenian government to put together a list of companies to be partly or completely privatized (most important among them: Adria Airways, Aero, Elan, Fotona, Helios, Telekom Slovenije, Cinkarna Celje, Gospodarsko razstavišče, Paloma, Terme Olimia, Unior in Žito). An obligation was also made to sell off and privatize the New Bank of Ljubljana and Abanka, two biggest state-owned banks. In addition, the Bank Assets Management Company (DUTB) was established to acquire the non-performing assets from four banks – NLB and NKBM in December 2013 followed by Abanka and Banka Celje in October and December 2014 (transfer value of 1.569,5 million euros).

Today, in the changed situation of the gradual comeback of Slovenian economy along with growing GDP and also credit ratings, the obligation to sell off the biggest and now again profitable bank NLB is seen by the public and government alike to be strategically a poor decision. Under such pressing time limitations, it would be a great risk that the NLB would be sold for a too low price, not even a satisfactory compensation when seen against the background of all the credit injections in the previous years. Often the case gets compared to the badly executed sell-off of another big public bank, the New Credit Bank Maribor (NKBM). Along with the same 2013 European Commission guidelines, NKBM was – after being supported by a capital injection - also sold for an extremely low price to a speculative found Apollo and European Bank for Reconstruction and Development.

Negotiations

The sanction for Slovenia determined by the Decision on State Support from 2013 (the agreement made with EC), in case it failed to fulfill its obligations, is to sell off the NLB branch banks in the Western Balkans area. This selling would then be organized and led by an independent supervisor, selected by the European Commission.

The initial obligation was that Slovenia has to sell 75% minus one stock until the end of 2017. This was partly changed (from 75% to 50%) in the negotiations at the beginning of 2017 and the sale offer for at least 50% of the bank shares was open in May, only to be closed again in June. PM Cerar and the current government then decided to insist on the view that Slovenia seeks to find replacement measures to substitute the original obligation. The goals are to fulfill the obligations while also paying attention not to go against the best interest of Slovenian taxpayers. It is also a goal of the government to keep the strong regional group NLB from falling apart and disintegrating. In the October meetings alternative scenarios for subsitute sanctions were put forward:

a) postponing the sale along with additional compensation measures

b) sell-off of a smaller share (smaller than the 50% negotiated in 2017) by the end of 2017

c) monetary sanction paid by the state in order to compensate the initially prescribed sanction of selling of the Balkan branches of NLB

An alternative that was suggested by several experts, but not pushed forward in the negotiations, a variant of b) scenario, was selling a smaller share of the NLB to European Bank for Reconstruction and Development (EBRD) which could also greatly benefit the credibility of the bank for future investment.

There were several consecutive negotiation meetings, most importantly in September and October by the Slovenian Minister of Finance, Mateja Vraničar Erman with the European Commissioner for Competition, Margrethe Vestager. The main argument for the postponed selling-off used on the Slovenian side, were the pressing obligations by the Croatian banks due to the above-mentioned legal suits over the succession of the deposits of Croatian bank clients. The c) option for susbstitute sanctions was most prominent in the negotiations, the Slovenian proposal being that the compensation for the sell-off of the Balkan branches would be in a so-called »fund of funds«, established at Slovenian Investment and Development Bank (SID Banka). This fund would then be used for financing of small and medium companies, being also available for all other banks except for NLB itself.

Proposals of the Slovenian side were rejected by the European Commission and another series of parallel upper-level meetings started, between Slovenian Prime Minister, Miro Cerar, and the President of European Commission, Jean-Claude Juncker.

Outcome and Possible Effects on Slovenian Economy and Politics

As of mid-November 2017 this issue is still open and despite the negotiations in Brussels, the European Commission has so far refused to agree on any of the alternative sanctions proposed by the Slovenian side. It can be expected that regardless of the outcome the issue will have to be resolved by the end of the year according to the legal obligations in the 2013 agreement. Two scenarios seem to be most possible:

- If the 50% of the bank shares are not sold by the end of the year (which due to the limited time is hardly possible) and no substitute compensation is agreed on by the European Commission, what follows is the selling of of the Balkan banks within the New Bank of Ljubljana Group, which could greatly affect the future of the NLB Group and perhaps limit the future scope of its growth. There are, however, analysts who claim that the risky investments within the Balkan branches of the NLB Group present a liability for the core and the selling off might not be such a negative strategy.
- If Slovenian side manages to negotiate some form of the alternative compensation which would include establishing the equivalent in the form of »fund of funds«, this might benefit the economy in general, but present a risk to

the NLB itself, especially because it needs to keep capital adequacy over 16% and the transfer to the »fund of funds« would only be possible in yearly packages, not at once.

While the governmental side seems to be greatly univocal about the preferred scenario, the opposition is split on this issue along the right-left divide. The right-wing opposition parties, Slovenian Democratic Party (SDS) and New Slovenia (NSi) generally advocate for less state ownership and in the case of NLB also stress the need for a successful selling off in order to compensate for the previous capital injections that were given from the budget. The Left (Levica) prefers the selling-off of the Balkan branches to the selling-off of the main NLB in order to keep as much state ownership as possible in the Slovenian part of the NLB Group. It could be predicted that this will become one of the main issues in the run for the upcoming parliamentary elections in early summer 2018. The government's public support is already very low and its failure to solve the NLB issue could be one of the deciding factors in the 2018 vote.