

Bad news for Polish banks after Supreme Court FX-mortgage ruling

The Polish Supreme Court has sided with debtors in a dispute over whether FX mortgages can be converted to the zloty while retaining LIBOR rates. It's a growing problem for local banks as well as PLN, as data from companies helping debtors shows a massive rise in interest



A woman inspects a model of a new housing development in Wrocław, Poland

Polish Supreme Court again sides with debtors

Poland's Supreme Court has sided with debtors, rejecting a Court of Appeal verdict that sought to invalidate FX-denominated mortgage loans. In its judgement, the Supreme Court wrote that indexation, a clause considered to be abusive, does not form the main part of the credit agreement. So once that is removed from the agreement (and effectively CHF capital is converted to PLN) the mortgage can then exist with PLN capital and Libor interest rates. It is possible because the key element of the agreement is the initial value of the credit (now considered in PLN rather than CHF) and the price of the credit (interest rate - CHF Libor in this instance) rather than the indexation mechanism.

In essence, the Supreme Court ruling confirms (contrary to a judgement from the European Court of Justice) that the most client-favourable way of exiting the FX mortgage, i.e. the conversion of CHF capital to PLN, with the FX loss becoming a burden to the bank, is possible. The alternative

option, i.e. credit capital conversion from CHF to PLN and the simultaneous termination of the contract, is unfavourable to clients because many of them would not be able to afford it and they may be unable to pay back the remaining part of the capital.

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The upshot is that the ruling may prompt new creditors to sue banks. While only 2% of such mortgages were disputed in court in the second quarter of 2019, the number is growing rapidly; it was up forty percent year-on-year in the first half of 2019. The alternative option (i.e. a CHF credit conversion to PLN which then has to be repaid immediately) was something we believed would discourage people from taking legal action, as they would have to repay loans that would normally last thirty years or even longer.

Based on reports from leading law companies offering legal assistance to CHF debtors, the number of clients signing contracts with them rose by up to ten times year-on-year when compared with the second half of 2018. Media coverage of the topic (before the ECJ ruling) massively increased debtor interest. Still, the numbers from the most active companies on the market are not representative of the whole sector. We're still waiting for more comprehensive data and will be able to offer an update soon.

The problem is growing for local banks and the zloty

We've already seen similar Supreme Court rulings, so the verdict itself is not a game-changer. Moreover, the court also offered guidelines in August suggesting that denominated credits may be converted back into PLN but retain Libor rates. Similarly, like with October's ECJ's ruling, it failed to translate into clear guidance for lower Polish courts. This is becoming more pronounced, seeing as the guidelines from both the ECJ and the Supreme Court don't fully match. The ECJ suggested the cancellation of the mortgage, rather than retaining a Libor rate for a PLN-denominated loan.

The court rulings appear to be shifting in favour of debtors in recent years

The court rulings appear to be shifting in favour of debtors in recent years, not least. In 2016 and 2017, more than 70% of court rulings in the first instance were in favour of the creditors. In 2019, that figures dropped to less than 20%. This all confirms that the problem of FX denominated loans, currently with an outstanding value of some PLN100bn (USD25bn), will remain a major issue for Polish Banks.

The FX mortgage problem is an issue for the zloty as well. Should conversion of credits occur, banks would no longer have FX assets, but FX liabilities would remain. Hence they would have to sell owned PLN for the Swiss Franc, for example. We consider this a major risk for the zloty in 2020 – and forecast €/PLN above 4.30 throughout next year, whereas our models put the fundamental

level at 4.20-25.

Settlements would be a game-changer but aren't likely soon

Since such court cases take years, there are concerns that should banks decide to settle with clients voluntarily, there could be a big short-term selloff in the zloty. In a vaguely similar case, Polish insurers decided to settle cases with products which had abusive clauses when 15% of those products were disputed in court. Even if the number of court cases over FX mortgages continues to rise, we're far from that figure and such an outcome is unlikely, at least for the moment.

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