



Gníomhaireacht Náisiúnta um Bhainistíocht Sócmhainní
National Asset Management Agency

27 September 2013

Mr Michael Noonan T.D.
Minister of Finance
Government Buildings
Upper Merrion Street
Dublin 2

Dear Minister,

We have the honour to submit to you the Section 53 Annual Statement for 2014 of the National Asset Management Agency.

Yours sincerely

Frank Daly
Chairman

Brendan McDonagh
Chief Executive

Section 53 Annual Statement 2014

Section 53 of the National Asset Management Agency Act 2009 (“the Act”), requires NAMA to prepare and submit an Annual Statement to the Minister for Finance three months before the financial year to which it relates. The Statement must specify:

- a) the proposed objectives of each NAMA group entity for the financial year concerned,
- b) the proposed nature and scope of activities to be undertaken,
- c) the proposed strategies and policies to be implemented, and
- d) the proposed application of resources.

The Act confers various powers and functions on NAMA in order to achieve its objectives. The Board has various statutory functions including ensuring that NAMA functions are performed effectively and efficiently, setting strategic objectives/targets and ensuring that appropriate systems and procedures are in place to achieve objectives/targets.

The following statement specifies the objectives, activities, strategies and resource allocation that the Agency proposes for 2014.

For the purpose of this Statement, NAMA and its group entities are considered as one.

Objectives

Section 10 (1) of the Act sets out NAMA's purposes, summarised as:

- a) Acquiring eligible assets from participating institutions,
- b) dealing expeditiously with acquired assets,
- c) protecting and enhancing the value of assets, in the interests of the State.

NAMA's principal commercial objective, based on Section 10 (2) of the Act, is to achieve the best achievable financial return for the State, having regard to the cost of acquiring and dealing with bank assets and its own cost of capital and other costs.

In the context of this overarching statutory objective, the NAMA Board has agreed five key objectives to guide its strategy and policies:

1. Over the projected ten-year life of NAMA, redeem, at minimum, the Senior Bonds issued as consideration for loans in addition to recovery of carrying costs and working and development capital advanced to debtors.
2. Consistent with the first objective, generate transactions which will aim to contribute to a renewal of sustainable activity in the property market in Ireland.
3. Meet its commercial objective (as at 1 above) over the shortest possible time span, having regard to market conditions and to optimising the realised value of its assets. Meet all of its future commitments out of its own resources.
4. Consistent with the first objective, aim to contribute to the social and economic development of the State¹.
5. Manage assets intensively and invest in them so as to optimise their income-producing potential and disposal value.

¹ Section 2 (b) (viii) of the NAMA Act.

Activities

As in 2013, NAMA's activities in 2014 will be focused on its management of debtors and of property assets and on maximising the proceeds to be realised from the portfolio of loans that it acquired under the NAMA Act 2009. It will also concentrate on putting in place the requisite operational and management arrangements and the appropriate strategies to deal with any loans it may acquire from the Special Liquidators under the IBRC Act 2013.

1. Engagement with debtors and receivers

Commercial arrangements were agreed with a majority of debtors during 2011 and 2012 and these are currently in the process of milestone implementation. This involves active engagement with the debtors and receivers who have control of the loans of the largest 189 debtor connections (aggregate par debt at acquisition of €61 billion). It involves ensuring that assets are offered for sale to the market in line with asset disposal schedules which have been stipulated by NAMA for each debtor connection. It also involves monitoring the cashflow generated by assets to ensure that it is properly applied towards debt reduction. The engagement also involves approval of new lending and of decisions in relation to property and asset management. In the case of debtors subject to enforcement, the management of the enforcement process requires intensive NAMA involvement.

Debtor connections other than those directly managed by NAMA are managed by the participating institutions/service providers under delegated authority from NAMA and in line with overall NAMA Strategy.

2. Asset management

This involves developing and implementing value-enhancing strategies that will deliver the best achievable return from certain key property assets under NAMA's control. There will continue to be a strong focus in 2014 on advancing development projects in conjunction with debtors, receivers and joint venture partners. NAMA plans to invest, given the right opportunities, at least €2 billion in Ireland in development capital in order to preserve, enhance and complete commercial and residential projects over the period to 2016. This includes the completion of properties which are currently under development and the

development of land in anticipation of future supply shortages and demand. Over the next three years, NAMA, in conjunction with a number of debtors, will be bringing to completion a significant development programme in London. A substantial number of development projects in Ireland, particularly in Dublin, will also be completed over that period.

A particular likely focus of attention in Ireland will be the Docklands area of Dublin, consistent with its designation as a Strategic Development Zone (SDZ). This area is expected to require significant new development over the medium-term, particularly of commercial office space, to accommodate the continued expansion of the financial services sector and the creation of new business and technology hubs. NAMA holds security over a considerable number of properties and lands in the Docklands area and has engaged, and continues to engage, actively with Dublin City Council in relation to the SDZ. NAMA is currently assessing the commercial feasibility of a wide range of projects, some of them subject to resolution of planning and infrastructural issues which may affect the scale and timing of investment.

3. Balance sheet management

Management of NAMA's Balance Sheet risks and liquidity requirements include the management of day-to-day funding and liquidity, as well as monitoring and forecasting medium and long-term liquidity needs. Asset and liability management will continue to be heavily focused on currency and interest rate risks. By reference to the loan portfolio acquired under the NAMA Act 2009, NAMA currently manages (a) foreign currency risk on about €6 billion of foreign currency loans and (b) interest rate risk on both its assets and liabilities, including some €24 billion of variable rate Senior Notes issued to various financial institutions.

As part of the Government decision in February 2013 to appoint Special Liquidators to IBRC, NAMA was directed by the Minister for Finance to establish a special purpose vehicle (*National Asset Resolution Ltd. - NARL*) to acquire a floating charge over certain IBRC assets. As consideration for the floating charge, NAMA issued to the Central Bank of Ireland some €12.9 billion of new variable rate Senior Notes. NAMA will actively manage in 2014 any foreign currency or interest rate risk which may be created through a mismatch between the currency and interest rate profile of loan assets acquired from the Special Liquidators

(some of which may be in non-Euro currencies) and the variable rate Senior Notes which have been issued to the Central Bank.

4. Engagement with key stakeholders

This involves engagement with key stakeholders other than debtors and includes Government and State agencies, public representatives, the media and members of the public.

A major objective of the Board is to contribute to the social and economic development of the State and to conduct the Agency's commercial activities, in so far as possible, so as to co-ordinate with that objective. Activity in 2014 will continue to be geared towards meeting public policy objectives, including, for instance, the provision of social housing from housing stock within NAMA's control. NAMA will continue to engage with Ministers, Departments, State agencies, local authorities and civic bodies to explore ways in it can advance public and social policy objectives.

In 2014, NAMA will continue to provide as much information on its portfolio and its activities as is possible within legislative and commercial constraints. It will continue to facilitate public scrutiny of its strategies, policies and activities through parliamentary questions and through direct engagement with Ministers, with members of the Oireachtas and with Oireachtas committees. Following the publication of the Freedom of Information (FOI) Bill in July 2013, it is expected that NAMA will come within the remit of FOI in 2014.

5. Acquisition and management of new IBRC portfolio

In February 2013, the Government decided to appoint Special Liquidators to IBRC with a mandate to value and offer for sale the loans in the IBRC portfolio. NAMA was directed by the Minister for Finance to acquire any loans left unsold after the Special Liquidators have completed their valuation and sales process. This portfolio has par debt of approximately €22 billion. The acquisition price for loans will be the reserve price as determined by valuers employed by the Special Liquidators and will be in line with Valuation Instructions issued to the Special Liquidators by the Minister for Finance in February, May and July 2013. The Valuation Instructions include specification of a discount rate of 4.5% for the valuation of loan cashflows. After acquisition, NAMA will be required, under IFRS accounting rules, to

conduct an independent fair value valuation review of the loans including an up-to-date assessment of loan cashflows and asset disposal values.

The outcome of the Special Liquidators' sales process is expected to be known towards the end of 2013 or the early part of 2014. It is envisaged that much of 2014 will be devoted to putting in place appropriate arrangements for managing the new portfolio and to developing strategies for managing individual debtor connections, portfolio sectors and the portfolio as a whole. After reviewing the acquired portfolio, including assessment of loan cashflows and the proceeds and timing of asset disposals, NAMA will be in a position to prepare a comprehensive management strategy and to come to an informed view of the value that may be generated from the portfolio and the time horizon over which that may be achieved. As with the current NAMA portfolio acquired under the NAMA Act 2009, a major objective will be to manage the new portfolio in a cost-effective and efficient manner on behalf of the taxpayer.

Strategies

One of the key objectives set by the NAMA Board is to redeem, at minimum, all €30 billion of Senior Bonds by 2020, in addition to recovering its carrying costs and any working and development capital advanced to debtors. Based on its analysis of the portfolio acquired under the NAMA Act 2009, the Board believes that this objective will be met. A first major interim milestone is the end-2013 bond redemption target of €7.5 billion (25% of Senior Bonds issued). Progress towards this target has been monitored, on a quarterly basis, by the EU/IMF/ECB troika. The Agency redeemed €1.25 billion of Senior Notes in 2011, €3.5 billion in 2012 and a further €1.5 billion in June 2013. It is expected that an additional €1.25 billion will be redeemed in the final quarter of 2013, thereby fulfilling NAMA's end-2013 debt repayment target of €7.5 billion.

The Board target is to redeem, by the end of 2016, 50% of the Senior Bonds issued as consideration for the portfolio acquired under the NAMA Act 2009. This corresponds to an aggregate redemption of €7.5 billion of Senior Bonds over the 2014-2016 period and it would bring the total redemption to €15 billion by the end of 2016.

In working towards achieving its 2016 and 2020 debt redemption targets, NAMA pursues two principal strategies:

1. Work with debtors/receivers to maximise the cashflow generated by the portfolio.
2. Pursue various initiatives aimed at increasing transactional activity.

1. Portfolio cashflow generation

Up to end-August 2013, NAMA had generated cashflow of €13.5 billion from its loan portfolio. This comprised €9 billion in asset disposal proceeds and €4.5 billion from other income, principally rental income from property assets controlled by debtors and receivers. Asset sales in 2014 will continue to take place in line with sales schedules agreed with debtors and receivers and the proceeds from these sales will be used to reduce debtor liabilities and ultimately NAMA's indebtedness.

In addition, NAMA will continue to advance funds to property assets through capital investment so as to yield an enhanced return to the taxpayer over coming years (including an investment of at least €2 billion in Irish assets).

Loan sales have become an increasingly important element in market activity in 2012 and 2013. NAMA is keen to attract international capital interested in acquiring loans or property assets under the control of its debtors and receivers. It has established two loan sales advisory panels to advise and assist it on the sale of loan portfolios. Up to end-August 2013, NAMA had completed sales of loans with par debt balances of €3.7 billion and it expects that there will be further significant activity in this area in 2014.

The drive to ensure that rental income is brought within NAMA's control and to reduce debtor overheads will continue in 2014. Some €800m has been yielded to the taxpayer to date from an intensive effort by NAMA to reverse the transfer of debtor assets to related parties and to obtain security over unencumbered debtor assets; any scope for additional income from such activity in 2014 will be fully pursued.

2. Increasing transactional activity

NAMA will continue to pursue a number of initiatives aimed at increasing transactional activity in the Irish commercial and residential markets.

Vendor Finance

It launched a vendor finance programme to address constraints arising from the lack of availability of finance for property transactions, particularly in Ireland. Some €360m in NAMA vendor finance transactions have been completed to date and up to €2 billion in vendor finance is available if required to facilitate transactions.

Multiple asset sales

NAMA is also actively assessing the scope for combining assets within its control with a view to offering them for sale to the many international and local investors seeking such portfolios including, *inter alia*, any REITs established following the enactment of REIT legislation in Ireland in 2013.

Joint Ventures

NAMA is also very receptive to joint venture (JV) partnership initiatives and this is an area in which there is expected to be increased activity in 2014. Among the joint ventures which have established precedents for further similar initiatives in 2014 are the following:

- The Project Aspen JV which involved the sale of a loan portfolio to a new JV entity owned by Starwood Capital Group (80%) and NAMA (20%).
- A JV between NAMA and Oaktree Capital Management in a new Qualifying Investor Fund under which the parties will combine their respective ownership of land with a development potential of up to 50,000 square metres in the Dublin Docklands area.

Based on its ongoing engagement with potential asset purchasers and investors, NAMA will explore the scope for other potential JV arrangements which may be of value in advancing its objectives.

Social housing

NAMA also launched initiatives to address constraints on residential market activity (the Deferred Payment Initiative) and to facilitate the provision of social housing. In the case of the latter, NAMA identified 4,300 houses as potentially suitable for social housing and demand has been confirmed by local authorities for over 1,750 of these. Demand is still being assessed for another 420 properties, bringing the total number of properties that may

ultimately be delivered under this initiative to over 2,000. Delivery, however, is ultimately subject to the expeditious purchase and leasing of suitable properties by local authorities and approved housing bodies.

Whilst the pace of delivery is not within NAMA's direct control, in order to help further streamline the process, the Agency established a special purpose vehicle, *National Asset Residential Property Services Ltd. (NARPS)*, to acquire properties directly from debtors and receivers for direct leasing to local authorities and approved housing bodies. It is intended that about 350 properties will be made available for social housing under the NARPS arrangement in 2014 with additional properties being delivered directly by NAMA debtors and receivers.

Resource Allocation

Table 1 below presents the main components of NAMA's projected 2014 Budget for the management of loans acquired under the NAMA Act 2009:

TABLE 1: NAMA PROJECTED 2014 BUDGET – existing portfolio

	2014	2013
	Budget	Budget
NAMA Direct Costs	(€m)	(€m)
Primary Servicer/Master Servicer Fees ²	56	71
Reimbursement to NTMA as Service Provider	51	42
Legal Fees	11	13
Asset Recovery/Asset Management	8	6
Accounting/Audit/Tax and other administrative costs	9	5
IT/MIS costs	2	3
Total - Direct Operating Costs	137	140

² Primary Servicer fees are paid to the participating institutions/service provider for the day-to-day servicing of NAMA loans. The fee – up to a maximum of 10 basis points - has been agreed, on a cost recovery basis, with the EU Commission.

The two principal elements of the projected Budget are the servicing fees payable to the participating institutions and to the Master Servicer (a projected €56m) and the reimbursement to NTMA for the cost of providing staff and for other services (a projected €51m).

Servicing Fees

Primary and special servicing on NAMA loans is provided by AIB, Bank of Ireland and Capita Asset Services. **Primary servicing**, also known as loan administration services, comprises the administrative and operational activities associated with the management of loans, including the processing and charging of loan interest and fees. **Special servicing** is also known as case management or relationship management and involves on-going interaction with debtors and the assets securing their loans with the objective of maximising the cash realised from loans and assets.

AIB, Bank of Ireland and Capita Asset Services carry out primary servicing on the full NAMA loans portfolio (currently €68.6 billion in par debt). They also provide special servicing on the loans of 586 debtor connections which are not directly managed by NAMA; the NAMA debt involved is €4.1 billion. The projected cost in 2014 of primary and special servicing of the portfolio acquired under NAMA Act 2009 is €53m.

Prior to the decision of the Government in February 2013 to appoint Special Liquidators to IBRC, IBRC had provided primary servicing for NAMA loans with nominal balances of €38 billion. It had also provided special servicing on the loans of over 300 debtors (acquisition value of €1.3 billion) under a framework of delegated authority from NAMA. Following the appointment of the Special Liquidators, NAMA experienced an unexpected disruption to its non-disposal cash collection: the bank and loan accounts of IBRC were frozen by the Central Bank and standing orders were blocked. Work is ongoing in respect of putting in place new rental payment structures in new banks and the collection of any outstanding cash due to NAMA.

In March 2013, NAMA appointed **Capita Asset Services** as its primary and special loan servicer on the NAMA loans which, prior to 7 February 2013, had been managed on its behalf by IBRC. Capita, which had acted as Master Servicer to NAMA since 2010, formally assumed its primary and special servicing obligations in August 2013.³ Arising from these new arrangements, NAMA is in the process of recruiting 40 additional members of staff who will have responsibility, in conjunction with Capita, for the servicing of the former IBRC-managed portfolio.

Staff and other costs – existing NAMA portfolio

As at the end of August 2013, the Board had approved a total staffing complement of 326 staff to manage the portfolio of loans acquired under the NAMA Act 2009. Excluding the Executive team of six, the approved allocation of permanent staff across the various divisions is as follows:

TABLE 2: STAFFING OF NAMA BUSINESS DIVISIONS⁴

Division	Responsibilities
Asset Recovery (174)	To implement business strategy, manage debtors, maximise income and minimise loss. Asset Recovery directly manages the largest 189 debtor connections, incorporating nominal debt of €61bn. In addition, it leads the recovery management of the residual portfolio which is managed by AIB, Bank of Ireland and Capita, comprising nominal debt of €13bn and 586 debtor connections.
Asset Management (16)	To identify and develop property assets with debtors, receivers and joint venture partners so as to create and add value and enhance asset cash flow.

³ This followed a transitional period between February and August 2013 during which primary and special servicing was carried out by IBRC (in Special Liquidation).

⁴ This includes 40 members of staff, currently being recruited, who will have responsibility, in conjunction with Capita, for the servicing of the former IBRC-managed portfolio.

Division	Responsibilities
Strategy and Communications (14)	To develop strategies that will deliver the best achievable return from acquired assets, and to coordinate engagement with the Oireachtas, media and other key stakeholders.
Legal (49)	To provide legal advice on a range of issues relating to the operations of the Agency, including enforcement and the management of litigation involving NAMA.
Chief Financial Officer (67)	To manage a number of key functions, including Finance, Operations, Systems, Treasury, Tax, Audit and Risk.

In addition to staff, the NTMA provides a number of services to NAMA, including HR, IT, office and business services and the costs of such services are reimbursed by NAMA on an annual basis. The projected reimbursement for 2014, including staff costs, is €51m. NAMA's operating costs - 2.6% of cash generated in 2012 - compare favourably with comparable international institutions.

Prospective IBRC loan acquisitions

As part of the Government's decision to appoint Special Liquidators to IBRC in February 2013, it was decided that NAMA would acquire any loans which were unsold after the Special Liquidators had completed a loan valuation and sales process. The size of the portfolio to be acquired by NAMA will only become known after this process has completed; this is expected to be in late 2013 or early 2014.

In preparation for the acquisition of loans, NAMA, in July 2013, selected a number of preferred bidders to provide services on two loan portfolios which it may acquire from the Special Liquidators. The larger of these is a portfolio of commercial property loans, residential investment and development loans and business banking loans which could potentially comprise aggregate nominal par debt value of €20.3 billion, depending on the outcome of the Special Liquidators' sales process. NAMA may also acquire a portfolio of personal loans, principally residential mortgage loans which could potentially comprise aggregate nominal par debt value of €1.9 billion. Following a number of issues which emerged in relation to the preferred bidder initially selected to provide services on this

portfolio, NAMA launched a new tender in September 2013 and the outcome of the tender is expected to be known by November 2013.

Notwithstanding the fact that much of the day-to-day management of the new portfolio will be outsourced, its acquisition will require NAMA to recruit additional staff: they will be required to carry out special servicing on the larger debtor connections to be acquired, to oversee the special servicing activity of external service providers in relation to other debtor connections and to provide legal, finance and operations services. The current estimate is that NAMA will require additional staffing within a range of 180 - 220 for this work; in addition, it is expected that up to 300 staff will be employed by NAMA's appointed service providers. (The corresponding number employed by IBRC to deliver the services was close to 800 at the point at which the Special Liquidators were appointed). NAMA's staffing estimate is particularly sensitive to the number of larger debtor connections (connections with aggregate loan exposures in excess of €75m) which may be acquired; in line with current practice, it is envisaged that the loans of these connections will be managed directly by NAMA.

While NAMA is actively preparing for the acquisition of loans which will transfer from the Special Liquidators, accurate estimation of the staffing requirements and of the budgetary implications of the acquisitions will only be possible after the scale of the transfer becomes clear.