4. FINANCIAL POSITION AND RISK EXPOSURE OF HOUSEHOLDS AND ENTERPRISES

(20) During the period, households remained inclined toward saving, but trending downward, while enterprises narrowed their net debt position. The growth of credit in lek to households and the fall of their deposits, affected the narrowing of their credit position.[13] For the same period, credit to enterprises fell at a higher pace than the fall in deposits, narrowing therefore their debtor[14] position. In annual terms, unlike the half-yearly trend, households show a slight expansion of the creditor position attributable to the creditor position in foreign currency[15]. Meanwhile, enterprises narrowed more considerably their net debtor position attributable to the considerable fall of credit and the expansion of deposits, mainly in foreign currency[16]. The loss loans write off from banks' balance sheets drove to a considerable annual improvement of the entire credit quality, and in particular of the unhedged foreign currency loans.

4.1 FINANCIAL POSITION OF HOUSEHOLDS AND ENTERPRISES

(21) During the period, the creditor position of households fell at ALL 765.4 billion, affected by the drop of deposits, mainly in foreign currency, and the increase of credit. The orientation of credit to households in the domestic currency contributed to the narrowing of the creditor position in lek at a higher pace than in foreign currency[17]. Also, enterprises narrowed their debtor position against the banking sector, standing at ALL 158.2 billion. The narrowing of the debtor position of enterprises was attributable to the faster contraction of credit compared with the fall of deposits.

[13] *Creditor position narrowed by around 2.3%, during the period, affected simultaneously by the fall in deposits by 1.4%, alongside the increase of credit by 2.9%. Credit in ALL grew by 4.9% compared the growth by only 0.5% of credit in foreign currency; while deposits in ALL and foreign currency fell by 1.8% and 1.0%, respectively.*

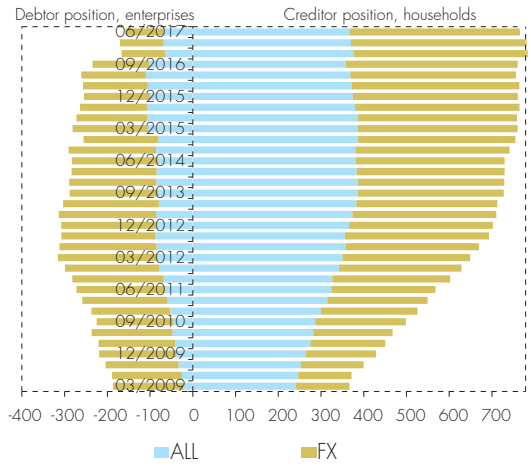
[14] *The debtor position narrowed during the period by 5.1%, due to the narrowing of the position in foreign currency (12.2%), mainly attributable to the fall of credit in this currency (6.6%). Meanwhile deposits fell by 1.4%, mainly affected by the fall of deposits in ALL by 2.4%, against the fall by 0.8% of deposits in foreign currency.*

[15] *In annual terms, creditor positions of households expanded by around 1.2%, attributable to the expansion of the position in foreign currency by 2.9%.*

[16] *The narrowing of debtor position, in annual terms, was around 39% and was affected by both, the narrowing of position, both, in ALL and in foreign currency (37.1 % and 41.1%, respectively). The fall of credit for both positions (ALL: 20.0% and foreign currency: 18.9%) was accompanied by a growth of the relevant deposits (20.6% and 23.7%, respectively).*

[17] *Creditor position in ALL fell at 2.4% against that in foreign currency by 2.2%.*

Chart 4.1 Financial position of households and enterprises, in ALL billion



Source: Bank of Albania, Financial Stability Department.

(22) Focusing on resident households, during the period, savings in the form of foreign currency deposits reduced and shifted to savings and investments in lek, in other assets of the financial system. Hence, the share of deposits in foreign currency against the total assets of resident households in the financial system dropped at 39.2%, while the share of investments in treasury bills, bonds and investment funds increased during the period (see Table 4.1).

Table 4.1 Households' assets in the financial system, ALL billion

	2010		2013		2016, June		2016, December		2017, June	
	ALL bln	Share %	ALL bln	Share %	ALL bln	Share %	ALL bln	Share %	ALL bln	Share %
ALL deposits	357.6	49.8	449.5	43.7	450.4	40.3	454.3	40.3	465.1	42.1
FX deposits	304	42.3	418.4	40.7	455.6	40.8	476.4	42.3	432.8	39.2
T-Bills	56.7	7.9	70.6	6.7	72.4	6.5	65.2	5.8	67.3	6.1
Bonds	0.37	0.05	39.8	3.9	66.4	5.9	64.5	5.7	67.9	6.1
Investment funds*	-	-	50.3	4.9	71.7	6.4	65.4	5.8	70.8	6.4
Private voluntary pension funds*	0.12		0.43	0.04	1.1	0.1	1.2	0.1	1.3	0.1
Households portfolio	718.8	100	1,029	100	1,117.60	100	1,127.00	100	1,105.20	100.00

Source: Bank of Albania, FSA.

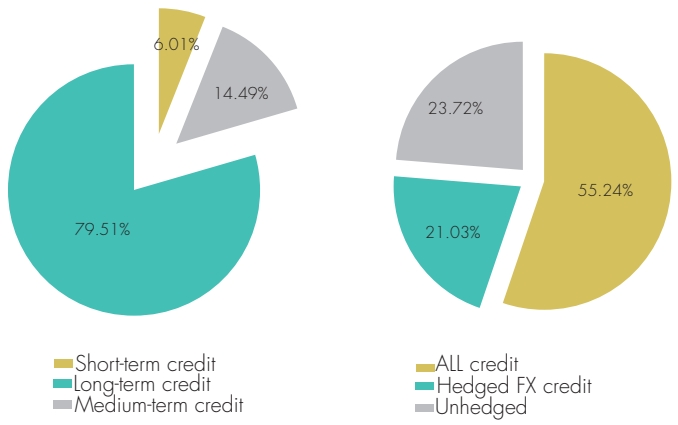
4.1.1 LENDING TO HOUSEHOLDS AND CREDIT RISK

(23) During the period, the expansion of credit to households was mainly attributable to the domestic currency, while credit in foreign currency expanded slightly. Hence, the share of credit in lek to households was up at 55.2%, around 3.3 percentage points higher than in June 2016. Unhedged loans to households in foreign currency fell both in annual and half-yearly terms, by reducing the exposure against the unfavourable movements of the exchange rate. The share of unhedged loans in foreign currency against the total outstanding credit in foreign currency to households dropped at 53.0%, from 55.1% and 53.9% in June and December 2016.[18] Around 79% of household unhedged loan consists in "House purchase loans", which fell by 3.3 percentage points, over a one year period. By maturity, long-term credit to households increased slightly by 1.1 percentage points, reaching at 79.5% of

[18] *The developments in the share of unhedged credit in foreign currency against total outstanding credit to households were at the same direction. This ratio fell both in annual and half-yearly terms. It stood at 23.7% in June 2017, compared with 26.9% and 25.7%, in June and December 2016, respectively.*

the portfolio; short-term credit fell at 6.0%, and medium-term credit accounted for 14.5% of the portfolio, down by 0.4 percentage point, respectively.

Chart 4.2 Structure of credit to households by maturity (left) and currency (right)

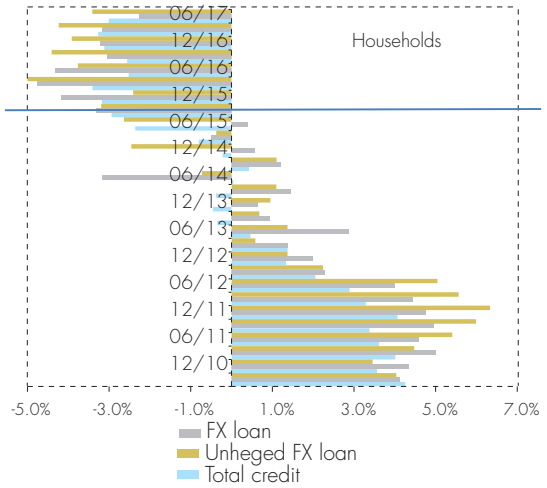


Source: Bank of Albania, Financial Stability Department.

(24) The quality of credit portfolio to households continued to improve, attributable to the loss loans write off from banks' balance sheets. The non-performing loans ratio for households fell at 9.4%, around 3.1 percentage points lower than in the previous year. The credit quality improved more considerably for the foreign currency credit, and for its part that is unhedged against fluctuations in the exchange rate. The ratio of non-performing loans in foreign currency to households dropped at 11.1%, down by 2.3 and 1 percentage points, in annual and half-yearly terms, respectively. The non-performing loans ratio of credit unhedged against the movements in the exchange rate further dropped at 10.6%[19].

(25) During the period, credit to resident households continued to accelerate, expanding both in annual and half-yearly terms, by 3.7% and 2.5%, respectively. This positive development was mainly affected by the expansion of credit for "non-durable goods" and for "real estate", where the latter shares 64% of total credit to this category of households.

Chart 4.3 Annual change of NPLR for households, in p.p.



Source: Bank of Albania, Financial stability Department.

[19] *This ratio was 14.0% and 11.2% at the end of June and December 2016, respectively.*

BOX 4.1. SURVEY RESULTS ON HOUSEHOLDS' FINANCIAL AND BORROWING SITUATION

The survey of households' financial and borrowing situation is conducted half-yearly. The survey is based on a randomly selected sample of 1,209 households, across around 55% urban areas and 45% rural areas.

In 2017 H1, the number of employed persons increased in annual terms, mainly supported by the employment in the public sector. The financial balance (income-expenses) of households was up, but the increase in expenses was higher, driving to a narrowing of households' financial balance (income-expenses). Around 28% of households say they have a loan to repay. This share is slightly lower from both 2016 H2 and the previous year.

In 38% of borrowing households had borrowed from formal sources (banks and non-bank institutions) in the form of credit products, and in 62% of cases from informal sources, mainly in cash. Compared with 2016 H2, this allocation has somewhat shifted in favour of the formal against the non-formal borrowing, as a result of the increase of bank borrowing. Consumption (40% of borrowing cases), purchasing/renovating a property (28% of cases) and business development (13% of cases) remained the top three purposes of borrowing. During the survey period, the shares of borrowing cases for consumption and purchasing property have been downward.

Total reported outstanding credit was up compared to both the previous survey, and the previous year. Around 80% of total outstanding credit is provided from formal sources and 20% from informal sources, remaining unchanged from 2016 H2. By currency, 92% of outstanding credit is in lek, and only 8% in foreign currency (mainly in euro). By purpose of use, around 56% of outstanding credit was for "Purchasing/renovating a property", 23% for "business development" and only 10% for "consumption" purposes.

The borrowing households say credit instalment during the referring period has fallen, reflecting the reduction of the weighted credit interest rate to households. The major part of borrowing households stated that their solvency has not changed during the period, while the rest mainly state a worsening. The major part of households (around 78%) does not expect any change of solvency in 2017 H2, the rest has optimistic expectation.

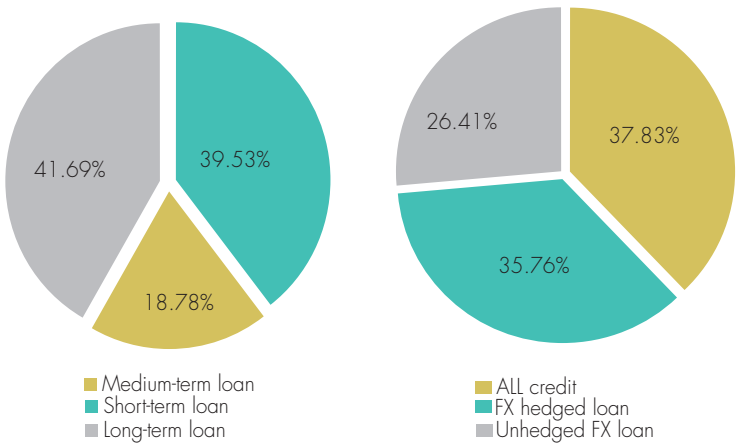
The possibility to receive a loan during 2017 H2 has resulted below the long-term average rate and trending down, by signalling a weakening of credit demand by households.

4.1.2 LENDING TO ENTERPRISES AND CREDIT RISK

(26) Credit to enterprises, accounting for 66% of total outstanding credit, fell slightly annually. In this portfolio, credit to resident enterprises had the main share, by 85%. It shrank both in half-yearly and annual terms, by 3.0% and 5%, respectively. During the period, outstanding credit for the "working capital" and for the "equipment purchase" shrank the most[20]. Meanwhile, annual developments show a fall in the credit stock also in the category "investments for real estate". By contrast, outstanding credit to non-resident enterprises expanded by 15.5% from the previous year, and around 2.1% during the period.

(27) In the structure of total credit to enterprises, the share of credit in the domestic currency was up, against the fall of credit in foreign currency. The share of credit in foreign currency in the total credit to enterprises dropped at 62.2% or 2.1 percentage points lower from the previous year. The outstanding credit unhedged against unfavourable volatilities in the exchange rate was also down; although its share in the total credit to enterprises has remained close the level of 26%.[21] In the structure of unhedged credit to enterprises, the shares of credit for "trade", for "real estate development" and for "business development" fell at 46.3%, 9.0% and 10.0%, respectively.

Chart 4.4 Structure of credit to enterprises by maturity (left) and currency (right)



Source: Bank of Albania, Financial Stability Department.

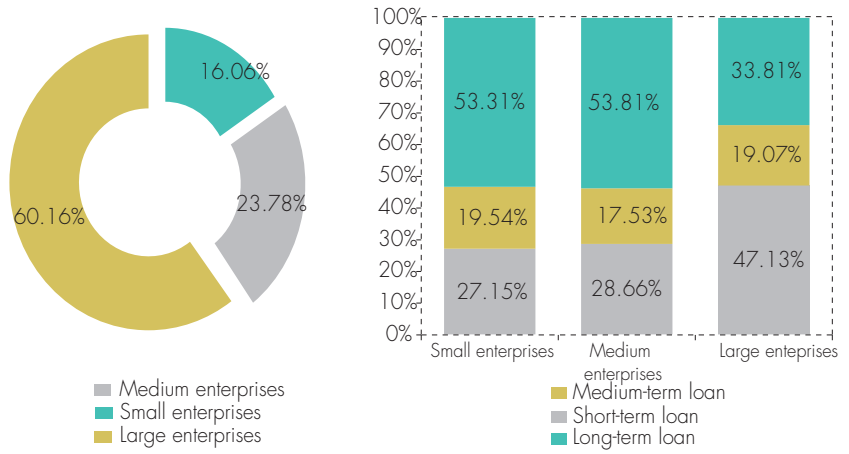
(28) In the stock of credit to enterprises, credit to large and medium-sized enterprises have the main share. The share of credit to large and medium-sized enterprises was up, accounting for 60.2% and 23.8% of the total, respectively. The share of credit to small enterprises fell at 16.1%. During the period, the small and medium-sized enterprises continued to increase the share

[20] *In more concrete terms, credit for working capital and equipment purchase fell half-yearly by 10.0% and 3.9%, respectively.*

[21] *Its share in June and December 2016, accounted for 26% and 27% of total credit to enterprises, respectively.*

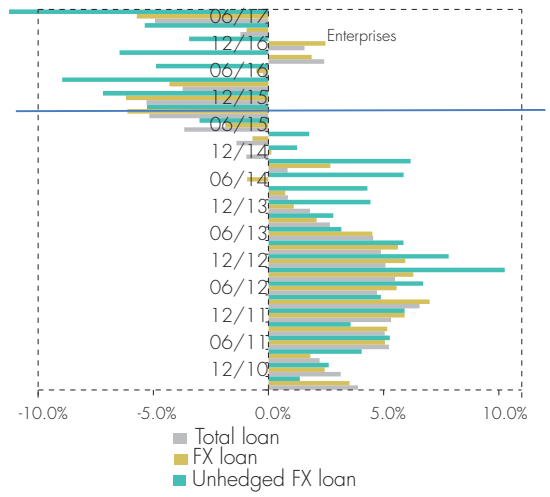
of long-term credit, whereas the large enterprises continued to be oriented towards the medium-term credit, recording small changes in the fall of long-term credit. By currency, the small enterprises decreased the share of credit in lek in favour of the one in foreign currency; while medium-sized and large enterprises expanded the credit in lek.

Chart 4.5 Structure of credit to enterprises by size



Source: Bank of Albania, Financial Stability Department.

Chart 4.6 Annual change of NPLR for enterprises, in p.p



Source: Bank of Albania, Financial Stability Department.

(29) Credit portfolio quality to enterprises, almost in all its components, improved considerably in annual and half-yearly terms. In June 2017, non-performing loans ratio to enterprises stood at 19.4%, from 23.0% in December 2016, and 24.4% in the previous year. The ratio of non-performing loans in foreign currency pursued a similar trend, falling at 19.6% at the end of the period, or 5.7 percentage points lower than the level of the previous year. The portfolio quality for unhedged foreign currency credit to enterprises improved significantly, annually and half-yearly, mainly affected by the loss loan write off process. At the end of the period, the ratio of non-performing loans for this category dropped at 16.7%, from 22.2% at the end of 2016, and 26.3% in the previous year.

BOX 4.2 SURVEY RESULTS ON ENTERPRISES FINANCIAL AND BORROWING SITUATION

The survey of enterprises' financial and borrowing situation is conducted half-yearly for eight years now. The latest survey was realised in the period May-June 2017, focusing on the developments in 2017 H1, while expectations refer to 2017 H2. The survey was conducted with a sample of 1,238 enterprises (small, medium-sized, and large enterprises), across the country, operating in major sectors of the economy. At the beginning of the year this sample was renewed for 10% of it.

During 2017 H1, competition continued to be considered by all groups of enterprises as the main problem to their activity. The importance of this factor is assessed upward to all sizes of enterprises, compared with 2016 H2. Finding a market also is assessed as another important limiting factor to the activity of the three groups of enterprises, in particular, to small and medium-sized enterprises. Problems related to access to finance are assessed as upward for small enterprises, while costs of financing are assessed as downward to medium-sized and large enterprises.

Medium-sized and large enterprises assess the level of sales as upward, during 2017 H1, while it was assessed as downward for small enterprises. Medium-sized and large enterprises assessed the financial result as upward, in line with the performance of sales, during the period. The positive performance of both sales and financial result was reflected in the expansion of the activity of medium-sized and large enterprises. Overall, the positive expectations of enterprises about the sales, the financial result and the expansion of the activity provide optimistic signals regarding their performance in the short and medium term.

During 2017 H1, almost half of respondent enterprises financed their activity through sales. Borrowing as a separate or combined source was used by 29.9% of large enterprises, 25.8% of medium-sized enterprises and 22.9% of small enterprises.

Around 40% of total enterprises (438 enterprises) state that they have a loan to repay. This share dropped compared to 2016 H2, for all the three groups of enterprises, but more emphasised for medium-sized enterprises. Around 89.3% of total borrowing enterprises state that they have turned to banks for borrowing. This share accounts for 92.1% of total formal sources (banks and non-bank financial institutions). Informal sources share 7.9% of total borrowing, where borrowing from natural persons has the highest share (2.8%).

Enterprises borrowed primarily to cover current expenditure and to conduct long-term investments. Compared to the previous survey, the share of enterprises that have borrowed to conduct long-term investments was up for the medium-sized and larger enterprises, while it was slightly down for small enterprises. Around 78% of small enterprises, 78.6% of medium-sized enterprises and 77.3% of larger enterprises consider the level of borrowing for financing their activity as adequate. Compared with 2016 H2, this share was up for both small and large enterprises, but downward for medium-sized enterprises.

Borrowing is reported in the domestic currency for 47.2% of total enterprises. Borrowing in the European currency has the main share of 49.4%, while the share in US dollar was 3.3%.

Only 10% of small enterprises and 11% of medium-sized and large enterprises report new borrowing during the period.

The overall value of the loan is about half the value of the enterprise's capital for 79.4% of borrowing enterprises. By size, debt share is higher for small enterprises, where around 24.3% of them stated that the value of the loan is equal or higher than the value of capital. The majority of borrowing enterprises (73.4%) state that the loan payment to revenues amounts up to 20% of revenues, trending down from the previous period. The burden of the loan payment appears to be heavier on small enterprises. The number of small enterprises reporting that the payment of the loan exceeds 20% of revenues accounts for around 33% of the total group.

Bank borrowing is assessed between "normal" and "difficult", while the importance of relationship with banks is assessed between "important" and "indispensable", for all the three groups of enterprises (small, medium-sized and large enterprises). More than half of the responded enterprises (51.3%) have reported that they do not intend to request a banking loan in the next half of year. This share is down for small and large enterprises, but up for medium-sized enterprises. There is an increase in the share of enterprises in the entire three groups reporting that there is a slight possibility to borrow in the next half of year.

4.2 REAL ESTATE MARKET

(30) The banking sector is exposed either directly or indirectly to the developments in real estate market[22], which consist in the performance of supply and demand, the volume of sales and performance of prices in the market. According to INSTAT data for the end of 2016, a considerable increase of the construction land and permits for housing was reported, while the construction cost continued the upward trend started since 2016 Q2. Also data reported by the banking sector for 2017 H1, show a slight increase of outstanding credit for real estate[23], accompanied by an increase of credit interest rates and slightly improvement of credit quality. The non-performing loans ratio for this type of credit dropped at 8.3%, from 8.8% in December 2016, and 10.4% a year earlier. Outstanding credit for construction has not changed considerably from December 2016, although it fell by 1.6% from the previous year, driving its share to be down at 13.6% of outstanding credit to enterprises, considerably below the level of around 20% recorded during the period 2007 – 2011.

(31) At the end of the period, banks reported a slight growth of real estate collateralised credits, at 50%, from 49% six months ago. Around 67% of

[22] *In this case, the exposures is represented by the loan granted or collateralised by real estate; loans to companies operating in construction sector; and the real estate loans portfolio that is established in banks as e result of taking the collateral following the execution of the obligation.*

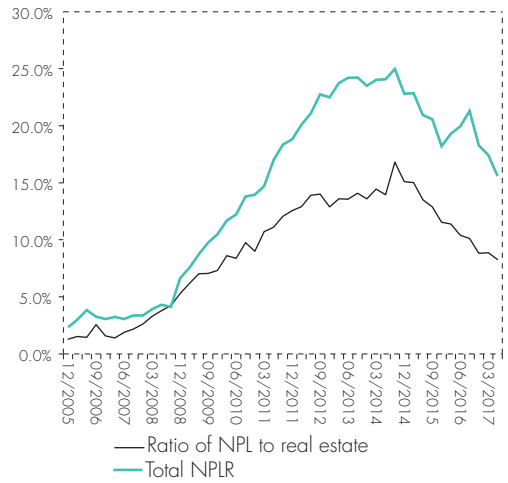
[23] *By only 0.2%*

credit to households and 43% of credit to enterprises was credit collateralised by real estate. This ratio was up for households and down for enterprises. Bank of Albania's bank lending survey for 2017 Q2 shows that households' demand for real estate credit was slightly up, while standards on credit approval were reported eased to

Chart 4.7 Credit for real estate purchasing and cost of credit payment

Source: Bank of Albania, Financial Stability Department.

Chart 4.8 Non-performing loans ratio



Source: Bank of Albania, Financial Stability Department.

households and somewhat less eased to enterprises[24].

(32) The weighted interest rate on the real estate credit[25] was 4.5%, slightly up during the period, but remaining in line with the downward trends in the recent years.[26] Along the same lines, the relative repayment cost[27] of real estate purchase increased, reflecting somewhat more tight conditions for real estate purchase from the borrower's perspective.

[24] *According to the Bank Lending Survey 2017 Q2, banks report that households' credit demand was slightly up for house purchase (the balance was slightly positive, at 1.6%).*

[25] *To calculate this rate, the interest rate is weighted for credit for real estate purchase to households, and for enterprises for real estate investment to enterprises.*

[26] *Average interest rate for real estate during 2008-2013 was 8.7%.*

[27] *The relative repayment cost of credit real estate purchase is measured as the difference between the interest rate on real estate loans and the average house price rise rate for the four previous quarters. The increase in this difference implies higher relative costs.*

BOX 4.3 REAL ESTATE MARKET AND HOUSE PRICE INDEX, 2017 H1 SURVEY

The situation in the real estate market is assessed through the field survey of a sample consisting in 230 real estate agents and construction firms, representing around 75-80% of the sample of these entities by size of activity. The Bank of Albania compiles the questionnaire and the data entry and processing, while the Institute of Statistics performs the field interviews, the main processes of sampling and the physical check of the filled questionnaires.

The net balance of responses of – 11.6% for the question "How do you assess the market situation compared with the previous period" shows a higher number of agents providing negative response (worse) than the positive response (better). This value is somewhat more negative compared with 2016 H2 (-8.6%), reflecting a slight worsening of agents' assessment for the market situation. As expected, the same indicator assessed only for the entities reporting sales during the period, shows a considerable more positive assessment; the net balance of responses on the overall situation by the entities reporting sales is around + 22%.

Fischer House Price Index, on a national level, was 5.3% higher than the level of the base period, year 2013. This development was affected by the increase in the sales volume in the other areas. On the other hand, price index at the national level is 7% lower from the previous period. For Tirana, the index fell slightly compared with the base period by 2.2%, and by 16.7% compared with the previous period. In the coastal areas, the agents reported lower average prices than those of the base period, but around 7% higher than those of 2016 H2.*

Agents report almost the same number of houses recorded in their books; the net balance between those reporting increase and those reporting decrease recorded in their books stands at slightly positive values. Related to commercial properties, the net balance is -3.8%, from the positive value 2.6% in the previous period. The number of unsold properties, both for residential and commercial buildings was down; the net balance was positive, showing less unsold properties, for the second successive period, since the start of the survey, though at more moderate values compared with 2016 H2.

The average time of sale for real estate, at the national level, is 10 months, or around 3.7 months shorter compared with 2016 H2. For Tirana, the respondent entities reported an average time of sale of 9.5 months, considerably lower compared to 13.8 months in 2016 H2. For the coastal area, the average sale time increased, from 8.4 months to 11.7 months, while for the other areas, the entities reported a considerable fall in the same sale time with the previous period, from 15 months to 9.7 months.

According to agents, around 72%, of properties for both, residential and commercial buildings sold by them, are purchased with loans. This figure is slightly up compared with 68% in the previous period. The loan-to-value ratio accounts for around 64% of the house value, higher from 53% in the previous period.

Agents are optimistic about the market performance in the territory they operate in the short-term future and considerably more positive for the long-term period (up to two years). The number of properties expected to be registered for sale during the forthcoming period is assessed as downward. Agents expect increase of real estate prices. The net balance was positive (11.4%), the most positive expectation since the beginning of the survey.

* *"Other areas" include all the areas, except for Tirana and the coastal area.*