Bank of Albania

FINANCIAL STABILITY REPORT

2020/H2

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Sheshi "Skënderbej", Nr.1, Tirana, Albania
Tel.: + 355 4 2419301/2/3; + 355 4 2419401/2/3
Fax: + 355 4 2419408
E-mail: public@bankofalbania.org

www.bankofalbania.org

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INTRODUCTION

This is the twenty-fifth issue of Bank of Albania's Financial Stability Report (hereinafter "the Report"), which is published half-yearly. The Financial Stability Statement, whose half-yearly release is a legal requirement, prefaces the Report. The purpose of this Report is to identify and assess risks to the financial system of the Republic of Albania and its infrastructure, and it assesses the ability of the financial system to absorb these risks. This Report makes it possible for public authorities to identify relevant measures for corrections, as necessary, in a timely manner.

In producing this Report, we have used data available from the Bank of Albania, and information from other authorities supervising the financial market. We have also used information and analyses from public and private, national and international financial institutions. The data and analyses cover mainly the developments over the second half of 2020 (hereinafter "the period"). Unless otherwise stated, the expectations for the economic and financial outlook extend through a period of up to 12 months.

The stability of the financial system has been assessed based on its performance, from its activity, and taking into account the risks arising from the system's interaction with the overall internal and external economic environment. In order to assess the risks arising from the system's interaction with the surrounding environment, this report analyses the latest developments in international financial markets, and in advanced and regional economies. We have also assessed the impact of these developments on the financial system and the banking sector in Albania. Concerning domestic indicators, this Report assesses the overall developments and expectations for economic growth, balance of trade, overall price levels, exchange rates and fiscal indicators. Also, by analysing the performance of employment, income, and specific surveys, it evaluates the financial situation of enterprises and households, and the impact on the solvency of borrowers in the banking sector.

The Report also presents the results of the stress test, which assesses the banking sector's resilience against macroeconomic and financial shocks, expressed in terms of capital adequacy.

The Financial Stability Report is compiled by the Financial Stability Department and is approved by the Supervisory Council of the Bank of Albania.

NOTES

As at the end of December 2020, the classification of banks in the Albanian banking sector is as follows:

I. According to the marginal contribution of each institution to systemic risk in Albania,[1] banks are grouped into:

- Systemically important banks: National Commercial Bank, Raiffeisen Bank, Credins Bank, Intesa Sanpaolo Albania and OTP Bank Albania.

- Other banks: Alpha Bank Albania, Procredit Bank, First Investment Bank Albania, United Bank of Albania, Union Bank, American Bank of Investments and Tirana Bank.

II. According to capital origin, banks are grouped into:

- Banks with foreign capital[2]: Raiffeisen Bank (Austria); Intesa Sanpaolo Bank Albania (Italy); Alpha Bank Albania (Greece); National Commercial Bank (Turkey); OTP Bank, Albania (Hungary); Procredit Bank (Germany); First Investment Bank, Albania (Bulgaria); United Bank of Albania (Saudi Arabia). These banks share around 69% of the banking sector's total assets.

- Banks with Albanian capital: Credins Bank, Union Bank, American Bank of Investments, Tirana Bank. These banks share around 31% of the banking sector's total assets.

III. Banks operating abroad:

- Banks showing an expansion of their network abroad include the National Commercial Bank with its affiliate in Kosovo, and Credins bank with its subsidiary in Kosovo.

Regarding the analysis used in the Report, the following should be taken into account:

[1] *For more information on determining banks with systemic risk consult the document "Methodology "On determining banks with systemic risk and the relevant capital buffer "and Regulation no. 41 dated 05.06.2019, "On macroprudential capital buffers," in Financial Stability/Macroprudential Policy on the website of the Bank of Albania.*

[2] *A bank is classified as having foreign capital, whenever the foreign capital amounts to more than 50% of the bank's paid-in capital.*

(1) The terms "loan" and "credit" are used interchangeably in this Report; "enterprises" and "firms" are also used interchangeably"; similarly, the terms "households" and "families" are used interchangeably.

(2) In this Report, "outstanding credit" refers to the balance of the account "relations with clients", as reported by banks in the balance sheets of the period under review. It includes outstanding credit granted by the banking sector to non-financial private and public, resident and non-resident entities. Outstanding credit is affected by non-performing loans (NPL) which have been written off from banks' balance sheets in the period under review. Hence, outstanding credit that is analysed in the Financial Stability Report is a different concept from that of credit to the economy that is addressed in the monetary policy reports. The latter, in addition to credit by banks, includes the credit by non-bank financial institutions. Also, the value of this credit includes only credit to the resident private sector and its value is not affected by the NPL's which have been written off from banks' balance sheets, as these loans are already obtained by the economic entities and have affected their economic value; their later write-off does not change this fact. Differentiation of these credit concepts should be considered when interpreting the relevant analysis of credit indicators (growth rate, quality ratio, allocation by sector, by currency, etc.) in various reports of the Bank of Albania.

FINANCIAL STABILITY STATEMENT FOR H2 2020

Pursuant to provisions under Article 69 of Law No. 8269, dated 23 December 1997 "On the Bank of Albania", as amended, and Article 8 of Law No. 9962, dated 18.12.2006 "On banks in the Republic of Albania", as amended, to inform the Assembly of the Republic of Albania and the Council of Ministers, and promote awareness among financial institutions and the public at large of the situation in the Albanian financial system and potential risks to its stability, the Bank of Albania releases this periodic statement. This statement is an integral part of the Financial Stability Report for the same stated period.

The Financial Stability Report and the Statement prefacing it assess the exposure of the banking sector to risks arising from its interaction with the external and internal economic environment, real economy agents, financial markets in Albania, as well as operational risks in the activity of the banking sector. Furthermore, these risks are assessed through the stress test and placed vis-à-vis the financial situation of the banking sector to assess its resilience.

The Bank of Albania deems that in 2020 H2 (hereinafter 'the period'), operations of the banking sector were stable. Financial intermediation proceeded with good pace, credit quality was maintained at acceptable levels, deposits grew considerably and other financial stability indicators remained at appropriate levels. The public measures undertaken in the fiscal, monetary and prudential areas helped the performance of lending, mitigated the pandemic shock and helped to control risks. Uncertainties continue to be considerable despite the expectations for a more stable performance while approaching the exit from the pandemic. Banks should remain vigilant particularly in relation to monitoring closely the solvency of their borrowers. As it has previously, the Bank of Albania stands ready to undertake all necessary actions according to the law, in order to support banking activity and contribute to the stability of the financial system.

Developments in this period revealed the following:

The evolution of the pandemic dictated economic developments around the world. Economic activity, both globally and in the Euro area, recovered during the third quarter of the year, but remained weak towards its end due to the return of restrictions related to the Covid-19 pandemic. Financing conditions remained favourable and many countries continued to support their economies with special fiscal packages. Inflationary pressures remained subdued given the deceleration of consumption and investments in the private sector. Similar developments were observed in the Euro area and the Western Balkans.

Assuming that acceleration of vaccination will bring the pandemic situation under control, the global economy is expected to take the road of a more sustainable recovery in H2 2021.

The economy of Albania contracted during 2020, but performance in the period was better, attributable to an increase in private consumption and investments. The contribution of the external sector of the economy was negative due to the expansion of current account deficit on the balance sheet, by around 2% in annual terms. Inflationary pressures were low and the accommodative monetary policy supported liquidity in the market. Fiscal policy played an active role in withstanding the shocks to the economy in the previous year, at first due to the consequences of the November 2019 earthquake, and then the pandemic. The measures undertaken included an extension to tax obligations; issuance of sovereign guarantees to protect employees' income and mitigate credit risk to borrowers; an increase in public spending focused on reconstructing buildings damaged by the earthquake and on meeting public health needs. As a result, similar to the experience of other countries, fiscal deficit and public debt recorded a rapid increase throughout 2020. In spite of expectations for a fast vaccination process and a gradual recovery of economic activity, the pandemic and its lingering effects of uncertainty are still evident in the economic environment. In these conditions, stimulating public economic policies are necessary, adapting to expectations for economic growth. In relation to fiscal policy, in the short run, it is efficiency and the financing method of fiscal stimulus that takes precedence, while in the long run, it will be necessary to preserve engagement and undertake measures for fiscal consolidation. The latter is necessary to mitigate risks related to high levels of debt and all which that entails.

Markets carried on their activity as normal, but with lower trade volumes. The level of government debt securities issued in lek was lower than in the first half of the year, while the average interest rate remained unchanged. The yield curve of the market had a normal slope. Activity in the secondary market of government debt securities was down in value and in volume of transactions. Investors started to show a preference for holding securities to maturity. The volume of transactions decreased in the interbank market. Interest rates fluctuated close to policy rate, reflecting the unlimited liquidity injection by the Bank of Albania. In the foreign exchange market, the lek exchange rate was stable, having a positive impact on reduction of financial stress in the market. The performance indicators of the real estate market have given mixed signals in relation to supply and demand performance in H2 2020. The real estate market had fewer transactions and a pessimistic outlook, given the impact of uncertainty caused by the pandemic. However, the periodic survey on real estate market shows that real estate agents reported higher sale prices compared with 2020 H1 and from the previous year.

The basic infrastructure for the clearing and settlement of payments in lek continued to function in a safe and efficient manner. During the period, it

was noted that there was an increase in the number and volume of small- and large-value transactions and the use of payment instruments.

Households and enterprises expanded their savings. Households recorded a further expansion of their financial position as net creditors and simultaneously, enterprises tightened their debtor position. The significant increase of bank deposits in lek and foreign currency was the main contributor for both groups. Survey data suggest that households' solvency slightly improved compared with 2020 H1, but it is weaker than last year. Households' loan demand may be higher in the first part of 2021. The survey data on enterprises show that the pandemic considerably affected their activity, by triggering more difficulties to market preservation and competition. Half of the enterprises declare that they financed their activity during this period through sales. The propensity to combine several sources of funding continues to have represented a considerable share during the period, but it decreased for all types of enterprises. Around 40% of total responding enterprises declare that they currently have loans to settle and this indicator increased during the last year. The total loan value is close to half of the capital value of enterprises for around 80% of the total borrowing enterprises and almost equal to the capital value for 9% of them. The majority of borrowing enterprises declare that loan payment reaches up to 20% of their income. In relation to borrowing plans in the upcoming six months and based on the responses of enterprises, it looks like credit demand is showing slight signs of recovery, even though decision-making regarding this objective is less certain.

A slight increase in the share of financial system assets[3] to Gross Domestic Product (GDP) was observed during the period. At the end of September, this share reached 119.4%. This performance was affected by the contraction of GDP, but also by the expansion of financial system activity, where the banking sector provided the main contribution.

The non-banking segment of the financial system had an overall good performance. Non-banking financial institutions and investments funds had the highest growth. Trade, services and agriculture sectors continue to represent the main economic activities that attract credit by non-bank and savings and loan associations. Loan quality granted by these entities until the end of the third quarter was relatively good, despite declining somewhat compared with last year. The exposure of the banking sector to the non-banking sector remains limited and unchanged during this period. The exposure of the non-banking sector to the banking sector remains high, as placements of non-banks in the banking sector in forms of deposits and capital instruments account for around 19% of non-banks' balance sheets.

[3] *The financial system consists of the banking sector and non-banking sector (non-bank financial institutions, credit savings associations, pension funds and investments funds). The database for the non-banking sector and GDP data are from 2020 Q3.*

The banking sector continued to support the economy with financing and other services despite the difficult situation created by the pandemic. Asset growth was underpinned by interbank investments and lending to the economy. The share of foreign currency activity decreased, but remained balanced on both sides of the banking sector's balance sheet. This fall reflected a faster growth of credit and deposits in Albanian lek. The statistical effect of the exchange rate on the equivalent value of the foreign currency balance had a non-significant impact. Deposits and own funds continued to be the main funding source of the banking sector's activity. Reliance on external funding sources remains at low levels. Assets placed with non-resident entities decreased during the period, due to the contraction of placements in the form of loans and current accounts with banks, financial and credit institutions. This has driven to the contraction of the net creditor position of the banking sector, by around 2 percentage points (pp) during the period.

The banking sector closed the year with a good level of capitalisation. The Capital Adequacy Ratio for the entire sector rose to 18.3% from 18.1% in the previous six months. The indicator was higher during the period due an increase of regulatory capital and a decrease of risk-weighted assets. In comparison with the previous year, this ratio was 0.4 p.p. lower and the decrease reflected a higher level of risk-weighted assets. Banks with European capital and systemically important banks show the highest level of Capital Adequacy Ratio. Banks with Albanian capital have the lowest level of Capital Adequacy Ratio; this ratio decreased slightly in 2020. The banking sector closed 2020 with a positive financial result of around ALL 17 billion. This result was 15% lower compared with the previous year. The increase in expenditure for loans provision provided the main contribution to the fall of the banking sector's profit. Meanwhile net interest income and other activities income were somewhat higher. The decrease in the profit of the sector is also reflected in the fall of the profitability indicators of the banking sector: RoA and RoE declined to 1.1% and 10.7%, respectively.

At the end of 2020, outstanding loans totalled approximately ALL 610 billion, higher by 3% over the period, and 6% from the previous year. The expansion of loan stock was mainly affected by an increase of new loans flow, used mostly by enterprises for short-term purposes. The higher level of credit stock was affected by the accumulation of unsettled liabilities, due to actions of banks for credit restructuring, in response to the accommodative measures of the Bank of Albania. A particularly good performance in the credit stock, over the period, was registered for credit portfolio of long-term maturity; loans in domestic currency and loans to enterprises. At the end of 2020, loans in foreign currency were 4% higher than the previous year, but maintained almost the same unchanged level over 2020 H2. By residence, credit growth over the period was affected almost entirely by an increase of loans to resident entities, which account for almost 96% of outstanding loans.

In 2020, the volume of written off loans from the banking sector's balance sheet was relatively low. A total of ALL 3 billion worth of loans was written off from the balance sheet, but more than half of them were realised in December 2020. The value of restructured loans, during 2020, was around ALL 23 billion, 90% of which was realised in the second half of the year. In most cases restructuring was realised upon client's request. The restructured credit, during the period, accounted for approximately 3% of total outstanding loans and around half of the non-performing loans stock.

Deposits held in the banking sector recorded high rates of growth over the period. The growth is distributed almost equally between households and enterprises and between lek and foreign currency deposits. Time deposits continued to contract, while the largest growth over the period in deposits by maturity was registered in current accounts followed by demand deposits. At the end of December, deposits registered around ALL 1,286 billion, up by ALL 56 billion during the period, and ALL 93 billion compared with the previous year. Around half of the overall stock of deposits is composed of time deposits, which decreased by around ALL 14 billion during the period. The share of time deposits to overall deposits stock continued to fall, favouring demand savings instruments. The average interest rates for time deposits both in lek and in foreign currency remain at low levels and their average ratio did not record significant changes during the period.

Overall, the risks to the Albanian economy increased in the period due to the impact of the pandemic.

According to the financial stability map, the main contributors to this performance were contraction of the domestic economy; weak progress of the international economy; and deterioration of the fiscal indicators related to public debt and budget deficit. Although the contribution of the fiscal policy in countering the effects of the pandemic mitigated its first impact on the financial situation of households and enterprises, the latter's' risk perception appears to be rising. The indicators of the financial system and the banking sector stand at good levels, showing an almost unchanged perception of risk. Over the period, entities were supported by the fiscal and monetary measures to counter the economic downfall, thus affecting a decrease in the indicators related to the materialisation of systemic risk and of financial stress. But the expectation of the longer-term impact of the pandemic on the economic, fiscal and financial indicators has led to a rise on the risk accumulation index. Banks share similar assessments related to risks driven by economic developments, probability of loan quality deterioration and the political climate related to the parliamentary elections.

In terms of more specific activity risks to the banking sector, the following is observed:

Credit risk was contained over the period under the impact of accommodative regulatory measures. The non-performing loans ratio showed low fluctuations and stood at 8.1% at the end of the year, around 0.3 percentage points lower than in the previous year. However, the improvement is driven by the faster increase of outstanding credit compared with the increase of non-performing loans stock. In fact, the absolute value of non-performing loans increased by almost ALL 1.6 billion during the period, climbing to ALL 50 billion. Within non-performing loans, the share of lost loans increased. Some complementary indicators that assess the performance of non-performing loans confirmed their increase. As a result, given the faster increase of provisioning reserves compared with the stock of non-performing loans, the provisioning coverage ratio increased to 65% from 59% in the previous year. The change in this indicator was concentrated in the first half of 2020. The collateralisation of the loan value was up to 80% and almost 2/3 of credit is collateralized by real estate.

The liquidity position of the banking sector is assessed as satisfactory. The liquidity indicators, both in lek and in foreign currency, remained significantly above the minimum regulatory ratios. The ratio of liquid assets to total assets of the banks' balance sheet remains high. Liquid assets of the banking system grew by ALL 40 billion, standing at ALL 550 billion. At the end of 2020, its value was 34.9%, and it increased by 1.6 p.p. during the period. The ratio of liquid assets to short-term liabilities increased by 1.4 p.p., standing at 47.5%. Deposits, as the main source of funding bank activity, cover twice the volume of loans of this sector. At the end of 2020, the "loans/deposits" ratio stood at 47.3%, slightly downwards during the period. At year-end, the values of this ratio were 47.6% for Albanian lek and 47.1% for foreign currency. Despite some small changes over the period, these ratios decreased significantly compared with one year before, due to a sharp growth of deposits in 2020.

Although banks are operating under ample liquidity conditions, the negative gap between assets and liabilities by residual contractual maturity segment, as a ratio to total short-term assets, remains at high levels. The negative gap between short-term assets and liabilities by residual contractual maturity segments for the period up to 3 months narrowed from 24% to 22% of assets.

During the period, an increase was observed in the average maturity mismatch between assets and liabilities, due to an increase of the average maturity of assets. At the end of the year, this mismatch was around 24 months, from 23.1 months in the previous six months. Deposits' residual maturity, which represents the most significant category of liabilities, remained almost unchanged at 7.7 months. The residual credit maturity increased significantly, from 45.7 months to 50.1 months, reflecting the banks' propensity to grant credit for longer-term periods. Similar to the previous six months, the banking sector did not report the use of funding lines by parent groups.

Market risks did not show significant changes during the period. At the end of 2020, the ratio of open foreign currency position to the regulatory capital of

the banking sector was 8.4%, from 5.3% at the end of the first half of the year. The performance has been dictated by the group of systemic banks, which have maintained a long open position. The exposure of the banking sector to the indirect exchange rate risk slightly decreased compared to the previous six months and to the previous year. The foreign currency mismatch index for all currencies declined. The exposure of the banking sector to interest rate risk has decreased. The weighed total net position in the banks' balance sheet against regulatory capital of the banking sector stood at 4.4% at the end of the year, down by 1.6 p.p. from the previous year. The weighted spread of assets with fixed interest rate liabilities (FIR) provided the main contribution to the decrease of this indicator, while the net position on variable interest rate (VIR) assets and liabilities slightly decreased. Given that the total net position is positive, the sector has relative exposure to a further decrease in interest rates. Currently, the room available for further decrease is limited and its effect on the financial result of the banking sector is assessed as insignificant. Regulatory capital coverage of the total net position of the banking sector is 25 times, whereas 5 times is the coverage provided for in the regulatory framework.

To assess the banking sector's resilience against the real economy or financial markets shocks in the medium-term horizon, the Bank of Albania carries out regular stress testing exercises.

Stress tests on capital adequacy show individual banks' degree of resilience in terms of capital and aims to identify its adequacy to withstand assumed shocks on economic growth, credit, exchange rate levels and interest rates. Stress tests on liquidity show the ability of banks to withstand a shortfall in liquidity capacity by selling liquid assets in a stressed market.

Overall, the stress-testing exercises carried out at the end of 2020 and spanning over 2021-2022 period, show that the banking sector appears resilient to the possible macroeconomic and liquidity shocks.

In conclusion, the Bank of Albania assesses that the financial system and the banking sector were able to withstand the economic shocks caused by the Covid-19 pandemic. The good financial conditions prior to the pandemic and the measures undertaken by public authorities helped to mitigate the shock and control the risks. Nevertheless, the uncertainties related to the pandemic remain present as the effect of supportive measures will eventually end. As a result, banks may face increased pressures in relation to the quality of credit portfolio. Based on these explanations, it is indispensable to actively monitor the solvency of borrowing clients and create the relevant funds in a timely manner. In parallel, it is necessary to assess the capital positions with a view to preserving adequate levels, in compliance with the assessed risks and the regulatory framework.

1. OVERVIEW OF THE MAIN RISKS TO FINANCIAL STABILITY

1.1 FINANCIAL STABILITY MAP

As at end of 2020 H2, data in the Financial Stability Map show, overall, increased levels of risk in the overall macroeconomic environment and in the activity of real economy agents. The risks related to the activity of the banking sector remain at contained levels, despite the unusual situation of the past year. In more concrete terms:

The Financial Stability Map shows, overall, increased levels of risk in the overall macroeconomic environment and in the activity of the real economy agents.

Risks related to the activity of the banking sector remain at contained levels, despite the unusual situation of the past year.

A. Overall economic environment:

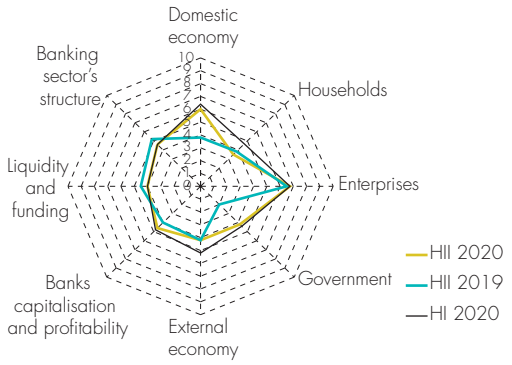
I. Risk from the "domestic economy" is rated as "moderate "and worsened over a one-year period. This was mainly driven by the expansion of the output gap and an increase in the size of the external debt.
II. Risk from the "external environment" remains at "average rate." This risk continues to primarily reflect the deep recession in the economies of our key trading partners and a decrease in the OECD-CLI[4] index, affected by the SARS-CoV-2 pandemic. The mitigation of this risk was mainly driven by the fall of both short-term financing rates and oil prices in international markets.

B. The main real economy sectors show the following:

I. Risk from "enterprises" is assessed as "moderate," maintaining the level of the previous year. In this category, notwithstanding the slight improvement in the quality of the credit portfolio to enterprises and the higher share of borrowing, the sub-indicator "financial position" and "private sector's expectations" appear deteriorated.
II. Risk from "households" continues to be assessed as "average," and it maintains the level of the previous year. The rate of this category was maintained by an increase in households' borrowing share, a rising pace of remittances and developments in the housing market, which have balanced the deterioration in their credit portfolio quality.
III. Risk from the "Government" is assessed as "average," but the rate of this category increased over the period. The main contributors to this development are the expansion of public debt; a significant increase of budget deficit; and the unstable performance of tax revenues.

[4] *OECD-CLI index (Composite Leading Indicator) gives early warning signals on the turning points of the business cycle at a global level. When the index falls, it signals a decrease in the long-term potential level of economic activity.*

Chart 1 Financial Stability Map



*Risk is assessed as: low for scores 0-3 in the map, average for scores 4-5, moderate for scores 6-8 and high for scores 9-10. The closer to the center, the lower the riks.

Source: Bank of Albania.

C. At the end of the period, the banking sector activity shows the following:

I. Risk from "capitalisation and profitability" continues to be assessed as "average," but it showed an upward trend over the last year, driven mainly by a fall in the interest income of the banking sector.

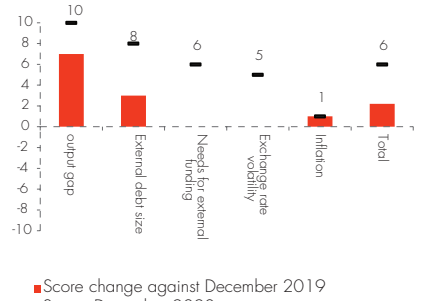
II. Risk from "liquidity and funding" continues to be assessed as "average," lower than a year earlier, reflecting an increase in households' deposits and low support from external funding sources.

III. The risk associated with the "banking sector structure" is assessed as "average," maintaining the level of the previous year. In this category, an increase in the level of risk, as a result of the increase of concentration in bank credit to enterprises, is balanced by a decrease in risk related to other indicators such as the indicator of deviation of the Capital Adequacy Ratio (CAR) value of the banking sector; the indicator of the market share of two major banks; and the indicator of concentration of the banking sector's funding sources.

BOX 1.1 FINANCIAL STABILITY MAP COMPONENTS

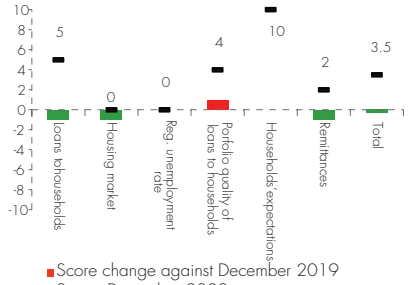
Risk from the "domestic economy" is assessed as "moderate" and rising during the year, due to the expansion of the output gap, an increase in the external debt stock and the performance of the inflation rate, which contributed to the raised risk rate. The need for external financing and exchange rate fluctuations maintained an unchanged level of risk.

DOMESTIC ECONOMY - DECEMBER 2020



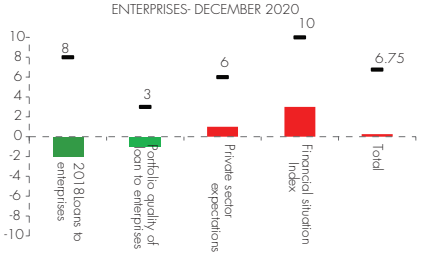
Risk from "households" is assessed as "average" and unchanged from a year earlier. The increase in households' borrowing share relative to GDP, the rising pace of remittances and developments in the housing market maintained the same risk level in this category, balancing deterioration in households' credit portfolio quality.

HOUSEHOLDS- DECEMBER 2020



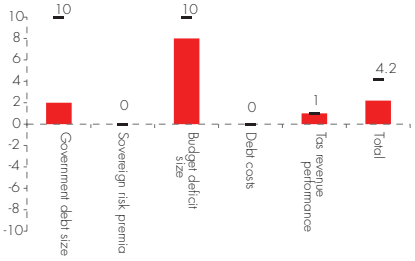
Risk from "enterprises" is rated as "moderate" without any change during the period. However, in this category an increase has been observed in the borrowing level of enterprises in relation to GDP as well as an improvement in the credit portfolio quality, while the financial situation index and the expectations of the private sector deteriorated compared with the previous year.

ENTERPRISES- DECEMBER 2020



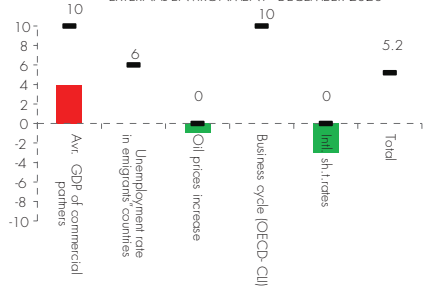
Risk from the "government" is assessed as "average," but trending upward over a one year period. The increased risk level is attributed to a considerable increase of budget deficit, an increase of public debt to GDP, and deterioration in the performance of tax revenues.

GOVERNMENT- DECEMBER 2020



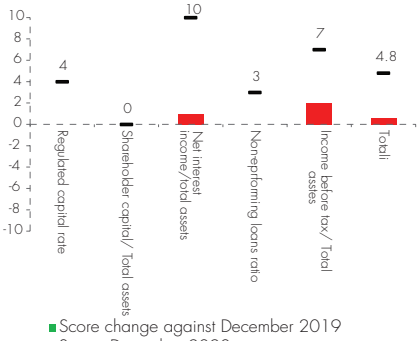
Risk from the "external environment" is rated "average". The significant increase in risk level is related to the economic slowdown of our trading partners and the business cycle deviation, affected by the global pandemic and the restrictive measures to put it under control, is somewhat mitigated from the fall in oil prices and the performance of the short-term funding rates in international markets.

EXTERNAL ENVIRONMENT - DECEMBER 2020



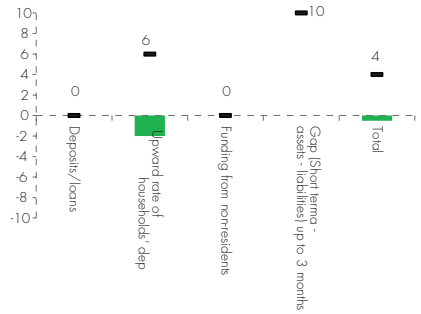
Risk from "funding and liquidity" continued to remain "average" and falling in annual terms, due to an increase of financing by non-residents. On the other hand, the risk related to a short-term assets and liabilities gap, up to three months, continues to remain wide and has not changed over the year.

CAPITAL AND PROFITABILITY - DECEMBER 2020



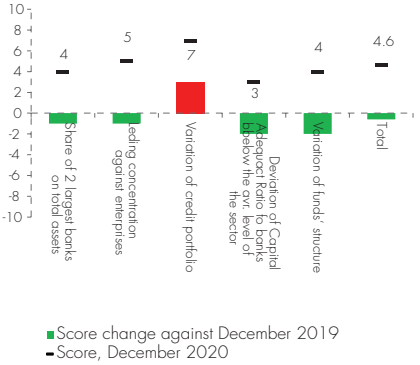
The level of risk from "capital and profitability" is assessed as "average," but trending slightly upward compared with one year earlier, due to the fall of the banking sector's revenues throughout last year against further expansion of assets.

FUNDING AND LIQUIDITY - DECEMBER 2020



Risk from the "banking sector structure" remains "average" but decreasing during the period. The indicator of credit portfolio fluctuations shows an increase in the banking sector's concentration of lending, while the positive performance of all the other sub-indicators has contributed to mitigating the overall risk level of this dimension.

BANKING SECTOR'S STRUCTURE - DECEMBER 2020



Source: Financial Stability Department, Bank of Albania.

1.2 SYSTEMIC RISK

The fall of unemployment and inflation and the stability of the exchange rate helped to mitigate systemic risk and financial stress. Meanwhile, the increase of accumulated risk is mainly related to the increase in public and private debt.
The banking sector perceives the deterioration of the economy and the possibility of a lower credit quality as the main increasing risks.

In order to assess and monitor the exposure of the banking sector to systemic risk, the Bank of Albania considers three aggregate indicators that reflect the accumulation and materialisation of systemic risk and the scale of financial stress, as well as a survey on banking sector perceptions regarding such risks[5]. Over the period, factors such as the performance of private and public debt, the increase of uncertainty in economic progress and borrower's solvency to serve loans, the performance of prices in the real estate market and the external economic environment, adversely affected the performance of indicators that reflect risk accumulation. On the other hand, a fall in the unemployment rate, the performance of inflation and the exchange rate, the good performance of the banking sector and the measures undertaken by the government to mitigate the effects of the pandemic on economic activity, helped to mitigate the materialised risk and the banking sector's perception of the level of systemic risk in the domestic economy.

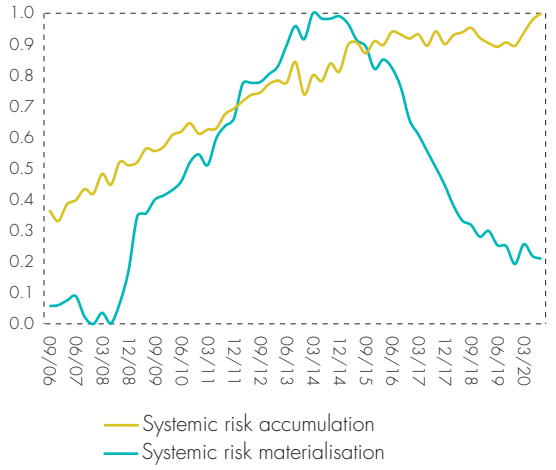
1.2.1 DEVELOPMENTS IN THE INDICES OF SYSTEMIC RISK

Over the period, the accumulation index and the materialisation index of systemic risk moved in opposite directions. The accumulation index of systemic risk increased due to the expansion of public debt and private sector debt, as well as the increase of real estate prices. The materialisation index fell due to positive developments in some macroeconomic factors such as a fall in unemployment, low inflation and a stronger exchange rate for Albanian lek. Given the method of construction and the phenomena that each risk indicator aims to reach, there is the possibility that the materialisation index will "withdraw" to an upward trend, following the accumulation index of systemic risk.

The financial stress index fell at the end of the period, despite its increase in 2020 Q3. The performance of this index mainly reflected the expansion of a deposit base gap, credit surplus and the net interest margin on their long-term trend. The money market effect remains unchanged, while the appreciation of the Albanian lek relative to main currencies lowered the level of stress during the period.

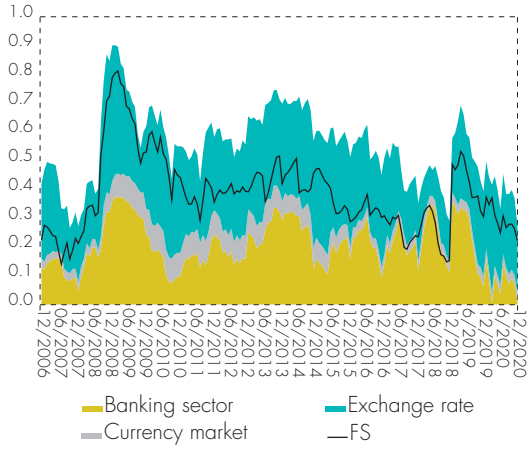
[5] *Banking sector perception related to main systemic risks in Albania is attained through an ad hoc survey.*

Chart 2 Accumulation and materialisation indices of systemic risk



Source: Bank of Albania.

Chart 3 Financial Stress Index



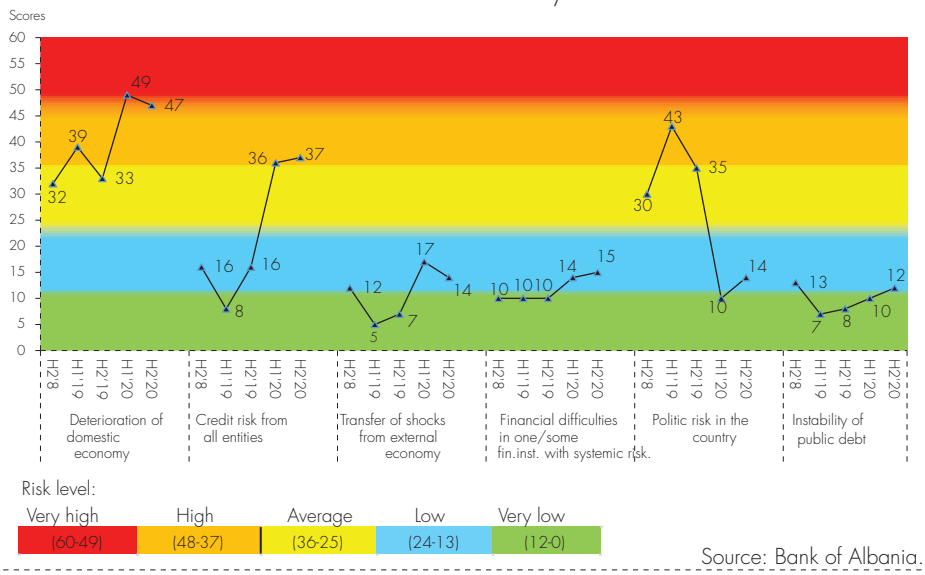
Source: Bank of Albania.

1.2.2 PERCEPTION OF THE BANKING SECTOR ON SYSTEMIC RISK

Survey results on the perception of the banking sector regarding systemic risk in Albania, continue to show "deterioration of the domestic economy" as the main risk, under the direct impact of the pandemic and the uncertainty surrounding it. "Credit risk from all categories of clients" continued to increase over the period due to banks' assessment of the deterioration of the financial situation of enterprises and households. A more pessimistic perception of clients' solvency increased the overall concern of the sector concerning "the financial performance of systemically important institutions." The global scale of the pandemic and the extension of movement restrictions between countries, which adversely affected, in particular, the tourism industry, international transportation and trade, increased the banks' perception in relation to "external shock risk" and the subsequent economic consequences.

Over 2020, banks made higher assessments on several new risks related to the pandemic such as "operational risk" and "cyber risk." These risks are related to the intensification and expansion in the use of technology to reach their objectives. In addition to the abovementioned risks, the banking sector shows increasing concerns regarding this year's parliamentary elections and the future political developments in Albania.

Chart 4 Bank's assessment on the main systemic risks in Albania



Source: Bank of Albania.

Regardless of banks' perception on the increased systemic risk in Albania, their trust in the stability of the financial system remained at good levels during the period. Banks' trust is based on good financial operational indicators and the measures undertaken by public authorities to mitigate the financial consequences of the pandemic. According to them, despite the challenges that characterised the domestic and external environment over 2020, the financial system in Albania continued to remain liquid and well-capitalised, and consequently, able to carry out its activity.

2. MACROECONOMIC AND SECTORIAL DEVELOPMENTS

2.1 INTERNATIONAL ECONOMIC AND FINANCIAL DEVELOPMENTS

Global and Euro area economic activity recovered in 2020 Q3, but it still remains weak due to the reconstitution of restrictions related to the Covid-19 pandemic at the end of the year. Financial conditions remain favourable and many countries continued to support the economy with special fiscal packages. Similar developments were noted in the Euro area and the Western Balkans. Under the supposition that the acceleration of vaccination will put the pandemic situation under control, the global economy is expected to embark on the road to recovery during 2021 H2.

Global economic activity continued to remain under the pressure of the Covid–19 pandemic during the period, regardless of the positive recovery signals. After the gradual opening of many countries and the removal of restrictive measures in May-June 2020, economic activity recovered considerably, manifested in particular in trade and consumption, driven by public financial packages in the form of financial transfers and fiscal and monetary easing. Normalisation of economic activity in China and the continuation of economic growth in the US, favoured by the early removal of restrictive measures, an increase in external demand and broad support from the public sector, provided an important contribution to global economic performance in this stage. At the end of 2020 Q3, the pandemic situation worsened once again due to the circulation of new coronavirus variants and an increase in the number of infections in most countries. As a result, many countries were forced to re-implement strong restrictive measures (even full quarantine), slowing down recovery of economic activity in the last quarter of the year. In spite of fluctuating developments in the real sector, financial market conditions in advanced regions and in some emerging ones, remain favourable. The performance of indicators in the securities markets was stable, while the normalisation of capital flows led to the fall of long-term yields and the narrowing of corporate obligations spreads and sovereign debt securities. It is worth emphasizing that the engagement of central banks and other monetary authorities across the world through further release of monetary policies, activation of quantitative easing programmes, and easing of macroprudential policies, has played a key role in maintaining trust and preventing escalation of the crises in the financial system.

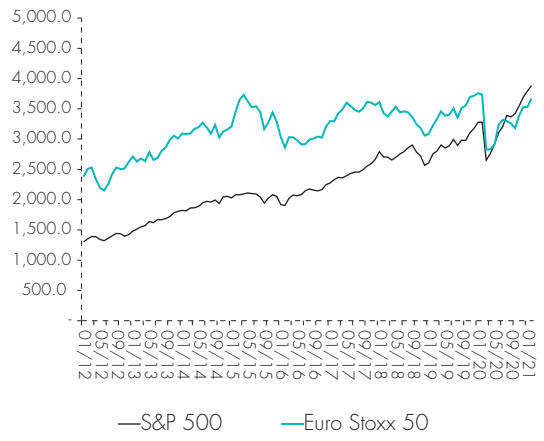
Given the volatility of global economic activity and weak demand, inflationary pressures remained contained. Inflation remained down at pre-pandemic levels in advanced regions, while it fell more considerably in emerging regions. Notwithstanding the upward trend in commodity prices and in some specific goods (such as medical and pharmaceutical equipment), inflationary pressures are expected to remain low, affected by the high level of free production capacities in most countries.

In the foreign exchange markets, the Euro appreciated against the major currencies during the May-September 2020 period, reflecting the positive trends of the markets after the economic revival of the Euro area. During the latter months of 2020, the Euro depreciated against the majority of currencies

of important trade partners, mainly against the British pound (by 2.8%). This also reflected the reaction of the market in relation to the EU-United Kingdom agreement concerning Brexit, and the increased uncertainties of economic performance of the Euro area.

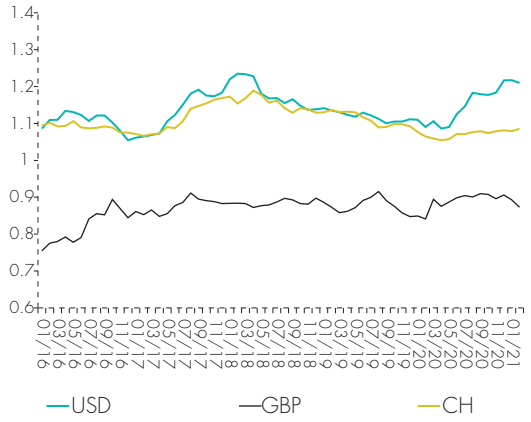
In commodities markets, oil prices went up during 2021 H2, driven by the recovery of global demand following the removal of restrictions, while the supply of producing countries was inadequate and oftentimes decreasing. Metal and food commodity prices were affected by the upward demand of emerging economies (particularly China) and public measures to support consumption. Prices in these markets are expected to rise during 2021, in line with the global recovery and the growth of demand, but will nevertheless remain under the 2019 average.

Chart 5 Main indices in shares market



Source: European Central Bank.

Chart 6 Euro exchange rates against other currencies



Source: European Central Bank.

Given the easing of restrictive measures and the restart of economic activity in the affected sectors, the global economy is expected to embark on the road to recovery during 2021 H2[6], supported by the continuation of aid programmes and the favourable conditions of financial markets. The eventual acceleration of the vaccination process and the possibility of improved medical therapies for treating Covid-19 restored hopes of bringing the pandemic under control and normalising the situation. Nevertheless, expectations carry a high level of insecurity and the speed of recovery is expected to differ from region to region, depending on structural characteristics, the performance of the vaccination campaign and the efficiency of supporting policies.

[6] *The IMF forecasts that the global economy will expand by 5.5% in 2021 and by 4.2% in 2022. (January forecasts, 2021, World Economic Outlook, update)*

EURO AREA

Following a historical economic contraction at the beginning of the year, under the restrictions of the pandemic, the economy of the Euro area recorded a considerable positive growth in the third quarter (+12.4% in quarterly terms and -4.3% in annual terms), underpinned by growth in domestic demand and the revitalisation of external trade. The last quarter of the year provided another view, since the acceleration of infections was accompanied by the re-implementation of restrictions in some Member states and increasing stress on economic developments. The economic decline mostly affected the services sector, which continues to remain the worst hit sector, while production activity showed a slight improvement.

Developments in the labour market were positively affected by the supportive effect of governments' schemes to safeguard jobs and to continue financial compensation. The unemployment rate in the Euro area was stable, trending downward at the end of 2020. Nevertheless, the unemployment rate remained lower than the pre-pandemic level. Inflationary pressures in the Euro area were quite low over the period, driven by a decrease in demand and a weaker labour and production market. Inflation remained in negative territory in 2020 H2, stabilising at -0.3% over the last three months. Against this backdrop, the European Central Bank continued its commitment to maintain an accommodative monetary stance to support the financial sector and the economy with liquidity, through quantitative easing actions.

In the medium run, economic recovery of the Euro area is expected to be widely underpinned by favourable financial conditions, the expansionary stance of fiscal policy and the strengthening of domestic demand, after the restrictive measures have been lifted and the uncertainty eased. However, forecasts are conditioned by the future dynamics of the pandemic and the performance of the vaccination campaign, officially launched in December 2020.

In the banking sector, lending growth to the private sector stood at 4.7% during the period, underpinned by favourable financing conditions and historically low interest rates. Nevertheless, survey results on bank lending in the Euro area show a constriction of lending conditions during 2020 Q4, mainly as a result of higher uncertainty on economic performance in the region, given the pressure of a new wave of the pandemic and tougher restrictions.

Table 1 Selected macroeconomic indicators for the U.S. and Euro area

	GDP changes (annual %)			Inflation (annual %)		Unemployment (annual %)		Government debt (% GDP)	
	Q3'20	Q4'20	2020p	Sept'20	Dec'20	Sept'20	Dec'20	Q2'20	Q3'20
USA	-2.8	-2.5	5.1			7.8	6.7		
Euro area	-4.2	-4.9	4.2	-0.3	-0.3	8.6	8.1	95.0	97.3
Germany	-4.0	-3.6	3.5	-0.4	-0.7	4.5	4.6	67.4	70.0
France	-3.7	-4.9	5.5	0.0	0.0	8.8	7.8	114.0	116.5
Italy	-5.2	-6.6	3.0	-1.0	-0.3	9.5	9.0	149.3	154.2
Greece	-10.5	-7.9	:	-2.3	-2.4	16.7	16.2	191.4	199.9

Source: European Central Bank, Eurostat, f-Forecast for January 2021 by the International Monetary Fund, Bureau of Economic Analysis (BEA). U.S. Bureau of Labour Statistics; ": ": no available data.

WESTERN BALKANS

The Western Balkans region continued to suffer the effects of the global pandemic crises, but with a lower intensity during 2020 Q3 due to the mitigation of the restrictive measures. GDP contracted by 4.5% in annual terms on the regional level in 2020 Q3 compared with 9.3% decrease in 2020 Q2, driven by a rebound in investments in some of the countries and a lighter fall in consumption and exports. Balance of payments pressures continued to increase considerably over the entire year, as a result of a considerable fall in inflows from tourism and remittances in some countries.

Contraction of the economies of the countries in the region continued to reflect a deterioration of labour market conditions and a fall in employment, albeit at a slower pace over 2020 Q3 compared with the previous quarter. The unemployment rate remained stable overall, also driven by the measures undertaken to safeguard job positions. The expansion of fiscal stimuli to mitigate the adverse effects of the pandemic on households and enterprises together with a general decrease in fiscal revenues, led to the further expansion of budget deficit and public debt in all the countries of the region.

Amidst the contraction of economic activity, inflationary pressures remained weak during the second half of the year. Nevertheless, inflation dynamics were different in November-December 2020, when rates increased for North Macedonia and decreased for Serbia, Montenegro and Kosovo. In these circumstances, monetary policies remained accommodative, supporting economic recovery and lending.

Table 2 Key macroeconomic and financial indicators for the Western Balkan countries

	GDP (real, annual %)				Unemployment (in %)		Credit growth (annual %)		Non-performing loan ratio (in %)	
	Q2'20	Q3'20	2020p	2021p	Q2'20	Q3'20	Q3'20	Q4'20*	Q3'20	Q4'20*
Bosnia and Hercegovina	-9.3	-6.3	:	:	16.0	:	0.4	-1.2	6.6	:
North Macedonia	-14.9	-3.3	3.8	3.5	16.7	16.5	7.5	5.5	3.3	:
Montenegro	-20.3	-26.9	6.8	3.7	15.7	19.6	5.7	5.0	5.6	5.9
Kosovo	-9.3	-7.3	:	:	27.2	24.6	7.1	6.9	2.5	2.5
Serbia	-6.3	-1.4	4.8	3.8	7.3	9.0	15.1	13.4	3.3	:
Albania**	-3.5	2.99	3.3	4.6	11.6	11.8	5.2	6.7	8.3	8.1

Source: Source: European Commission, respective central banks. f- Forecast for January, 2021; ':' no available information; "": data refer to November 2020 (with the exception of Albania where the data is from December 2020) "**": data refer to 2020 Q4.*

Bank credit growth continued to be positive, driven by monetary easing, the support of fiscal packages to decrease credit risk and other supportive policies provided by central banks. Banks' balance sheets improved during the period and the non-performing loans ratio was lower compared with the previous year. This indicator was affected by the extension of measures on the temporary suspension of credit classification, thus, the full impact of the pandemic on the financial system is not yet reflected.

2.2 MACROECONOMIC ENVIRONMENT IN ALBANIA

Although prior data show that in the last quarter of the year economic activity in Albania contracted by around 3.31% in 2020, there was a recovery. This recovery, which showed its first signs at the end of the third quarter, culminated in an annual economic growth of 2.99% at the end of December 2020. GDP growth during 2020 Q4 was driven by an increase in private consumption and investments, as well as a higher volume of trade exchanges in goods and services. During the fourth quarter, considerable annual growth was registered in the sectors of construction, financial activities and security, and information services. Meanwhile, the energy extraction, processing and production sector registered a production hike in annual terms. The production of agricultural and trade sectors fell in annual terms. Gross domestic product grew by 1.15% compared with the previous quarter. Analysis by production of sectors of goods and services showed that, with the exception of a decrease registered in "agriculture, forests and fishery," all other branches of the economy registered an increase during the last quarter of the year, which was particularly high in the branches of "industry, energy and water" (9.9%), "financial and security activities" (9.1%) and "trade, transport and hotels" (7.4%). In the labour market, the number of employed and unemployed did not experience strong fluctuations, while the unemployment rate in the fourth quarter stood at 11.8% from 11.6% in the third quarter of the year.

The domestic economy contracted in 2020, but showed positive signs in 2020 Q3 and in particular in Q4, thanks to an increase in private consumption and the expansion of investments and foreign trade. The contribution of the external sector of the economy was negative due to the expansion of the current account deficit in the balance of payments, to around 2% in annual terms, amounting to EUR 350 million. This performance was driven by the expansion of trade deficit for goods and the negative balance of primary income.

On the other hand, the external sector contribution to the economy was negative due to the expansion of the current account deficit in the balance of payments

by about 2% in annual terms, at EUR 352 million. This performance was driven by the expansion of trade deficit in goods and the negative balance of primary income. The trade of services registered a positive balance expansion by about 11% in annual terms, driven by the expansion of surplus in travel services and other business services. Foreign exchange assets in the form of remittances are estimated at around EUR 203 million, with an annual term of 12%. Meanwhile, the flow of direct foreign investments is estimated at EUR 257 million, with an annual decrease of around 10%. At the end of the period, foreign reserve assets covered 9.6 months of average imports in goods and services.

Fiscal deficit and public debt expanded considerably due to a fall in revenues, an increase in expenditures and the issuance of sovereign guarantees.

Fiscal policy played an active role in facing the shocks to the economy during the previous year, firstly due to the consequences of the November 2019 earthquake and secondly due to the pandemic situation. The measures undertaken include postponing of tax obligations, issuance of sovereign guarantees to continue employees' income and to mitigate credit risk to borrowers, an increase in public expenditures concentrated on the reconstruction of objects damaged in the earthquake and meeting public health needs during the pandemic situation. As a result, in a fashion similar to that seen in other countries, fiscal deficit and public debt registered a rapid increase throughout 2020. It is estimated that by the end of 2020, the budget deficit had increased by around 7% of GDP (or around ALL 110 billion) and public debt by about 80% of GDP by the end of the period. The budget deficit was mainly financed by both foreign and internal borrowing.

The pandemic remains present and its effects are marked by uncertainties in economic development. Should the process of vaccination accelerate and be effective, as expected, the impact of the pandemic on economic developments will decrease. This will have a positive effect on economic growth if all other factors are unchanged. Nevertheless, the speed of the process will be determined by developments in other foreign countries which are partners in trade and services. It is necessary for public economic policies to remain stimulating and to adapt to economic growth trends until trust in exiting the pandemic is accounted for in full by economic entities and private consumption and investments recover in a sustainable manner. As regards fiscal policy in the shorter-term period, importance is put on the efficiency of utilising fiscal stimulus and its financing. While, in the longer-time period, it is necessary to remain engaged and take measures for fiscal consolidation. The latter is necessary to mitigate the risks related to high debt levels and its content.

2.3 FINANCIAL POSITION OF HOUSEHOLDS AND ENTERPRISES

In 2020 Q2 households registered a further expansion of their net creditor position and simultaneously, the debtor position of enterprises continued to

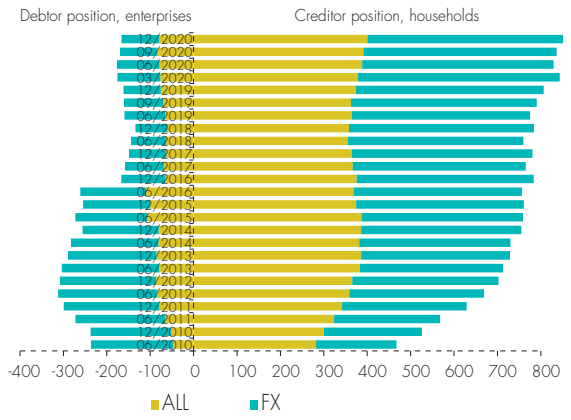
narrow. For both groups, the main contribution was the significant growth of deposits in banks. Households recorded a simultaneous growth of deposits base and outstanding loans, with the main contribution from domestic currency. For households, banks reported an expansion of deposits by around ALL 30 billion and credit by around ALL 6 billion. For enterprises, growth of around ALL 15 billion of loans, mainly in ALL, was accompanied by an ALL 25 billion growth of deposits, mainly in foreign currency. In annual terms, this position reflects an expansion of around ALL 5 billion, with a contribution almost entirely from domestic currency. As a result, at the end of December 2020, creditor position of households was up at around ALL 850 billion, while debtor position of enterprises contracted by around ALL 166 billion.

2.3.1 HOUSEHOLDS' FINANCIAL AND BORROWING SITUATION

Resident households increased their savings by around ALL 25 billion during the period. This increase, mainly in the form of deposits in lek and foreign currency, was at similar levels to the previous six months (at ALL 24 billion). Foreign exchange and lek deposits continue to maintain equal shares in deposits stock held by resident households. At the same time, households' investments in Government short-term securities declined, while investments in private pension funds and investment funds increased, expanding their share in the total households' investment portfolio.

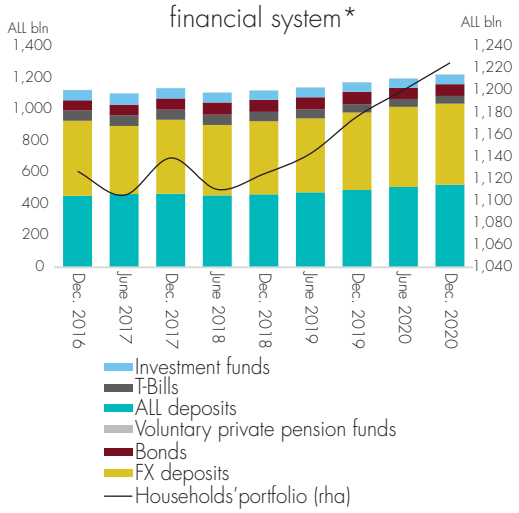
In 2020 H2, households' savings increased and their creditor position expanded, driven mainly by deposits growth in lek and foreign currency.

Chart 7 Financial sectorial position (in ALL billion)



Source: Bank of Albania.

Chart 8 Resident households' activities in the financial system*



Source: Source: Bank of Albania and AFSA.

**Values for investment and private pension funds belong to Q3-2020.*

Households' solvency has slightly improved compared to 2020 H1, but it appears weaker than in the previous year. Households' credit demand may be higher during 2021 H1.

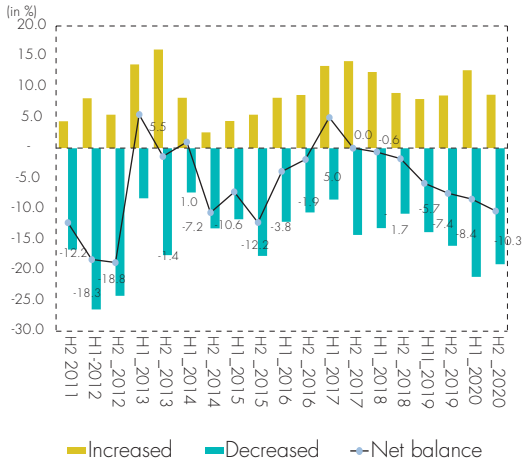
The periodical survey was conducted with a sample of 1210 households[7] in order to assess the performance of net households' assets in relation to their debt burden. The response scale to the survey was 88%. Around 24% of interviewed households state that they had at least one debt to repay at the moment of the interview. This share has slightly increased compared to the previous six months and to the previous year, but it remains below the historical average for this indicator.

Households' solvency was weaker during the period. Around 58% of borrowing households declared that their solvency "has not changed" during 2020 H2, and this share increased by 3 percentage points compared to the previous six months. The rest of the interviewees reported a decline in their solvency, reflecting the deterioration of their financial situation due to the Covid-19 pandemic. This is also reflected in the negative expectations of households in relation to their future solvency, which appear to have sharpened in comparison with the preceding survey. Therefore, 72% of borrowing households do not expect their solvency to change in 2021 H1. This rate increased by 6 percentage points compared to the preceding survey, while the net balance of the rest of responses was -10.3 percentage points, resulting in a decrease of the overall assessment.

Chart 9 Solvency in the previous six months

Source: Bank of Albania.

Chard 10 Solvency expectation in the following six months.



Source: Bank of Albania.

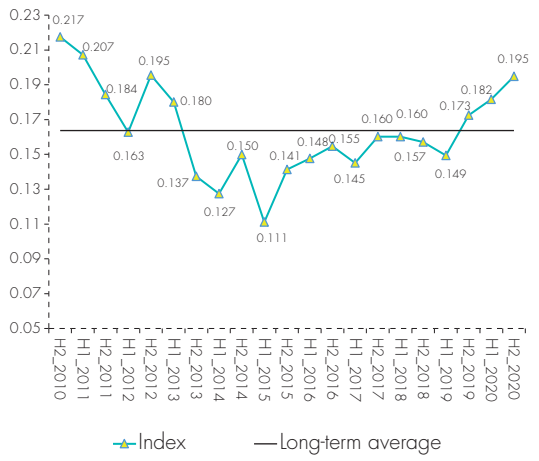
Households' credit demand during 2021 H1 may be higher. Around 57% of responding households declared that they do not plan to borrow in the next six months. Meanwhile 43% or 460 households declared that they are considering, at different safety scales[8], the possibility of borrowing/re-borrowing. This share has slightly increased compared to the previous six months and has gone up by 3.3 percentage points compared to the previous year. As e result, "the new

[7] *The sample is selected and periodically reviewed by the Institute of Statistics based on the registrars used by the agency for households' questionnaires.*

[8] *The given alternatives are: "less likely", "very likely, "and "certain."*

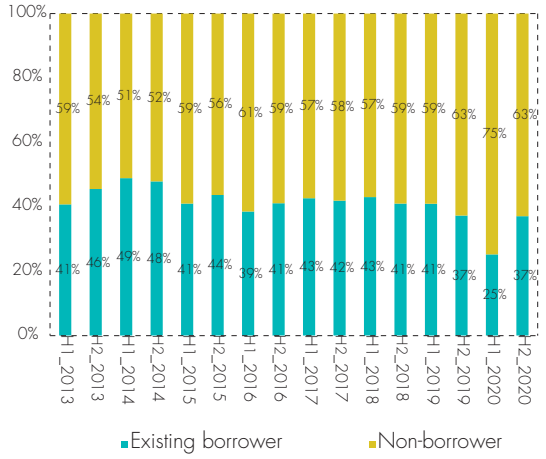
borrowing planning/rollover index" stands at 0.195, moving upward from the two previous surveys and surpassing its long-term average. In the group of households planning to take a new loan, around 63% of them are "new borrowers," meaning they did not have any debt to repay at the moment of interview. This share has declined by 12 percentage points in semi-annual terms, but it is at the same level in annual terms.

Chart 11 New borrowing planning/rollover index in the following six months



Source: Bank of Albania.

Chart 12 Households planning to borrow in the next six months



Source: Bank of Albania.

2.3.2 ENTERPRISES' FINANCIAL AND BORROWING SITUATION

A special periodical survey conducted by the Institute of Statistics is used to assess the financial and borrowing situation of enterprises. This survey was conducted on a sample of around 1374 enterprises of various sizes, geographically located in various regions of the country and operating in the main sectors of the economy. 82% of total enterprises participated in the survey by fully or partially answering the questions of the survey.

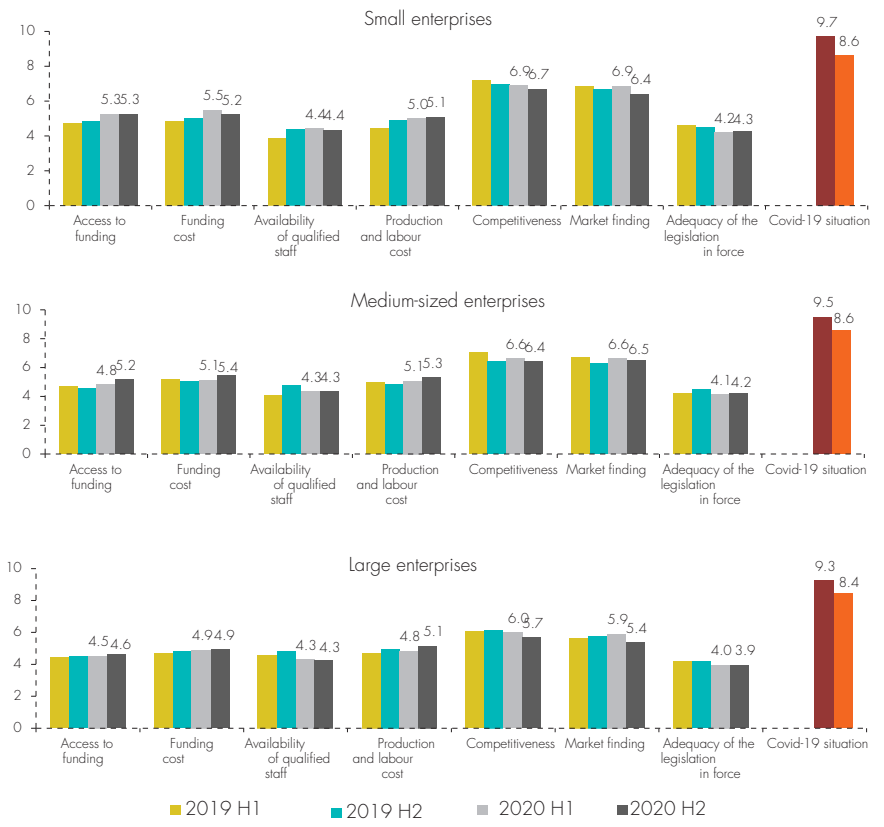
During the period, it is assessed that the highest impact on enterprises was the "situation created by the pandemic[9]" which has put a burden on other issues that they are facing. Enterprises report that "competition" and "finding a market" continue to remain challenging to their activity. The significance of the competition factor appears to be lower compared with the previous period across all three groups of enterprises, as is the challenge of finding a market. "Financial access," "financial cost" and "cost of production and labour" are some of the other important elements of operation, which have increased during the period, particularly for medium-sized and large enterprises.

For most enterprises, the situation created by the pandemic continued to be the main factor affecting their activity during 2020 H2, as well.

Medium-sized and large enterprises reported a better sales performance and financial situation compared to the previous six months, and they did not report changes to the cost of debt. Small enterprises, on the other hand, reported weak sales, pessimistic expectations and increases to the cost of debt during the period.

[9] *This issue is specified under the "Other" alternative and was indicated by 19% of the sample of responding enterprises. In 2020 H1, this issue was specific for 37% of the responding sample.*

Chart 13 The assessment of some factors on enterprise activity



Source: Bank of Albania.

Sales and financial results appear to have improved compared with 2020 H1, albeit all enterprises regardless of their size, continue to report lower sales than prior to the pandemic. Expectations on overall sales in the upcoming six months appear positive for large enterprises and slightly more optimistic for medium-sized enterprises. Meanwhile, small enterprises appear pessimistic for 2021 H1, expecting a further decline in the level of sales. Regarding the expansion of activity or increase of investments, small and medium-sized enterprises declare a contraction, while large enterprises report a slight expansion over the period. The evolution of the pandemic will significantly affect the decision-making of enterprises regarding investments or expansion of their activity. In regard to expectations for the following six months, large enterprises expressed optimism, albeit at a lower rate than the previous period, meanwhile small and medium-sized enterprises are pessimistic for the next period.

Half of the total enterprises declare that they have financed their activity through sales. Reliance on this source alone has increased for all three groups of enterprises, while the propensity to combine several sources of funding continued to have a considerable share during the period, but has fallen for all three groups of enterprises. Financing through the combination of sales with allocated reserves holds the main share. Around 40% of the total of responding

enterprises (466 enterprises) declares that they are currently indebted. This share increased by 2 percentage points compared with 2020 H1 and by 4 percentage points with the previous year.

Among the borrowing enterprises, around 73% of small enterprises, 84% of medium-sized enterprises and 83% of medium-sized ones consider their level of borrowing to fund the activity as adequate. Borrowing in lek totalled 55% for small enterprises, 50% for medium-sized enterprises and 46% for large enterprises, while the rest was in foreign currency and/or combined currency.

The total value of debt was approximately half of enterprises' equity, for around 80% of borrowing enterprises, and equal to the value of equity for 9% of them. The debt/equity ratio was higher for large and medium-sized enterprises, with 23% and 22% of them declaring that this ratio is equal or exceeds the value of equity, implying a higher debt burden. In 2020 H2, this ratio increased for small and medium-sized enterprises by 3 percentage points and 5 percentage points, respectively. By sector, debt burden continues to remain high for enterprises operating in services and in trade sectors.

Table 3 Share of enterprises whose debt value is equal or higher than equity, by sector

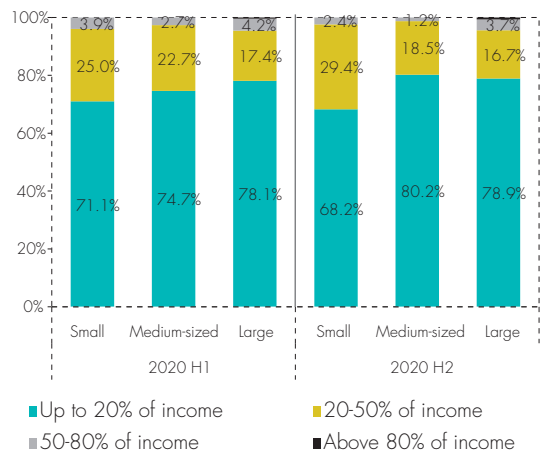
Share of industries with credit equal or higher than capital, by sectors				
	Industry	Services	Construction	Trade
2019 H1	26.8%	18.5%	18.3%	28.8%
2019 H2	20.4%	28.0%	13.4%	26.5%
2020 H1	16.4%	22.9%	19.7%	22.2%
2020 H2	19.7%	25.0%	17.6%	21.9%

Source: Bank of Albania.

Most borrowing enterprises (77%) declare that loan repayment amounts to 20% of revenue and this share has increased by 1 percentage points compared to the previous period. Debt payment seems to be more burdensome on small enterprises, with enterprises which report that it exceeds 20% of revenues accounting for 32% of the total of the group[10], while for medium-sized and large enterprises, this share accounts for 20% and 21%, respectively. Asked if the debt repayment has changed during the period, most (84%) of small enterprises, 89% of medium-sized enterprises and 87% of large ones) state that this repayment has not changed, while the rest resulted in net positive balances for all sizes of enterprises, showing an increase of this expenditure in relation to income. For small enterprises, this balance has increased for the third consecutive six months, showing their difficulty in debt repayment.

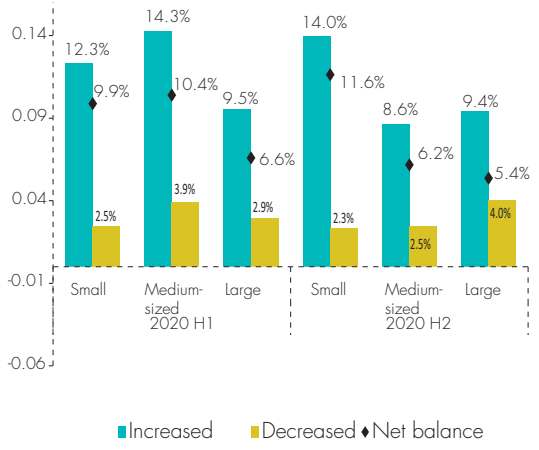
[10] *Calculated as the sum of weight for responses: "20-50% of total income","50-80% of total income" and "higher than 80% of total income".*

Chart 14 Enterprises by size and debt instalment/income ratio



Source: Bank of Albania.

Chart 15 Enterprises that declare a change in their debt instalment during the period



Source: Bank of Albania.

Enterprises' credit demand in the next six months, judging by their responses related to bank borrowing planning, has given upward signals, and though decision-making regarding this objective seems more uncertain. Banks' borrowing planning index in the next six months[11] remained unchanged for enterprises on the whole. This index appears higher for small and medium-sized enterprises compared with the previous period.

[11] *To assess the responses of the enterprises, it is constructed the credit planning index, calculated by weighting the share of responses of enterprises to the total of responses by a coefficient, which increases with the probability of lending. The coefficient for the alternative: "unlikely" = 0.25; "little unlikely" = 0.5; "very likely" = 0.75; "certain" = 1.*

3. MARKET AND PAYMENT SYSTEMS

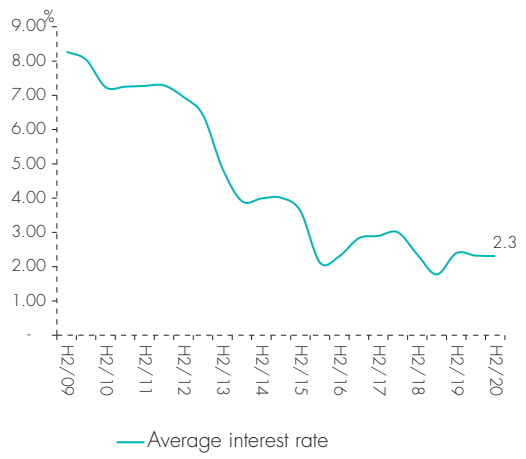
3.1 EQUITY AND FOREIGN EXCHANGE MARKET

PRIMARY MARKET OF SECURITIES

The issuance of government debt securities was lower compared to 2020 H1, while the average yield remained unchanged. A decline in the issuance of securities during the period was driven by a reduction in the issuance of short-term securities, while the issuance of long-term securities increased, but at a lower amount.

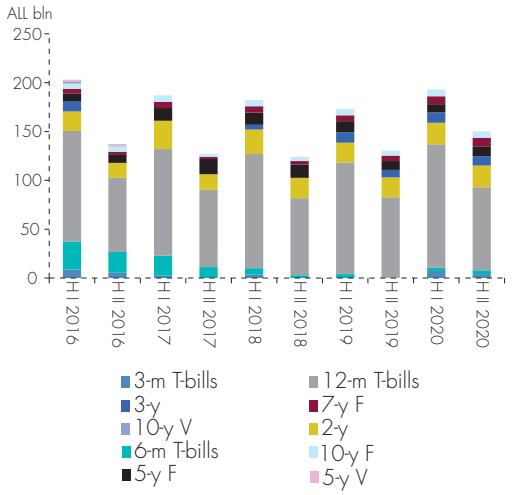
The primary market of securities is dominated by government debt securities. Securities issued in the second half of the year were entirely in lek and amounted to ALL 150 billion. Securities issued decreased by 22% or ALL 43 billion compared with 2020 H1, but increased by 15% or ALL 20 billion from the same period of the previous year. The average yield of debt in lek remained unchanged at 2.3%. The issued debt securities consisted of ALL 93 billion in bonds and ALL 57 billion in long-term debt securities. The structure of domestic debt continues to be dominated by the short-term debt, around 62% of the total. Nevertheless, this share has decreased by 9 percentage points from the level of 71% at which it stood at the end of 2020 H1.

Chart 16 Average yield on debt securities, in %



Source: Bank of Albania.

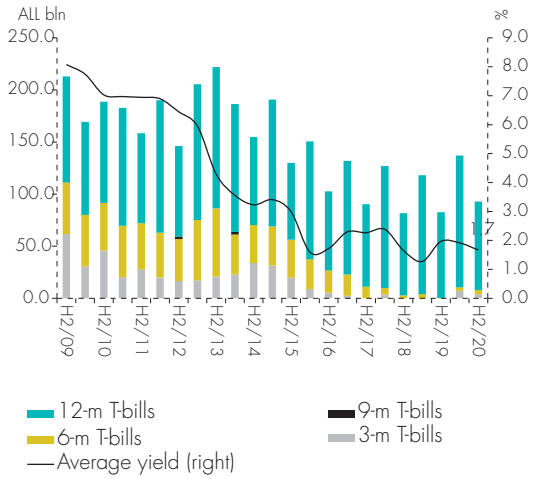
Chart 17 Composition of issued debt during 2016-2020 H1



Source: Bank of Albania.

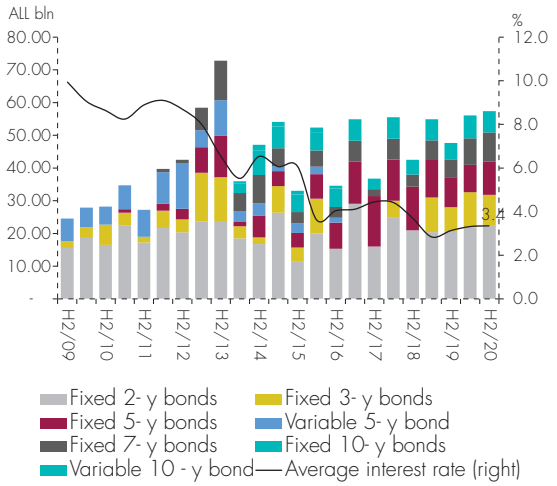
During the period, the issuance of 12-month Treasury bills decreased by 33%, 3-month T-bills fell by 44%, while 6-month T-bills increased by 15%. The short-term domestic debt is dominated by 12-month Treasury bills, albeit its current share of 91.5% decreased during 2020. The average yield on short-term securities declined by 0.3 percentage points in annual terms. Overall, the bid for investment in treasury bills was equal or higher than government's demand for borrowing.

Chart 18 Volume and weighted average yield on T-bills in the primary market



Source: Bank of Albania.

Chart 19 Volume and weighted average yield on bonds in the primary market



Source: Bank of Albania.

Long-term debt securities issued during the period were around 2%, or ALL 1 billion higher than in 2020 H1. The issuance was around 20% higher, or ALL 10 billion more compared with the same period of the previous year. Around 40% of the issued long-term debt securities had a 2-year maturity term, recording a slight increase from the volume issued in 2020 H1. Securities with 5-year maturity consist of 18% of the long-term debt, recording the highest increase in the securities of different maturities during the period, while 3- and 10-year maturity were lower. The average yield on long-term debt stood at 3.4%, remaining almost unchanged from 2020 H1, but somewhat higher than the 3.1% average registered during 2019 H2. Overall, investment bidding for long-term securities has exceeded government demand for borrowing.

SECONDARY MARKET OF SECURITIES

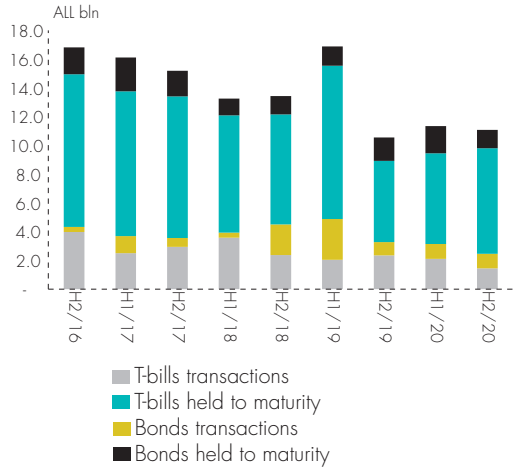
Activity in the secondary market of government debt securities registered a decline in value and number of transactions.

The market yield curve shows a normal slope, but investors continue to show a preference for keeping securities up to maturity.

During the period, the secondary market of government debt securities registered a decline in value and number of transactions. The volume of both long- and short-term securities retail transactions carried out in the secondary market was around ALL 2.5 billion, and 21% lower compared with 2020 H1 and 25% lower from the same period of the previous year. The number of transactions was around 800 purchase/sell transactions of Treasury bills and government bonds, from 1000 transactions registered in the previous six months. The main impact in this trend came from a decline in volume and number of long-term securities by 31% and 25%, respectively. The number of long-term transactions registered a 10% increase compared with the previous six months, nevertheless volume of trade remained at the same level of ALL 1 billion.

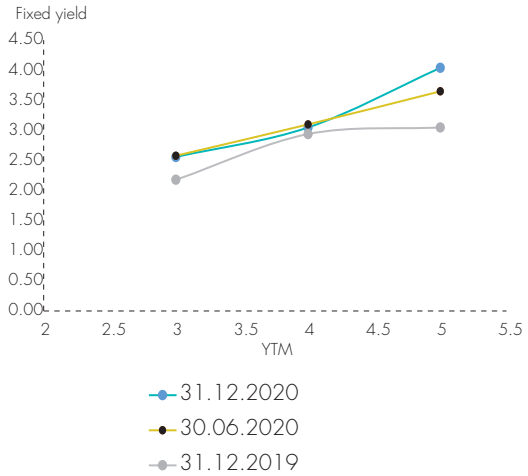
Bond transactions dominate securities transactions in the retail market, accounting for 85% of the traded quantity. Investors in the retail secondary market continue to show a preference to keep securities until maturity. Only 20% of them are traded.

Chart 20 Volume of securities trasnactions in secondary market, in billion lek



Source: Bank of Albania.

Chart 21 Yield Curve (YTM) on 31.12.2020



Source: Bank of Albania.

Market makers have continued the daily quotations of benchmark securities (reference bonds with 3 and 5-year maturity). During the period, their traded value increased slightly by 2% compared with the previous six months, while the number of transactions decreased by 6%. The daily quotation of benchmark securities allows for calculation of the yield curve, which serves as reference for other debt securities in the market and increases transparency by providing real-time information on securities prices. The yield curve shows a normal slope with higher average yields on longer-term maturities. Average yields increased during the period compared with the previous six months and the previous year.

INTERBANK MARKET

During the period, the volume of interbank transitions contracted, while interest rates fluctuated near the policy interest rate decided by the Bank of Albania. The interbank market continues to be dominated by one-week transactions (90% of the volume of interbank borrowing) followed by overnight transactions (9%). The volume of overnight transactions has declined by 60% from the previous six months and 68% compared with the previous year. Meanwhile, one-week transactions have declined by 20% compared with 2020 H1, but they have increased by 12% compared with the previous year. Interest rates remained near the policy interest rate of 0.5%. Overall, this trend reflects the unlimited liquidity injection by the Bank of Albania.

During the period, the number of interbank transactions declined significantly compared with 2020 H1, but it was higher than the previous year. Interest rates fluctuated near the policy interest rate of 0.5%. This trend reflects the unlimited liquidity injection by the Bank of Albania.

During the period, ALL maintained a stable rate against the Euro and appreciated against the US dollar.

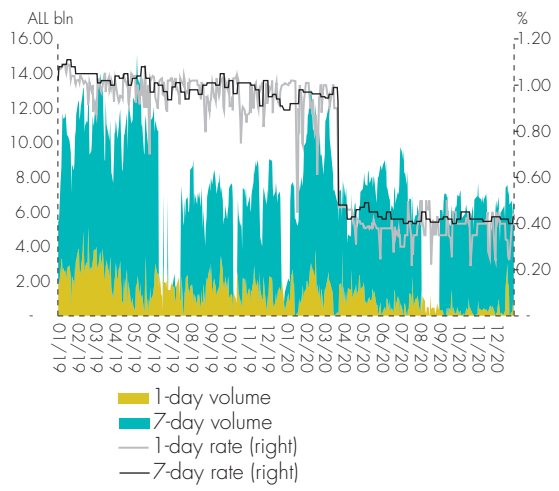
Overall, developments in the foreign exchange market during the period have had a positive impact in mitigating the financial stress of the economy.

FOREIGN EXCHANGE MARKET

In 2020 H2, the foreign exchange market was characterised by stability in the ALL/EU exchange rate. During the period, ALL/EU exchange rates registered slight fluctuations near the 124.0 ALL/EU average, however compared with the same period of the previous year, ALL depreciated by 1.1%. At the end of 2020 H2, the EU currency was exchanged on average with 123.6 ALL. The ALL/USD exchange rate mainly reflected the performance of the US dollar in the international markets where the US dollar depreciated against the Euro.

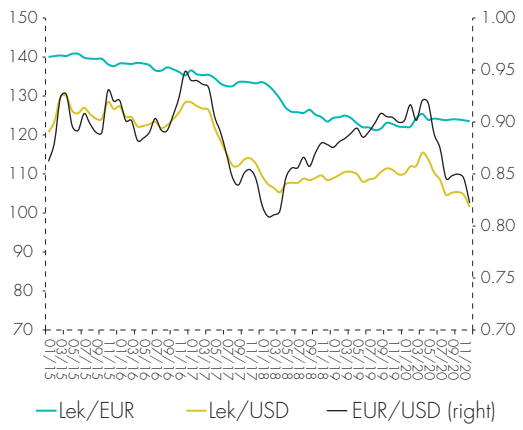
As a result, at the end of the year ALL appreciated by 8.7% against the US dollar compared with the previous six months and by 8.2% compared with the previous year. At the end of 2020, the average exchange rate of lek against the US dollar was 101.6 lek. The trends in the currency market and the foreign exchange market during 2020 H2 have overall helped to maintain financial stability and to keep under control some risks related to the domestic economy and financial stress in the economy.

Chart 22 Interest rates in the interbank market



Source: Bank of Albania.

Chart 23 Interest rate in the foreign exchange rate market



Source: Bank of Albania.

3.2 REAL ESTATE MARKET

Transactions and expectations in the real estate market continue to be affected by the uncertainty of the pandemic.

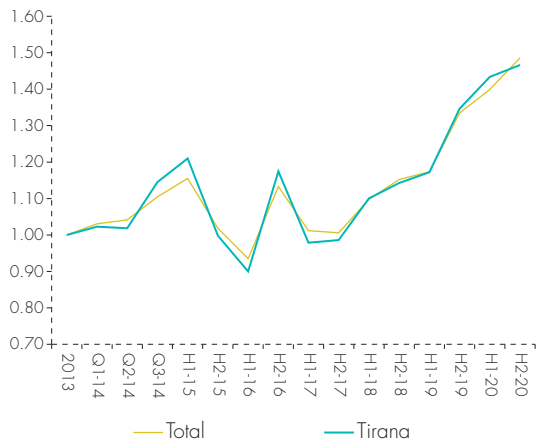
Real estate prices and loans increased during the period. Banks facilitated the conditions for this type of lending, while the demand for it is assessed as weak.

Indicators of the performance of the real estate market give out mixed signals regarding the trend of demand and supply in 2020 H2. On the side of demand, the qualitative indicators indicate easing conditions of banks for real estate loans, but households' demand for financing the purchase of houses has been weaker. On the other hand, lending surplus for real estate increased, while real estate agents reported a decline in the number of unsold properties and an overall increase in selling prices. With regard to supply in this market, lending for construction was lower compared with the previous half-year but higher compared with the previous year, while the number of construction permits granted in the third quarter was lower than the same period of the previous year.

The periodical survey of the real estate market shows that real estate agents, in aggregate, reported higher selling prices compared with the previous half-year and the previous year.

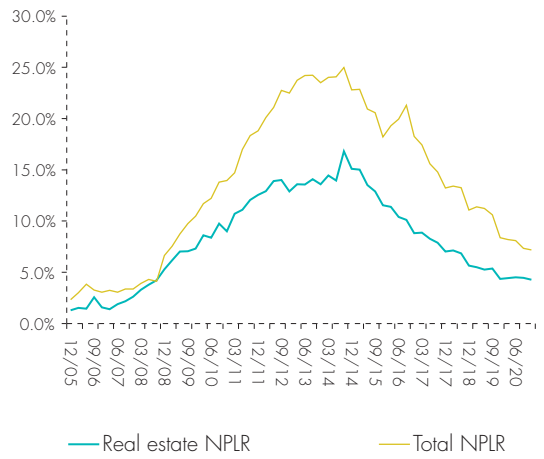
House prices, calculated based on the Fischer Index for sales carried out during the period, increased by 6.2% compared with the previous half-year and by 11.3% compared with 2019 H2. For sales realized in the Tirana area, which includes the downtown, suburbs and the area outside the city, the Index registered an increase of 2.3% compared with 2020 H1 and 8.9% compared with the same period of the previous year. As was expected in this period, agents were relatively pessimistic on developments in the real estate market, assessing the situation of the market as deteriorated. Agents also remain pessimistic regarding the successive period, but are more optimistic for the future of this market in the long term.

Chart 24 Fischer Index of House Prices – National level and Tirana



Source: Bank of Albania.

Chart 25 Credit quality for real estate purchase



Source: Bank of Albania.

Banking sector data show an increasing level of lending surplus for real estate and an improvement of its quality for the period against the previous year.

Lending stock for real estate purchase for households registered around ALL 120 billion at the end of 2020 and was around 5% and 8% higher compared with the end of June 2020 and December 2019. The performance of this credit is also favoured by somewhat lower and stable interest rates for this category of lending. The non-performing loans ratio for this type of lending decreased to 4.2%, from around 4.4% in the previous half-year. Outstanding loans for construction decreased compared with 2020 H1 (by 2%) and increased compared with the previous year (by 8%). The share of loans for construction accounts was 13% of outstanding loans to enterprises, maintaining levels almost unchanged with the previous periods. At the end of the period, the stock of loans collateralized with real estate increased, with no differences between currencies. Within this subdivision, 64% of the stock is held by the households sector and the rest by the enterprises sector.

BOX 1 SUMMARY OF RESULTS FROM THE "REAL ESTATE MARKET" SURVEY AND THE PERFORMANCE OF THE HOUSE PRICES INDEX FOR 2020 H2

Data on the performance of prices and the assessment of the situation by real estate market agents is collected through the field survey of a sample composed by 230 subjects whose main activity is trading real estate. The selected subjects are real estate agents and construction companies whose sales represent 75%-80% of the turnover of the entire population. The Bank of Albania conducts the drafting of the questionnaire as well as the submission and processing of the results, while the Institute of Statistics conducts the interviewing on-site, the main sampling and the physical control of the completed questionnaires.

General assessment: The assessment of the agents on the overall situation of the market shows a significant deterioration compared with the previous period, reflecting market uncertainties in the situation created by the COVID-19 pandemic. Responding to the question "How do you assess the market situation compared with the previous period (six-months)?" the net balance of responses was [-29] % and only 6% of agents gave positive responses (better). Meanwhile around 60% of responses were neutral - "no change". This balance is notably lower than the long-term average for this indicator. The same indicator assessed only for subjects that have reported sales during the period resulted with a less negative value of [-19.7] %, and has maintained the same trend as in the previous period.

Performance of prices and sales: At the end of the period, Fischer House Prices Index, on a national level, registered an increase of 11.3% compared with the previous year and an increase of 6.2% compared with the previous six-months. Sales volumes have declined in the central areas of Tirana but have increased in coastal areas and other areas of Albania. The Price Index for Tirana increased by 8.9% compared with the previous year and by 2.3% compared with the previous period. Average prices in Tirana are reported to have increased by 16% in central areas, but agents reported a slight decrease in prices in areas outside the city. For coastal areas, agents reported almost a doubling in prices, while changes in prices for other areas** were unnoticeable.*

Number of listed proprieties: Agents report a lower number of new proprieties listed in their books; the net balance of those reporting an increase of the number of listed proprieties and those that report a decrease was around [-9.3]%, showing a decrease from the previous period. The number of unsold proprieties, both for residential and commercial buildings, has been down for several consecutive six-months.

Average sale period: The average sale period of properties, at the national level, is reported to be 10.6 months, and remains unchanged compared with the previous six-month. For Tirana, interviewed subjects reported an average sale period of 9.8 months. For the coastal and other areas, the sale periods were 10.6 and 11.4 months, respectively.

Financing through bank credit: According to agents, as in the previous period, around 60% of both residential and commercial properties which they sold were purchased with a bank loan.

Expectations for the future: In contrast with other periods, agents have negative expectations about market performance in the territory in which they operate for the short-term future, but they are optimistic for a longer-term future (up to two

years). New listings for sale in the forthcoming period are expected to experience a decline (net balance resulted [-8] %). Agents do not expect essential changes or increase of real estate prices, while net balance was positive for commercial (15.8%) buildings, reflecting that agents are optimistic.

Rent price: According to the agents interviewed rent prices have increased. Rent demand has not changed compared with the previous period. It should be emphasised that these responses are concentrated in Tirana.

* *This high discrepancy in average prices in the seaside areas is explained by the fact that during the period there were more residences sold in areas close to the sea, in comparison with residences within the cities, such as Saranda and Durrës.*

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

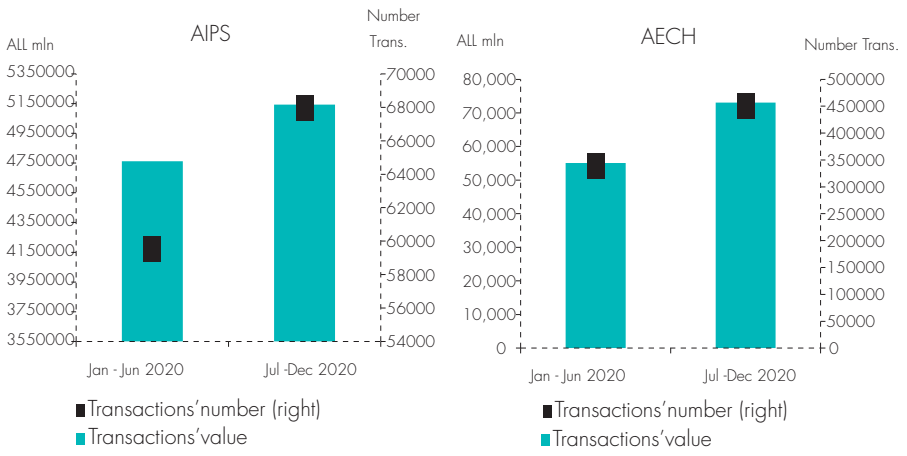
3.3 PAYMENT SYSTEMS

The core infrastructure for clearing and payment settlements in lek has continued to function reliably and efficiently.

During the period, there was a significant increase in the number and value of small and large payments, as well as an increase in the use of payment instruments, including those in non-paper form.

The core infrastructure for clearing and payment settlements in the domestic currency has continued to function reliably and efficiently, supporting financial stability and implementation of monetary policy. At the beginning of 2020 Q2, the Bank of Albania, together with a number of measures which aimed at supporting banks and borrowers during the period of restriction and challenging economic situation, approved a Decision.[12] The purpose of this Decision was to facilitate the cost of payments for clients and banks and encourage the use of Home banking services. During the period, compared with 2020 H1, there was a significant increase in both volume and value of small and large payments cleared through the AECH and AIPS systems.

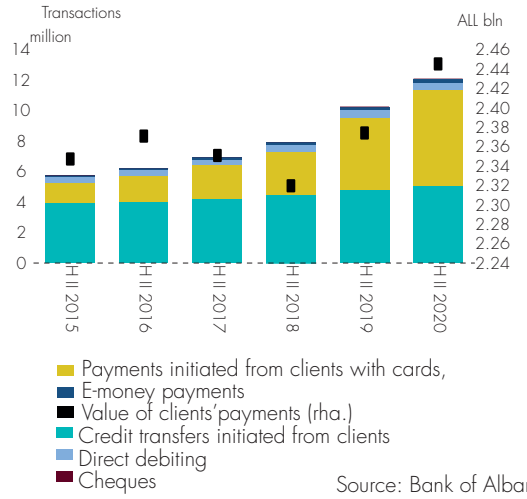
Chart 26 Performance of the AIPS and AECH in 2020 H1 and H2



Source: Bank of Albania.

[12] *Decision of the Supervisory Council of the Bank of Albania "On removing commissions applied by banks on the non-paper based credit transfers in ALL, from their clients, and the fees charged to participants in the AIPS and AECH systems operated by the Bank of Albania", starting from 9 April 2020*

Chart 27 Performance of payment instruments in number (left) and value (right)



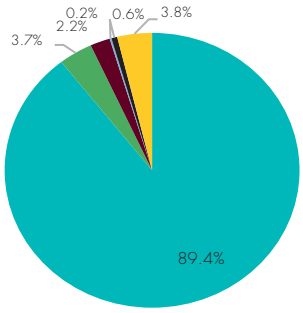
Source: Bank of Albania.

Use of payment instruments increased during the period compared with 2020 H1, in both number and value, by 26% and 22%, respectively. Card payments have the main share in payment instruments with 50% in number, exceeding for the first time paper credit transfers. On the other hand, an increase was reported in the number and value of transfers in non-paper form (internet banking, mobile banking), as well as an increase in the number and value of transactions carried out by card.

4. FINANCIAL SYSTEM

During 2020 H2 there was a significant increase of the share of financial system assets[13] to Gross Domestic Product (GDP) and by the end of the period this value amounted to 119.4%. This performance was driven by GDP contraction and also by the expansion of financial system activity where the banking sector provided the main contribution. The other financial system segments such as the non-bank group, insurance companies and interment funds have also registered an expansion of their activity during 2020 and the period under review. At the end of the year, the share of the banking sector to GDP increased to 106.8% from 102.2 %, whereas the share of the non-bank sector increased to 13% of GDP from 12% at the end of 2020 H1. Financial system performance indicators, including capitalisation, profitability, liquidity and asset quality, remain at good levels.

Chart 28 Share of financial system segments to the total system assets, December 2020



Source: Bank of Albania and Financial Supervisory Authority.

Table 4 Share of financial system segments to GDP over the years (in %)

Licencing and Supervising Authority	Bank of Albania			Financial Supervisory Authority			Financial Intermediation
Financial system	Banking sector	NBFIs	SLAs and Unions	Insurance companies	Pension funds	Investment funds	
2011	88.1	2.7	0.8	1.5	0.0		93.1
2012	92.1	2.7	0.8	1.6	0.0	1.2	98.6
2013	94.8	2.7	0.7	1.7	0.0	3.9	103.8
2014	97.6	3.0	0.8	1.9	0.0	4.8	108.2
2015	97.3	2.9	0.8	2.1	0.1	5.0	108.0
2016	100.5	3.0	0.6	2.1	0.1	4.7	111.0
2017	99.4	3.1	0.6	2.1	0.1	5.0	110.3
2018	96.0	3.5	0.6	2.1	0.2	4.5	106.9
2019	95.5	4.2	0.7	2.2	0.2	4.3	107.2
2020	106.8	4.4	0.8	2.6	0.2	4.6	119.4

Source: Bank of Albania and Financial Supervisory Authority.

[13] *The financial system consists of the banking sector and the non-banking sector (non-bank financial institutions, savings and loans associations, insurance companies, pension funds and investment funds). The database of the non-bank sector and GDP data are from 2020 Q3.*

4.1 THE BANKING SECTOR

4.1.1 MAIN DEVELOPMENTS IN THE BANKING SECTOR

The banking sector continues to support the economy with funding and other banking services regardless of the difficult situation created by the pandemic. The increase of assets is supported by the increase in interbank investments and credit to the economy.

The banking sector's assets expanded by around 3% during the period and by 7% compared with the end of 2019. Regardless of the difficult situation created by the pandemic in Albania, the sector has managed to carry out the main functions of its activity and has supported the economy with funding. The reported value of assets increased to ALL 53 billion during the period, reaching around ALL 1,580 billion. The main contribution in assets' increase came from the expansion of interbank investments by around ALL 40 billion and lending activity by around ALL 20 billion.

Securities investments had a negative contribution in asset performance and the contraction reflects the reduction in banks' portfolio in securities with fixed foreign currency income issued by non-resident entities. Provisioning funds of the banking sector expanded the level of assets by around ALL 0.7 billion during the period.

Table 5 Structure of banks' balance sheets and annual change, December 2020

Assets	% of assets	Annual change,%	Liability	% of liabilities	Annual change,%
I. Treasury and interbank transactions	30	0	I. Treasury and interbank transactions	6	-1
II. Customer transactions (credit)	38	6	II. Customer transactions (deposits)	81	8
Of which: public sector	2	-35	Of which: public sector	1	22
Of which: private sector	37	6	Of which: private sector	80	8
III. Securities transactions	30	19	III. Securities transactions	0	35
IV. Created reserve funds	-2	13	IV. Other liabilities	1	34
V. Other*	4	5	V. Permanent sources	12	5
			Of which: Subordinated debt	1	-13
			Of which: Shareholders' equity	10	7
Total assets	100	7	Total liabilities	100	7

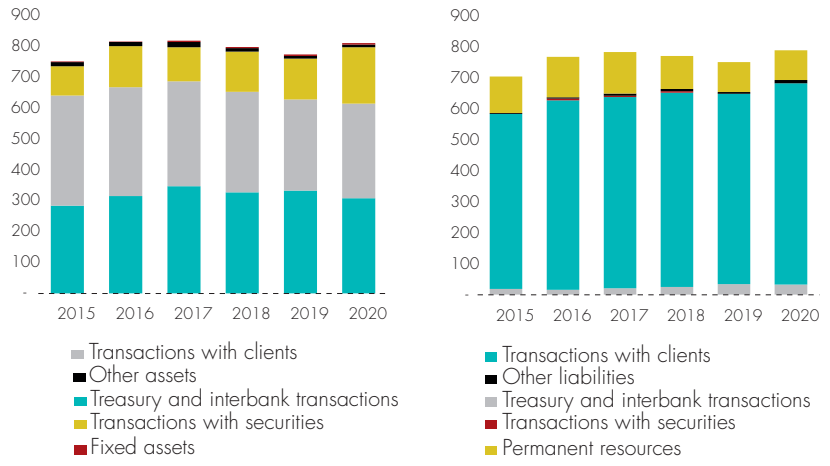
Source: Bank of Albania.
**The item "Others" in the balance sheet refers to "Other assets", "Sustainable assets" and "Calculated interest".*

The share of foreign currency assets and liabilities to total balance is around 50% and has slightly decreased over the year due to a stronger increase in lending and deposits in lek.

At the end of 2020, foreign currency assets and liabilities in the banking sector constituted 51% and 50%, respectively of total balance, reaching around ALL 800 billion. These reports decreased compared with the previous period. This decline reflects the faster increase of credit and deposits in the domestic currency. Foreign currency assets and liabilities to total balance have almost always had similar values, reflecting a balanced and congruent exposure of foreign currency activity regarding the banking sector.

Regarding foreign currency assets, lending activity and interbank investments continue to be the main items, meanwhile in the last two year there was an increase in the share of securities investments. Regarding foreign currency liabilities, the structure reflects more stability over the years, and is dominated by foreign currency deposits. The abovementioned components mostly determined the banking sector's sensitivity to foreign currency exposure. The statistical impact of the exchange rate on the change registered in the equivalent value in lek of the foreign currency balance during the period was negative, but quite small and without a significant impact[14].

Chart 29 Foreign currency assets (left) and foreign currency liabilities (right)

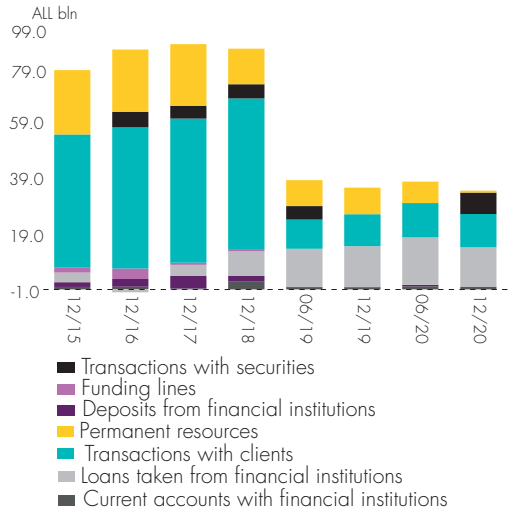


Source: Bank of Albania.

Deposits and own funds continue to be the main funding source of the banking sector's activity, accounting for 93% of total liabilities and this structure was stable during the period. Reliance on external funding sources remained low. These sources are mainly in the form of loans to financial institutions from non-resident entities. Loans from these entities have decreased and this has determined the performance and liability level toward non-residents. Assets of non-residential entities declined during the period due to the contraction of loans and current accounts to banks and financial and lending institutions. This has affected the narrowing of the net credit position of the banking sector. At the end of the period, claims against non-residents were 21% of total assets, while liabilities against non-residents were only 2% of total balance sheet. The net credit position narrowed in both absolute and relative terms, reaching around 19% of the total balance from 19.4% in the previous period and 21% in the previous year.

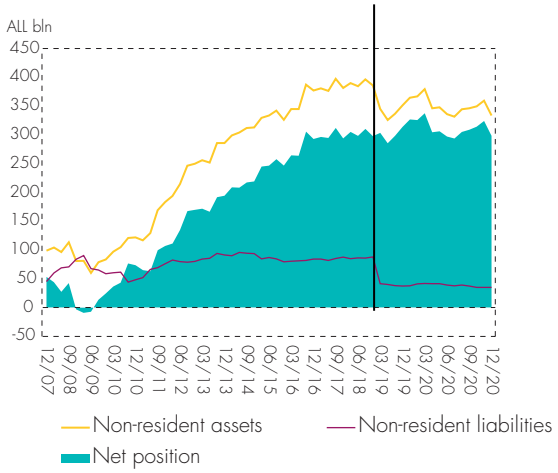
[14] *Without the effect of the exchange rate, the increase by ALL 19 billion of the foreign currency balance during 2020 H2 would have been ALL 23 billion or around 3%.*

Chart 30 Structure of non-resident liabilities



Source: Bank of Albania.

Chart 31 Net position with non-residents*



The vertical black line (right) represents the period of transformation of the NCB branch in subsidiary.

Source: Bank of Albania.

4.1.1.1 Banking soundness index

The improvement of profitability, efficiency and liquidity produced a slight improvement in the banking soundness index in 2020 H2.

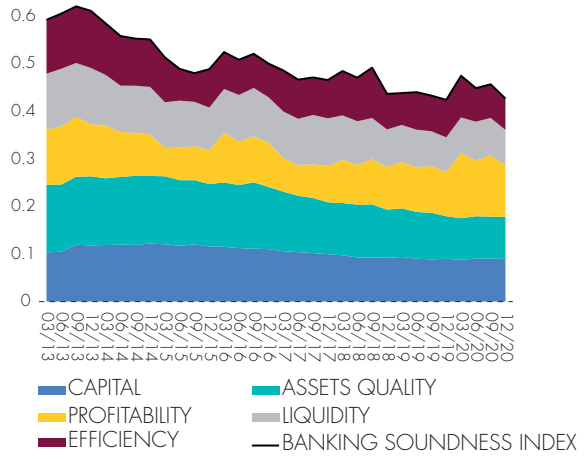
Profitability, which was negatively impacted by the decrease of profit and net interest margin, continues to provide the largest contribution to the assessment of the banking sector.

The banking soundness index has slightly improved[15] during the period, but has recorded the same level as at the end of 2019. During 2020, this index registered a weaker performance in the first quarter, while in the last quarter index performance improved. This performance was affected by improvement in stability, efficiency and liquidity indicators, while asset quality and capitalisation indicator have not recorded significant changes. In annual terms and more extended in time, the profitability of the banking sector was somewhat weaker given the decrease of the profit rate and the gradual decline of the net interest margin starting from 2015. As a result, the profitability sub-index provided the main contribution to the overall performance of the indicator and has increased from 0.46 to 0.54 during 2020, registering higher values from 2013.

Liquidity risk increased slightly during the last year due to a small decrease in the liquid assets to overall assets ratio, but the contribution of this component to the aggregate level of risk over time has been stable overall.

[15] *The value of the index and the assessment of the soundness of the banking sector are inversely related.*

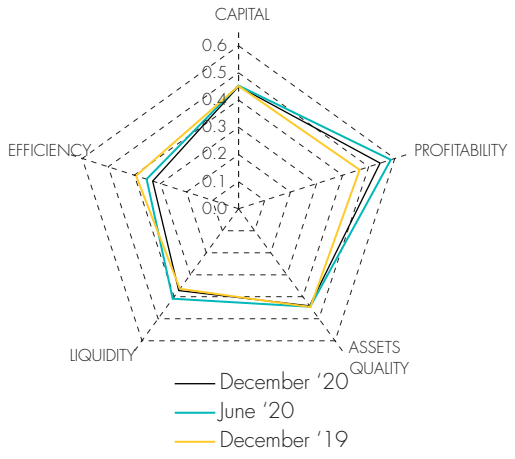
Chart 32 Banking soundness index*



*The increase of the indicator shows a lower stability. The width of each dimension shows its contribution to risk.

Source: Bank of Albania.

Chart 33 Banking soundness map*



*Away from the centre means increased risk, in a 0 to 1 range.

Source: Bank of Albania.

Asset quality is stable and the contribution of this dimension to overall risk has trended downwards over the last few years. Since the beginning of 2015, the contribution of asset quality to the level of risk has decreased significantly and constantly. The value of this indicator decreased from 0.71 in March 2015 to 0.44 in December 2020. This performance was mainly affected by a lowering of the non-performing loans ratio. The capitalisation indicator has not recorded any changes compared with the previous year and previous six-months, while within the indicator there were small movements noticed in the sub-indicator values of the financial leverage and capital adequacy ratio. The efficiency dimension improved during 2020 due to a slight increase in interest revenues.

The soundness index for banks of systemic importance indicates a somewhat weaker situation compared with the previous year. The profitability indicator has deteriorated, while efficiency and liquidity indicators have improved for this group of banks. Compared with the previous year, the index has improved for other banks (non-systemic), reflecting improvements in efficiency and asset quality. Meanwhile, the liquidity indicator reflects a weaker health for this group of banks compared with the previous year. Overall, during 2013-2020 the aggregate banking soundness index has declined, demonstrating a better soundness and higher stability of the banking sector.

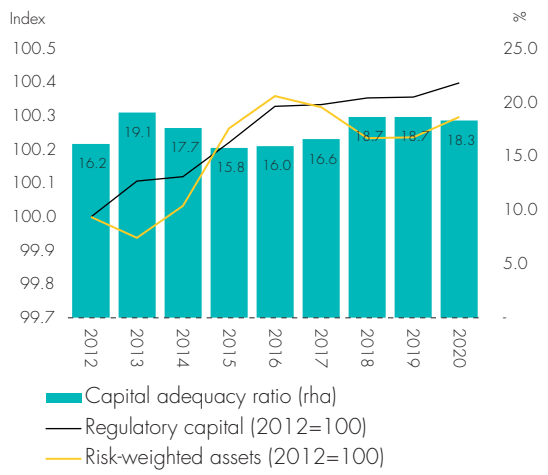
4.1.1.2 Capitalisation of activity

The banking sector continues to maintain a good level of capitalisation. The capital adequacy ratio increased to 18.3% from 18.1% and for 9 banks this indicator is 16%.

During the period, the increase of CAR reflects an increase of regulatory capital and a decrease of risk-weighted assets.

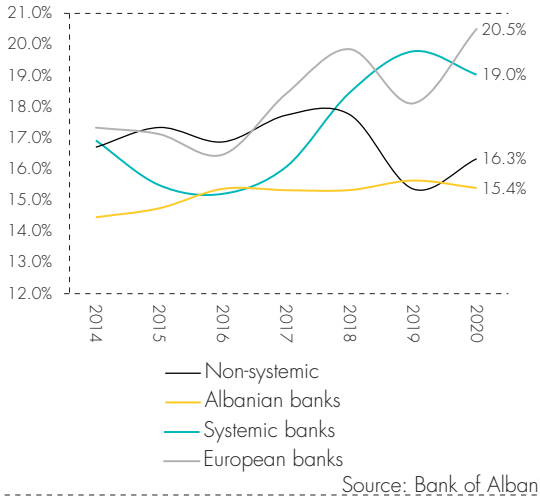
The banking sector concluded the year with a good level of capitalisation. The capital adequacy ratio for the whole sector increased to 18.3% from 18.1% in the previous six-month. A growth of regulatory capital and a decrease of risk-weighted assets affected the increase of the indicator during the period. In annual terms, the capital adequacy ratio declined by 0.4 percentage points, reflecting the increase of risk-weighted assets. Banks with European capital and systemic banks report the highest capital adequacy ratio. Banks with Albanian capital have the lowest capital adequacy ratio and this ratio declined slightly during 2020. The high capitalisation level of the banking sector is reflected in the distribution of the capital adequacy ratio according to certain ranges. There are currently 9 banks with a capital adequacy ratio over 16% and this value increased compared with the end of the previous year.

Chart 34 Capital adequacy ratio



Source: Bank of Albania.

Chart 35 Capital adequacy ratio for groups by importance and by origin of capital



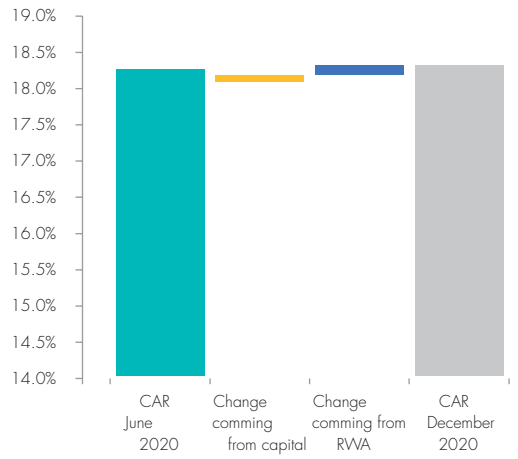
Source: Bank of Albania.

During the period, the regulatory capital of the banking sector registered a slight increase reaching ALL 153 billion at the end of December. The increase in banks' regulatory capital was affected by a growth in paid capital and by the overall good performance of the banking sector. Retained profit from previous periods has been the main contributor to the increase of equity and regulatory capital during the last two years. During 2020, the preservation of retained profit from the previous periods was affected by the Decisions of the Bank of Albania, in April and July[16], on suspending the distribution of profit from banks. The other component which determines the performance of the capital

[16] *Decision No. 24, dated 08.04.2020 and Decision No. 40, dated 01.07.2020 "On the suspension of profit allocation from banks" in force until the end of June 2020 and December 2020. The allocation of profits by banks, the profit carried over from previous periods, profit realised in 2019 and profit which would have been realised in 2020 H1 and 2020 H2 have been suspended in accordance with these Decisions.*

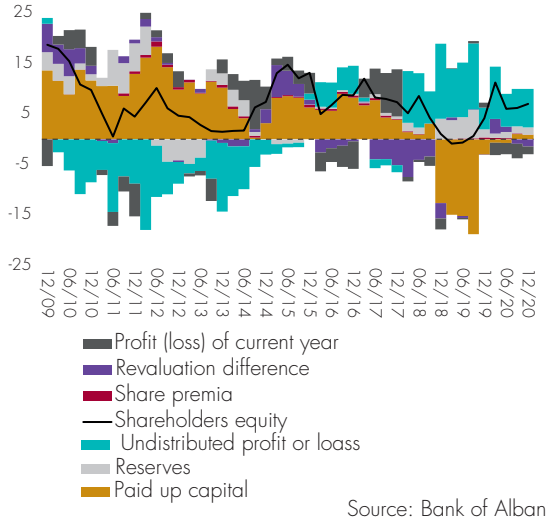
adequacy ratio, risk-weighted assets, decreased by around ALL 6 billion and at the end of the period was at ALL 830 billion. The decline of risk-weighted assets contributed by 0.14 percentage points to the capital adequacy ratio's increase of 0.2 percentage points.

Chart 36 Contribution of capital adequacy items (in p.p.)



Source: Bank of Albania.

Chart 37 Annual contribution in capital increase by component instruments (in p.p.)



Source: Bank of Albania.

The structure of risk-weighted assets by risk has not changed during the period and continues to be dominated by risk-weighted assets for credit risk (87%) followed by risk weighted-assets for operational risk (10%) and market risk (2%). Risk-weighted assets for market risk contracted while those for operational risk increased by ALL 6 billion, reaching ALL 20 billion and ALL 85 billion, respectively.

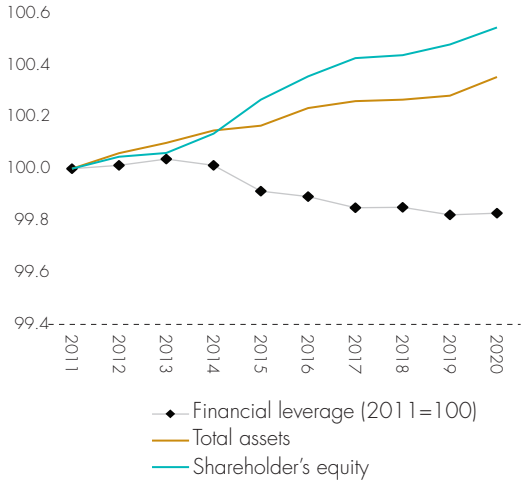
Banks classified with systemic risk register high exposure for credit to trade companies (corporations), non-performing loans, and loans to other institutions supervised by the Bank of Albania and the Financial Supervisory Authority. Other banks (non-systemic) register exposure towards retail portfolios as well, in addition to exposure to corporation loans. Banks with European capital have a higher exposure towards the classes "corporation loans and non-performing loans" and "retail portfolio," while banks with domestic capital in addition to the above-mentioned exposures also register exposures towards portfolios classified as high risk and uncovered from exchange rate fluctuations.

The Albanian banking sector is characterised by an adequate financial leverage ratio which confirms a good level of capitalisation. The financial leverage ratio[17] in December was 9.6 times, slightly higher compared with the end of 2019 and near the 5-year average of 9.8 times. Analysis of the financial leverage ratio for certain groups of banks shows that the level of leverage for

[17] *Financial leverage is measured as the ratio of assets to equity.*

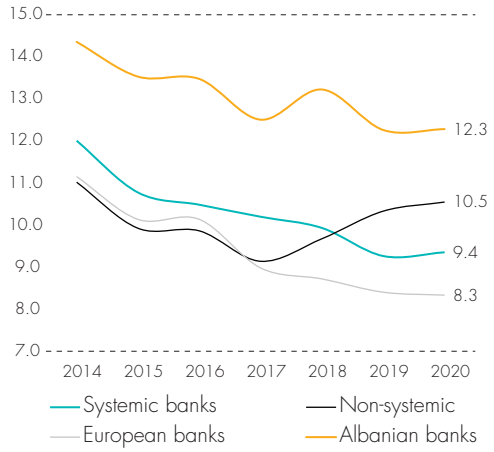
systemic banks determines the level and performance of the financial leverage for the entire banking sector. Banks with Albanian capital have the highest level of financial leverage due to the lowest level of equity compared with banks with foreign equity.

Chart 38 Financial leverage performance by components



Source: Bank of Albania.

Chart 39 Financial leverage of banks according to systemic risk and the origin of capital, in times.



Source: Bank of Albania.

4.1.1.3 Financial result

The annual decline of the financial result by 15% was affected by an increase of expenditures for credit provisions.

Income from interest and other income have slightly increased while banking sector expenditures were similar with the previous year.

The banking sector closed 2020 with a positive financial result of around ALL 17 billion, or with a profit around 15% lower than the previous year. The banks' assets share with negative result against banking sector assets remains insignificant, but compared with the previous years there is a considerable decline in the share of banks with RoA higher than 1%. The decline of the profit of the sector is also reflected in a decrease in average profitability indicators of the banking sector, where RoA decreased to 1.1% from 1.4%, while RoE decreased to 10.7% from 13.5% in the previous year.

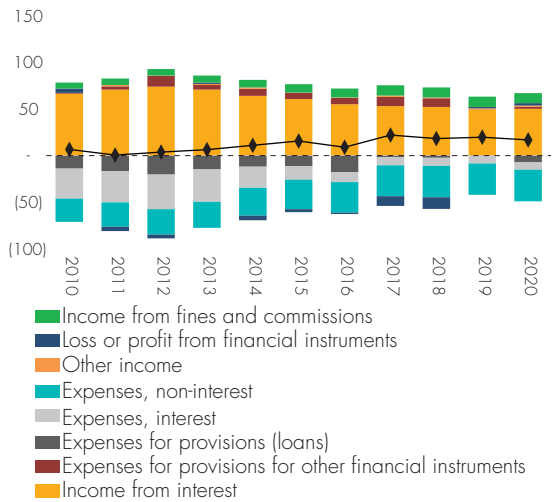
Table 6 Income and expenditure of the banking sector for 2019-2020 (billion lek)

	2020			2019
	ALL	FX	Total	Total
Income from interest	31.8	18.6	50.4	49.7
Expenses from interest	5.6	2.0	7.6	8.2
Net income from interest	***26.2***	***16.5***	***42.8***	***41.6***
Income not from interest	***8.8***	***6.2***	***15.0***	***13.5***
Fines and commissions	6.3	4.6	10.9	11.1
Loss or profit from financial instruments	1.2	1.5	2.7	1.5
Expenses not for interests	***26.4***	***7.5***	***33.9***	***33.7***
Provisions (net)	***4.8***	***0.6***	***5.4***	***(0.2)***
For loans	5.9	1.3	7.2	0.2
For other financial means	(1.1)	(0.7)	(1.8)	(0.4)
Common items	(0.8)	(0.4)	(1.2)	(0.7)
Tax on revenue	2.8	-	2.8	3.0
Net result	***1.9***	***15.0***	***16.9***	***19.2***

Source: Bank of Albania.

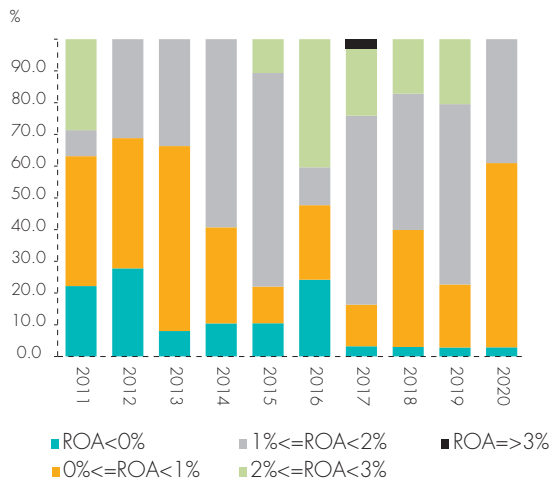
The main activity of banks, reflected in net interest income, registered growth, while the general expenses of the activity did not change essentially. Net result from interests registered ALL 43 billion or ALL 1 billion higher than the previous year. This development was affected in the same degree by both a decrease of interest expenses and an increase of interest income. Despite positive developments in the main banking activity and an increase in the net result from interest, net margin from interest remained unchanged at 3.4%, given that the average assets which bring income recorded an annual increase of 6%.

Chart 40 Financial result components



Source: Bank of Albania.

Chart 41 ROA by banks' share in sector assets.

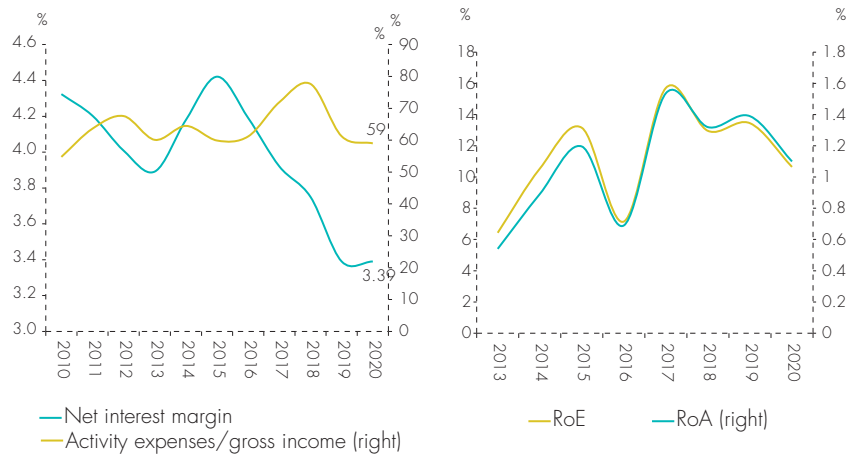


Source: Bank of Albania.

The increase of provision expenses for credit was the main factor after the decline of the sector's financial result, since banks reported expenses of around ALL 7 billion, while in 2019 this item registered a negligible value. On the other hand, expenses on provisioning other financial items registered a value of around ALL 2 billion greater as provision returned, which had a positive impact on the net result of the banking sector. Income from other activities also increased by ALL 1.6 billion as a result of an increased investment in financial instruments.

The net result was mainly affected by activity in lek, while activity in foreign currency did not register significant changes. Banking sector activity in lek continues to generate the major part of interest income (around 60%) as well as withdraw most of the non-interest expenses. At the same time, the increase of provision expenses for credit was observed in the lek activity of the banking sector. Activity costs were adequately covered by activity income. The ratio of activity expenditure to income was around 59% or somewhat lower than the previous year, due to an increase of activity income.

Chart 42 Profitability and expense indicators of the banking sector



Source: Bank of Albania.

4.1.1.4 Loans

The increase by 3% of loans stock during the period reflects an increase in the flow of new loans.

Long-term loans, loans to enterprises and loans in lek registered an increase, in particular in annual and semi-annual terms, while the growth of loans in foreign currency has slowed down.

At the end of 2020, the amount of outstanding banking loans was around ALL 610 billion. Overall, loans increased during the period by 3%. Compared with the end of the previous year, outstanding loans were 6% higher. The expansion of loans stock during the period was mainly affected by tan increase of new loans flow, which was used particularly by enterprises for short-term purposes. The increased value of loans stock was also affected by lower settlements as a result of banks' activities for credit restructuring in response to the easing measures of the Bank of Albania[18]. A particularly good performance of loans stock during the period was registered by the portfolio of loans with long-term maturity (+8%), loans in domestic currency (+6%) and loans to enterprises (+4%). At the end of 2020, loans in foreign currency were 4% higher than the previous year, but it has maintained almost the same level as during 2020 H2.

[18] *The amendments allowed the extension of payment instalments, given that lending entities enjoyed some facilities related to the implementation of regulatory requirements on the classification of loans and the creation of relevant provisions. The validity of this provision with 3-months initial maturity (March-May 2020) was extended to also convert the period June-August 2020, and was later accompanied by similar definitions for restructured loans until March 2021.*

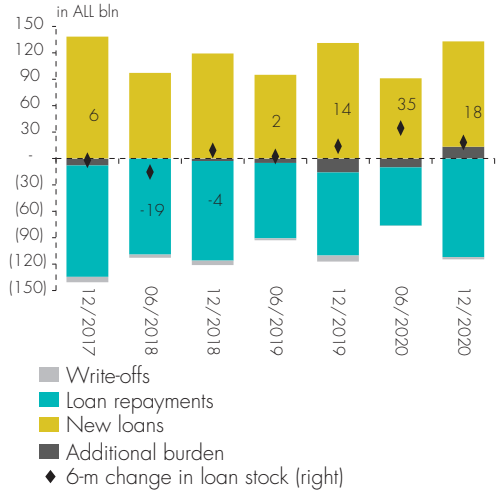
Table 7 Loans performance by maturity, sector and currency

	ALL bln	Share (%)		Change (%)	
	12/2020	12/2020	12/2019	6-M	Annual
Lek	303	50	49	6	8
Currency	306	50	51	1	4
Public sector	20	3	5	-14	-35
Enterprises	390	64	62	4	9
Households	200	33	32	4	7
Short-term	154	25	28	-4	-5
Medium-term	94	15	17	-2	-1
Long-term	361	59	55	8	14
Loans	609	100	100	3	6

Source: Bank of Albania.

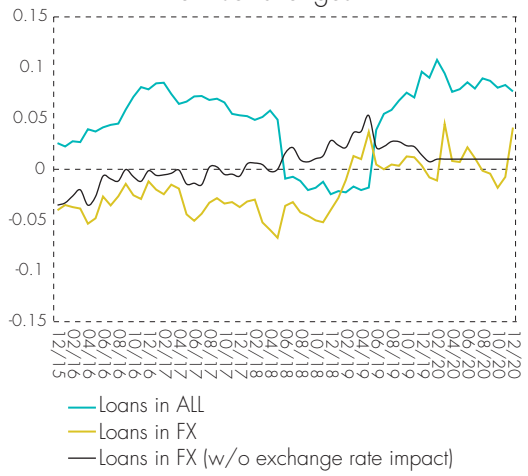
The statistical impact of the exchange rate on the equivalent value in lek of loans in foreign currency was positive, but significantly lower compared with the previous six-months. Without this impact, the annual change of loans in foreign currency would be 1 percentage point lower, at 3%. During 2020, banks continued the process of removing lost loans from balance sheets, but the volume of written-off loans was lower. In total there were ALL 3 billion loans written off, but more than half of them were realised in December. The value of written-off loans during 2020 was 6% of the total outstanding non-performing loans in banks' portfolio at the end of December, while for 2019 this ratio was equal to 17%. If the volume of written-off loans had been included with outstanding loans, credit annual growth would be somewhat over 6%.

Chart 44 Six-month change in outstanding loans by component elements



Source: Bank of Albania.

Chart 45 Loans in lek and loans in foreign currency including and excluding the exchange rate impact, annual changes



Source: Bank of Albania.

LOANS TO RESIDENT ENTITIES – ENTERPRISES

Loans to resident entities represent 96% of outstanding banking loans and this credit expanded by 3% during 2020 H2. Loans to resident enterprises, which account for over 60% of the total resident loans, increased during the period by ALL 14 billion or 4%, reaching ALL 370 billion. The increase of loans to resident entities was mainly due to an increase of mortgages stock

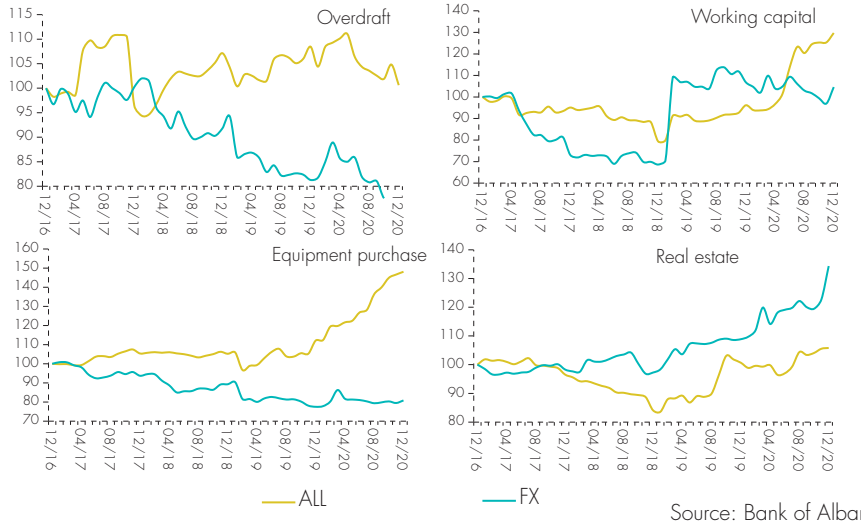
The increase of loans to resident enterprises and households was supported by the expansion of loans stock for real estate.

Loans to enterprises continues to be dominated by loans in foreign currency, while in households' credit portfolios, credit growth was driven by an increase of loans for consumption and real estate purchases in the domestic currency.

and equipment purchase loans. Each of these two categories account for around 30% of loans stock to resident entities and the increase during the six-months for each was 12% and 7%, respectively. Compared with the previous year, outstanding loans to enterprises increased by 10%, affected by an increase in mortgages, for equipment purchases and circulatory capital. Besides a considerable increase of the flow of new loans for this category, stock expansion was also affected by non-timely settlement of standard and special mention loans, following the easing measures of the Bank of Albania on the extension of payment terms for clients of lending financial entities.

By currency, an increase in the preference of loans in lek is observed. Therefore, for equipment purchases and circulatory capital loans, enterprises continue to prefer borrowing in the domestic currency, and these two sub-categories of loans registered a significant increase in 2020. Loans for mortgages were oriented mostly towards foreign currency (Euro). In 2019-2020, banks reported a particularly strong increase Euro credit portfolios granted to enterprises for mortgages. "Overdraft" loans stock in foreign currency decreased significantly, while "overdraft" loans in lek, besides short-term fluctuations, have not recorded significant changes over the past four years.

Chart 46 Annual performance of loans to enterprises by purpose of use and currency, (2016=100)



Source: Bank of Albania

By size, during the period, the share of loans to small enterprises increased slightly from 22% to 23%, while the share of loans to medium-sized enterprises declined to 25% from 27%. Large enterprises continue to hold around ½ of the stock of loans for non-financial corporations, and the share of this portfolio did not register changes in 2020[19].

[19] *These values recorded: 51% (Large E.); 25% (medium-sized E.) and 24% (small E.) in December 2019; while in June 2020 they were 51%, 27% and 22%, respectively.*

By maturity, for three groups of enterprises by size, an increase in the share of long-term and medium-term loans is noted, while the share of short-term loans declined.

BOX 2. LOANS BY SECTORS OF THE ECONOMY AND ITS PERFORMANCE DURING THE PANDEMIC

Banks registered an increase in loans stock for most sectors of the economy in 2020. The distribution of outstanding loans continues to be dominated by loans to trade (41%), followed by loans to the processing sector (14%) and those to the construction sector (13%). Credit growth to manufacturing and services sectors was affected not only by a new flow of loans, but also by an accumulation of unsettled instalments in the regular credit classes as a result of the extension to payment terms for enterprises in need. Although credit quality for most of the sectors has improved, within non-performing loans stock there is an increase in the share of lost loans. The ratio of lost loans against outstanding loans (rate of "bankruptcy") increased by 4% from 3% in the previous year. This rate increased significantly for the construction sector (from 2% to 6%) and the processing industry (from 4% to 7%). For the real estate sector, however, this ratio declined to close to zero, from 3%. By the end of the period allowed for the extension of payments term, assigned as 31 March 2021, there is a need for banks to carefully monitor non-performing loans portfolios and the share of the portfolio represented by rescheduled/restructured loans.

Table 8 Loans by sectors of the economy

		Annual change 2020 (%)		Bankruptcy ratio (%)	
Enterprises by NACE code	Outstanding loans share	Loans stock	Non-performing loans	2019	2020
Agriculture, forest and fishing	2	15	20	2	4
Manufacturing industry	14	10	-13	4	7
Quarrying industry	3	11	-28	0	1
Electricity, waste and water management	11	-14	0	1	1
Construction	13	8	-4	2	6
Trade transportation, storage	41	9	-4	5	6
Information and communication	2	65	0	0	0
Financial and insurance activities	0	-21	0	0	0
Real estate activities	1	-6	-21	3	0
Scientific, professional and administrative activities	2	33	-38	1	0
Public admin, education, health and social work	3	-2	-41	3	1
Arts, entertainment, leisure, other services	9	17	197	1	1
Total	100	7	0	3	4

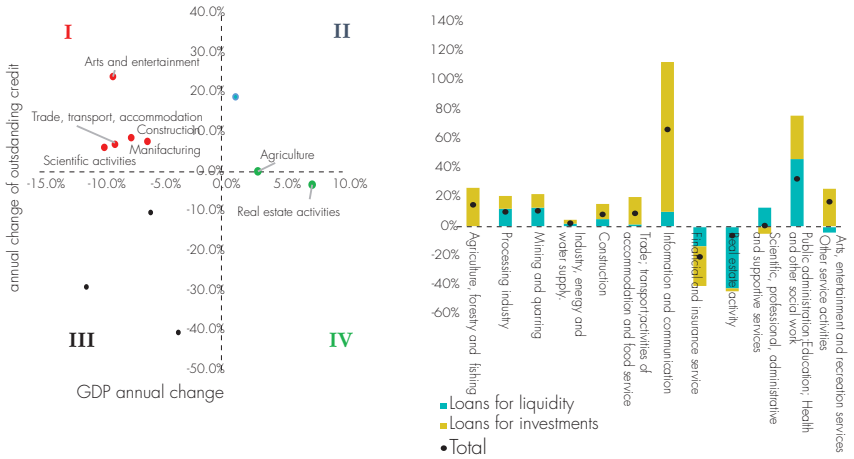
Source: Bank of Albania.

During the first nine months of 2020, the domestic economy contracted by around 5%, and the strongest decline for most of the sectors was observed during 2020 Q2. The 10% contraction of the economy during 2020 Q2 was mostly due to a strong decline in the sectors of trade, industry, construction and scientific, professional and administrative activities. At the same time outstanding loans fort these sectors during 2020 increased with high ratios ranging from 8-10% (industry, trade and construction) to 33% (scientific, professional and administrative activities). Loans to hotels and restaurants, which are included in lending to accommodative services, expanded by over 50% in the time frame*

of one year. During 2020, lending to this sector was mainly used for short-term purposes or liquidity, which shows the need of this sector to withstand last year's losses caused by the restrictions related to the pandemic. The share of this sector in loans to enterprises is low (7%), while the non-performing loans ratio and loans bankruptcy ratio are relatively high and higher than the average of all sectors (NPLR= 15.5% and "lost loans/outstanding loans" = 10%).

The construction sector holds a special place in the economy of Albania. The share of this sector is 10 % of GDP. Over one year, this sector registered a decline by over 7%, while outstanding loans for construction expanded by 8%. Credit growth for construction reflects the expansion of loans for investments, which accounts for the main share of loans to construction and increased during the year by 10%. The only sectors which registered an annual economic growth were real estate and agriculture sectors, which until the end of September 2020 recorded an increase of 7.5% and 3%. The share of credit for these sectors declined during 2020. Overall, it seems that lending activity is oriented by its history with few shifts towards new sectors.

Chart 47 Credit performance and economic growth (with data until September 2020) for all the sectors of the economy (left) and by purpose of use (right).



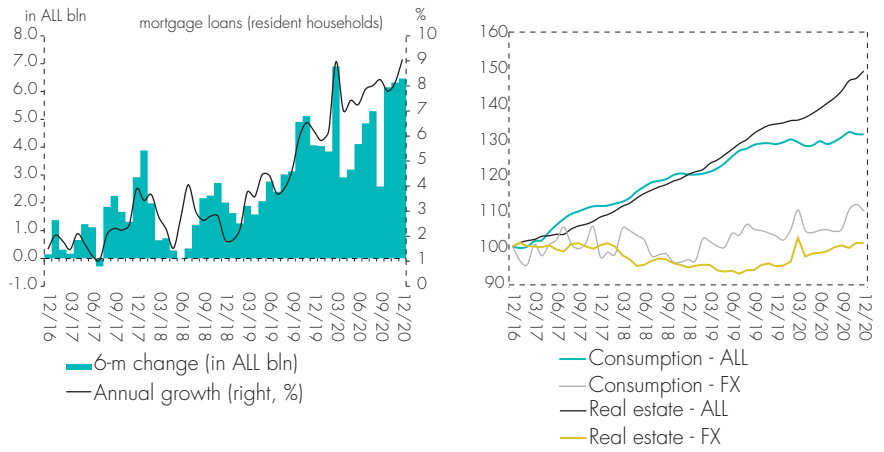
Source: Bank of Albania.

* *The simple average of annual GDP changes for the Q1, Q2 and Q3 (-2.5%, -10.2% and -3.5%).*

LOANS TO RESIDENT ENTITIES – HOUSEHOLDS AND PUBLIC SECTOR

Loans to resident households expanded by 4% during the period. The fastest growth was registered in mortgages and consumer loans for durable goods. During the last two years there has been a considerable growth in outstanding loans to households for real estate. This credit stock increased by around 5% during the period and by 9% compared with the previous year, reaching about ALL 130 billion. Mortgages have the main share (64%) of loans to households. The rapid increase in the stock of loans to households during the last four years was affected by a considerable increase in the stock of loans in lek, while loans to households in foreign currency remained overall unchanged during the period. Loans to the public sector continue to account for a small share in total loans (3%), while by the end of the year, this credit had contracted by about 40%.

Chart 48 Performance of mortgages to resident households (left) and by purpose of use and currency (2016=100) (right)

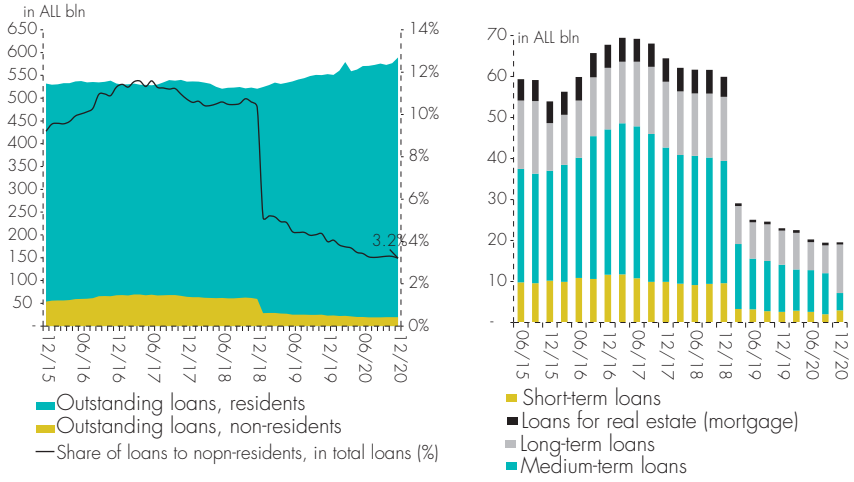


Source: Bank of Albania

LOANS TO NON-RESIDENT ENTITIES

Loans to non-resident entities continued to contract during 2020 H2 as well. At the end of December, loans to non-resident entities was around ALL 20 billion and accounted for 3% of outstanding loans in the banking sector, from 3.4% at the end of the previous six-month. The highest decrease in loans to non-residents was registered in loans to enterprises, in foreign currency with medium-terms. These are at the same time the categories with the highest share in the stock of loans to non-resident entities.

Chart 49 Loans to residents and non-residents (left) and loans to non-residents by maturity (right)



Source: Bank of Albania.

UNHEDGED FOREIGN CURRENCY LOANS

Outstanding unhedged foreign currency loans and their share of the total overall foreign currency loans registered a slight increase during the period, signalling a slight increase in the indirect exchange rate risk for the lending activity of banks.

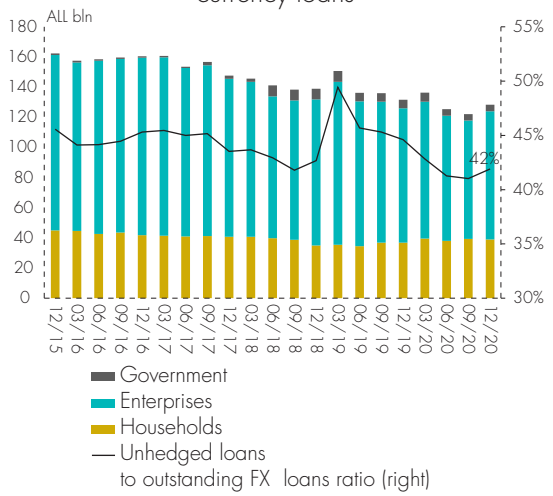
The growth rate of unhedged foreign currency loans and its share in relation to overall foreign currency loans are two of the indicators monitored to assess indirect foreign exchange risk. The performance of these indicators during 2020 H2 signals a slight increase of this risk. The stock of unhedged foreign currency loans expanded by around 2% during 2020 H2, and an increase of this stock was affected by loans granted to enterprises for investments in commercial real estate, which increased by 25%. The same performance was also observed in the stock of unhedged foreign currency loans to households. Nevertheless, given that the unhedged loans to households account for only 30% of the share of unhedged loans, the impact of growth of this portfolio on the increase of the overall stock of unhedged loans is limited.

At the end of 2020, the share of unhedged foreign currency loans against overall outstanding loans was 21% or 0.2 percentage points lower than at the end of 2020 H1. This decline is related to the performance of overall foreign currency loans that grew at a slower pace compared with loans in domestic currency. At the same time, the share of unhedged loans in the portfolio of foreign currency loans increased to 42% from 41% at the end of 2020 H1.

BOX 3 THE BANKING SECTOR AND UNHEDGED FOREIGN CURRENCY LOANS

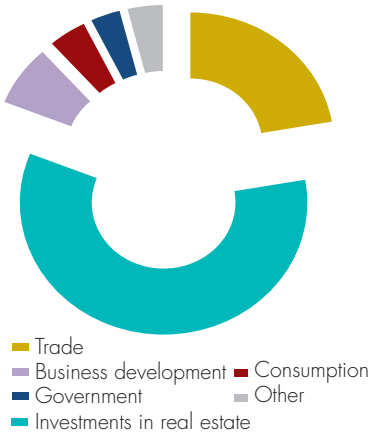
During 2020 H2, unhedged foreign currency loans expanded by ALL 3 billion, reaching ALL 128 billion, due to an increase by 6% of unhedged loans in European currency. Loans to enterprises constitute 66% of outstanding foreign currency loans unhedged from the exchange rate risk, while loans to households and to government account for 30% and 4%, respectively. The increase of outstanding unhedged loans is mainly related to the expansion by 2.4% of unhedged loans to enterprises. Unhedged loans to households during the period increased by around 2.7%, while those to government did not change. In annual terms, unhedged foreign currency loans contracted by 2.5%, due to a decline of loans to enterprises and loans in US dollars.*

Chart 50 Performance of unhedged foreign currency loans



Source: Bank of Albania.

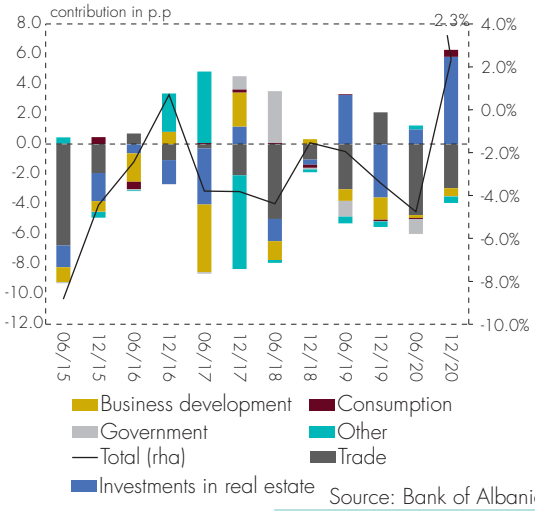
Chart 51 Unhedged foreign currency loans by purpose of use, %



Source: Bank of Albania.

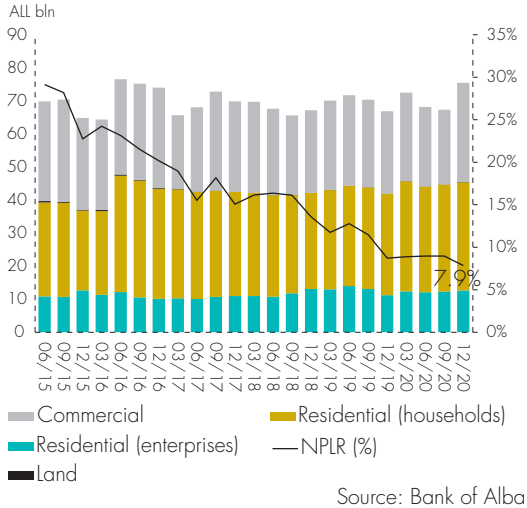
Unhedged loans granted for investments in real estate continue to account for the main share (around 60%) of total unhedged foreign currency loans, followed by loans for trade (20%). The rest of the unhedged foreign currency loans were granted for business development, consumption and other purposes. The performance of outstanding loans unhedged against the exchange rate risk during the period was mainly affected by the expansion of unhedged loans for investments in real estate and, at a lower scale, by the expansion of loans for consumption. These were the only categories of unhedged loans that registered an increase (by around 11%) over the period.

Chart 52 Six-month performance of unhedged foreign currency loans (contribution by sector)



Source: Bank of Albania.

Chart 53 Unhedged foreign currency loans for real estate and its quality



Source: Bank of Albania.

Unhedged loans for real estate are granted in the purchase of residential, commercial real estate and land. Unhedged loans for residential real estate granted to households continue to have the main share (43%), which expanded by 3% during the period. Nevertheless, the main contribution to the performance of unhedged loans for real estate over the period came from the expansion by 25% of unhedged loans for commercial real estate. The share granted for investments in commercial real estate to the total unhedged loans for real estate increased from 35% to 40% over the period.

* *Outstanding euro loans, when the borrower's income is in Albanian lek, account for 90% of the outstanding unhedged foreign currency loans.*

NEW LOANS

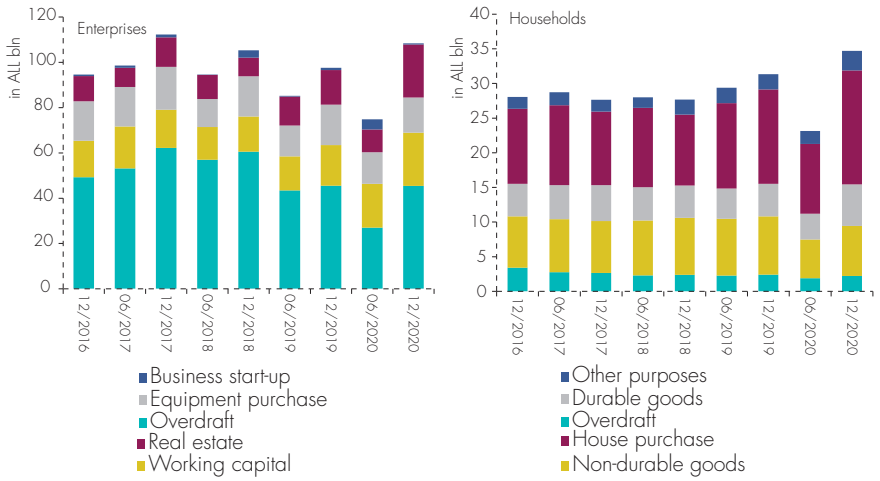
New loans granted by banks during the period were around 50% higher than 2020 H1; the increase is observed in both loans in lek and in foreign currency.

Enterprises received more loans for investments in real estate and "overdraft" loans, while households received more loans for housing purchases.

New loans granted by banks during 2020 H2 registered around ALL 150 billion. This flow was around 50% higher compared with new loans granted during 2020 H1 and around 12% more than new loans reported during 2019 H2. The increase in flow is observed in both new loans in lek and new loans in euro. The main contribution to the increase of the flow of new loans came from the business sector, which attracted a flow around 44% higher compared with 2020 H1. During 2020 H2, enterprises received more new loans for real estate investments, mainly commercial, and new loans in the form of "overdraft." The latter continues to account for the main share of new loans to enterprises (around 40%) and the higher demand for this type of loan over 2020 H2 is related to enterprises' short-term needs to finance the recovery of activity suspended during the period March-May.

New loans to households registered 50% higher than those granted during 2020 H1. This development was affected by an increase in the flow of loans for housing purchases and those for consumption of durable goods. New loans for housing purchases account for the main share of new loans to households (47%). Around 70% of new loans to households were in the domestic currency.

Chart 54 New loans to enterprises (left) and households (right) by purpose of use



Source: Bank of Albania.

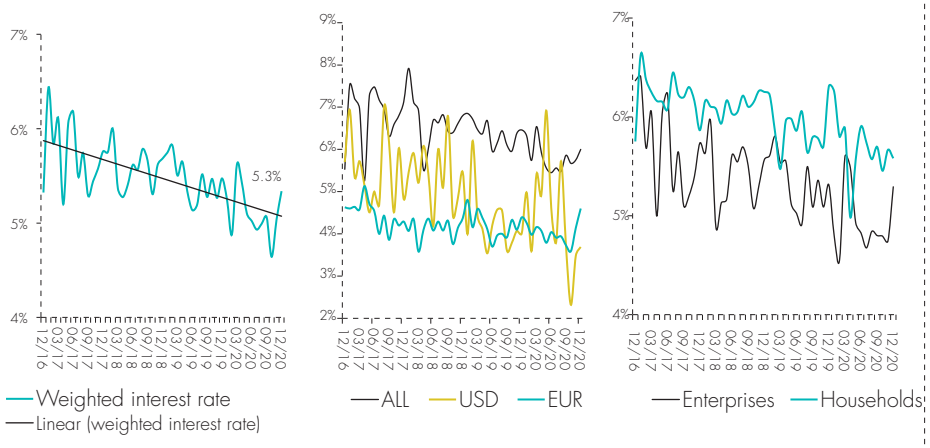
The weighted interest rate on new loans granted over the period[20] registered a decline compared with the previous six-months. Compared with the average weighted rate of new loans granted during 2020 H1, the average weighted rate of new loans granted during 2020 H1 was around 0.2 percentage points lower. In December, the weighted interest rate was 5.3%, while over the period it fluctuated to around 5.0%. In 2020 Q4, there was a rise in the average weighted interest rate. The biggest fluctuations were noted in the interest rate for new loans in foreign currency and that of new loans to enterprises.

The weighted interest rate on new loans granted over the period registered a decline.

Analysis of interest rates by currency indicates that the interest rate of new loans in lek continues to register higher levels than the other two currencies (euro and US dollar) and this interest rate has shown an upward trend in 2020 H2. Compared with the previous year, the interest rate of new loans in lek fluctuated around a lower average value and in December 2020 this rate registered 6.0% from 6.5% in the previous year. The interest rate on new loans to households continues to remain higher compared with the interest rate on loans to enterprises. During the period, this rate fluctuated around the value of 5.6%, and the value registered in December 2020 remains under the level registered in June 2020. The average interest rate on new loans to enterprises fluctuated around an average value of 4.9% in 2020 H2[21].

[20] *Calculated as six-month average.*
[21] *Its value in December 2020 is more than its June 2020 level.*

Chart 55 Weighted interest rates on new loans, in %; aggregate rate (left); rate by currency (middle); rate by entity (right)



Source: Bank of Albania.

BOX 4 RESTRUCTURED LOANS IN 2020

The value of restructured loans in 2020 was around ALL 23 billion, from which ALL 21 billion (90%) was the value of loans restructured during 2020 H2. In most cases restructuring is realised upon a client's request. The restructured loans during the period accounted for 3% of the total overall outstanding loans and half of the stock of non-performing loans. The majority of restructured loans, or around 90%, are loans granted to enterprises. Restructured loans over the period account for around 5% of the outstanding loans granted to enterprises.

From the sectors of the economy by type of manufacturing activity, the industry sector is the one with the highest demand for loan restructuring. Borrowing enterprises of the industry sector have restructured around 11% of the overall stock of loans, and the restructured loans for this sector accounted for around 40% of the entire volume of loans restructured by the banking sector over the period. During 2020, the industry sector was one of the sectors with the strongest decline in production and with the highest contribution to the contraction of the domestic economy. The decline of industry's production by 6% has also challenged the solvency of borrowing enterprises in this sector. The year 2020 was difficult for the tourism and trade sectors as well. Both of these sectors registered a contraction compared with the previous year and the effect of economic decline is also reflected in the performance of loans for those sectors. Restructured loans for these sectors were around ALL 6 billion, ¼ of the overall restructured loans for the year. The negative impact of the pandemic was noted in particular in the performance of loans for tourism given that around 11% of the loans stock granted to this sector was subject to restructuring.

The banks' reporting show that restructured loans were mainly loans denominated in Euro (around 42%), while the rest were loans denominated in US dollar and domestic currency.

Loans affected by restructuring were for the most part classified as performing loans, whereas loans classified as non-performing were restructured as well. Standard loans account for the main share of restructures but the volume of restructured loans was only 2% of outstanding standard loans. Regarding the "special mention" class restructuring during 2020 H2 was 19% of loans stock. The value of restructures for non-performing loans during 2020 H2 was relatively lower (around ALL 5 billion), but as a share against outstanding non-performing loans, this volume was considerable (around 9%).

The main forms of restructuring used by banks were extension of maturity term, capitalisation of interest and/or charges payable for default, changes to principal and assigning a grace period for the principal or credit interest. Over 60% of restructured loans were carried out in the form of maturity extension. The rest was carried out through capitalisation of interest or charges payable for default, providing an overdue period for the principal or interest and changing the principal. In the next few periods, the Bank of Albania will continue to follow and analyse attentively the progress of loans requested and approved for restructuring through regular reporting and special banks' reporting, not only to monitor the effects of the pandemic on the performance of credit portfolios and the financial situation of domestic enterprises, but also as a standard part of its analysis on credit quality.

Table 9 Data on restructured loans during 2020

	06/20	12/20	Share*		06/20	12/20	Share*
% of restructured loans				% of restructured loans			
Entity				Restructuring form			
Households	18	11	1	Extension of maturity term	55	63	
Enterprises	82	89	5	Capitalisation of interest and/or charges payable for default	5	10	
Large	28	62	7	Changes to payment frequency	0	3	
Medium-sized	21	8	2	Changes to principal	0	13	
Small	33	20	5	Period of principal/ interest granting	29	9	
Currency				Other	10	2	
Lek	27	25	2				
Foreign currency	73	75	5				
Classes				Sectors of the economy			
Standard	38	56	2	Trade, automobile repair	27	13	2
Special mention	31	23	19	Construction	1	4	2
Substandard	5	7	11	Industry	37	42	11
Doubtful	11	7	11	Energy, gas, water	0	6	5
Loss	16	7	7	Agriculture, Forest, Fishing	3	2	5
Destination				Hotels and restaurants	8	11	11
Loans to enterprises	82	91		Other	24	22	9
Mortgage credit	12	5					
Consumer credit	5	4		Restructured credit (flow, ALL bln)	2.4	20.9	3

Source: Bank of Albania.
**Share in outstanding loans.*

4.1.1.5 Deposits

Deposits growth was high during the period, mainly supported by households' demand deposits and lek deposits. The share of demand deposits and current accounts continues to expand against the decline of the share of time deposits.

Deposits held by the banking sector registered high growth rates during the period. The growth is distributed almost equally between the households and enterprise sectors and between lek and foreign currency deposits. Time deposits continued to contract, while the highest growth during the period of deposits by maturity was registered in current accounts, followed by demand deposits. At the end of December, the level of deposits registered ALL 1,286 billion. Deposits grew by ALL 56 billion during the period and by ALL 93 billion compared with the previous year. Around half of the total deposit stock consists of time deposits, which declined by around ALL 14 billion over the period. The share of time deposits to total deposit stock continued to decline in favour of demand savings instruments.

Table 10 Data on the performance of deposits by maturity, sector and currency

		December 2020		December'20/June'20		December'20/December'19	
		ALL bln	% to total	Change (%)	Contribution in p.p.	Change (%)	Contribution in p.p.
By maturity	Current account	495	39	12	4	20	7
	Demand deposits	173	13	11	1	16	2
	Time deposits	600	47	(2)	(1)	(2)	(1)
By entity	Public sector	33	3	1	0	22	0
	Enterprises	192	15	15	2	18	2
	Households	1,061	82	3	2	6	5
By currency	Lek deposits	637	49	5	2	10	5
	FX deposits	650	51	4	2	6	3
	Deposits stock	1,286	100	5	5	8	8

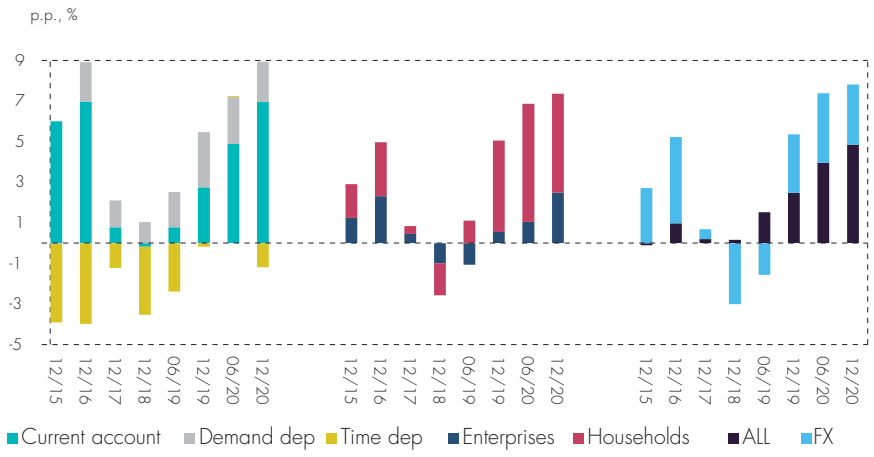
Source: Bank of Albania.

The average rate of annual growth for stock deposit over the period was around 8%, whereas in 2018 and 2019 this rate has not surpassed +0.5%. Lek deposits have maintained positive rates in annual terms since the first months in 2019 and their expansion was especially fast during the last months.

Over the period, foreign currency deposits increased by 4.2% from the level registered at the end of the first quarter, contributing to the overall growth of base deposits to the same level as lek deposits. Fluctuations in the exchange rate of lek against the US dollar and the Euro during the six-months has not made a considerable contribution to the equivalent value in lek of deposits in foreign currency. This impact, in contrast with the one calculated for the first six-months, recorded a negative but insignificant value in relation to the total volume of deposits in foreign currency.

Growth in current accounts and demand deposits continued during the period as well. Compared with the previous year, during this period current accounts and demand deposits expanded by 20% and 16%, while compared with the previous period, these deposits were 12% and 11% higher, respectively. Time deposits had maintained almost the same level since the end of 2018, but declined by ALL 13.6 billion during 2020 H2. Interest rates for time deposits in lek and in foreign currency continued to be low and their average rate did not record significant changes during 2020 H2.

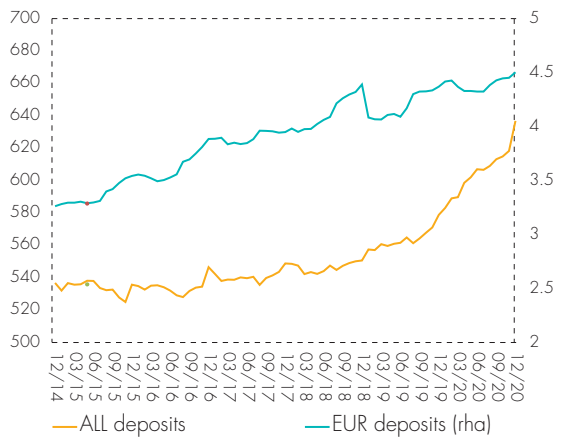
Chart 56 Performance of deposits by maturity, sector and foreign currency (contribution to the annual interest change)



Source: Bank of Albania.

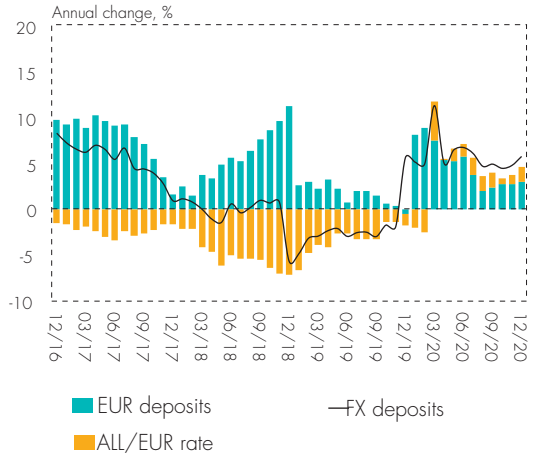
Lek deposits contributed for the most part to the annual growth of deposits during 2020 H2 compared with those in foreign currency. During the past five years, lek deposits as well as euro deposits, which account for 90% of foreign currency deposits, have maintained a positive and comparable growth trend, but the growth in lek deposits has been faster during 2020. The annual growth of euro deposits has been continuously positive, but the growth rate of foreign currency deposits has also been affected by the statistical impact of the exchange rate. The latter, given the strong appreciation of the domestic currency during 2018-19 against the two main foreign currencies, caused the stock of foreign currency deposits converted in lek to register negative growth rates over this period. During the period, the statistical impact of the exchange rate over the reported value of deposits was negative by around ALL 8 billion.

Chart 57 Performance of foreign deposits in lek and Euro (in bln units)



Source: Bank of Albania.

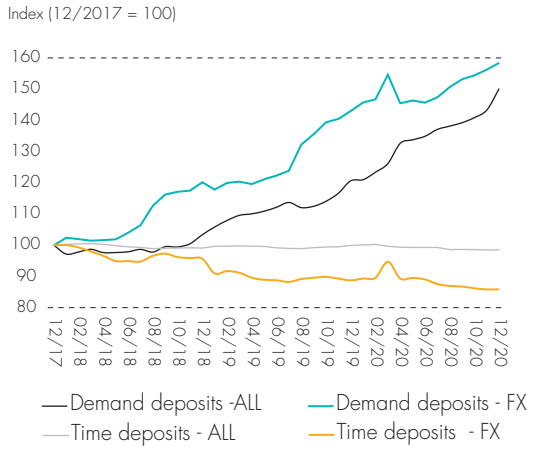
Chart 58 Exchange rate impact in foreign currency deposits



Source: Bank of Albania.

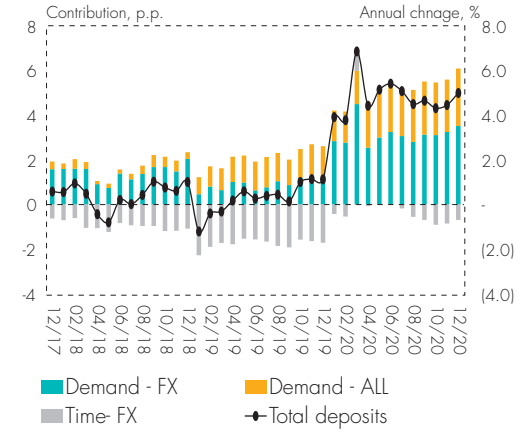
The detailed data of households' deposits by currency and maturity show that time deposits in lek have slightly declined, while demand deposits in foreign currency reflect a notable downward trend. The growth of demand deposits[22] is distributed equally between lek deposits and foreign currency deposits. Since the end of 2017, the stock of demand deposits of households in foreign currency expanded by around 33%, while those in lek deposits expanded by over 50%. The decline in the stock of demand deposits for households over this time frame is concentrated in foreign currency deposits.

Chart 59 Performance of households deposits by maturity and currency (index)



Source: Bank of Albania.

Chart 60 Performance of households deposits by maturity and currency (contribution in annual growth)



Source: Bank of Albania.

Interest rates for demand deposits in lek fluctuated around the 0.7% level during 2020 H2, not registering major changes during the period. Regarding time deposits in euros, the average interest rate of demand deposits was almost

22 *To facilitate the interpretation current accounts are included as well.*

unchanged compared with the previous period, while in US dollar deposits there was a slight increase in the average interest rate.

4.1.2 RISKS TO THE ACTIVITY OF THE BANKING SECTOR

4.1.2.1 Credit risk

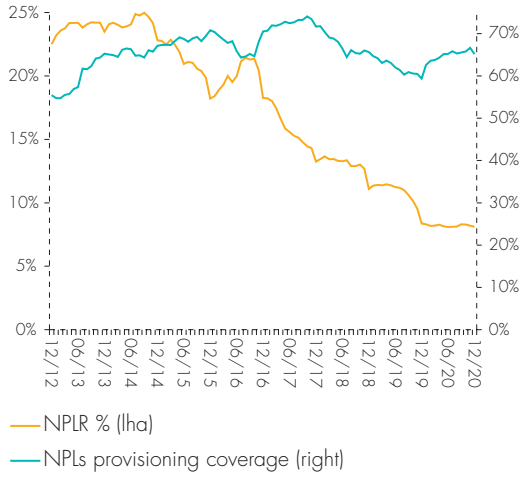
The easing measures implemented by the Bank of Albania, initially to extend loan instalments as part of the Moratorium, and then to restructure them, affected the low fluctuation of the non-performing loans ratio (NPLR) during the period. NPLR was 8.1% at the end of the year, from 8.4% in the previous year. During the period, the increase of the non-performing loans ratio was comparable to the overall growth rate of credit (around 3%). In absolute value, non-performing loans increased by ALL 1.6 billion, reaching around ALL 50 billion at the end of the year. This increase reflected the introduction of new classes of non-performing loans and at the same time a slowdown of payments in these classes. The values of the latter were around 30% lower compared to payment settlements in 2019 H2. The process of writing off lost loans from banks' balance sheets continued also in 2020, but the quantity of write-offs was considerably lower compared with the previous year. From the total of ALL 3 billon, around ¾ was written-off from balance sheets in 2020 H2. The written-off loans were loans mainly disbursed to enterprises and granted in lek.

The non-performing loans ratio remained almost unchanged during the period. The value of non-performing loans recorded an increase similar to the growth ratio of loans, affected by new flows and lower payments. Within the Supervisory Council, the share of lost loans has increased.

The increase of the provisioning ratio and collateral coverage ratio signal that banks are working to strengthen safeguards against credit risk.

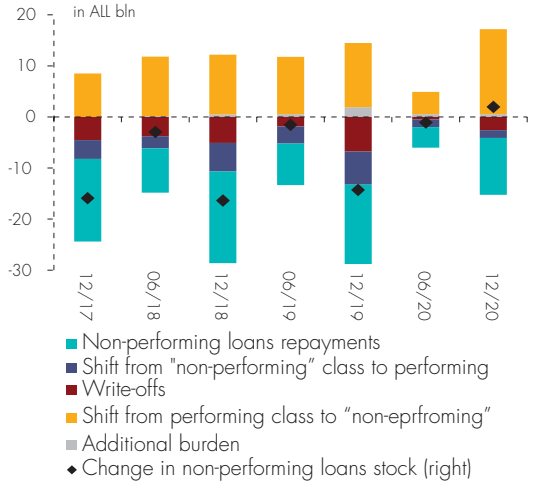
During January 2015- December 2020 period, banks wrote off around ALL 70 billion of lost loans from their balance sheets. Albanian banks continued to provision for non-performing loans and given the faster increase of provision reserves compared with the non-performing loans stock, the provisioning ratio reached 65% from 59% in the previous year.

Chart 61 Non-performing loans ratio and provisioning



Source: Bank of Albania.

Chart 62 Contribution in the semi-annual change of non-performing loans stock

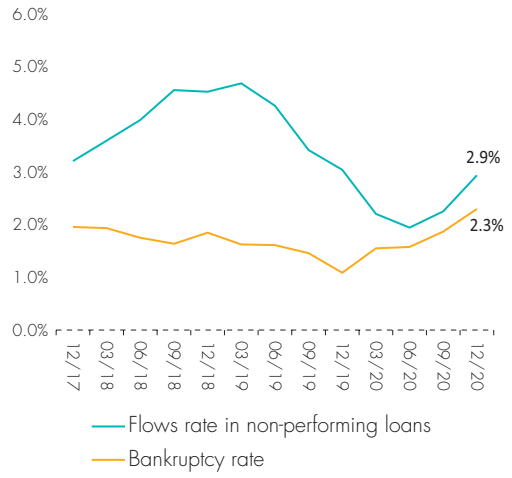


Source: Bank of Albania.

Over the last year, there has been a share shift within outstanding non-performing loans, from the "substandard" and "doubtful" classes to the "lost loans" class. The share of lost loans in the outstanding non-performing loans reached 46% from 36% in the previous year. Compared to the previous year, the quality of credit has deteriorated for the category of long-term loans, loans to households and loans in the domestic currency. The highest values of NPLR are reported for loans to enterprises (9.9%), foreign currency loans (8.9%) and long-term loans (8.5%).

The gradual decline in credit portfolio quality during 2020, resulting from the economic downfall and the financial difficulties of businesses due to the pandemic, is also reflected in the slight, but notable increase of the three complementary indicators of credit quality which are: the flow of non-performing loans ratio[23]; the bankruptcy ratio[24]; and the recovered non-performing loans ratio[25]. Starting from 2020 Q2, the flow of non-performing loans ratio has increased and at the end of the year this ratio reached around 3%, from almost 1% at the end of 2019. It is necessary to keep monitoring this indicator given the waning effects of the easing measures undertaken by the Bank of Albania during 2020 for borrowers in financial difficulties. Another important indicator of the quality of credit portfolio is the accumulation ratio of lost loans against overall loans. The value of new lost loans accumulated in banks' balance sheets during 2020 was twice as high as the flow of 2019. This development is reflected in the increase of the bankruptcy rate to 2.3% from 1.1% in the previous year, whereas since the end of 2017 this ratio has not exceeded 2%. At the same time, a significant decline in the recovery ratio of non-performing loans was observed in 2020. This ratio fell at 6% from 20% in the previous year and stands below all the values of this indicator since the end of 2017.

Chart 63 Non-performing loans ratio and bankruptcy ratio



Source: Bank of Albania.

Chart 64 Recovered non-performing loans ratio

Source: Bank of Albania.

23 *The flow of new non-performing loans during the period against outstanding regular loans at the end of the period.*

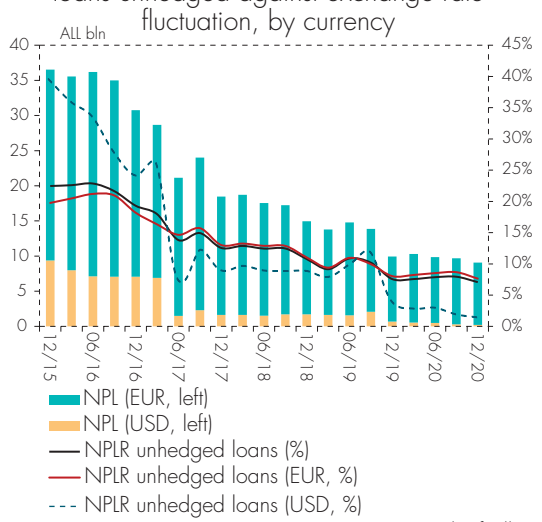
24 *The flow of new lost loans over one year against the overall outstanding loans at the end of the period.*

25 *The flow of non-performing loans which moved to performing classes over the year against the outstanding non-performing loans at the end of the period.*

Foreign currency loans unhedged from exchange rate fluctuations have improved notably compared to the end of the previous six-months and the previous year. The non-performing loans ratio for this loan fell to 7.1% at the end of 2020 compared with 7.9% in June and 7.6% in December 2019. The improvement of unhedged credit quality was affected by a reduction of the stock of non-performing loans in euro, by sectors and in all its forms of use. The main share[26] in the outstanding loans unhedged from exchange rate fluctuations continues to be held by loans for investments in real estate and the NPLR for this category of loans declined by around 8% from 9% one year ago.

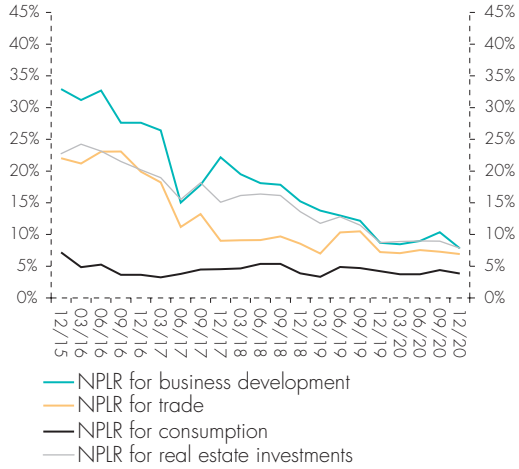
The quality of credit granted by Albanian banks for non-residents continues to be good, since the NPLR remains close to 2% and recorded a slight improvement during the period. However, it should be emphasised that the entire stock of non-performing loans held by non-residents is currently classified under the "lost "class and is represented by loans disbursed to businesses in euros.

Chart 65 Non-performing loan performance for loans unhedged against exchange rate fluctuation, by currency



Source: Bank of Albania.

Chart 66 Non-performing loans for unhedged loans against exchange rate fluctuations, by purpose



Source: Bank of Albania.

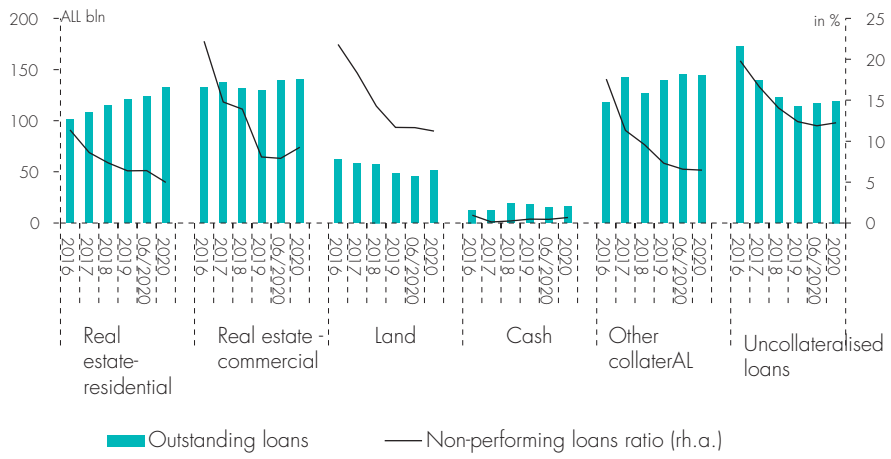
During 2020 H2, the level of hedging of non-performing loans with reserve funds did not register changes, while in comparison with one year ago it increased by 6 percentage points, to 65%, due to the faster increase of reserve fund stock compared with the increase of the non-performing loan stock. The provisioning ratio for individual banks fluctuates between 50% and 85% range. Capital coverage of net non-performing loans[27] fell to 8.8 times from 9.1 times at the end of 2020 H1. This decline was mainly driven by an increase of net non-performing loans by about 4%. In December 2020, the net non-performing loans ratio registered 2.8%.

The capital coverage ratio of loans increased slightly during the second half of the year, reaching 80% at the end of the year. This ratio increased by around

[26] *Around 65% of the total.*
[27] *Non-performing loans after discounting provisions.*

10 p.p. during the period of March 2017- December 2020. Loans with collateral in the form of real estate account for the main share of collateralized loans (around 70%) and 54% of overall outstanding loans. This part of the credit portfolio increased by 5% during 2020 H2, while loans unhedged by any form of collateral increased by 2%. The collateralized credit quality has slightly declined during the period but the NPLR for this type of loan (7.2%) continues to remain below the NPLR of overall credit and around 5.5 p.p. below the uncollateralized NPLR, which marked 12.3% at the end of the year. Among the portfolios collateralized with various types of collateral, loans collateralized with residential real estate, land and other collateral have the best quality and have registered positive developments in 2020. At the same time, for collateralized loans and loans collateralized with commercial real estate an increase of NPLR is observed, particularly during the second half of the year.

Chart 67 Outstanding loans and non-performing loans ratio by collateral



Source: Bank of Albania.

4.1.2.2 Liquidity risk

The liquidity position of the banking sector remains at good levels and liquidity indicators continue to remain notably above the regulatory limits.

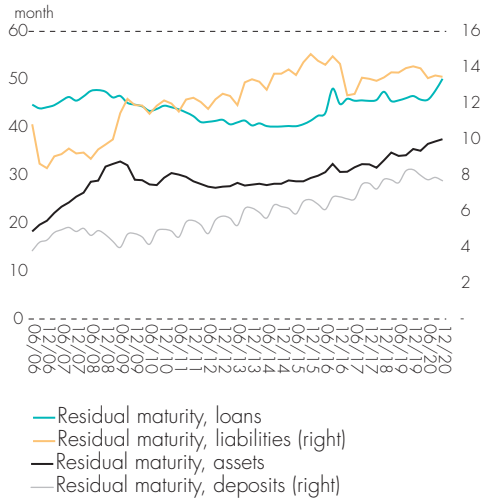
The negative gap remaining between assets and liabilities for the first two maturity baskets has deepened due to expansion for the period of 3 months to 1 year.

The liquidity position of the banking sector is assessed at satisfactory levels. The liquidity indicators, both in lek and foreign currency, stand above the minimum regulatory ratios. Deposits remain the main source of funding, which cover twice the volume of sector's loans. At the end of 2020, the "loans/deposits" ratio registered 47.3%, slightly decreasing during the period. At the end of the year, this ratio stands at 47.6% for the national currency and 47.1% for foreign currency. Although with fewer changes over the period, compared with the previous year these ratios have declined considerably as a result of a strong growth of deposits during 2020.

During the period, liquid assets of the banking sector increased by ALL 40 billion at ALL 550 billion. Liquid assets to total liabilities in banks' balance sheets remain high. At the end of 2020, its value was 34.9% with an increase of 1.6 percentage points during the period. This performance reflects a significantly

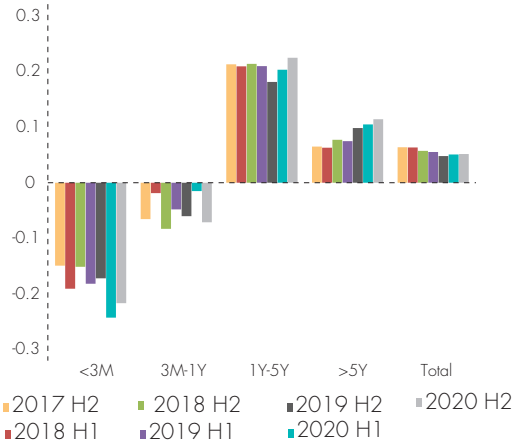
high-paced increase of liquid assets in banks' balance sheets compared with total assets. For the same reason, the ratio of liquid assets to short-term liabilities increased by 1.4 percentage points, during the period, to 47.5%.

Chart 68 Average residual maturity



Source: Bank of Albania.

Chart 69 Maturity mismatch between assets and liabilities*



*Off-balance sheet assets and liabilities are also included.
Source: Bank of Albania.

Although banks are operating under ample liquidity conditions, the negative gap between assets and liabilities by segments of residual contractual maturity, vis-a-vis the total assets in short-term, remains high. For the period up to 3 months, the negative gap between assets and short-term liabilities by segments of residual contractual maturity[28] decreased to 22% from 24% of assets. On the other hand, this gap has expanded significantly for the maturity period of 3 months to 1 year reaching 7% from 2%, and has registered small relative expansions for the gaps of 1-5 years and over 5 years. The overall gap continues to be positive and has not registered notable changes compared to the previous periods, supported by high positive values for longer-term maturities. This gap of 2-3 years has fluctuated around 5% of assets in the banking sector.

During the period there was an increase in the mismatch between average maturity of assets and liabilities, due to an increase in the average maturity of assets. At the end of the year this mismatch was around 24 months, from 23.1 months at the end of the previous six-months. Deposits' residual maturity, which represents the most significant category of liabilities, remained almost unchanged during the period, at 7.7 months. Residual credit maturity increased significantly from 45.7 months to 50.1 months, reflecting the banking sector's propensity to grant credit for longer-term periods. Similar to the previous six-months, the banking sector did not report funding lines by parent groups.

[28] *Calculated as the ratio of 'difference between assets and liabilities' to 'total assets' for each basket of residual maturity. Off-balance sheet items are included in the value of assets and liabilities.*

4.1.2.3 Market risks

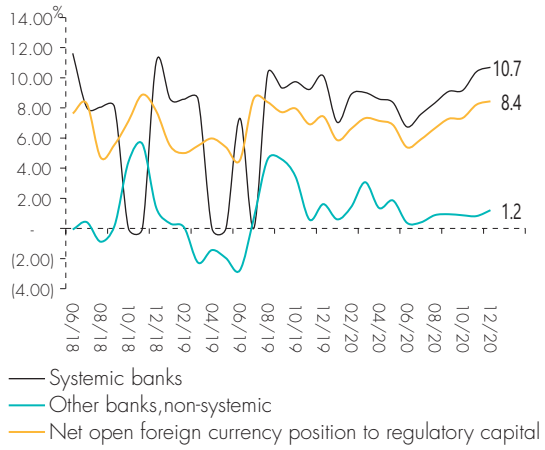
EXCHANGE RATE RISK

The net open foreign currency position of the banking sector increased but remains at limited levels and significantly below the regulatory limit. The banking sector's exposure to indirect exchange rate risk decreased due to a decline in exposure of banks with systemic risk.

The net open foreign currency position indicates an increasing but limited exposure to the direct impact of exchange rate fluctuations on the balance sheet. The aggregate indicator for all banks, as well as the indicator for group of banks by importance has very low values compared with the upper limit of 30% of regulatory capital defined by the respective regulation. At the end of 2020, the open foreign currency position marked 8.4% of regulatory capital of the banking sector, from 5.3% at the end of the previous six-months. Performance is determined by the group of systemic banks, which have maintained an open foreign currency long position. This position was as much as 10.7% of their regulatory capital, from 6.7% six months ago. The group of other banks presents a lower exposure to the exchange rate, with a net open foreign currency long position as much as 1.2% of their regulatory capital.

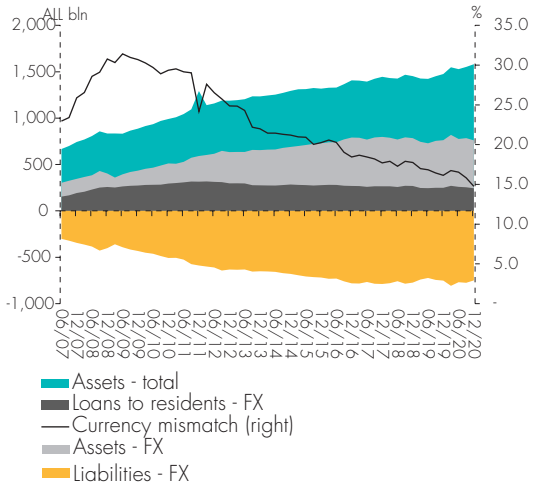
The exposure of the banking sector to indirect exchange rate risk decreased slightly compared to the previous six months and the previous year. The foreign currency mismatch[29] for all currencies decreased to 14.7% from 16.5% and 16.1% at the end of both previous periods. Although foreign currency assets and liabilities decreased with the same relative rate (about 2%), the mismatch index reflected the decline by 6% of foreign currency credit for residents. The performance of this part of the credit portfolio determines the performance of indirect risk from exchange rate fluctuations as well. The overall index continues to dominate the Euro index, which has also slightly declined during the period.

Chart 70 Open foreign currency position to regulatory capital for the sector and groups



Source: Bank of Albania.

Chart 71 Performance of Indexes components for the banking sector

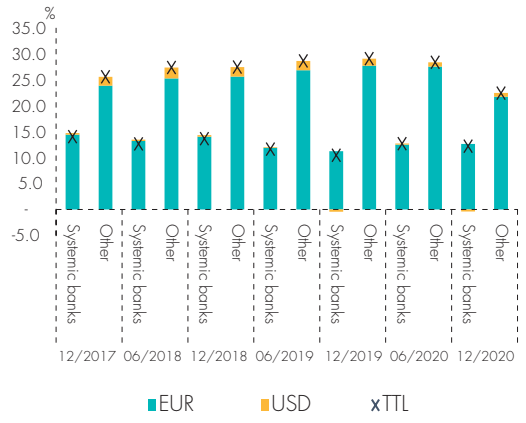


Source: Bank of Albania.

[29] *The foreign currency mismatch indicator measures the hedging rate of the banking sector's liabilities with assets offset by resident credit in foreign currency. A low value of this indicator's ratio to assets shows a low exposure to fluctuations in the exchange rate. The methodology for calculating the mismatch indicator has been published in the Financial Stability Report 2016 H1.*

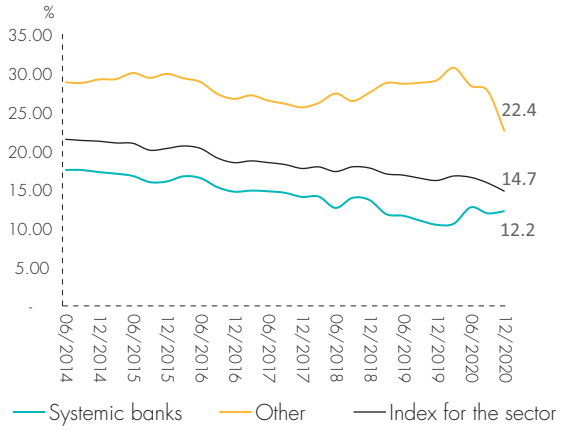
The group of systemic banks continues to make the main contribution to the performance of the foreign currency mismatch index. For this group of banks, the indirect exchange rate risk has slightly decreased during the period, but has increased compared to the previous year. At the end of the period, the index for systemic banks registered as much as 12.2% of assets from 12.7% in the previous period and 10.4% in the previous year. By currency, the main contribution of this group was made by the decline of 0.6 p.p. by the US dollar index to the level of -0.4%, while the index of the European currency increased slightly by 0.1 p.p. against the previous six months to the level of 12.6%. During the period the index of the group of non-systemic banks recorded 22.4% of assets. Compared with the previous six months and the previous year, this indicator has decreased by about 6 percentage points.

Chart 72 Currency mismatch by groups and currency



Source: Bank of Albania.

Chart 73 Performance of foreign currency mismatch indicator for bank groups



Source: Bank of Albania.

INTEREST RATE RISK

The exposure of banks to interest rate risk decreased during the period and remains at low levels, given that the relevant indicator has a very low average compared with the regulatory limit of 20%. The weighted total net position on the bank's balance sheet against regulatory capital of the banking sector recorded 4.4% at the end of the year. The main contribution to the decrease of the indicator was made by the weighted spread of assets with fixed interest rate liabilities (FIR)[30]. The net position for assets and liabilities with variable interest rate (VIR) recorded a slight decline as well. Given that the total net position is positive and the volume of claims that collect interest is greater than the liabilities for which interest is paid, a decline in the interest rates would expose the banking sector to the risk of immediate reduction of interest revenues. Although the interest rate risk remains present, there is limited room for further decrease of interest rates, while the regulatory capital hedging of the total net position of the banking sector is 25 times, compared to 5 times the

The banking sector's exposure to interest rate risk decreased during the period. The indicator of exposure to this risk remains significantly below the regulatory limit.

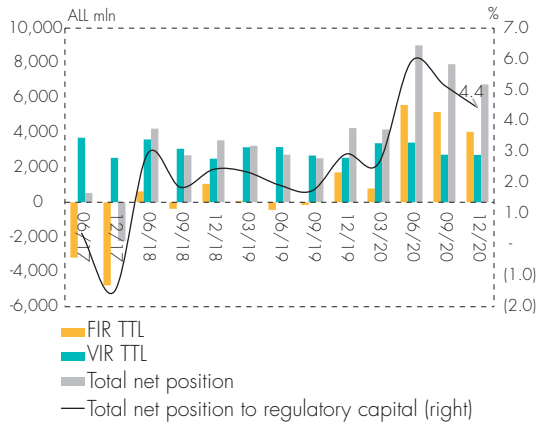
The banking sector is more exposed to the interest rate risk for the position in Euro, fixed interest rate and for medium and long-term maturity.

[30] *Positions sensitive to interest rate are classified in positions with fixed interest rate (FIR) and positions with variable interest rate (VIR), by maturity and currency.*

hedging provided for in the regulatory framework. The current values of the net position indicators suggest that the potential cost which may come to the banks due to the further decrease of interest rates can be easily absorbed.

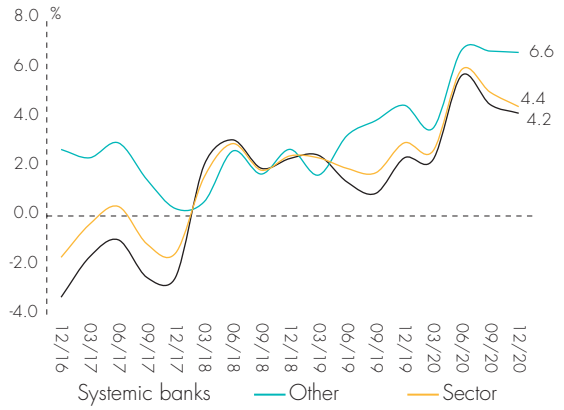
During the second half of the year, banks' exposure against interest rate risk has decreased consistently, but compared to the previous year, this exposure has increased. Systemic banks have a lower exposure compared with non-systemic banks, while for both groups the exposure has declined during the second half of the year. Compared to the previous year both bank groups present a higher exposure to the interest rate risk[31]. For systemic banks the exposure of assets and liabilities to both fixed and variable interest rate fluctuations is approximately 2% of the regulatory capital. For non-systemic banks, the exposure is higher to fixed interest rate fluctuations (around 6%) while exposure to variable interest rate fluctuations is almost insignificant.

Chart 74 Weighted total net position in bank's balance sheets against regulatory capital, in %



Source: Bank of Albania

Chart 75 Performance by groups of weighted net position against regulatory capital, in %



Source: Bank of Albania

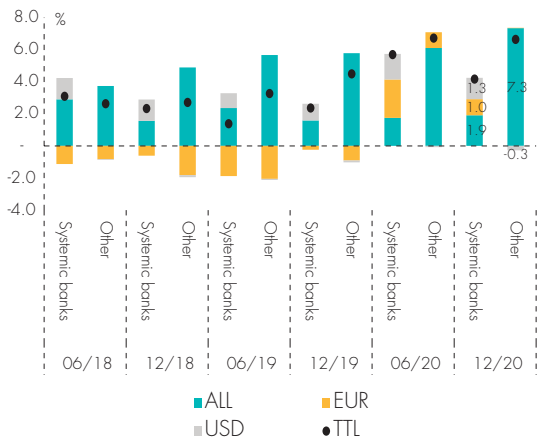
The decline of the total net position to regulatory capital was dictated by a decrease of 1.3 percentage points of the net position of the European currency, which was as much as 0.8% of the regulatory capital of the banking sector. The determinant of this position was the net position in euro for systemic banks, which recorded 1.0% during the period, from 2.4% six months ago. The exposure indicator to interest rate fluctuations in the national currency recorded 2.8% of regulatory capital, maintaining the average rate of the previous 12 months. The group of systemic banks recorded a slight increase of the indicator in lek at 1.9% of regulatory capital compared with the previous six months and the previous year (1.8% and 1.6%, respectively). For the group of non-systemic banks, the entire exposure is in the national currency and the position indicator is as much as 7.3% of regulatory capital, while exposure in euro and US dollar is insignificant[32].

[31] *One year ago, the indicator recorded 4.5% of regulatory capital for other banks and 2.5% for systemic banks.*

[32] *Respectively 0.0% and -0.3% of their regulatory capital.*

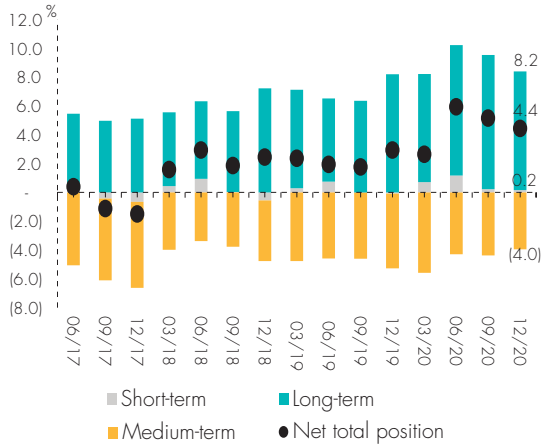
The largest exposure to interest rate fluctuations comes from the basket with long-term maturity, which marked 8.2% of regulatory capital, decreasing slightly from the level of the previous six months. However, the difference in the overall net position is affected mainly by the position of short-term maturity, which over the period fell to an insignificant level from 1.2% at the end of June. For instruments with medium-term maturity there is a reduction of the negative position between assets and liabilities sensitive to the interest rate at 4.0% respectively from 4.3% six months ago.

Chart 76 Gap by group and currency against regulatory capital, in %



Source: Bank of Albania.

Chart 77 Weighted net position by maturity against regulatory capital, in %

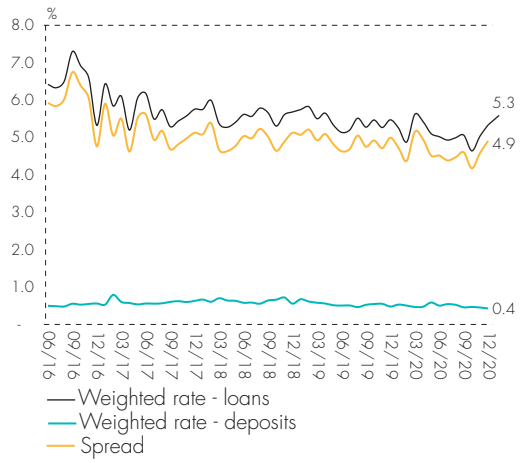


Source: Bank of Albania.

Indirect risk to interest rate change[33] was almost unchanged over 2020. During the first half of the year, there was a slight downward trend of the spread, while during the second half of the year, it increased by 0.4 percentage points. As a result of this performance, compared to the end of 2019, the spread marked only 0.1 percentage points, marking a decline. The overall spread between credit interest rate and deposit interest rate was 4.9%, only 0.1 pp lower than the level of 5.0% in the previous year. By currency, a positive contribution to this performance was due to the positions in lek and euro, while the US dollar position had a negative effect.

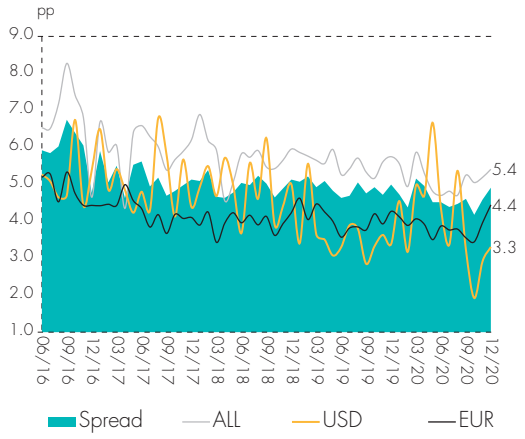
[33] *This risk refers to the impact that the change in the interest rate has on banks' clients. For example, despite the fact that the increase of the interest rate may have a positive impact on bank's balance sheet (due to positive value of the net position between assets and liabilities sensitive to the interest rate), this increase will have a negative impact on the solvency of bank's borrowers when loans are granted with variable interest rates (indirect risk).*

Chart 78 Loans and term deposits weighted interest rates and interest rates spread, in %



Source: Bank of Albania.

Chart 79 Spread of weighted interest rates of loans and term deposits by currency, in p.p.



Source: Bank of Albania.

4.1.3 BANKING SECTOR RESILIENCE

The results of the resilience test exercises for capital adequacy and for the liquidity situation realised for 2021-2022 show that the banking sector is stable against potential macroeconomic shocks and shocks that may cause temporary lack of liquidity in the banking sector.

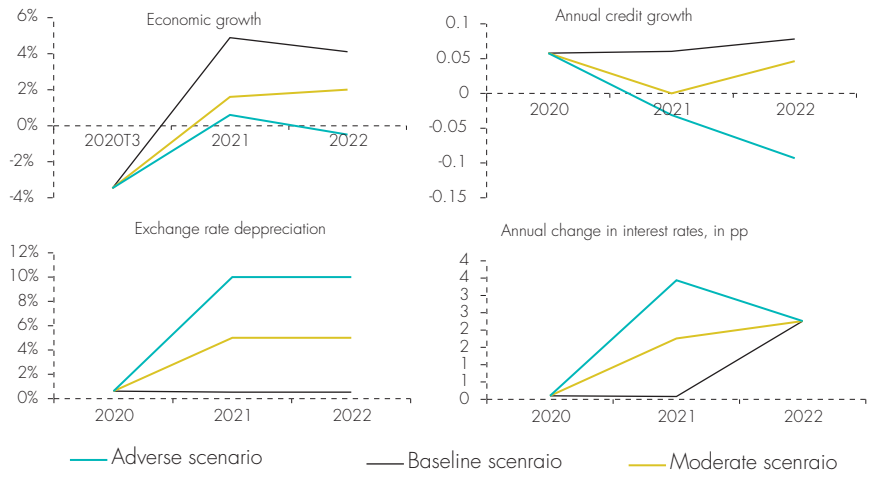
To assess the banking sector's resilience against shocks from the real economy or financial markets over a medium-term horizon, the Bank of Albania conducts resilience test exercises in a periodical manner. The resilience test for capital adequacy shows the degree of resilience of individual banks in terms of capital and aims to identify its adequacy to withstand supposed shocks on economic growth, credit, exchange rates and interest rates. The liquidity resilience test demonstrates the capability of banks to withstand a decrease of liquidity capacities through sales of liquid assets in a stressed market. Overall, these exercises carried out for the end of 2020 and extended in the period 2021-2022, show that the banking sector is stable against potential macroeconomic shocks and shocks to the liquidity situation.

For the first exercise which is based on three scenarios with an increasing escalation of negative shocks ("baseline, moderate, adverse") and with a corresponding decreasing escalation of the probability of occurrence, the banking sector proved able to maintain stability even in the adverse scenario, during the first year of the exercise. If this scenario extends also to the second year of the exercise, capital needs for specific banks are sensitive, affecting the overall capital level of the banking sector as well. The results of the resilience test exercises for liquidity show that the resilience of the banking sector against potential liquidity shocks is assessed as strong and better compared with the previous two years. The improvement of the banking sector resilience's was affected by a significant increase in expanded liquid assets that may be used as counter value capacities for the liquidity gap.

4.1.3.1 Stress-testing for capital adequacy

The stress test exercise for capital assesses the banking sector's resilience in terms of capital adequacy based on assumed economic and financial developments during the period 2021-2022. The exercise assumes that the bank does not increase the value of paid-in capital during the period. The exercise is performed based on three scenarios: a baseline scenario, a moderate scenario and an adverse scenario. The assumptions adopted for each of them are presented in the chart below. The last two scenarios have a lower probability of occurrence and more extreme assumptions. The assumptions of the stress test exercise include the effects of the pandemic shock, through potential channels of transmission in the domestic economy during 2021 and 2022. The scenarios are constructed under the assumption that the measures taken by the Bank of Albania on suspending the changes to non-performing loans classification and their provisions are repealed.

Chart 80 Assumptions to construct the stress test



Source: Bank of Albania.

The baseline scenario assumes positive economic growth in 2021 and 2022. In this scenario, economic growth is accompanied by credit growth and improvement in the credit portfolio quality based on the expected write-off process of lost loans from banks' portfolios. In the moderate scenario as well, a positive economic growth rate is assumed for both years of exercise, but this rate is lower compared to the baseline scenario rate; while in the adverse scenario a low positive rate is assumed for 2021, followed by an economic contraction in 2022.

Assumptions of weak economic performance in the moderate and adverse scenarios were coupled with relevant assumptions on depreciation of the exchange rate, increase of interest rates and a slowdown of credit growth to lending suspension or contraction. These developments are reflected in a deterioration of the credit portfolio quality. More specifically, until the end of

2022, the ratio of non-performing loans worsens by 5.7 p.p. for the moderate scenario and by 8.9% pp for the adverse scenario against the factual value of 8.1% at the end of 2022. The results on the increase of credit stock and non-performing loans ratio are also reflected in the decline of the capitalisation indicator for individual banks and the overall banking sector, particularly for 2022. In the adverse scenarios, the effects of declining credit quality are coupled with the effects of market and operation risks.

Stress test results in terms of capital adequacy show the following:

1. Developments during the first year of exercise and the needs for additional capital[34]:

- In the baseline scenario, the capital adequacy ratio (CAR) of the banking sector is stable and above the factual value at the end of 2020, reaching up to 19.8% at the end of 2021. For systemic banks, this ratio registers 20.5%, while for other banks it has a value of 17.9%. These developments reflect assumptions for a slight growth in credit for 2021, further improvement of the non-performing loans portfolio and a favourable exchange rate performance. Stress test results present a stable situation and high levels of capitalisation for the entire banking sector and individual banks, taking into consideration the minimum level required and additional regulatory requirements;
- In the moderate scenario, the banking sector's CAR increased by 14.7% by the end of 2021. The CAR for systemic banks is 15.4%, while for other banks this indicator is 12.7%. These rates continue to remain within the determined regulatory requirements, despite the scenario's assumptions for a weak performance of economic activity, a shortage of lending, depreciation of the national currency, a deterioration of credit portfolio quality and supposed losses in the securities portfolio. Based on the abovementioned assumptions and the test results, individual banks show the need for increased capital. More concretely, five banks fall below the required capitalisation level and they account for about 25% of the sector's assets. In this case, the need for additional capital is assessed to be around ALL 10 billion;
- In the adverse scenario, the banking sector's CAR dropped to 13% by the end of 2021. By groups of banks, CAR for systemic banks is 13.8%, while for other banks it dropped to 11%. Seven banks appear to be below the capitalisation level. The adverse economic developments included in this scenario assume contraction of lending and further deterioration of the credit portfolio quality. This scenario also assumes a loss in the securities portfolio and an increase of exposure to operational risk. In this case, the need for additional capital reaches ALL 22 billion.

[34] *Calculation for "additional capital" refer to the specific regulatory limit of CAR for each bank.*

2. Developments during the second year of the exercise and the needs for additional capital

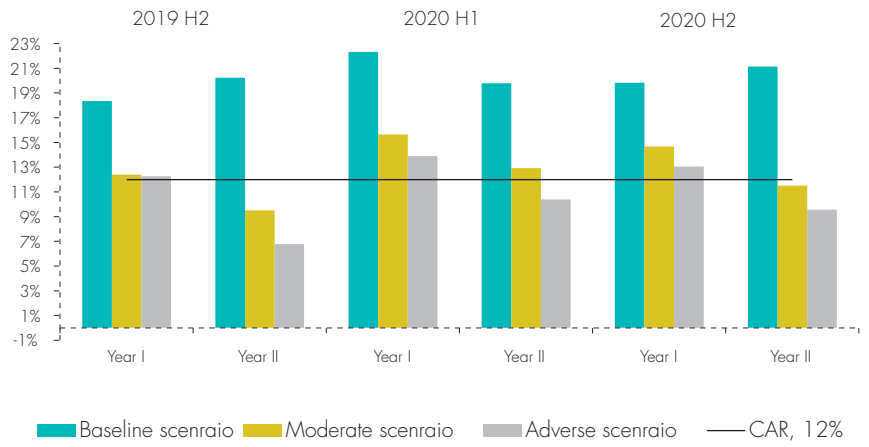
- In the baseline scenario, the capitalisation of banks appears stable registering 21.8% for systemic banks and 19.4% for other banks. The overall banking sector reaches a capitalisation rate of 21.1% at the end of 2022, based on assumptions for a positive credit growth as well as an improvement in the credit portfolio quality as well as a stable exchange rate during 2022.
- In the moderate scenario, the banking sector's CAR drops to 11.5% by the end of 2022. The group of systemic banks have a CAR of 12.2%, while for the group of other banks this rate is at 9.5%. This rate is affected by assumptions of a slower credit growth, a depreciation of the national currency, a worsened credit portfolio quality and loss from the securities portfolio. There are seven banks that appear below the level of capitalisation; and these banks account for 36% of the sector's assets. In this case, the needs for additional capital are assessed to be around ALL 31 billion;
- In the adverse scenario, the banking sector's CAR drops to 9.6% by the end of 2022 affected by the very extreme assumptions of this scenario. In this case, the group of systemic banks also register under-capitalisation, for which CAR falls to 10.4%, while other banks have an even lower rate of 7.4%. In this scenario, there are eight banks that fall below the required capitalisation level. The assumptions on very adverse macroeconomic developments and the significant contraction of lending, included in this scenario, impact the considerable deterioration of credit portfolio quality. This scenario also assumes losses in the securities portfolio and higher exposure to operation risk. In this case, the need for additional capital reaches up to ALL 45 billion.

The high levels of additional capital in the adverse scenarios for both years of the exercise, reflect mainly the extremity of assumptions used and have a low probability of occurrence.

If we compare the results of the stress test, we observe that the changes to the capital adequacy ratio after the application of shocks show some stability. Nevertheless, overall, it seems like the capital position of the banking sector appears low in the last exercise compared with the previous one. The fluctuation appears more pronounced in the results of the "baseline" scenario for the first year of the exercise. For this scenario, the main effect on the deterioration of results came from the group of other banks, while in the moderate and adverse scenarios the largest impact came from systemic banks. For the second exercise year, there is an improvement of capitalisation ratios for the baseline scenario, while these ratios appear lower for the two adverse scenarios. The main contribution to these results is attributed to the capitalisation ratio of systemic banks. Compared with the results of the previous year, there is a good capitalisation of the banking sector in the current period of the resilience

exercise, for three scenarios and for two exercise years, affected by the level of capitalisation of the group of other banks. Overall, the stress-test results are also affected by the factual situation of capital and the content of the balance sheet at the end of the period, existing vulnerabilities in the balance sheet and the degree of assumed shocks in each exercise.

Chart 81 Capital adequacy ratio, by stress test scenarios



Source: Bank of Albania.

4.1.3.2 Liquidity stress test

The purpose of the liquidity stress test is to assess the capability of individual banks and of the banking sector overall to withstand extreme but possible shocks in financing their activity. These tests aim to reveal weaknesses and deficiencies of the sector and particular banks in particular currencies, instruments and time periods; to assess banks' readiness to cope with extreme liquidity shortfall scenarios; as well as to assist the supervision authority to undertake specific policies that address liquidity management, including measures aimed at reducing exposures or creating specific reserves. The liquidity stress test is implemented according to the "top-down" approach with data reported by banks annually, at the end of the year. The exercise uses data on inflow and outflow forecasts of money according to the main instruments and for a time period constituted by 8 maturity baskets that cover a period from "up to 1 day" to "over 1 and up to 2 years."

The test is implemented for the Lek, Euro and US dollar and is supported on the condition that the liquidity outstanding on a currency may not be used to cover the liquidity shortfalls in other currencies, due to the probability of fast depreciation of the exchange rate during liquidity crises. In real situations, this is not a limiting element. For the calculation of the liquidity gap specific coefficients are used for the withdrawal of funding sources (of deposits) and for the reinvestment of assets (loans) by all the maturity baskets. For financing

sources, the coefficient shows only that part of the liabilities amount which matures in the relevant basket, and which will be withdrawn and will not be reinvested by clients. For money inflows, the reinvestment coefficient means that part of the amounts that mature in the relevant basket will be converted in money inflows and will not be reinvested by banks. A bank is considered as failing the stress test only if extended liquid assets, which are sold with haircuts defined by the exercise, shrink to the level when additional liquidity is needed by the Bank of Albania in the form of "loan for liquidity support."

RESULTS

The results of the stress test show that the resilience of the banking sector to possible liquidity shocks according to the data of November 2020, for the time horizon 2021-2022, is assessed as strong and appears better compared to the previous year.

The improvement of the banking sector's resilience was influenced by an increase of about 30% in the expanded liquid assets that may be used as counterweighting capacities of the liquidity gap. The simple gap between the inflows and outflows expected over the time period of the exercise is almost the same as the one reported one year ago. The expected inflows and outflows are comparable with the ones recorded by banks in the previous year, while the volume of expected outflows is somewhat lower. The gap between inflows and outflows is negative and the highest values are seen for the baskets "up to 1 day," "1-2 months" for Lek and Euro and "6-12 months" for Euro, while for the basket "1-2 years" expected inflows are higher than outflows. The resilience of banks differs based on currency and is considered to be "very good" for lek and US dollar and "good" for euro. For the Lek currency banks overall have a larger negative gap between inflows and outflows than for the Euro, but extended liquid assets of banks in lek are around 1.5 times higher compared with those in euro.

Table 11 Stress-test results for the simple gap by currencies and baskets

	(11 banks)	<1 day	1 day - 1 week	1 week - 1 month	1 - 2 months	2 - 3 months	3 - 6 months	6months - 1 year	1 - 2 years
Lek	No of banks with a negative gap	10	10	10	10	10	8	3	2
	Gap as a % of assets	-4	-5	-6	-6	-5	-3	-1	-1
	No of banks that do not pass the test	1	1	1	1	1	0	0	0
Euro	No of banks with a negative gap	4	3	4	4	4	4	5	5
	Gap as a % of assets	-2	-2	-2	-2	-2	-2	-3	-3
	No of banks that do not pass the test	2	1	1	1	1	1	2	3
USD	No of banks with a negative gap	4	1	1	1	1	1	1	1
	Gap as a % of assets	-1	0	0	0	0	0	0	0
	No of banks that do not pass the test	1	0	0	1	1	1	1	0

The maximum number of banks that have a negative gap for each basket in lek, euro and US dollar is 10, 5 and 4, respectively, and these results are comparable with those of the previous year, with the exception of the euro results that show an improvement toward narrowing the negative liquidity gap to banks' assets. The maximum value of the liquidity gap in relation to banking sector assets ranges from an almost inconsiderable value for the US dollar up to 2-3% for the euro and 1-6% for the Lek. From the scenario that assumes to use counterweighting capacities for closing the gap in each basket, the maximum number of banks that continue to have a negative gap in at least one of the baskets is 1, 3 and 1 for activity in Lek, Euro and US dollar. Compared with the results of one year ago, the banking sector has significantly improved its resilience in euro. This is reflected in the lower number of banks that do not pass the test as well as reduction of the liquidity gap to assets in euro. The improvement of the Euro is related not only to an increase in the volume of counterweighting capacities, but also to the expected improvement in money inflows and outflows that mainly reflect credit inflows and deposit outflows.

4.2 NON-BANK SECTOR

The majority of the non-bank sector expanded its activity during the second half of the year.

The credit quality of SLAs remains good but has decreased slightly. The exposure of this sector against the banking sector remains high but has diminished due to the decline of deposits of non-banks to domestic banks.

The second half of the year[35] was characterised by an overall good performance of non-bank financial institutions. The highest increase was observed in the segment of non-bank financial institutions and investment funds, whereas a positive performance was reported also on the other segments of the market. The sectors of trade, services and agriculture continue to represent the main economic activity that attract credit by non-banks and SLAs, while the quality of credit granted by these entities until the end of the third quarter is relatively good, but lower compared to the previous quarter and the previous year. The exposure of the banking sector to the non-bank sector remains limited and has not changed during the period. The exposure of the non-bank sector to the banking sector continues to remain high, since non-bank deposits to the banking sector, in the form of deposits and capital instruments account for 19% of the non-banks' balance sheet.

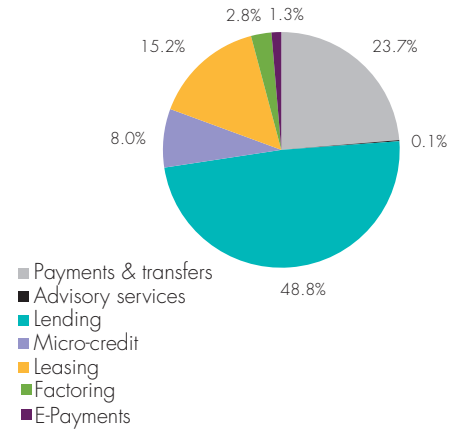
INSTITUTIONS SUPERVISED BY THE BANK OF ALBANIA

During the second half of the year, non-bank financial institutions (NBFIs) expanded their activity due to the positive performance of investments in the form of current accounts in banks and securities. At the end of the third quarter, the financial system contained 30 NBFIs, with total assets of around ALL 66 billion. The balance of NBFIs was 1% and 5% higher compared to the first half of the year and the previous year. The largest part of this financial system segment consists of NBFIs that carry lending activity, followed by those that carry out payments and transfers. Domestic capital accounts for around 70%

[35] *The data for the non-bank sector are from 2020 Q3.*

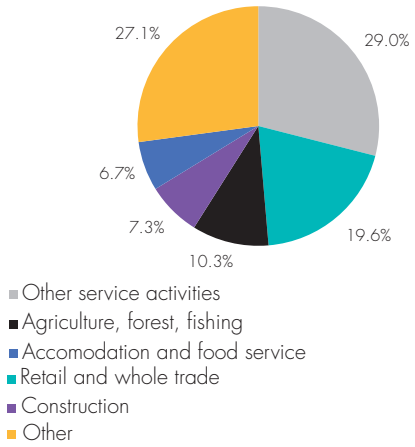
of the shareholders' equity of these entities. NBFIs are more active in lending to service activities (around 29%) and wholesale and retail trade (20%). NBFIs ended the period with a positive financial result (around ALL 1.9 billion), lower, however, compared to the previous year. The capitalisation activity of these entities continues to remain at satisfactory levels. The portfolio quality of loans declined slightly, as the ratio of non-performing loans at the end of 2020 Q3 reached around 12% from 11% and 10% in the previous quarter and year.

Chart 82 Structure of NBFIs by type of activity September 2020



Source: Bank of Albania.

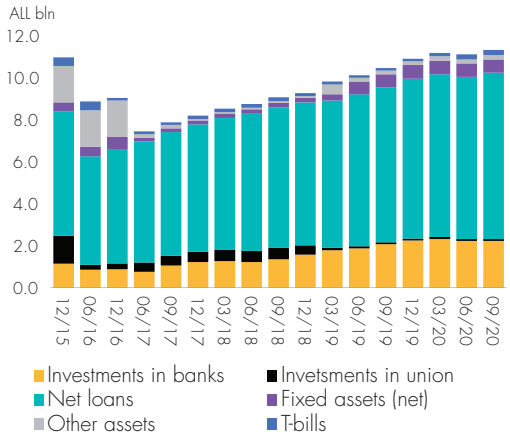
Chart 83 Structure of loans portfolio by economy sector, September 2020



Source: Bank of Albania.

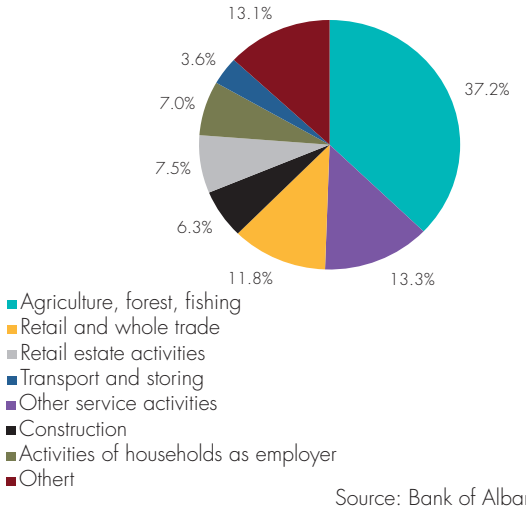
The activity of Savings and Loans Associations (SLAs) expanded in quarterly and annual terms supported mainly by the growth of net loan (activity of the members). The financial result of SLAs was positive and improved compared to the previous year. Net loan to members and investments in banks represent the main items of these institutions' assets. The sector that has attracted the largest funding from the activity of members is the agricultural sector, followed

Chart 84 The assets' structure of Savings and Loan Associations



Source: Bank of Albania.

Chart 85 Loan portfolio structure by economic sectors, September 2020



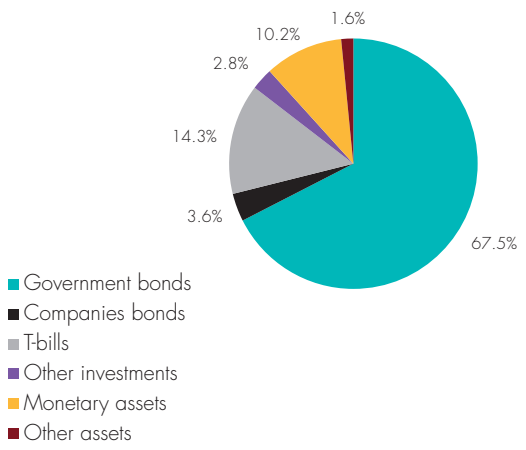
Source: Bank of Albania.

by the services sector. At the end of the period, fourteen savings and loans associations and one Union operated in the Albanian market.

INSTITUTIONS SUPERVISED BY THE FINANCIAL SUPERVISION AUTHORITY

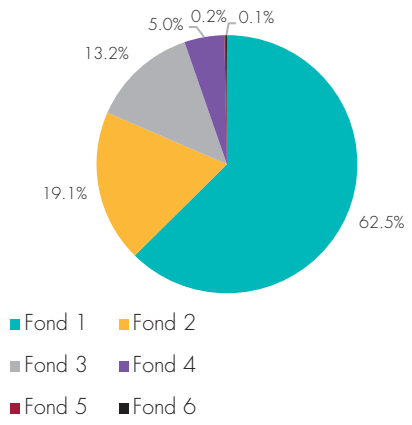
In 2020, the insurance market declined by about 6% compared with 2019, due to a decrease in the volume of gross written premiums. Gross written premiums[36], with the main contribution made by non-life premiums (93%), which represent the main funding source for insurance companies' activity, contracted by about 6% in annual terms, while the costs incurred increased significantly by around 19%. There are 12 licensed insurance companies operating in the domestic market that provide out life insurance (4 companies) and non-insurance (8 companies). The assets of these institutions[37] grew by 13% annually, reaching ALL 39 billion. Investments in banks held the main share (around 33%) on insurance companies' balance sheets. The level of net assets of investment funds[38] remained unchanged compared to the end of 2019, at ALL 67 billion. The performance of government securities in the form of T-bills was positive. There are 6 active investment funds in the Albanian financial system. The investment fund market is a market with a relatively high concentration, since two of the investment funds own around 80% of the total net assets of funds. Investment funds' assets are mainly invested in bonds issued by the Government of the Republic of Albania, which provide high return compared with alternative investments.

Chart 86 Structure of the assets of Investment Funds, September 2020



Source: Bank of Albania.

Chart 87 Share of Investment funds in the market, According to assets' net value, September 2020



Source: Bank of Albania.

36 *AFSA, Statistical Report, the Insurance Market, 2020.*
37 *The insurance companies' balance sheets belong to 2020 Q3.*
38 *AFSA, "Collective investment undertakings market", 30 September 2020.*

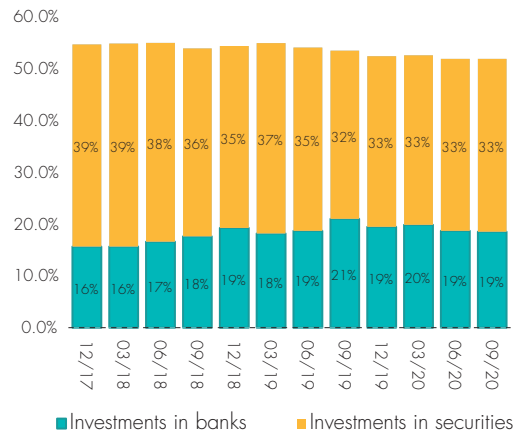
Supplementary Private Pension Funds[39] have expanded their activity during the period. In Albania, there are four supplementary private pension funds operating in the financial market. The assets of these funds, at the end of 2020 Q3 registered ALL 3 billion, or 18% more compared to the end of 2019. The activity of pension funds is dominated by investments in government debt securities.

During 2020, the value of transactions carried out by the Albanian Securities Exchange (ALSE)[40] contracted significantly due to a decrease in interest rates of government securities and the effects of the COVID-19 pandemic on financial markets in Albania. The activity of ALSE, during the period, consisted in transactions with government debt securities. The ALSE counts 4 members, which are banks and one Brokerage Company. According to the statistical data of the ALSE, during 2020[41], the value of traded bonds was about ALL 1.4 billion and the value of T-bills about ALL 183 billion. Regarding instruments traded in AFSA, both in number and value; the transactions conducted for the account of customers are dominant.

RISKS AND EXPOSURES BETWEEN THE BANKING AND THE NON-BANKING SECTOR

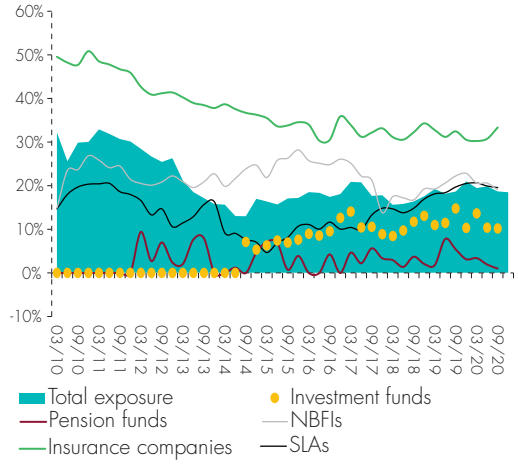
The exposure of the banking sector to the non-banking sector in Albania is limited with no changes during the period. This exposure on the side of banks' assets is represented by loans granted to non-bank financial institutions, which accounts for only 1% of the total assets of the banking sector. On the side of liabilities the exposure is in the form of funds collected by banks (various accounts, time deposits or demand deposits), and accounts for only 2% of the value of the banking sector's assets.

Chart 88 Investments of the non-bank sector in banks and government securities, to total assets of the non-bank sector (share, in %)



Source: Bank of Albania, Financial Supervision Authority.

Chart 89 Investments of non-bank sector manila institutions in the banking sector to their total assets (in %)



Source: Bank of Albania, Financial Supervision Authority.

[39] *AFSA, Statistical Report "Developments in the private supplementary pensions", 30 September 2020.*

[40] *ALSE was licensed by the Financial Supervision Authority in July 2017 and started its activity in February 2018.*

[41] *AFSA, Monthly Publication No. 140, January 2021.*

This ratio has maintained the same level in the past two years, and it is considered very low compared with the threshold levels applied by the Bank of Albania for monitoring the risk of exposure and concentration of activity between different segments of the financial system.

The sensitivity of the non-banking sector to the activity of the banking sector remained relatively high, however lower compared to the previous year. The exposure of non-banks to the banking sector at the end of the third quarter accounted for 19% of the assets of the non-bank sector, compared with 19.5% at the end of 2019 and 21% in the previous year. Savings and Loans Associations (SLAs) show the highest exposure to the banking sector, since their placement in banks in the form of deposits and capital instruments, account for 33% and 20%, respectively, of relevant assets. Regarding non-bank financial institutions (NBFIs), exposure and sensitivity to the developments of the banking sector decreased, given that these entities decreased their time deposits in the banking sector. The exposure of the non-banking sector to the banking sector is regularly monitored by the Bank of Albania in the context of periodic assessment of systemic risks and monitoring of the fulfilment of the intermediate objectives of macro-prudential policy.

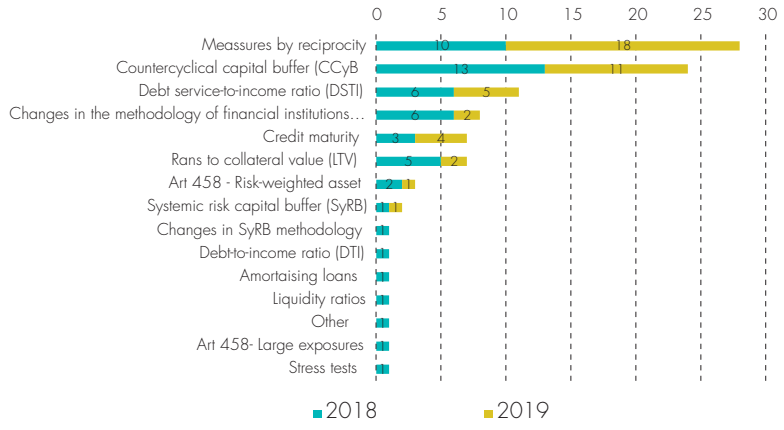
5. MACRO-PRUDENTIAL POLICY

5.1 MACRO-PRUDENTIAL MEASURES IN THE EUROPEAN UNION

During 2020, the economic and social situation was conditioned by the health situation created by the Covid-19 pandemic. The start of the vaccination process in Europe and other countries gives more hope for normalisation of the situation. Many countries have opened main economic activities to allow for a gradual return to normality, but others are faced with new pandemic views. Therefore, developments are still highly uncertain.

Due to reforms in international standards on the quality and quantity of banks' capital, the pandemic found European banks in better capital positions. Until the end of 2019, many countries applied macro-prudential capital buffers, making banks in these places more capable to withstand various losses and shocks.

Chart 90 The main measures taken in EU countries, by type



Source: ESRB.

The pandemic during 2020 was a hard and uncongenial blow, which tested the success of the undertaken measures. In response to its effect, European authorities eased regulatory requirements regarding the classification and provisioning of loans, which were the subject of the Moratoriums approved by the Member States of the European Union. While expecting an increase of non-performing loans and accompanying financial losses, and in order to adequately protect credit levels, authorities in many Member countries

extended, suspended or lowered macroprudential capital buffers. The biggest moves were observed in the use of the countercyclical capital buffer, which is conceptualised to adapt to the cyclical movements of the economy. The size of the movement is defined by the level of buffers adopted prior to the pandemic.

Similar measures were also implemented in some the Western Balkan countries.

5.2 MACRO-PRUDENTIAL MEASURES IN ALBANIA

Also during 2020 H2, the Bank of Albania retained prudential measures undertaken to facilitate the requirements on the classification and provisioning of loans that were affected by the pandemic, even under the condition of being restructured. Given the higher possibility of increasing non-performing loans following the removal of these measures and the need to have adequate capital levels, the Bank of Albania determined certain restrictions related to the distribution of banks' profit in the form of dividend.

Throughout 2020, these measures were assessed to be appropriate, taking into consideration:

- the structure of the banking sector, the characteristics of the economy and the need to operate with relatively high levels of capital;
- the opportunity provided by prudential regulatory easing in order for banks to mitigate the shock in their financial indicators, including capital levels as well;
- The need to preserve the space to act in case this becomes necessary depending on future developments.

Under these conditions, in accordance with the Regulation "On macroprudential capital buffers," decisions of the Governor[42] have continued to be published for the implementation of said buffers.

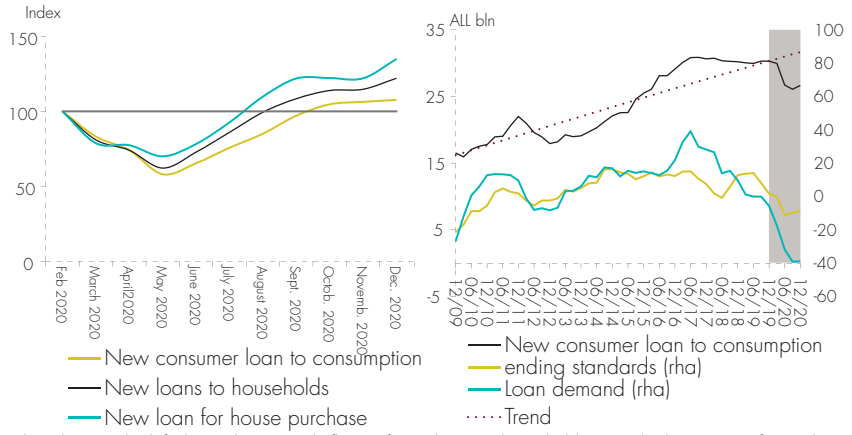
In parallel, the Bank of Albania has continued the operationalisation of capital values that hedge structural risks in the financial system, and the conception of instruments that prevent excessive credit and debt growth, mainly by households. Important in this regard is the development analysis of real estate and consumption credit. A more detailed analysis is given in Annex I regarding the latter.

[42] *Can be found in the following link: https://www.bankofalbania.org/Financial_Stability/Macro-prudential_policies/Instruments_of_Macroprudential_Policy/Instruments_and_Decisions/*

ANNEX 1 DEVELOPMENTS IN CONSUMER CREDIT AND FINANCIAL STABILITY RISKS UNDER THE CONDITIONS OF THE COVID-19 PANDEMIC

The continuation of lending is essential for fulfilment of the liquidity needs of households throughout the Covid-19 pandemic crisis. The contraction of new credit immediately following the beginning of the pandemic is notable in all its main categories, but consumer credit was hit particularly hard, dropping drastically from the first month of the crisis blowout. The economic shock caused by the pandemic was accompanied by a record decline in consumption and had considerable effects in the consumer credit market by significantly contracting its demand and supply. The contraction of consumer credit climaxed at the end of 2020 Q2 by -39.7% and has gradually recovered during 2020 H2. Starting from 2020 Q3, banks eased the standards of lending, despite the macroeconomic situation in the country, while credit demand is expected to recover further during 2021[43]. During the last quarter, consumer credit increased by 7.4%, a level higher compared with the average lending flows of the pre-Covid-19 period[44]. The banking sector has played a positive role in not amplifying any further the decline of consumption that might have been caused

Chart 91 Some indicators of consumer credit indicators



1. The Chart on the left shows the quarterly flows of new loans to households since the beginning of Covid-19. The index is constructed by taking the average flow of new loans prior to the pandemic equal to 100;
2. The Chart on the right shows the flow of new consumer loans in annual terms (the left axis); the index of consumer credit demand and the standards of consumer credit lending (right axis); on the right axis of the chart, the negative value demonstrates banks that have tightened lending standards and vice-versa. Also, a positive value shows an increase of credit demand while a negative balance shows its decline.
Source: Bank of Albania.

by a strong and lengthy credit contraction.

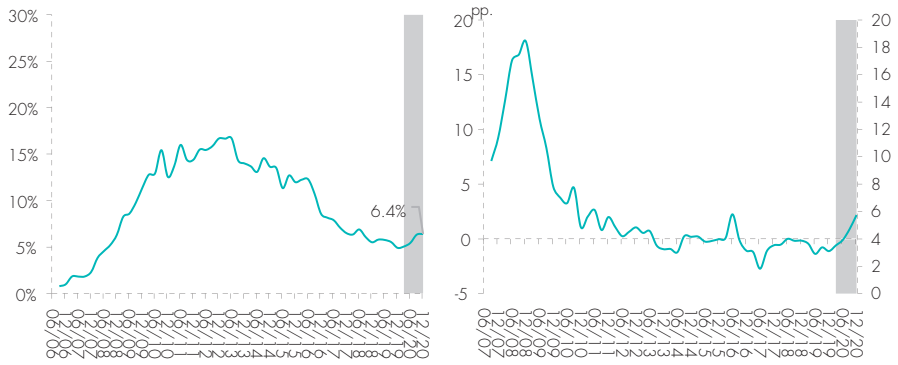
In terms of costs, the average interest rate on consumer credit continued to remain at historically lowest levels, ranging between values similar to the previous year. A positive development during 2020 was a significant increase in new contracts with short fixed maturities (up to one year) as of the end of June. However, during the second half of the year, the structure of the initial

[43] *For more information, see "Bank Lending Survey" at: https://www.bankofalbania.org/Monetary_Policy/Surveys_11282/Bank_Lending_Survey/*

[44] *More details regarding the historical performance of consumer credit in Albania and its components have been discussed in previous financial stability reports.*

period of interest rate fixation returned to a composition similar to that of the pre-pandemic period, where the dominant part of new consumer loan contracts (around 80%) had an unchanged interest rate. With regard to the quality of credit, the ratio of non-performing consumer loans remains at relatively low levels, although it has slightly increased during 2020 H2 registering 6.4% at the end of December, increasing by 1.5 p.p. compared with the end of last year. Under the new conditions caused by Covid-19, the credit risk for this segment is expected to further materialise, thus making it necessary to continue monitoring the quality of credit. However, it must be enunciated that these risks remain under control because they are mitigated by the relatively low exposure of the banking sector to this segment compared with the total loans given to the private non-financial sector. At the end of December 2020, consumer loans accounted for 10.9% of loans granted to private non-financial sector and only 4.1% of the banking sector's balance sheet assets.

Chart 92 The ratio of non-performing consumer loans (chart to the left) and the contribution of consumer credit to the increase of non-performing loan stock (chart to the right, in percentage points)



Source: Bank of Albania.

The recovery of lending in the recent months shows that consumer credit will remain an important instrument of consumption in the economy. The demand for consumption financing is expected to increase during 2021. On the other hand, banks are ready to further facilitate demand conditions. Furthermore, an environment with low interest rates is expected to be a feature of the economic situation in the future as well. Under such circumstances, the potential for further growth of consumer credit is good, despite looming uncertainties due to the pandemic.

ANNEX 2 THE MAIN INDICATORS OF FINANCIAL SOUNDNESS

In %	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Capital-based indicators														
Regulatory capital to risk-weighted assets	17.1	17.2	16.2	15.4	15.6	16.2	18.0	16.8	15.7	16.0	17.0	18.7	18.5	18.3
Tier 1 capital to risk-weighted assets	16.0	16.3	15.3	14.5	14.3	14.6	14.9	13.8	13.5	14.1	15.5	17.4	17.3	17.2
Shareholders equity to total assets	7.6	8.6	9.6	9.4	8.7	8.6	8.4	8.6	9.5	9.7	10.2	10.1	10.5	10.4
Asset quality														
Net NPLs to regulatory capital	10.1	21.7	28.2	35.9	52.0	55.6	40.2	38.3	24.3	23.1	15.7	15.5	13.6	11.3
NPLs (gross) to total loans	3.4	6.6	10.5	14.0	18.8	22.5	23.5	22.8	18.2	18.3	13.2	11.1	8.4	8.1
Profitability														
ROE (annual basis)	20.7	11.4	4.6	7.6	0.8	3.8	6.4	10.5	13.2	7.2	15.7	13.0	13.5	10.7
ROA (annual basis)	1.6	0.9	0.4	0.7	0.1	0.3	0.5	0.9	1.2	0.7	1.5	1.3	1.4	1.1
FX net open position to captial														
FX net open position to regulatory capital	1.7	4.3	3.9	5.0	3.9	4.0	4.1	8.5	7.7	7.0	6.7	7.8	7.4	8.4
FX net open position to Tier 1 capital	1.8	4.5	4.1	5.3	4.3	4.4	4.9	10.4	9.0	8.0	7.3	8.4	8.0	9.0
Asset-based indicators														
Liquid assets to total assets	49.8	42.8	27.6	25.9	26.5	29.4	27.6	31.9	32.3	31.3	30.2	34.2	35.7	34.8
Liquid assets to sh.t. liabilities (up to 1 year)	74.0	64.9	32.6	30.6	33.1	36.7	34.7	40.4	41.4	40.6	40.8	46.2	49.4	47.4
Client deposits to total loans	215.5	162.6	154.3	166.4	163.2	171.6	180.8	180.2	187.8	192.8	194.0	203.2	207.2	211.3

Source: Bank of Albania.