

B a n k o f A l b a n i a

TRENDS IN LENDING

ERJONA SULJOTI AND OLTA MANJANI
MONETARY POLICY DEPARTMENT

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The views expressed herein are solely of the authors and do not necessarily reflect those of the Bank of Albania.

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This analysis presents a detailed overview of the most recent lending developments in Albania. To this end, the analysis studies the monetary data on the credit portfolio by economic agents, as well as lending standards. In addition, this analysis will present a summary of trends in lending in Central East and South East Europe (CESEE) countries.

The main statistics taken into account in this analysis are:

- Data on the lending activity for the resident sector of economy.
- Qualitative data from the bank lending survey. Based on this survey results, non-price elements of lending activity are also analysed.
- Statistics on credit price, represented by the average interest rate weighted with the new credit, denominated both in lek and in euro.
- Monetary data for the loan volume of lending for the regional countries. In more concrete terms the countries included in the analysis are: Bulgaria (BU), Croatia (CR), Romania (RO), Serbia (SR), Poland (PL), Hungary (HU), the Czech Republic (CZ), and Former Yugoslav Republic of Macedonia (MK).

The analysis covers data published as at 23 July 2015, which include information for monetary and financial data for May 2015 and data from the bank lending survey 2015 Q2.

SUMMARY

Lending activity improved slightly in April-May 2015, from the previous quarter, reflecting the seasonal impact of this period. The good performance of lending in lek continued to sustain lending to resident private sector. Lending in foreign currency was weak and shrank moderately than previously.

Lending to businesses increased at higher paces in April-May compared to the first quarter. In the short term, contraction of lending to business is related to the sluggish seasonal activity during the period under review. In a longer-term context, business demand for financing remains weak, conditioned by the presence of unutilised capacities and businesses low appetite for investment. By the offer-side, banks applied more eased standards than in the first quarter, but in a longer-term point of view these standards remain tight. The tightening of standards was more pronounced for the lending for investments purposes. Banks replying to the demand of businesses for financing are low in number and are concentrated on definite segments of economy.

Lending to households performed better and was more stable. Households' demand in this quarter was oriented mainly for consumer loan, driven by attractive offers from banks for this product. Banks reported eased lending standards and increased demand for the mortgage loan as well. Nevertheless, the annual increase of this portfolio remains close to the average rates of the first quarter.

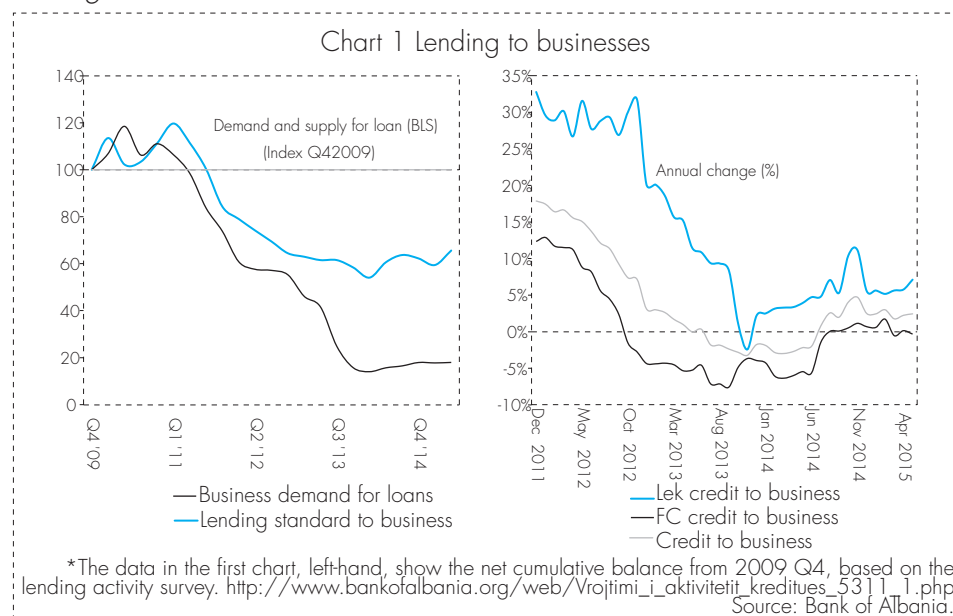
Interest rates on loans remained low, despite the slight increase in the first months of year. Interest rates increased on lek loans for liquidity purposes. In parallel, credit interest rates on euro loans, overall, were down. Intermediation margins showed a slight increase, albeit remaining close to low historic rates, compared to the cost of funds as well as among currencies.

The comparative analysis of credit in the regional countries shows that the Central, Eastern and South-eastern Europe (CESEE) continue to suffer the process of large European banks withdrawal, but at slower pace than previously. Meanwhile, the results of last survey on lending activity for the region confirm the improved lending demand and easing of lending standards. Lending activity improved gradually. Nevertheless, the geographical differences are still present. Central European countries manifested a clear and steady tendency of credit recovery, both for businesses and households. Excluding FYROM, lending in the other Balkans countries is not recovering yet, mainly as a result of the sluggish performance of loans for businesses.

1. LENDING TO BUSINESSES

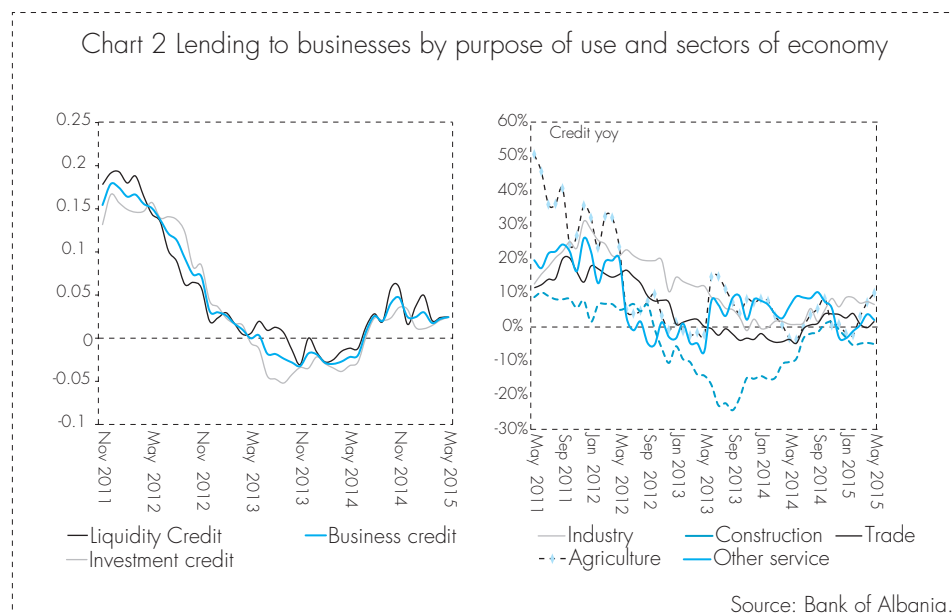
The short-term dynamic of lending to businesses was more positive than in the first quarter. The positive change in April and May marked a turning point, compared to the closure in the first quarter. This performance was positively affected by the loan for liquidity and for investments purposes. In a longer-term point of view, the increase in credit portfolio for businesses remains volatile and at moderated levels. Lending standards, in this quarter, were eased and this trend is expected to continue in the forthcoming quarter. While, banks assessed the lending demand from businesses as downward, and do not expect and recovery of the latter in the third quarter of year.

The annual growth rate of loan portfolio for businesses stood at 2.4%¹ in May, or 0.7 percentage point higher from the end of the first quarter. This increase was supported at the same degree by the improved loan portfolio for liquidity and investments, which were 2.4% and 2.5%, respectively. Positive developments in April and May were in line with the seasonal behaviour of credit for businesses in this period. In a longer-term point of view, the growth pace of loan for businesses remains moderate, reflecting the tightening of lending standards and a low demand.

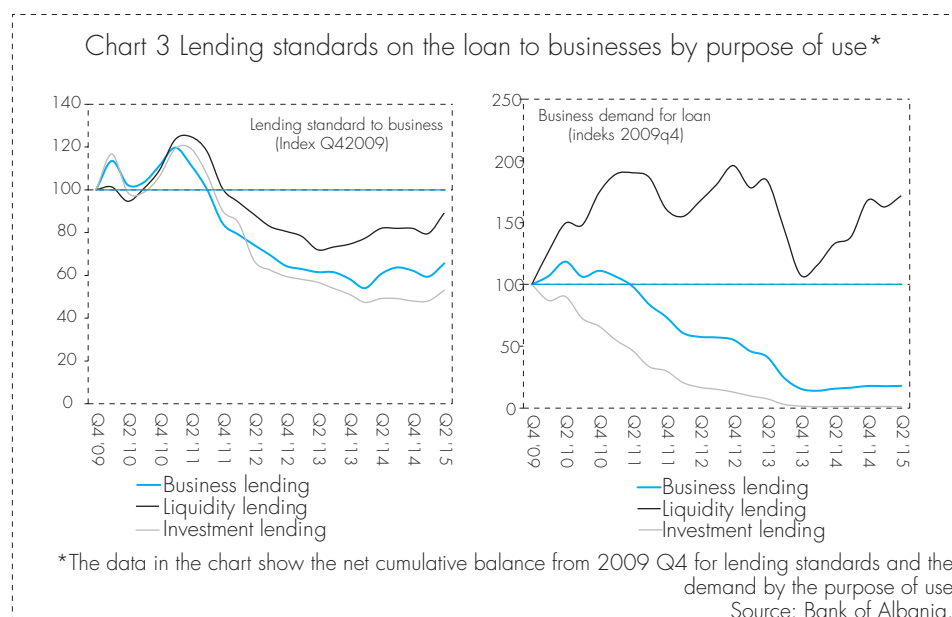


¹ During 2015, the lending portfolio performance was determined by non-performing loans write offs from banks balance sheets, in compliance with the requirements of the regulatory framework that entered into force at the start of the year. For more, refer to http://www.bankofalbania.org/web/Annual_Report_of_Banking_Supervision_56_2.php?kc=0,8,6,0,0.

Lending in lek to businesses supported the positive performance of loan in lek for businesses, by recording an annual growth of 7.1%, from 5.6% in the first quarter. The orientation of loan demand to cover the needs for liquidity, along with the narrowing of the spread of interest rates on lek and euro loans, sustained the shift of loan portfolio for businesses to lek lending. In May, lending to businesses and households was 0.3% lower than in the previous year.



Lending to businesses was supported by the loan to industry, which continued the improved trend, increasing by 6.6% yoy. Positive lending dynamic of this sector drove to the increase of its share to the total at 30.6%, from 24.7% at the end of 2008. Also, agriculture showed an annual growth of 9.9%. This rate fluctuates considerable on monthly basis. The share of this sector in credit portfolio remains low, at 1.8%. Problems in agriculture related to



the formalisation or concentration of agriculture output, kept this sector far of financing from banks. Lending to trade continues to dominate the financing of businesses, accounting for 37.6% of total credit to businesses. The annual rate of this portfolio improved by 0.8 percentage point, standing at 1.6%, as at end of May. Lending to construction dropped further, falling -5% in annual terms at the end of May.

In 2015 Q2, banks eased the lending standards to businesses, particularly those on the loan for liquidity. Albeit the easing of lending standards to businesses, they continue to be broadly tightened than at the end of 2009. Lending survey data show that lending standards applied for investment purposes are considerably more tightened than those for liquidity. A tightened offer followed by a particular weak demand for investments was reflected in a weak performance of the loan portfolio for investments. The weak demand for investments was determined also by the spare capacities in production and the performance of economy under potential. Liquidity demand was up since the end of 2013. In 2015 Q3, banks expect to further ease lending standards to businesses. While they expected that the weak demand of businesses for financing is present in the quarter to come.

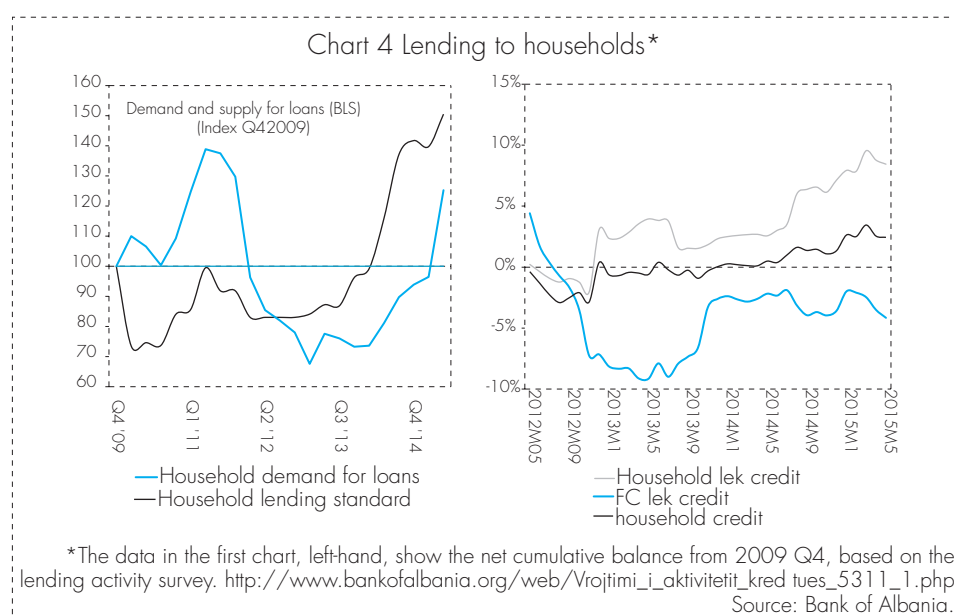
The main factors that have affected the performance of lending standards, as identified by banks, remained the high level of non-performing loans, the current and expected macro-economic situation and the problems related to specific sectors of economy. The ample liquidity of banks, competition and the monetary policy were the main factors contributing to the easing of lending standards.

Banks identified the current and expected macroeconomic situation, the lack of the demand for investments and alternative sources of financing, as the main factors contributing to the weak demand of businesses. In parallel, the factors that sustain the increase of the demand are the favourable monetary conditions and the needs for liquidity.

2. LENDING TO HOUSEHOLDS

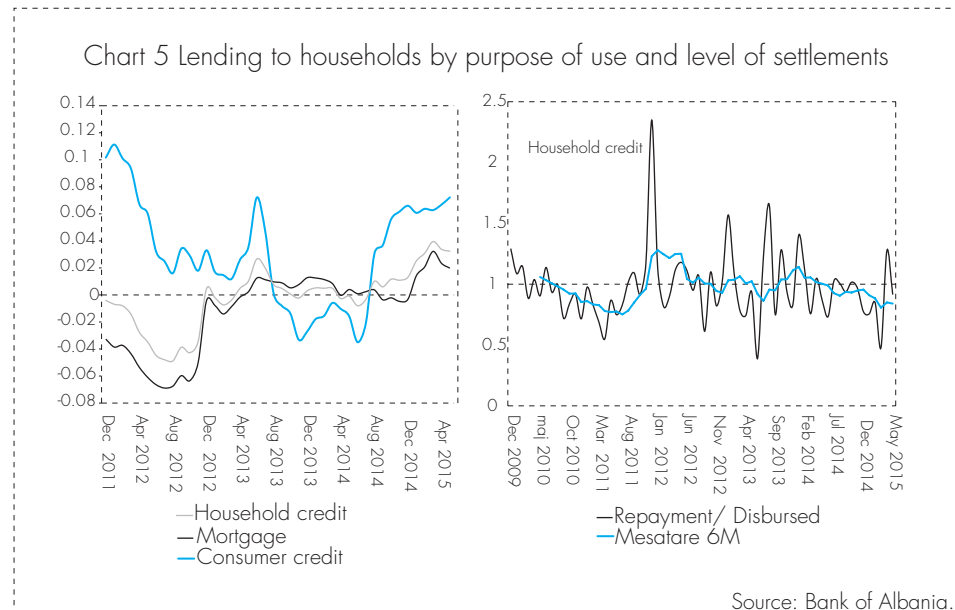
Lending to households grew at stable pace in 2015 Q2, mostly reflecting the well performance of consumer loan. While, loan for house purchase continued to be weak. This positive dynamic was sustained by the favourable lending standards and an increasing demand, especially for consumption. The easing of lending standards to households, in the second quarter of year, is expected to continue in the next quarter. The eased offer was followed by a higher demand that is expected to continue even in the third quarter.

The loan portfolio for households continued to increase in 2015 Q2. Annual rate of 3.2% was slightly lower from the first quarter. Developments in loan portfolio for households are sustained by the easing of standards from more than two years and the increased demand for loans. By currency, it is noted that the well performance of lending in lek for households (by an annual growth of 8.5%) determined the loan trajectory for households. The enlightening of households on the exchange rate-related risk and the further cut of interest rates on lek loans compared to euro loans, sustained the financing to households in the domestic currency. Also, the high demand for consumer loan dictated the higher financing of loan in lek for households.

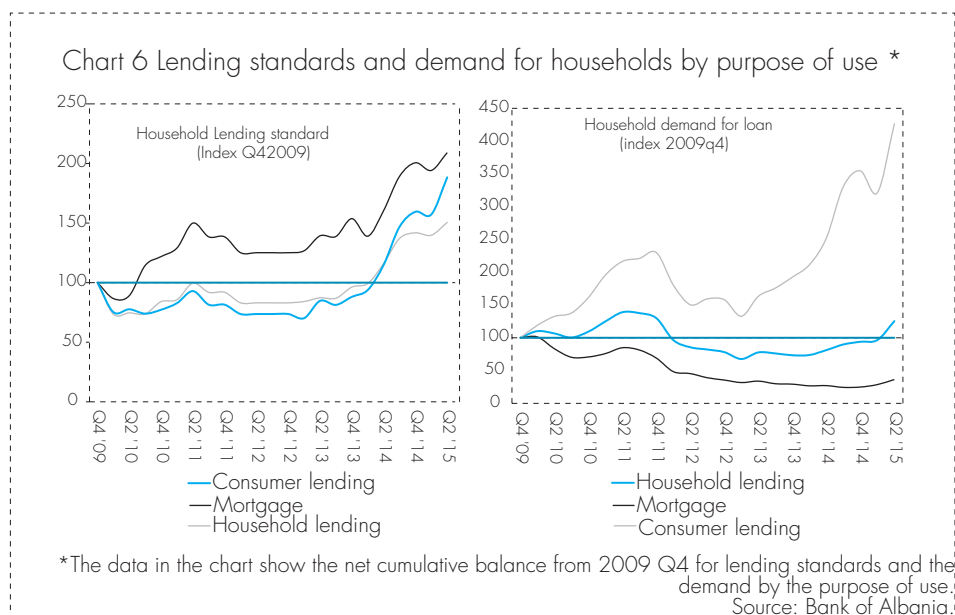


The better performance of consumer loan compared to mortgage loan, appeared to have determined the positive developments in loan portfolio. In May, annual mortgage loan increased by 7.2%, 0.9 percentage point higher from the previous quarter. The good performance of consumer loan was sustained not only by the easing of lending standards on consumer loan, but

also by the higher demand for this loan. The loan portfolio for households was exposed to high payments, due to the short-term maturity period of consumer loan.



Lending for house purchase recorded an annual growth of 2.0%, or 1.2 percentage points lower from the first quarter, albeit the easing of lending standards applied from some years. This performance was conditioned by the weak demand for house purchase. The cumulative index of factors that affected the demand, shows the low consumer confidence and the problems in housing market, the two main factors that affect this weak demand for mortgage loan².



² According to results from the bank lending survey. http://www.bankofalbania.org/web/Vrojtimi_i_aktivitetit_kreditues_5311_1.php

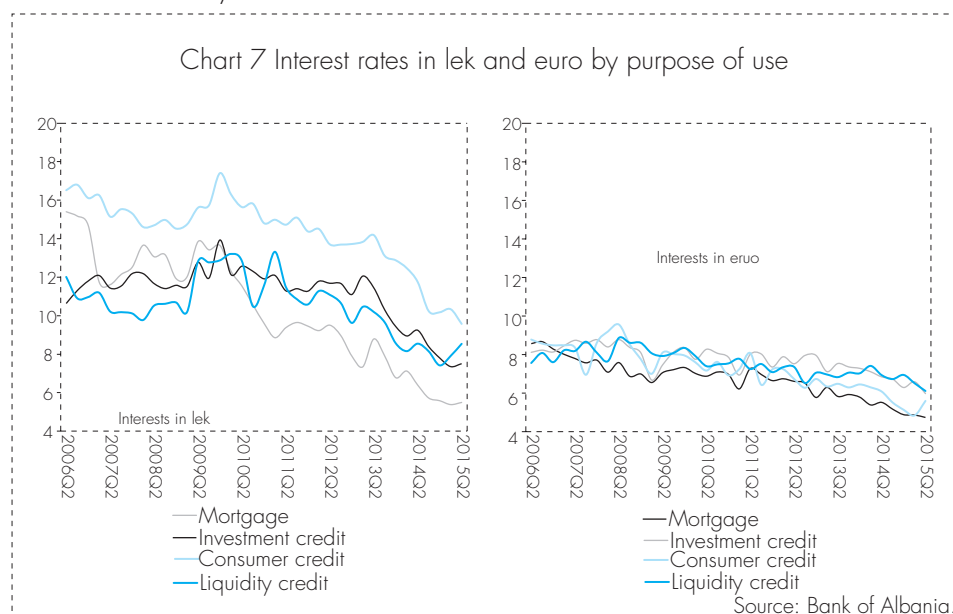
Lending survey results show that: the current and expected performances of banks' liquidity, the competition in the banking system and the easing of monetary conditions in Albania, have sustained the easing of lending standards for households. The performance of non-performing loans, the financial situation of households and the macro situation or housing market continue to determine the conservative policies of banks to households.

Loan demand of households appears to have improved in the second quarter and banks expect this trend to continue in the third quarter. The main factors that sustain the demand continue to be lending standards and Bank of Albania's monetary policy, households' needs to finance consumption and house purchase. Consumer confidence and other alternative opportunities for lending contributed to the negative direction.

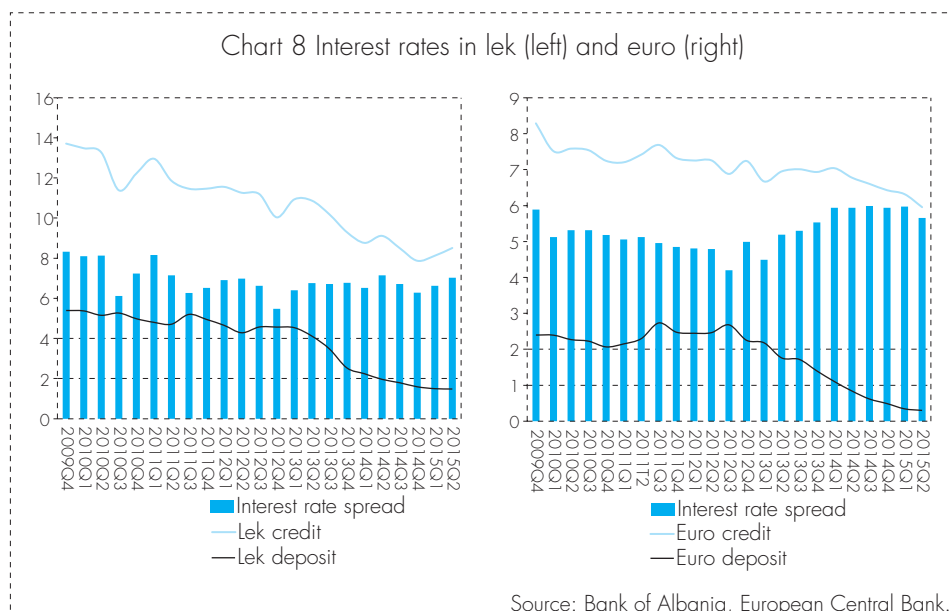
3. CREDIT PRICE AND OTHER STANDARDS

Interest rates on loans stand higher in April-May than in the first quarter, mainly due to the increased interest rate on the loan to businesses for liquidity purposes. In parallel, the interest rates on loans in euro decreased compared to the previous quarter, and the loan to businesses provided the highest impact in this regard. The spread between interest rates on loans and deposits increased for lek. Other lending standards were eased, particularly those to households.

Interest rates on lek loans recorded averagely 8.5% in April and May. This rate was 0.4 percentage points higher, from the average in the first quarter. The increase in lek loan cost was impacted by the lending to businesses for liquidity. The latter dominated the loan granted during this period. Meanwhile, loans for investment purposes showed a slight increase of interest rates, by around 0.1 percentage point. Intermediation cost in lek was slightly up due to the maintenance of the same interest rates on lek deposits. Notwithstanding the short-term fluctuations, interest rates on lek loans remain at low historical levels. The reduction in lending cost has reflected the transmission of the key rate cut by the monetary policy, and the policies of banks on orienting the lending activity toward the domestic currency. The more rapid fall in interest rates on lek loans contributed to the considerable narrowing of the spread between lek loans to euro loans, by sustaining the better performance of lending in the domestic currency.



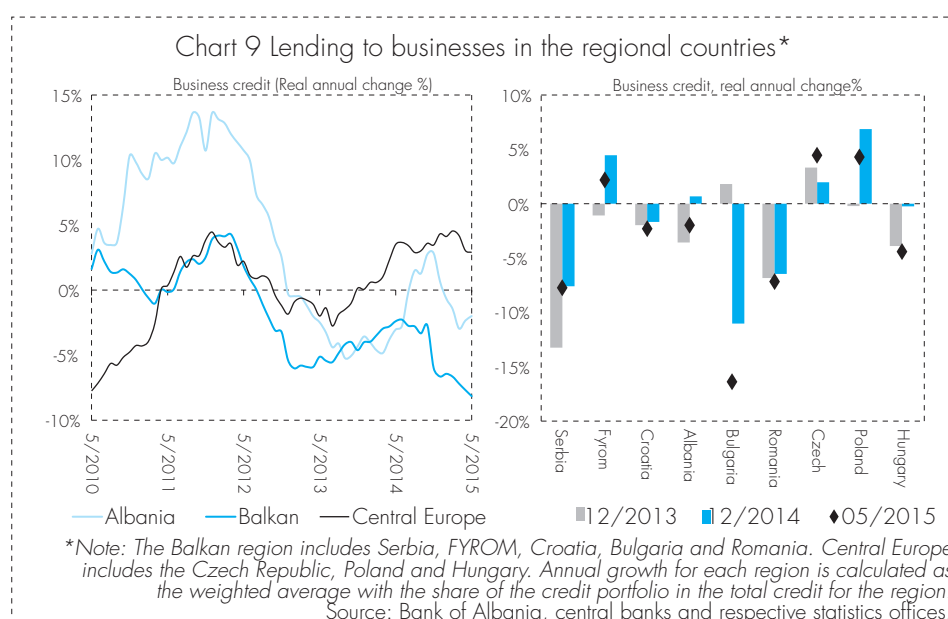
The average interest rate on euro loan of 5.7% fell by 0.3 percentage point, compared to the end of 2015 Q1. This performance was impacted by the fall of interest rates in all credit segments, which was more evident on the loan for investment purposes. Notwithstanding the average interest rate on euro deposits fell further at 0.3%, the intermediation cost in euro was reduced by 0.3 percentage point, due to the higher fall in the euro loan interest rate.



In addition to the increase in interest rates, overall, banks reported eased lending standards to businesses. The margin for risk-bearing loans was the only factor acting in the tightening side. Meanwhile, in 2015 Q2, banks eased the collateral requirements as a ratio to credit, extended the maturity of the granted loans and applied low commissions. Overall, the same factors were used to ease the standards for households.

4. TRENDS IN LENDING IN THE COUNTRIES OF THE REGION³

In the region, lending to the private sector continued to remain segmented. Central European countries, notwithstanding the slowdown trend of growth rates in the recent months, performed notably better compared to Balkan countries. Overall, Balkan countries continued to be characterised by shrinkage of credit portfolio for private sector. FYROM recorded the highest growth rates.



Credit portfolio for businesses in Albania was notable better than in the rest of Balkan countries. In terms of credit to households, this portfolio was up and above the regional average.

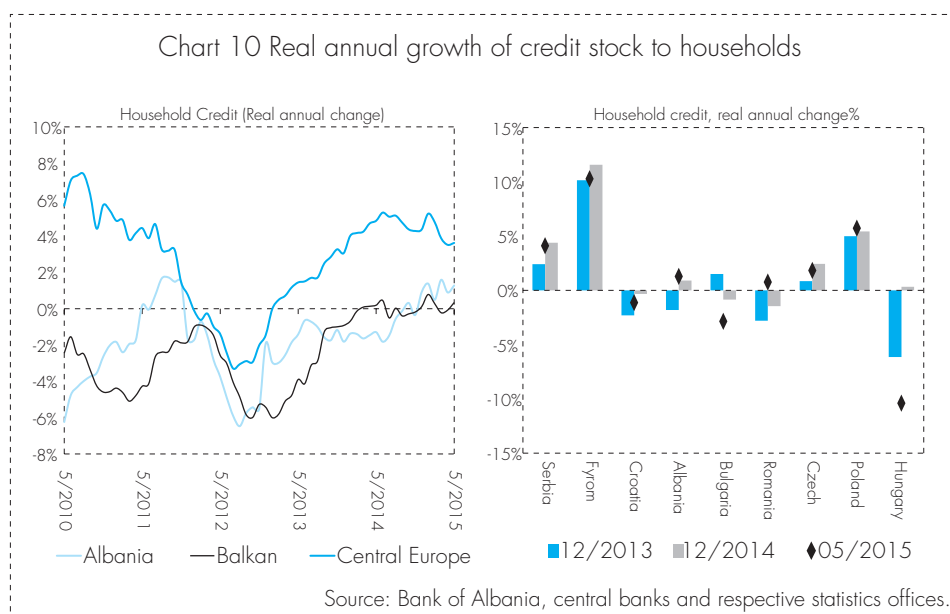
Credit to private sector slowed the growth rates in the last two-three months, by recording a real annual rate of 1.4%, from 1.9% in March. Given the considerable number of foreign-capital banks, all regional countries were affected by the strategies of parent banks to consolidate their balance sheets. The ultimate lending survey in regional countries (EIB H12015)⁴ confirms that banking groups continue to lower the use the leverage, albeit the pace of this process is expected to slow down. This approach resulted more pronounced for the Balkan countries, where the market potential for lending was considered as medium or low by the foreign capital banking groups, compared to the Central European countries, which in general are considered with high or medium potential. By geography, the shrinkage of credit rates for privates

³ Lending in the countries of our region is analysed in real terms, which is excluding the effects from the exchange rate and inflation.

⁴ For more information, see: http://www.eib.org/attachments/efs/economics_cesee_bls_2015_h1_en.pdf

sectors deepened further almost across all Balkan countries. Meanwhile, the countries in Central Europe showed decrease in growth rates, being affected by both, the slowdown in the expansion of positive rates and the further shrinkage in the countries with a fall of outstanding credit for the private sector.

Lending to businesses in the region slowed down slightly, at 0.6% in May. Like in the previous quarters, the overall situation reflects the different developments across the countries. Balkan region depend the shrinkage of credit portfolio for businesses in April - May, except FYROM which recoded a growth in this regard. Central European region recorded a growth of outstanding credit for businesses, albeit at a lower rate. Czech Republic and Poland provided the positive contribution in this growth. They are characterised by a steady expansion of credit to businesses. These countries implemented financial schemes for small and medium-sized businesses, with the purpose the increase of financing in strategic sectors.



Lending to households continues to perform better than the lending to businesses and remains the main source of credit growth in the region. Lending growth to households in CSEE countries, in real terms, averaged around 3% in May, almost equal to the end of the previous quarter. The analysis by geographical areas shows that developments in lending to households, overall, pursued an upward trajectory. Balkan region recorded a lower growth of this portfolio, albeit at an improved trend. The performance of outstanding credit for households in the Central European countries was characterised by steady growth rates. A slowdown in this portfolio's rates was noted in the last two months, mainly affected by its negative performance in Hungary. Lending to households in Albania continues to maintain the positive growth rates showed during 2015, sustained by the fast and stable expansion of the loan in the domestic currency.