Bank of Albania

TRENDS IN LENDING

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

C O N T E N T S

INTRODUCTION

This analysis aims to present an overview of the trends in lending in Albania. To fulfil this goal it analyses the monetary data on the credit portfolio, as well as lending standards. In addition, the analysis includes an overview of the most recent trends in lending in Central, Eastern and South Eastern European (CESEE) countries.

The main statistics taken into account in this analysis are:

- Data on lending for the resident sector of the economy;
- Qualitative data from the bank lending survey;
- Statistics on credit price, for both the Albanian lek and the euro loans;
- Monetary data for the credit volume for the countries of the region.

The analysis includes these countries: Bulgaria (BU), Croatia (CR), Romania (RO), Serbia (SR), Poland (PL), Hungary (HU), the Czech Republic (CZ), and Macedonia (FYROM).

The analysis covers data published as at 21 January 2017, including information for monetary and financial data for November 2016, and data from the bank lending survey 2016 Q4.

SUMMARY

The annual growth of credit to the private sector was 3.2% in October-November 2016, similar to 2016 Q3, reflecting the acceleration of growth in domestic loans and the sluggish performance of foreign currency loans. The portfolio expanded compared to September due to the positive seasonality of the last quarter. The performance of credit to the private sector is supported by continuous improvement of credit to households, while the recovery of lending to enterprises remains fragile.

The annual growth of loans to households in October and November 2016 is higher than in Q3, on average by 5.1%. Good credit conditions coupled with the improved financial situation and improved confidence of households have supported the expansion of credit growth to households. The good performance of consumer loans was the main contributor to the expansion of the household credit portfolio. Meanwhile, mortgage slowed down the growth rates, reflecting thus the households's weak demand for house purchase . Credit to households expanded supported by lending in domestic currency.

Loans to enterprises continues to appear concentrated and with moderate growth rates. In October-November, the portfolio growth rates slowed to 2.3%, due to both tight loan supply and weak demand. Loan for liquidity purposes has slowed down the growth rates, yoy and qoq. These two months, the expansion of loans to enterprises is determined by loans for investment purposes, although this portfolio has shown a slowdown in its annual growth rates. The performance of loans to enterprises reflects a segmented demand for funding by enterprises and tight financing conditions by banks. Banks have applied tighter conditions in Q4 by strengthening the collateral requirements.

Interest rates on new loans in domestic currency in October and November 2016 are slightly higher than in 2016 Q3, driven by the increase of interest rates in the short-term segment, mainly for enterprises. Meanwhile, interest rates of loans in euro have been stable for enterprises and have increased for households. Other non-price conditions of lending tightened for loans to enterprises for collateral requirements and eased for loans to households.

During the last quarter, credit to the private sector in CESEE region followed a similar trajectory to that of the previous year, recording moderate growth rates. In regional terms, the slowdown in lending during this quarter is mainly determined by the performance of lending in Central European countries. By economic agents, credit to private sector expanded during 2016 Q4 due to the growth of loans to households. The latter recorded steady growth rates, in the Balkan countries as well as in those of Central Europe.

BOX. METHODOLOGICAL CHANGES IN MONETARY AND FINANCIAL STATISTICS

Besides its primary function to draft, implement and adopt the monetary policy in Albania, the Bank of Albania plays an important role in processing and publishing monetary and financial statistics. In this context, the Bank of Albania is in a constant process of improving and enriching the statistical data. During 2016, the Department of Statistics at the Bank of Albania compiled and published monetary and financial data under a new methodological standard and also finalized the application in practice of an automated system for collecting data. Both these two factors contributed to the improvement of the statistics' quality as well as their alignment with the ESA 2010 European statistical framework[1].

The main purpose for these methodological changes is to re-classify institutional sectors, and detail sub-sectors and main financial instruments. More specifically, classification by institutional sectors consists of, and has as a counterparty, financial instruments by sectors of the economy. Sectors' classification is based on the breakdown and defining of the sub sectors and their activity. So, the non-financial corporate sector consists of these sub sectors: private and public non-financial corporates. These are independent legal entities and their main activity is to produce non-financial goods and services. Financial corporates consist of the central bank, other deposit-taking corporates, investment funds, other financial intermediaries, excluding insurance companies and pension funds, financial auxiliaries, insurance companies and pension funds, which carry out financial functions[2].

For the first time, the new data with the new standard were published in November 2016, which belong to the monetary and financial data for September. This publication reviewed the entire period from December 2015 to September 2016 using the new methodology. For the benefit of analysis and decision-making process of the monetary policy, the extension of the series before this period is performed through statistical evaluation which better aligns them with the dynamics of previous years. For this reason and due to the above-mentioned re-classifications, some of the monetary and financial indicators reflect changes in value, mainly in loans' data, deposits, interest rates and indices built on them. Despite all these changes, the new standard does not affect substantially the framework and the monetary and financial indicators.

1 The methodological changes are in compliance with the "Methodology of the European System of accounts ESA 2010","Guidelines for the drafting of monetary and financial statistics, IMF 2008", the "Manual of monetary and financial statistics, IMF 2000" and "Methodology of monetary and financial statistics, Bank Albania, July 2003".

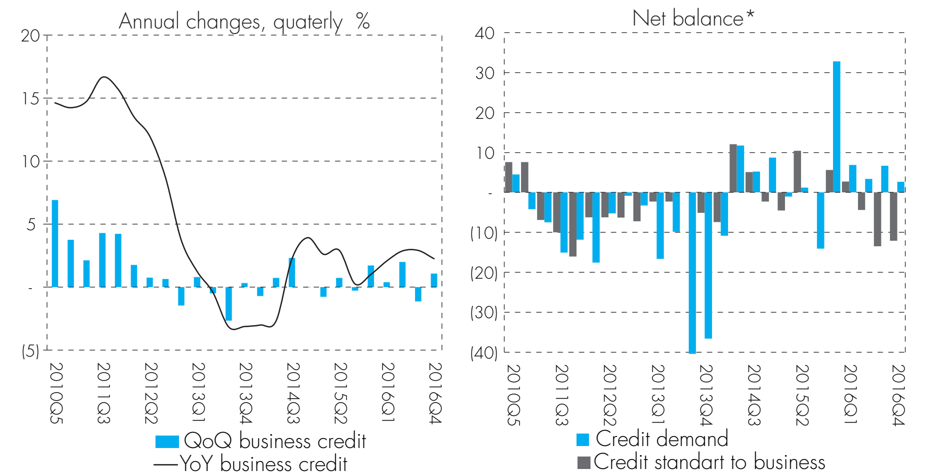
2 More details can be found in the paper "Methodological explanatory for monetary and financial statistics" at : https://www.bankofalbania.org/web/pub/statistikat_monetare_dhe_financiare_sipas_standardit_te_ri_2_8906_1.pdf

1. LOANS TO ENTERPRISES[3]

Loan to enterprises slowed down the growth rates at 2.4% on average for October-November. However, short-term dynamics shows that net flows for this period are higher than in the third quarter, as expected from its seasonal behaviour. These developments confirm that loans to enterprises remain fragile and subject to a tight supply of loans by banks as well as to a slow recovery of demand for financing. Lending standards remain tight for the larger enterprises, and unchanged for small and medium-sized enterprises. Banks expect a similar situation to continue in 2017 Q1

The improved economic activity and recovered business confidence in some sectors of the economy were reflected in firms' higher demand for bank financing. Yet, demand remains low and, in the face of a tight supply the business loan portfolio is set on a fluctuating trajectory. Business loan growth by 2.3% in October-November is 0.6 percentage point lower than in the previous quarter. However, compared with September, the portfolio grew by around ALL 4.5 billion, signalling an improvement in net flows, in line with the year-end seasonal behaviour.

Chart 1 Loans to enterprises



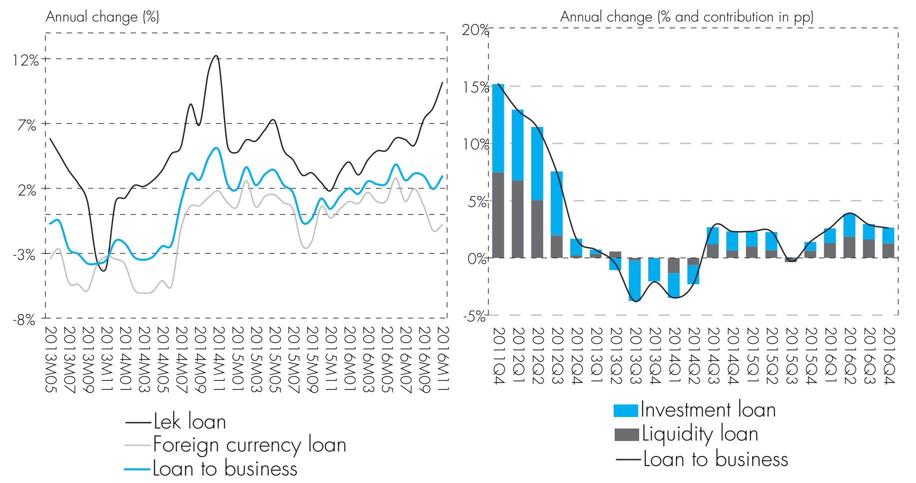
*Positive net balance shows easing of conditions and vice versa.
Source: Bank of Albania.

Lending in lek supported the positive performance of loans. The average annual rate of this portfolio accelerated in the past two months to 9.1%, against 6.2% in the previous quarter. Total loans in these two months were granted in the Albanian lek, offsetting thus the contraction of loans granted to enterprises in foreign currency. In annual terms, loans in foreign currency

[3] Data of Loans to enterprises exclude the effect of reclassified loans at off-balance sheet items.

shrank by 1.3% on average. At the end of November, lek loans accounted for about 36.5%, or 2.2 percentage points higher than in 2015. The shifting of the business portfolio towards lending in lek is linked to the reduction of financing costs during the year and the purpose of use of these funds, mainly for liquidity. Compared to a year earlier, this year, lending in lek is used to finance investments.

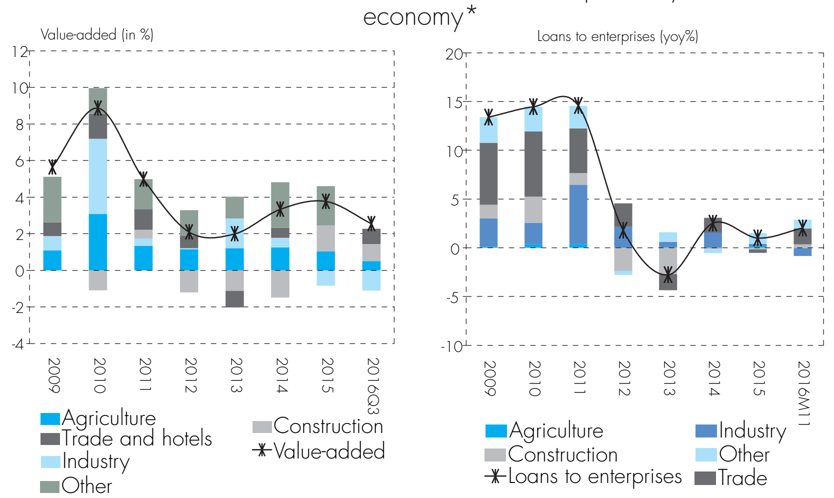
Chart 2 Loans to enterprises by currenc and purpose*



Source: Bank of Albania.

The slowdown in growth rates of loans to enterprises reflected lower growth of loans for liquidity and investment purposes. The annual growth of these portfolios recorded an average of 3.1% and 1.5%, respectively, in October and November, compared to 4.3% and 2.0% in 2016 Q3. However, these two months, the expansion of portfolio is completely driven by the growth of loans for investment, whilst loans for liquidity remained unchanged from September. At the end of November, loans for liquidity purposes accounted for about 45.5% of total loans to enterprises and ranged around these levels throughout the year.

Chart 3 Value-added contribution and loans to enterprises by sectors of the economy*



Source: INSTAT and Bank of Albania.
*Data of value added are until Q3,while loans by sector are until November 2016.

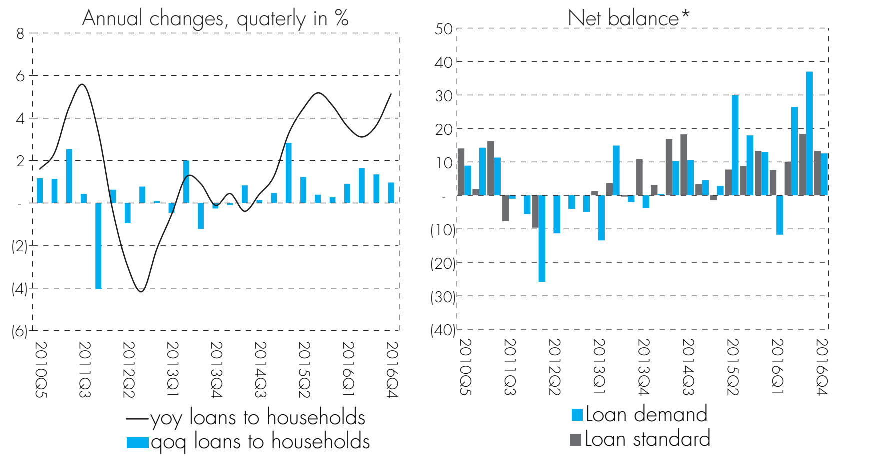
In 2016 Q4, loans to enterprises supported the services sector but less the construction sector, whereas loans to industry and agriculture sectors shrank. The annual dynamics of these portfolios shows that the growth of loans to the sector of trade, hotels and restaurants slowed down to an average of 1.4%, compared with 2.8% in 2016 Q3. Meanwhile, lending to "other services" maintained high growth rates of 10.4%. Loans to the construction sector showed 1.2% growth, higher than the 0.8% rate in the previous quarter. In October-November, loans to industry and agriculture sectors shrank -1.9% and -4.8%, respectively, yoy. These developments seem to reflect the performance of both economic activity and the confidence indicators in 2016.

2. LOANS TO HOUSEHOLDS[4]

Loans to households improved its growth rates during the last quarter of the year. This performance reflected the easing of lending conditions for several consecutive quarters to this segment and increase of household's demand for loans. Its expansion in annual terms was supported by the growth of consumer, and mortgage. Banks are optimistic about the outlook in 2017 Q1, as they foresee further easing of loan conditions and increased demand by households.

Loan to households improved the growth rates in 2016 Q4, marking an annual rate of around 5.1% in October-November 2016, compared with the average of 3.7%, in the previous quarter. The expansion of household’s loan portfolio is supported by both the demand for loans and the improved supply conditions. Households’ demand for loans was driven by the strengthening of the consumer confidence, by improved conditions in the labour market as well as by increase of disposable income. At the same time, continuous easing of lending conditions by the banking system has supported lending in this segment.

Chart 4 Loan to households



*Net balance shows easing of conditions and vice versa.
Source:Bank of Albania.

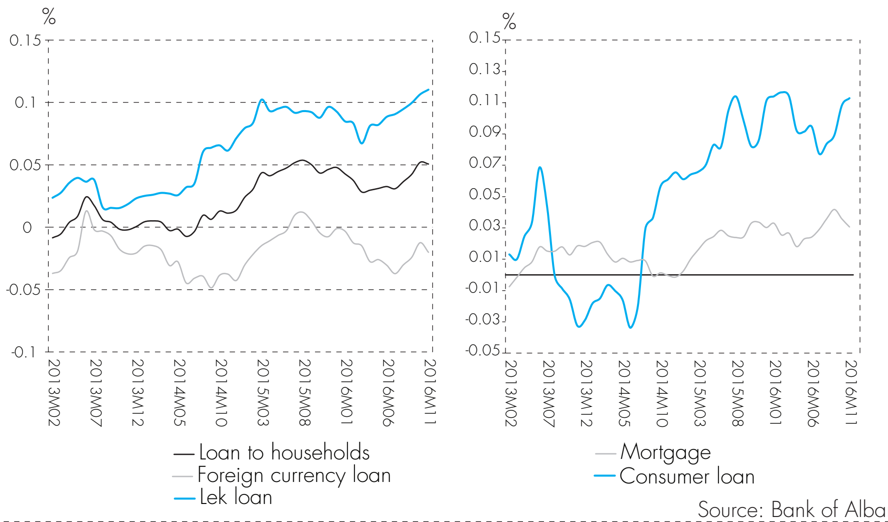
Positive developments of loans to households have reflected expansion of consumer loans, qoq and yoy. This portfolio grew by 11.4% in October-November 2016, improving the annual rate by 2.7 percentage points compared to the previous quarter. Home loan portfolio has shown a slowdown of the annual growth rates from October to November, to 3.3%, against the

4 Loan data for individuals exclude the effect of reclassified loans in off-balance sheet items.

average of 3.6% in the third quarter of the year. This performance reflected the reduction of the stock of loans in absolute terms in October and November 2016.

Lending in domestic currency continues to fully support the extension of loan to households. The stock of loan in lek recorded an average annual growth of 10.8% in October-November 2016. Lending in lek is supported both by low interest rates, as well as the households awareness of the exchange rate risk. On the other hand, the foreign currency loan portfolio shrank in nominal terms. The performance of the latter, from October to November, was driven on the one hand by a significant appreciation of lek against euro, on the other hand, by the depreciation of lek against the US dollar; such developments have contributed to opposite directions and in different scale. Adjusted for these effects, the foreign currency loan portfolio for households remained almost at the same level as a year earlier.

Chart 5 Loan performance to households by currency and use, annual change in %



Source: Bank of Albania

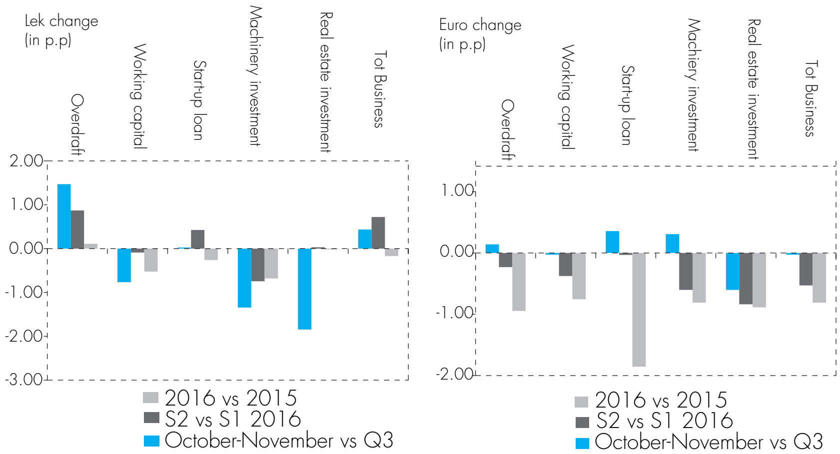
3. LOAN PRICE AND OTHER LOAN CONDITIONS

Loan interest rates in October and November increased slightly, thus reflecting mainly the developments and volatility in short-term maturities. By contrast, the interest rates of long-term loan for investment purposes have shown a downward trend. Interest rates in lek decreased slightly for households and increased for enterprises. Meanwhile, interest rates on loans in euro have been stable for enterprises and have increased for households. Besides low rates of interest rates for households, banks have offered better non-price conditions for loans. Meanwhile, for loans to enterprises, collateral requirements were tightened.

The average interest rate on loans in the domestic currency in October and November was respectively 7.64% and 8.21%, up from the previous quarter. By maturity, the interest rates on short-term loans increased, while those with long-term maturities decreased. On average, these two months the interest rate is 0.41 percentage point higher than in the third quarter of the year and largely unchanged from a year earlier. Interest rates on new loans in euro were 4.91% and 4.59%, respectively in October and November, remaining at almost the same levels with the average of the third quarter. This performance reflected the increased interest in the short-term loan segment, which was offset by decreased interest rates on medium and long-term maturities.

The average interest rate on new lek loans to enterprises in October and November increased by about 0.44 percentage point from the third quarter. By purpose of use, interest rates increased for loans for overdraft and business startup purposes. Meanwhile, they decreased for loans on working capital and investments. Cleaned form the effect and share of a certain bank in the overdraft, the analysis presents an opposite picture with interest rates on loans to enterprises being downward. The extension of the analysis horizons for the entire year shows that interest rates on lek loans to enterprises in October-November decelerated the reduction and ranged around the 9-months average. In annual terms, the loan interest rates applied to businesses declined (-0.2pp), which has been more pronounced in loans for investments. Interest rates on loans for liquidity purposes were formed mainly by the rate on overdrafts, which is a high and fluctuating rate.

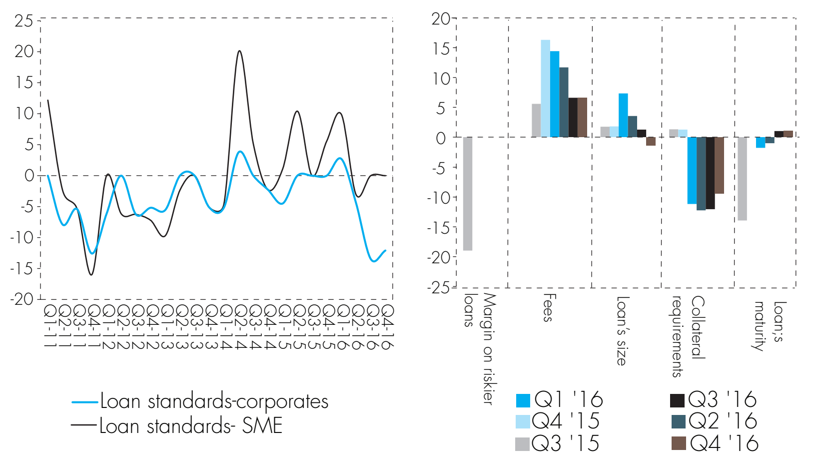
Chart 6 Interest rates in ALL and EURO on loans to enterprises



Source:Bank of Albania.

The average interest rate on new euro loans to enterprises, in October and November, decreased by 0.03 percentage point, from the third quarter. By purpose of use, interest rates decreased for loans for investments and increased for loans for overdraft purposes. Meanwhile, they remained almost unchanged for working capital and increased for equipment purchase. During 2016, the average rate of euro loans to enterprises is lower by 0.71 percentage point in 2015 and by 1.7 percentage points in 2014. Its reduction is present across all types of business funding in euro.

Chart 7 Loan to enterprises performance (net balance*)

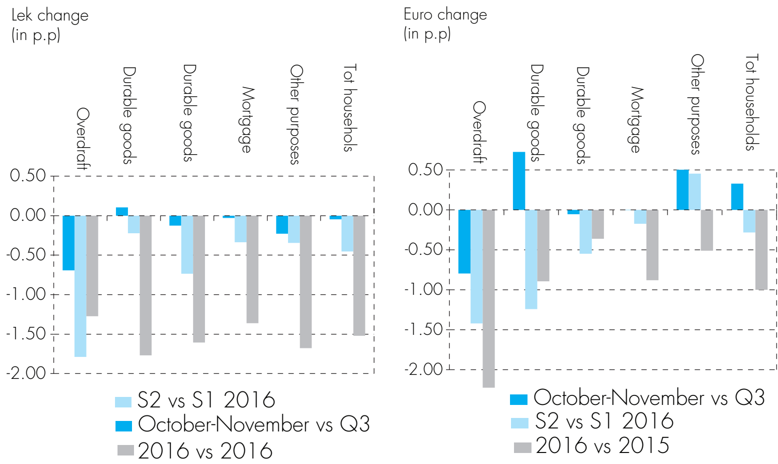


*Net balance shows easing of conditions and vice versa.
Source:Bank of Albania.

In 2016 Q4, banks tightened lending standards for large enterprises and kept them unchanged for small and medium-sized businesses. By purpose of use, the tightening has been present across all types of funding. The standards were tightened by increasing collateral requirements. This standard has been tightening for over a year, reflecting the difficulties faced by banks in the loss loan collateral executions. Other non-price elements, like commissions, loan maturity or average margin, result on the easing side of lending standards, but to a lesser extent.

The average interest rate for loans in domestic currency to households in October and November remained almost unchanged, standing 0.04 percentage point lower than in 2016 Q3. By purpose of loan use, lower rates were recorded for overdraft loans, loans for consumption of durable goods and real estate loans. Interest rates on loans to households increased for the consumption of non-durable goods. On average, during July-November 2016, the interest rate on lek loans to households is 0.45 percentage point lower than in the first half of the year and 1.76 percentage points lower than in 2015. The reduction of interest rates continues to be pronounced for consumer and mortgage loans, and less for overdraft loans and those for operating activities.

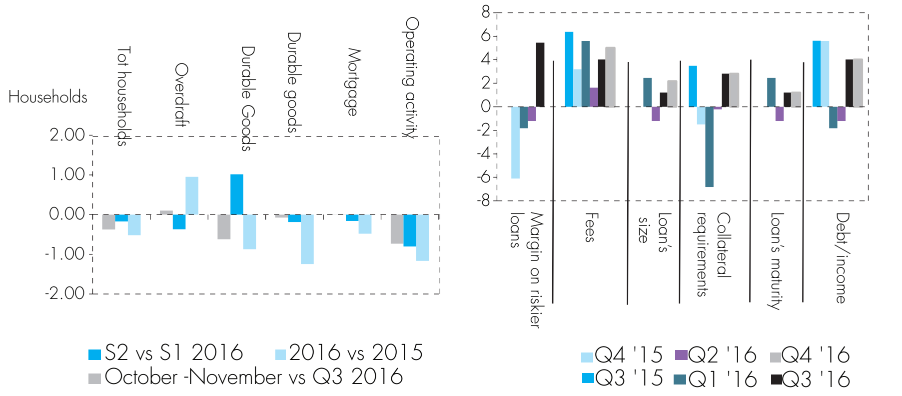
Chart 8 Interest rates in lek and euro loans to households



Source: Bank of Albania

Interest rates for loans in euro increased slightly for households. In October and November, the average interest rate on such loans averaged 0.33 percentage points higher than in 2016 Q3. Interest rates increased in the category of durable goods consumption and operating activities, whilst interest rates on overdraft decreased. In average terms, interest rates on mortgage loans did not change these two months, but still remains at historical low levels. Similar to lek loans, interest rates on euros loans in 2016 are lower than in the previous year, but to a lesser extent. The average interest rate for the first 11 months of this year is 1.0 percentage point lower than in 2015 and 1.37 percentage points lower than in 2014.

Chart 9 Spread of loan interest rates in lek and euro (left in pp) and lending conditions (in net balance* right) to households



*Positive net balance shows easing of conditions and vice versa.
Source:Bank of Albania.

The spread of interest rates on loans in domestic currency versus those in euro in the segment of households continues to shrink. In October-November, this spread was 2.5 percentage points compared to 2.9 percentage points in 2016 Q3. On average terms for 2016, it is 0.6 percentage point lower than in 2015. The narrowing of this spread has supported growth in the lek loan portfolio for households especially in mortgage loans. For this category, the spread in interest rates during recent months often fluctuated below zero, reflecting a further reduction of interest rates on mortgage loans in the domestic currency.

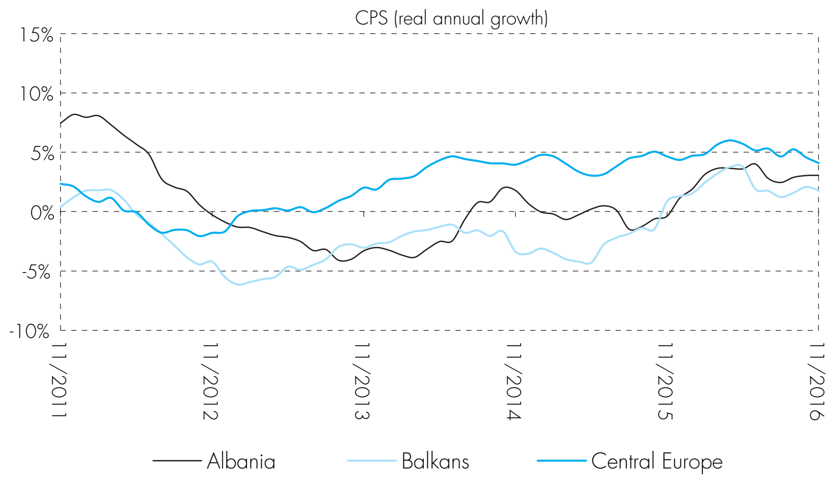
In 2016 Q4, banks continue to ease the lending conditions to households. This performance is determined by easing the conditions for consumer loans, while mortgage loan conditions did not change. To ease the conditions of loans to households, banks have used the loan price and all the other non-price elements. The easing was most pronounced in the reduction of the average loan margin, higher instalment to income ratio, the size and maturity of the loan and lower commissions.

4. LENDING TRENDS IN THE REGION

The performance of loans in the CESEE region continued to feature more contained growth rates during 2016 Q4[5]. Loan growth in this region is driven by Central Europe, whose performance has dictated the decelerating rates of recent months. Credit to the private sector in the Balkan region, albeit more stable, appears to grow at lower levels. Loan developments by economic agents are characterized by faster growth rate of loan to households.

The stock of credit to the private sector in the CESEE region expanded by 3.6% in October-November, compared with around 4.1% in 2016 Q3. In regional terms, the slowdown is dictated by the performance of the loan in Central Europe, as well as of that in the Balkan region. Bank lending surveys in the CESEE region for 2016 H1 indicate that credit conditions on the supply side have remained broadly unchanged against the perception for demand improvement[6]. This has further deepened the gap between supply and demand. Changes in the regulatory framework, constraints on banks' capital and non-performing loans at group level are reported to be among the key factors contributing to the tightening of supply terms in lending. On the other hand, demand for credit has continued to increase and factors which affect it, have positively contributed, thus supporting the expansion of loan in the CESEE.

Chart 10 Loan to private sector in the countries of the region

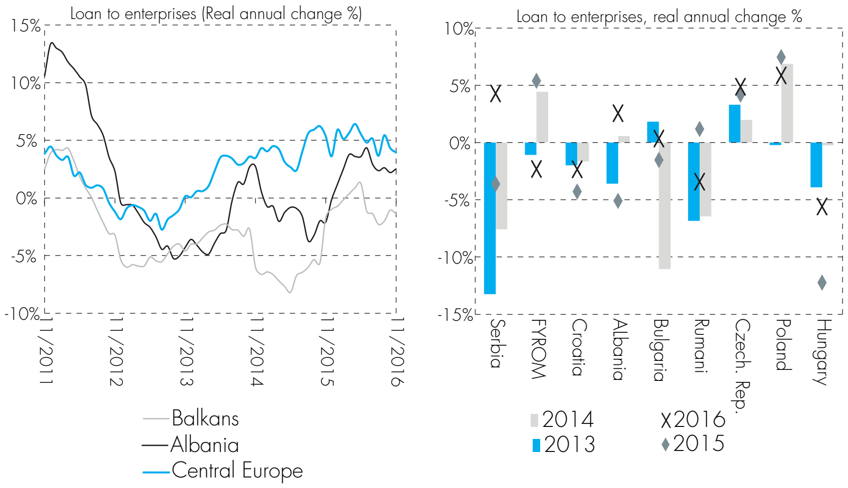


Source: Bank of Albania.

[5] The analysis of monetary and financial data for the region inlcudes October and November 2016.

[6] Survey on lending activity in the countries of Central and Eastern Europe. 2016 H1. http://www.eib.org/attachments/efs/economics_cesee_bls_2016_h2_en.pdf

Chart 11 Loan to enterprises in the countries of the region

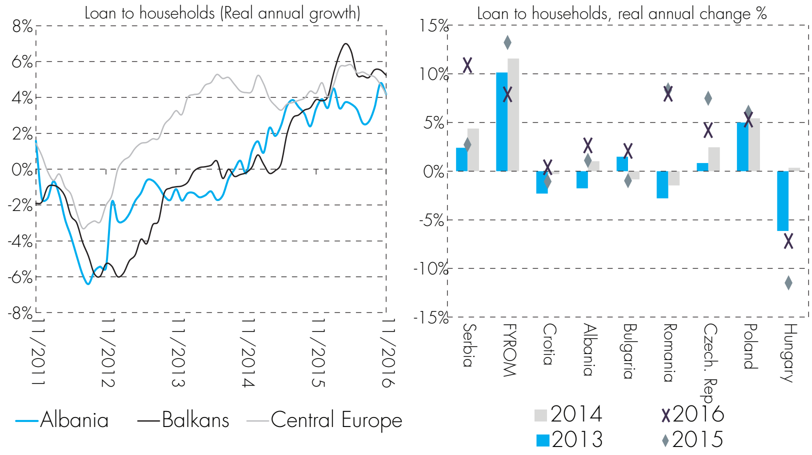


Source: Bank of Albania.

Developments in regional terms continue to show a relative segmented performance, where Central Europe has contributed mostly to the increase of lending in the CESEE countries. However, the slowdown of lending rates in the region during recent months, in parallel with a slight increase trend of lending in the Balkan countries, have contributed to the narrowing of the gap between the performance of lending in these two regions. The slowdown in lending rates in the region of Central Europe is mainly driven by the deepening of loan contraction in Hungary, along with more contained rates of growth recorded in Poland and the Czech Republic during October-November. Developments in the Balkan region reflect the positive performance of lending in Romania, Bulgaria and Serbia. Albania ranks well in terms of growth of credit the private sector, which is faster than the average of the Balkan countries in annual terms.

Business loan portfolio marks a steady growth in the countries of Central Europe. The bank lending survey in the region of CESEE reports for slightly improved conditions for loans to large enterprises. Loans to enterprises performance remains in negative territory for the Balkan region, although more moderate compared to the third quarter of the year. Loans to enterprises in Albania marked a low but relatively stable increase.

Chart12 Loan to households in the region



Source: Bank of Albania

Loans to households leads the expansion of the loan portfolio to the private sector. Its performance is stable, both in Central Europe countries as well as in the Balkans. According to the lending activity of CESEE, factors such as consumer confidence, developments in the housing market and consumer spending not for housing, have positively led to the increase of households demand for loans.