Bank of Albania

TRENDS IN LENDING

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C O N T E N T S

INTRODUCTION

"Trends in Lending" presents a detailed overview of the most recent credit developments in Albania and in the region. To this end, it studies the monetary data, interest rates and credit conditions outlined in the Bank Lending Survey. In more concrete terms, Trends in Lending takes into account the following key statistics: a) statistics of real flows [1] for the lending activity of banks in the private sector; b) qualitative data from the Bank Lending Survey; c) statistics on loan interest rates, both in lek and euro; d) monetary data and interest rates for lending activity in the countries of the region.

The regional countries covered in the analysis are: Bulgaria (BU), Croatia (CR), Romania (RO), Serbia (SR), Poland (PL), Hungary (HU), the Czech Republic (CZ), and the Republic of North Macedonia (RNM).

The analysis covers the data available as at 22 January 2022, which include preliminary information for monetary and financial data as at December 2023, and data from the Bank Lending Survey 2023 Q4. Data on credit in regional countries are as at November 2023.

[1] *Data on lending are obtained from banks' balance sheets and refer to funding to the resident private sector- enterprises and households. Starting from 2022, the analysis of the loan portfolio is based on the new set of data prepared by the Financial Statistics Department, in line with the ECB methodology on "real" credit flows, which excludes both the exchange rate fluctuations and written-off loans from balance sheets. Data for December are preliminary.*

OVERVIEW OF RESULTS

Credit expansion to the private sector followed a decelerating trend until the third quarter of the year, and then it improved, similar to the trends observed in the economies across the region and in partner countries. Developments in lending performance show that:

- ***Loans to private sector in the country** maintained stable growth rates, close to the average levels of the first half of the year. On the other hand, the short-term dynamics in the last quarter display a rapid expansion, especially in December, affected by the high demand of enterprises for financing, especially for investments.*
- ***Financing of enterprises and households was mainly denominated in lek**, influenced, among other things, by the continuation of the tendency of enterprises and households to replace loans in euro with loans in lek. Lower interest rates for loans in lek and appreciation of the exchange rate are considered to be the main factors behind this phenomenon. This trend is also reflected in the shift in the structure of the loan portfolio towards lending in lek.*
- ***By size of enterprises**, lending to large and medium-sized enterprises, after slowing down until the third quarter, it improved in the last quarter, but at a slower pace compared to the first six months. The opposite has happened with the financing of small enterprises, where lending has been improving throughout the year, shifting to positive territory after June. By sector of the economy, banks increased lending to enterprises in the tourism and service sectors and slowed it down for enterprises operating in the sectors of trade, construction and agriculture. Enterprises in the industry sector are the only ones to have reduced bank borrowing at stable rates.*
- ***Growth rates of loans to households** slowed slightly in the second half of the year, reflecting both a steady demand for funding and eased conditions from banks as well as the structural shift among segments. Thus, the expansion of the growth rates of consumer loans was balanced by the slowdown of loans for house purchase. By currency, the acceleration of growth rates of loans in lek has offset the slowdown of loans in foreign currency.*
- *In parallel, in the second half of the year, **the price and non-price conditions** of the loan supply, appear more relaxed, reflecting a reduction of the risk perceived by banks and their willingness to take more risk in the face of increased competition and a positive economic outlook. However, interest rates for loans in lek to both enterprises and households increased in the last quarter, reflecting the change in the policy rate in November.*
- *In the countries of the region, **credit to the private sector** continued to slow in 2023 H2, reflecting the weak growth of loans to enterprises. Meanwhile, loans to households, has signalled for improvement. Credit conditions continue to tighten since the first months of 2022, while loan demand is reported to be improving. Most countries in Balkan region continue to report satisfactory credit growth rates, despite the slowdown compared to the first half of the year. Credit growth in Albania is comparable to the average rate recorded in these countries.*

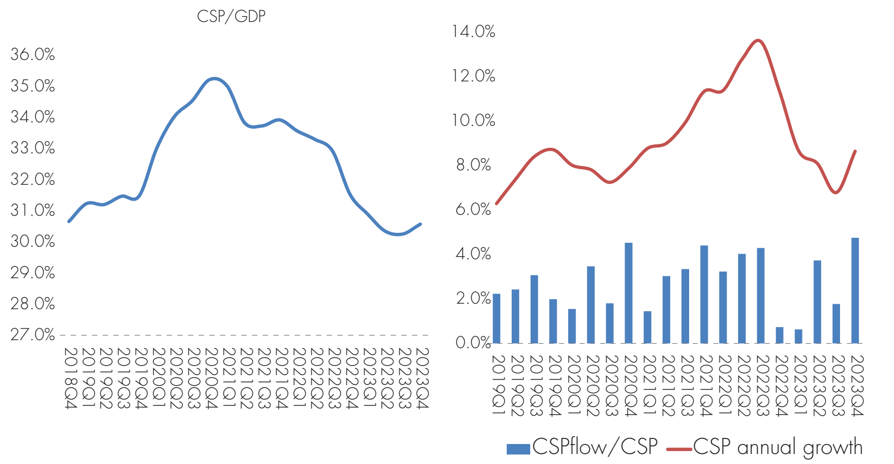
1. CREDIT TO PRIVATE SECTOR

Credit to the private sector in Albania showed stable growth rates, close to the average levels of the first half of the year. The short-term dynamics, in the last quarter display a rapid expansion, especially in December, driven by the high demand for financing from enterprises, especially for investments. Price and non-price conditions of loan supply appear more relaxed, reflecting the reduction of risk perceived by banks and banks' risk appetite given the increased competition and positive economic prospect.

Lending activity in Albania expanded at a steady pace in the second half of the year, reflecting the increased demand for financing from economic agents and the eased supply conditions. The average annual growth rate of 8% was the same as that of the first six months. However, during this period, the growth rates of the loan portfolio for the private sector slowed down until September, changing side in the last quarter- especially in December. This volatility is mainly due to the performance of loan portfolio to enterprises while that for households has steadily slowdown.

By maturity of the approved loan, it is noted that lending has shifted from credit to cover short-term needs toward long-term ones. Thus, the annual credit growth rate on short-term loans halved from 5.7% to 2% in the second half of the year, while medium-term loans increased by about 4.5 pp to 6.9 pp for the same period. Long-term loans maintained the same growth rate of 9%, unchanged from the first half of the year. The positive performance of loans for investments- to both enterprises and households- has underpinned these developments, in response to the high demand from the private sector and banks' higher risk appetite.

Chart 1 Loan performance to the private sector in Albania as a ratio to GDP

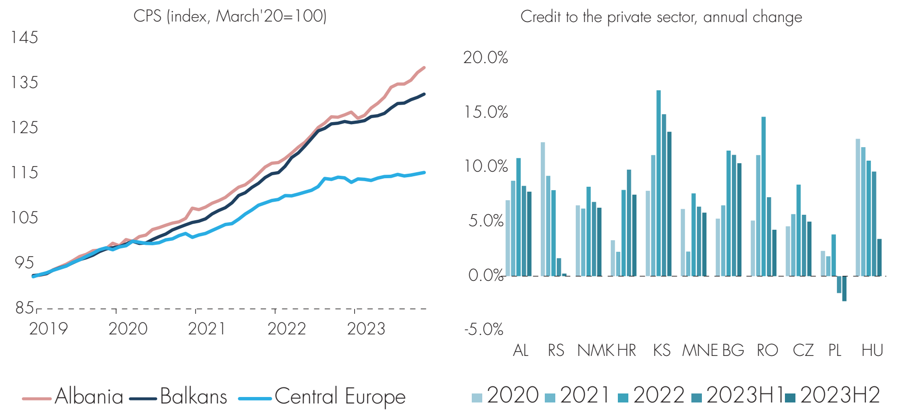


Source: Bank of Albania.

Loans to the private sector decreased to 30.6% or 1.2 pp less than a year ago against GDP, reflecting the rapid expansion of economic activity in the country as well as the strong appreciation of the lek against the main currencies. In the absence of this appreciation, credit flows remain high, at around 2.8% of GDP during the year (from 3.1% in 2022). The dynamics of lending by currencies show that the rapid growth of loans in lek during the year led to the significant expansion of loans in lek in relation to GDP at 17.3% (by 1 pp), while loans in foreign currency shrunk at 13.3%. While according to bank clients, it is noted that loan to households remained at the same level as in the previous year at 12.3% of GDP, while loans to enterprises shrunk by 1 pp, at 18.3%.

Credit to the private sector in the countries of Balkan and Central Europe has slowed further in 2023 H2 as a result of the weaker performance of loans to enterprises. The divergence across countries regarding the credit performance has deepened. The countries of the Balkans continue to perform better when compare to the countries of Central Europe. The countries of the Balkan region continue to show a comparatively better performance than those of Central Europe, mainly due to the fact that interest rates in the latter increased more aggressively. In the Balkans, Romania and Serbia are examples similar to the CE countries. Albania ranks among the countries with the highest credit growth rates. In the first months of 2024, a rebound in loans for investments and purchase of real estate is expected; these segments were the ones that mostly suffered the lower lending over the course of past year.

Chart 2 Performance of loans to the private sector in the both Balkan and Central European regions



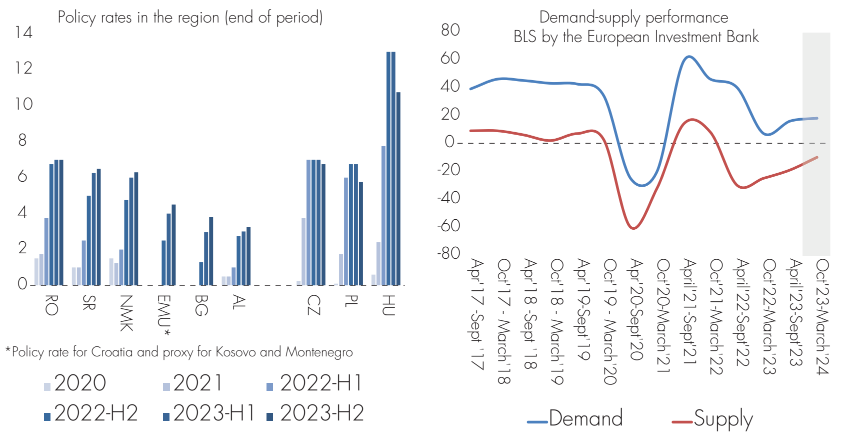
Source: Bank of Albania; Banks of regional countries; EIB; staffs' calculations.

Bank lending survey conducted by the European Investment Bank[2] shows that the performance of lending in the countries of the region has been mostly a factor of the tightening of supply conditions, at a time when loan demand

[2] *As reported in the BLS for CESEE countries complied by the European Investment Bank. For more detailed information, please refer to the Bank Lending Survey section at: https://www.eib.org/en/publications/20230288-cesee-bls-2023-h2*

has continued to remain positive, despite its slowdown. The tightening cycle of lending conditions in the region, which began in the first months of 2022, affected first by the war in Ukraine and then by the high inflation and rising interest rates, has continued. Conditions are expected to tighten further, at least until the first quarter of 2024, where the main concerns remain the performance of the economy and expectations for deterioration of the credit portfolio quality in the future. The last factor, although not materialized yet, continues to be considered by the banks as the main element in their prudent approach regarding lending. As for demand, it grew the lowest at the end of 2022 and early 2023, and later on it improved. In addition to investments for real estate, where demand has decreased in most countries, credit demand remains resilient.

Chart 3 Policy rates, credit demand and supply (right) in the Balkan and CE countries



Source: Bank of Albania; Banks of regional countries; EIB; staffs' calculations.

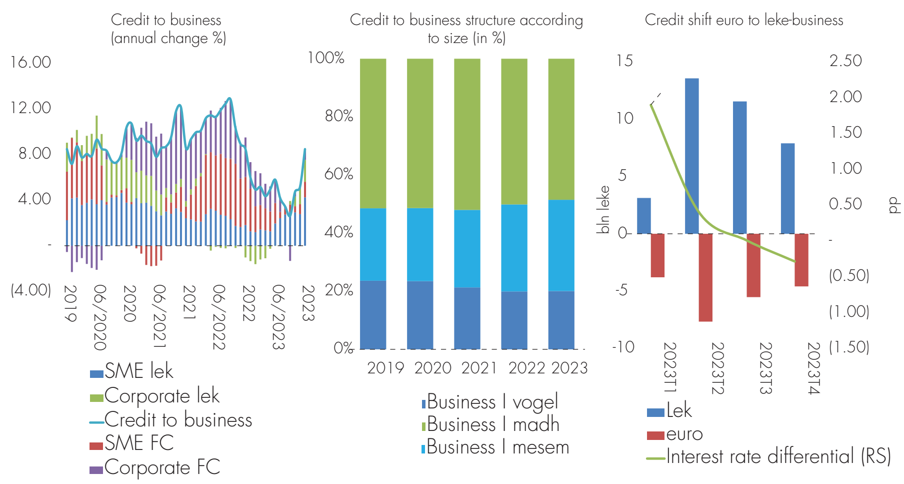
In addition to tight supply conditions, loan interest rates in the region have also been high, following increases in the policy rate, being an important factor in discouraging credit demand, the long-term loans in particular. The most aggressive policy rate hikes in response to higher inflation have been undertaken in CE countries, significantly impacting the curbing of lending in these countries. In the last quarter of 2023, central banks of these countries started the lowering cycle of interest rates; by reflecting this reduction on loan interest rates, lending is expected to rebound during 2024.

2. LOANS TO ENTERPRISES

Banks financing to enterprises has fluctuated in the second half of year, affected both by their abundant liquidity and by a shift in the structure towards lending in lek and for investments. However, the dynamics of the last quarter show an improvement in financing to enterprises, driven both by the growing demand - especially in December, and by the easier terms credit supply conditions from banks. Credit improved across all sub-segments regardless of size. But it was more pronounced in small and large enterprises. By sector of the economy, in the last quarter, lending to the sector of tourism and services improved. These two are also the main sectors that contribute to the growth of economic activity in Albania.

In the second half of the year, the growth rates of loans to enterprises, averaging around 5%, are close to the average levels recorded in the first half of the year. But in contrast to the beginning of the year, there is a shift towards financing in lek and for covering investment needs. Short-term dynamics show that loans to enterprises improved in the last quarter of the year, showing a different approach from that observed until September. Thus, the average growth of the portfolio by 6.1% was around 2.7 pp higher than that of the third quarter. The improvement in growth rates was observed in all sub-segments by size, mostly evident in small and large enterprises. This development was supported by the good performance of the economic activity in the country, the high level of confidence and prices in addition to the still accommodating credit conditions.

Chart 4 Loans to enterprises by currency and size

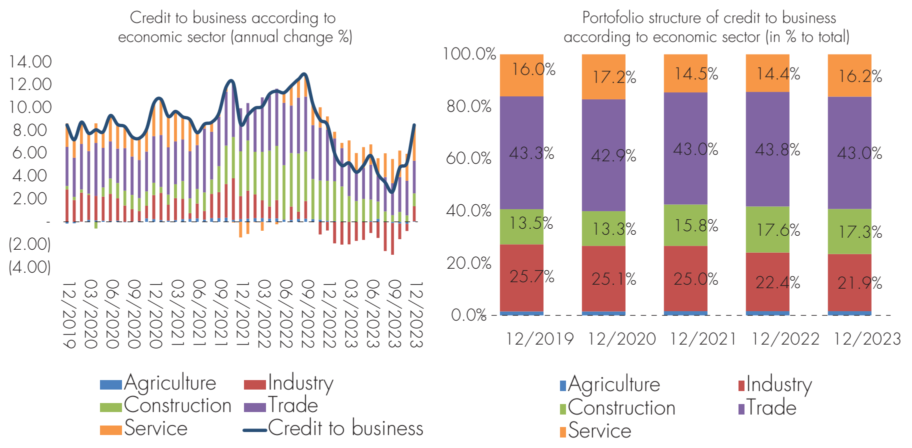


Source: Bank of Albania.

Credit portfolio to small enterprises grew by 6.8% in the last quarter, or twice from the level in the third quarter. Meanwhile, loans to large enterprises, after stagnating in the previous quarter, has revived to 3.4% yoy at the end of the year. By currency, the increase was more pronounced in lek-denominated loans, which offset the slowdown of loans in foreign currency. The shift of the portfolio of loans to enterprises from loans in euro to loans in lek continued in the last quarter as well. This phenomenon has been supported both by the transition to negative territory of the interest rate spread for loans to enterprises and by the continuation of appreciating pressures in the foreign exchange market. In the last quarter, about 90 loans in euro were granted amounting at ALL 4.6 billion. Compared to the third quarter, the number of granted loans is about three times higher, while the slightly smaller amount signals that this phenomenon has been more widespread in smaller loans, mainly related to small and medium-sized enterprises. It is precisely these two segments that have supported the significant increase in loans in lek for credit to enterprises.

By sector of the economy, it is noted that financing for the industry sector has continued to shrink even in the second half of the year, by around 5% year on year, lower compared to the contraction of around 7% of the first half of the year. Meanwhile, loan to the tourism and service sectors **improved compared to** the first six months of the year, at 12% and 16%, respectively. Financing of the agriculture, construction and trade grew at slower rates compared to the first six months, at 4.8%, 5.2% and 5%, respectively. These developments are in line with the contribution that these sectors give to the growth of the economic activity in the country. **In reflection of these dynamics, significant changes are noted** in the sectoral structure of the credit portfolio. Thus, compared to the previous year, there is a decrease of about 0.5 pp of **the share of loan to the sectors of industry and construction, and a more significant decrease of about 1.8 pp** in the trade sector. At the same time, the share of lending to the tourism sector increased at 8.9% (by 0.8 pp yoy) and the share of lending to services increased at 16.2% (by 1.8 pp yoy).

Chart 5 Loans to enterprises by sector of the economy

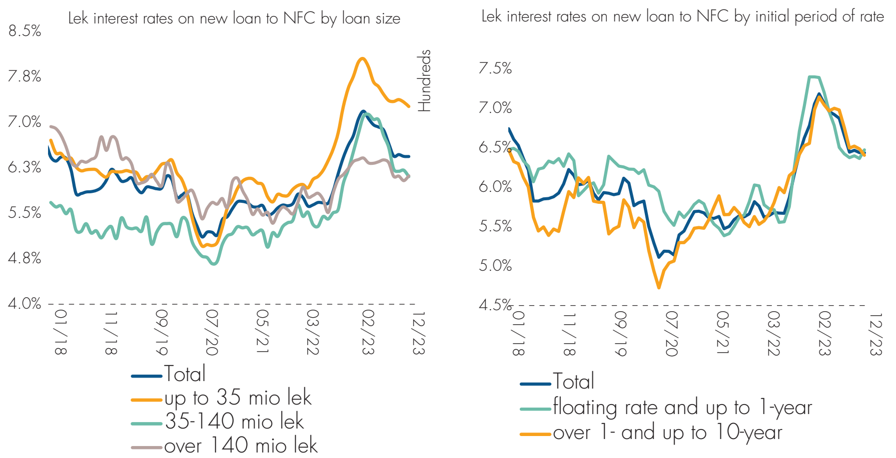


Source: Bank of Albania.

Interest rates of loans in lek to enterprises increased slightly in the last quarter, following the change in the policy rate in November. The transmission of this increase varied in relation to the loan size, being more pronounced for large loans. The loan interest in this category is higher than their level before the start of the tightening of the monetary policy cycle. Loan interest rate for small amounts fluctuates in values close to those of the previous months. Loan interest in euro continue to gradually increase. They are reflecting the increases in the policy rate of euro by the ECB throughout this period.

In the last quarter, the average interest rate on new loans in lek to enterprises, was 6.5% from 6.4% in the previous quarter. Interest rate increased mainly for loans over ALL 35 million, which went up in the last two months. The average interest for these loans reached 6.5% in December from 6.2% in the third quarter. The category of loans amounting up to ALL 35 million, which is mainly used by small enterprises, decreased slightly at 7.2%, from 7.4% and 7.3%, respectively in the previous two quarters. Compared to other categories, interest rates of this category are often affected to a large extend by the performance of the 12-month T-bills yield. Meanwhile, the cost of financing for short-term liquidity slightly decreased, where the interest rates on overdraft and working capital in the last quarter were 6.1% from 6.4%, respectively, in the first nine months of 2023. The analysis by interest rate fixation period shows the increase of interest rates on loans with a fixed initial rate of up to one year, whilst those with initial fixed interest rate over one year have not changed. In 2023 Q4, interests in both these categories were 6.7% and 6.4%, from 6.3% and 6.4% in the third quarter.

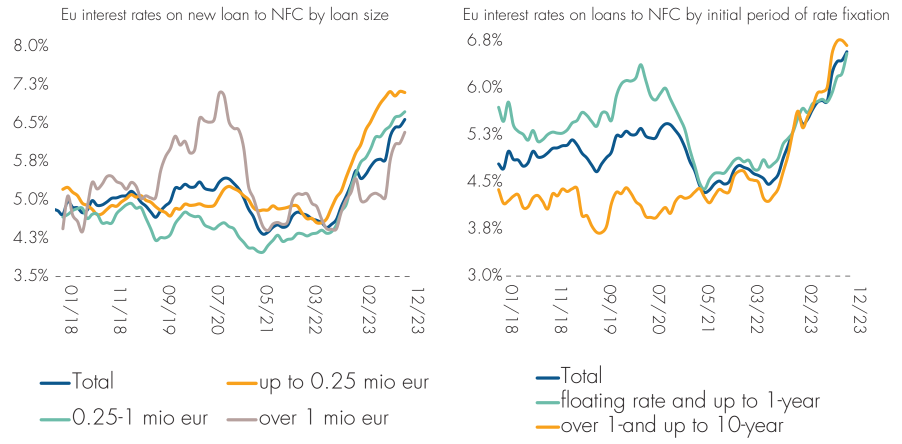
Chart 6 Interest rates on loans in lek by size of the loan (left) and the initial interest rate (right) to private enterprises



Source: Bank of Albania.

The interest rate on loans to enterprises in euro, was 6.8% in the third quarter, from 6.4% and 6.1% in the two previous quarters, respectively. By size of loan, analysis shows that the increase in interest rates was pronounced for loans over EUR 250,000(6.8% from 6.1%), while interest rates on loans to small enterprises slightly decreased in this quarter (6.9% from 7.3% in the previous quarter). The increase in the policy rate for the euro by the ECB during this year, is gradually being reflected in the interest rates on loans in euro to enterprises. The analysis according to the period of initial fixation of the interest rate shows that during these months, the category with initial fixed interest rate up to one year, increased its rates higher compared to that with initial fixation over one year. Meanwhile, the interest rates on overdraft and working capital regularly increased every quarter, resulting 6.4% in the last three months, from 5.7% during January-September of this year.

Chart 7 Interest rates for loans in EUR by size of the loan (left) and the initial interest rate (right) to private enterprises

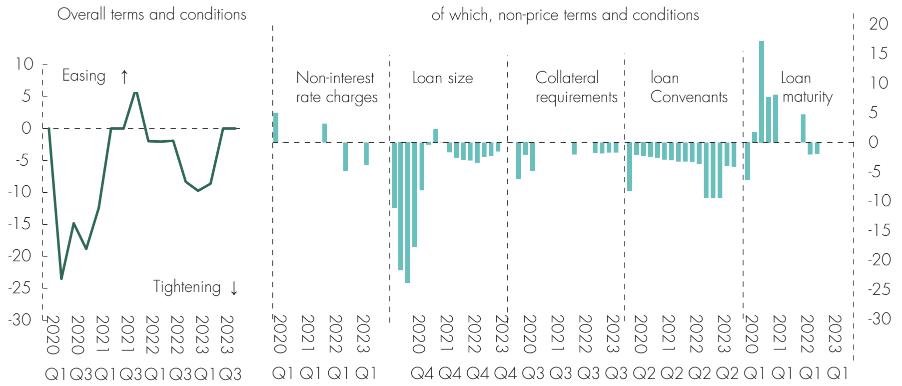


Source: Bank of Albania.

Banks did not change credit standards, terms and conditions for loans to enterprises, for the first time, since the beginning of the normalization of monetary policy, under the increased pressure from competition in the banking system.

In 2023 H2, banks perceived, overall, a more favourable macroeconomic situation and an optimistic outlook for the main macroeconomic indicators. In particular, banks perceived lower risk for enterprises' balance sheets and their solvency during the second half of the year. Although banks remained cautious when assessing the risk of loans to enterprises, in the second half of the year, lending policies were based on wider risk tolerance corridor. Under the increased pressure from competition in the banking system, banks maintained credit standards, terms and conditions on loans to enterprises, unchanged, for the first time, since the beginning of the normalization of monetary policy by central banks in both Albania and abroad.

Chart 8 Non-price terms and conditions for new loans to enterprises

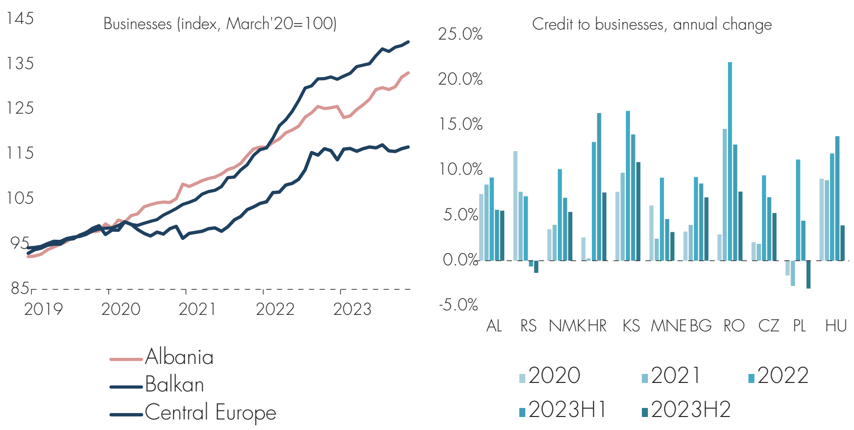


For more detailed information please refer to the Bank Lending Survey section: https://www.bankofalbania.org/Monetary_Policy/Analyses/Trends_in_lendings/

Source: Bank of Albania and staffs' calculations.

The implementation of the same terms and conditions in the second half of the year (after the tightening taking place in the first half of the year) was supported, on the one hand by lower margins on new loans to enterprises. On the other hand, despite still present, constrains in the loan covenants between banks and enterprises were lower compared to the first half of the year. Other non-price elements that determine the entire credit terms and conditions, such as commissions, collateral requirements and maximum loan maturity, recorded balances similar to the first six months of the year.

Chart 9 Credit to enterprises in the region of Balkan and Central European



Source: Bank of Albania; Banks of regional countries; EIB; staffs' calculations.

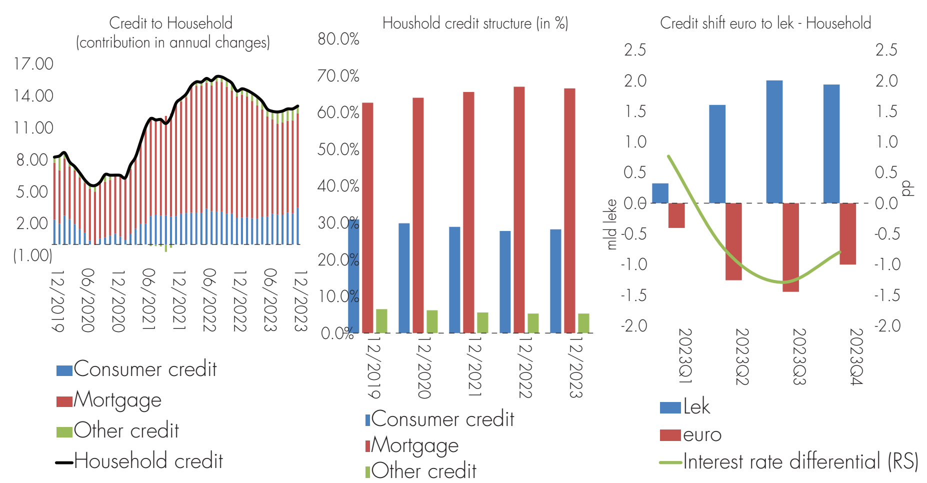
Credit to enterprises slowed its growth rates in almost all countries of the region. In the face of a weaker performance of the economy and an increase in interest rates, enterprises' demand is focused on short-term loans for the purpose of financing liquidity needs, while demand for investments continuous to decline. The weak performance of loans to enterprises is more pronounces in the CE countries (Poland and Hungary). Meanwhile, in most of Balkan countries, the increase of loans to enterprises remains strong despite the slowdown, particularly in Kosovo and Croatia. The growth in loans to enterprises in Albania is close to the average increase in the Balkan countries. According to the EIB' survey, expectations point to a recovery in loan demand for investments in the countries of the region in the next months, alongside the expectation for a continuation of loan demand for liquidity.

3. LOANS TO HOUSEHOLDS

The developments in the loan to household's portfolio were more stable. The growth rate of this portfolio was reduced compared to the first six months, reflecting the structural shift between segments. Thus, the expansion in the growth rates of consumer credit was balanced by the slowdown of loans for house purchase. Similar to the trends observed in loans to enterprises, the financing of households has mostly been in lek, the growth of which has offset for the slowdown of financing in foreign currency.

Bank lending to households continued at high rates, but decelerating during the second half of the year, where the average growth of 12.7% yoy was 1.2 pp lower than in the first half of the year. The slowdown in loans to households by currency reflected the acceleration of the growth rate of loans in lek to 13.4% on average, while the growth of credit in foreign currency has slowed by 10 pp at around 10%. Similar to the developments observed in enterprises, households have continued to prematurely close part of their loans in euro - and have replaced them with loans in lek. But in contrast to enterprises, the amount of this shift has been the same throughout the quarters, while the number of loans has been smaller compared to the number of loans in the summer months. As before, the main factors that have supported this shift have been the appreciation of the domestic currency, the lower interest rates of the mortgage loan in lek compared to that in euro, as well as the regulatory facilities for switching currency with no penalties.

Chart 10 Loans to households by currency



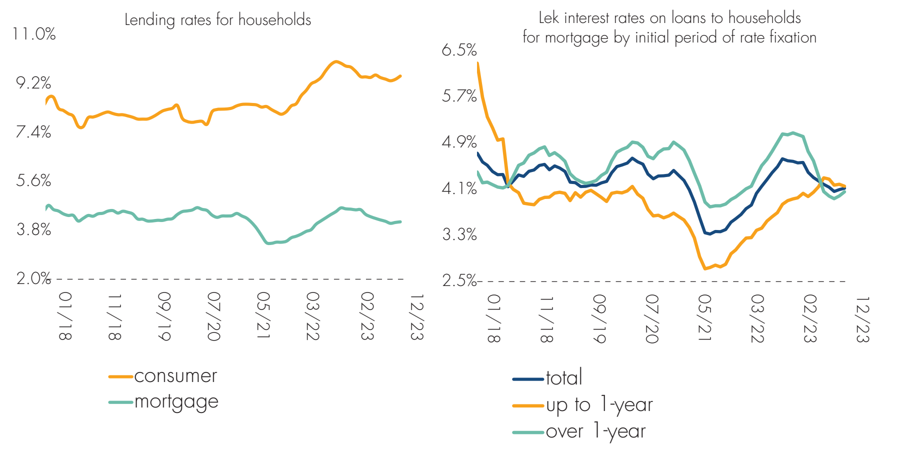
Source: Bank of Albania.

By purpose of use, credit for house purchase slowed down, while the consumer loans accelerated. The growth by 13.1% of loans for house purchase, in the third quarter was about 3 pp lower than in the first half of the year. Despite the high competition between banks and the continuous easing of conditions in this segment, households demand slowed down reflecting the increase in the cost of loans for house purchase and the tightening of the family budget as a result of high costs of living. On the other hand, consumer credit grew at a higher pace than in the first half of the year. The average annual growth of 10.6% in the second six-months was about 2 pp higher than the average in the previous period.

Interest rates on loans in lek to households have increased. This increase has reflected the change in the policy rate as well as the performance of the 12-month T-bills yield, which is used in indexing most of loans in this category. Loan interests to households increased mainly for consumer credit, while the growth of loans for house purchase has been more contained. Meanwhile, the interest rate on mortgage loans in euro decreased slightly during these months, reflecting the performance of the Euribor in the European/international market, which is widely used as a parameter for indexing these loans. This development has affected the narrowing of the interest rate gap with the loan in lek, which still remains on negative territory.

Interest rate on loans in lek to households increased in the last quarter for both consumer and mortgage loans. The average interest for consumer loans was 9.6% from 9.3% and 9.4% in the two previous quarters. Loan interest rate for house purchase was 4.2% from 4.0% in the previous quarter. Interests increased mainly during the last two months, reflecting the change in the policy rate and the performance of the 12-month yield over this period. The analysis according to the period of initial fixation of the interest rate shows that the increase in interest was formed in loans with initial fixation over one year (4.4% from 3.7%), while those with initial interest fixed up to one year have slightly decreased.

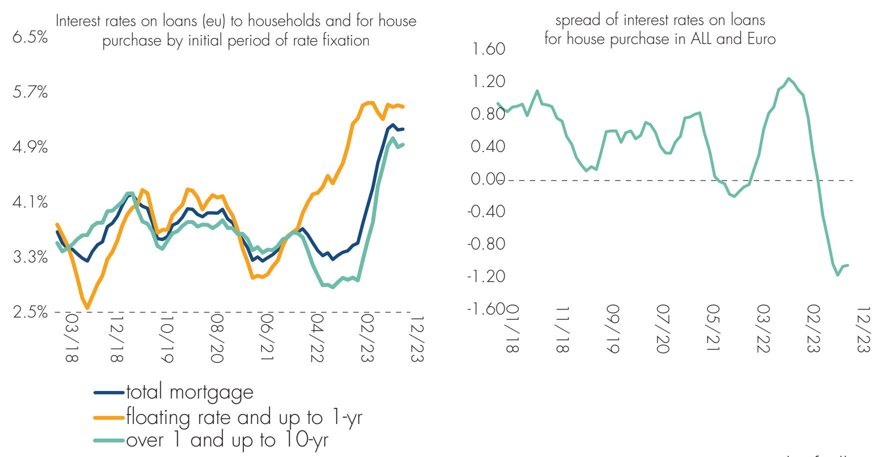
Chart 11 Interest rates of loans to households in lek



Source: Bank of Albania.

In 2023 Q4, the interest rate on new loans in euro to households averaged 5.2%, slightly decreasing from 5.5% in the previous quarter. Interest rates on loans in euro decreased for mortgage loans (5.0% from 5.3% in the third quarter), reflecting the reduction in reference rates. Unlike the interest rates of the mortgage loans in lek, the analysis according to the initial fixation of the interest shows that for the loans in euro, the interest rate decreased mainly in the category of loans with the initial rate fixed over one year. The spread between mortgage loans in lek and in euro during this month narrowed, though it remains in a negative territory.

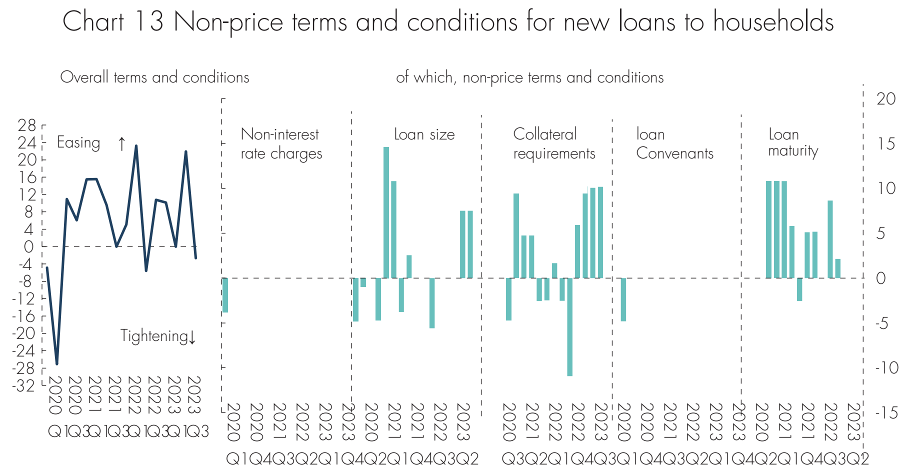
Chart 12 Interest rates on mortgage loans to households in Euro



Source: Bank of Albania.

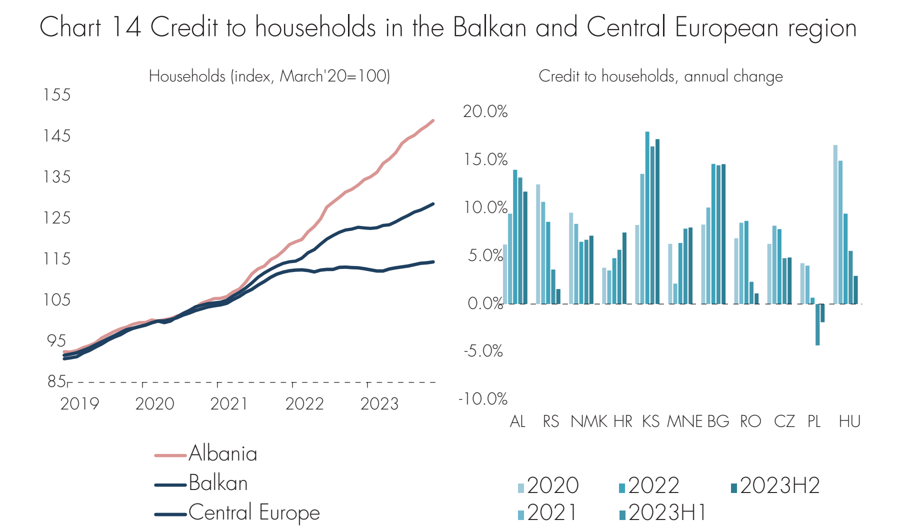
Lending terms and conditions for new loans to households were eased as a result of increased competition among banks.

In the second half of the year, banks appeared more proactive in lending to households, compared to the first half of the year. Lending standards were further eased during this period, driven by banks' positive perception of borrowers' solvency. Likewise, the competitive environment in which banks operate influenced not only the easing of standards, but also the terms and conditions of loans to households in the second half of the year. The price conditions in new loans to households remained almost the same as in the first half of the year. On the other hand, the more favourable formulation of non-price elements from the first half of the year reflected to the greatest extent the facilitating approach of banks towards lending to households. Thus, banks set lower collateral requirements in mortgage loans and approved higher loan sizes to households, thus meeting the growing demands of households for financing from the banking system. Other non-price elements, such as commissions, conditions from the loan covenants, as well as loan maturity remained unchanged compared with the first half of the year.



For more detailed information please refer to the Bank Lending Survey section at: https://www.bankofalbania.org/Monetary_Policy/Surveys_11282/Bank_Lending_Survey/
Source: Bank of Albania and staffs estimates.

Loans to households in the majority of the Balkan countries continued to steadily grow during 2023 H2. Serbia and Romania are an exception, since the growth of loans to households has significantly slowed. In other Balkan countries, loans to households during this period maintained stable rates with those of the first six months of 2023 and 2022. Compared to these countries, the annual growth of loans to households in Albania is close to the average of the Balkans (excluding Serbia and Romania). In the CE countries, the picture is more heterogeneous, where the Czech Republic stands out for stable growth of loans to households, while the latter has slowed down significantly in Hungary and continues to shrink in Poland. In these two countries, the segment of mortgage loans was the most affected one, enduring a drop in loans demand in the face of increased interest rates. The bank lending survey for the countries of the region expects a positive performance of loans for real estate during the first months of 2024.



Source: Bank of Albania; Banks of regional countries; staffs' calculations.