BANK OF ALBANIA

TRENDS IN LENDING

Olta Manjani, Erjona Suljoti, Medvin Shehu and Anjeza Gazidede
Monetary Policy Department, Bank of Albania

JULY 2019

C O N T E N T S

INTRODUCTION

Trends in Lending presents a detailed overview of the most recent credit developments in Albania. To this end, it studies the monetary data and credit terms and conditions, based on the Bank Lending Survey. In addition, it includes an overview of the most recent credit developments in Central, Eastern and South Eastern European (CESEE) countries.

- Trends in Lending takes into account the following key statistics:
- Data on bank lending activity in the resident sector of the economy;
- Qualitative data from the Bank Lending Survey;
- Statistics on credit price in lek and euro;
- Monetary data for credit volumes in the countries of the region. The countries covered in the analysis are: Bulgaria (BU), Croatia (CR), Romania (RO), Serbia (SR), Poland (PL), Hungary (HU), the Czech Republic (CZ), and North Macedonia (NMK)

Data on lending are obtained from banks' balance sheets and refer to funding by domestic banks to the resident private sector - enterprises and households. The loan portfolio analysis is based on data adjusted for the exchange rate effect. Also, these data take into account written-off loans, a process that banks have taken pursuant to Decision No 50, dated 30.03.2015 "On amendments to the Regulation 'On Credit Risk Management".

The analysis covers data available as at 26 July 2019, which include information for monetary and financial data as at June 2019[1], and data from the Bank Lending Survey 2019 Q2. Data on credit in regional countries are as at May 2019.

[1] *Data for June 2019 are preliminary.*

OVERVIEW OF THE RESULTS

Credit to the private sector showed higher growth rates over the second quarter, sustained by the expansion of loans to enterprises. Lending in lek continues to provide the main contribution, although an upward trend of lending in foreign currency was also confirmed in the second quarter. Lower credit risk and entry of new actors into the banking market, coupled with increased demand from the private sector, appear to support credit recovery in Albania.

Short-term developments confirm signals of a recovery of loans to enterprises. For this segment, the pace of growth improved, driven by credit to both small and medium-sized enterprises (SMEs) and corporations. Unlike in the previous quarter, in this round, it was credit to SMEs that showed the most notable expansion. From a longer-term perspective, the banking sector has been showing, for a number of years, a more favourable approach to SMEs, as a less credited segment, yet with a potential for contributing to economic development in the future. By sector of the economy, trade remains the most credited sector by banks; meanwhile, the industry sector has also shown positive developments in recent years.

In 2019 Q2, loans to households showed similar growth rates to the previous quarter. This portfolio expanded mainly on the back of a good performance of mortgage loans. By currency, loans to households seem to be granted almost entirely in the domestic currency. The analysis in geographical terms confirms loans to households are concentrated mostly in Tirana, especially credit for house purchase.

Interest rates on new lek loans have decreased for enterprises and remained unchanged for households, reflecting a more positive approach by banks toward lek lending and the favourable funding conditions, domestically. Non-price conditions remain slightly tightened for loans to enterprises, and on the easing side for loans to households.

Credit growth to the private sector in the CESEE region remained at moderate levels in April and May 2019, dictated mainly by the performance of loans to enterprises. Growth rates in this segment showed a more notable slowdown than in loans to households. In geographical terms, developments point to similar behaviour across the board, with credit growth rates slowing down both in the Balkan region and in Central Europe.

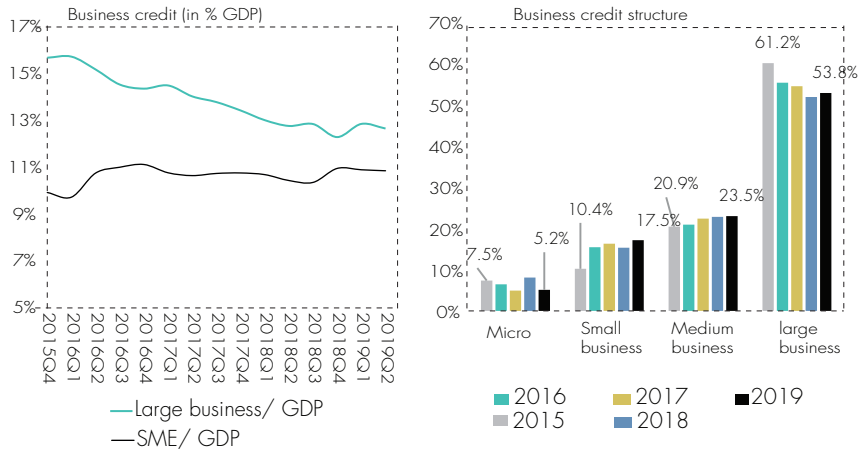
1. LOANS TO ENTERPRISES[2]

Loans to enterprises increased in 2019 Q2, confirming the trend that started at the end of 2018. Unlike in 2019 Q1, in this quarter, the improvement came from loans to small and medium-sized enterprises.

Loans to enterprises have dominated bank credit for years, reflecting a structure of financing the domestic economy based on the banking sector. At the start of the decade, loans to enterprises accounted for around 61% of credit to the private sector; currently, they account for around 66%. In relation to the Gross Domestic Product, this portfolio peaked at 27.2% in 2012, but later followed a downward trend, driven by a lower growth of credit to this segment compared to economic growth. In June 2019, loans to enterprises as a ratio to the Gross Domestic Product amounted to around 23.4%[3], 0.7 p.p. higher than at the end of 2018. The expansion of this ratio in the last two quarters reflects the recovery of loans to enterprises over this period.

In 2019 Q2, **loans to enterprises** grew by ALL 7.3 billion, reflected in the improvement of this portfolio's growth pace to 7.2% (from 6.2% in March 2019). Loans to enterprises appear on a positive trajectory since the end of 2018, sustained by the somewhat more positive approach of the banking sector toward enterprises, following structural changes that took place in the previous year as well as increased demand from this segment.

Chart 1 Loans to enterprises by size of enterprise



Source: Bank of Albania.

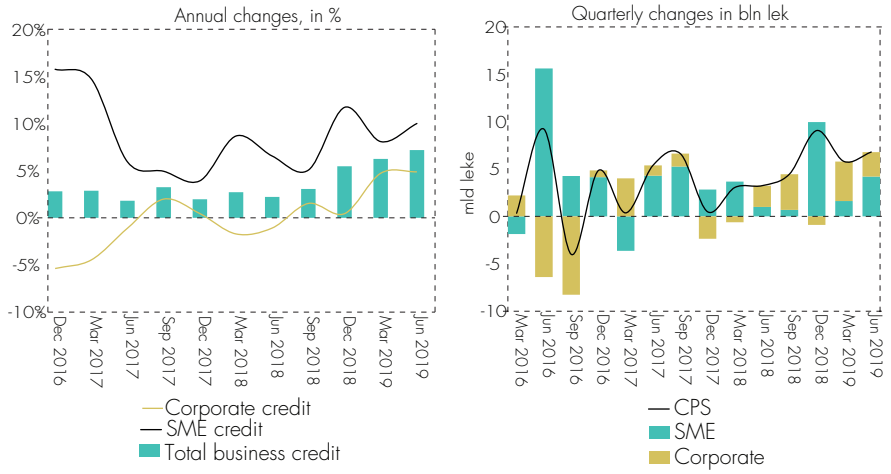
The improvement in the growth pace of loans to enterprises was mostly fuelled by loans to small and medium-sized enterprises (SMEs), up by ALL 4.5 billion in 2019 Q2. In annual terms, the growth rate of loans to SMEs accelerated on average to 9%, or 4 percentage points higher than in the first quarter. Within this category, positive developments have been noted especially in loans to small enterprises. The growth rate of corporate loans slowed down to

[2] *Data for loans to enterprises are adjusted for written off loans and exchange rate volatility.*

[3] *In calculating the loan to GDP ratio, the Bank of Albania estimates on the Gross Domestic Product for 2019 Q2 has been used.*

5.3% from 6.2% in the first quarter, shrinking its contribution to the expansion of the credit portfolio over this quarter. These developments have reflected an improvement in demand and supply for loans to SMEs, and worsening for corporations, as shown by the results in the Bank Lending Survey for 2019 Q2.

Chart 2 Loans to enterprises by size



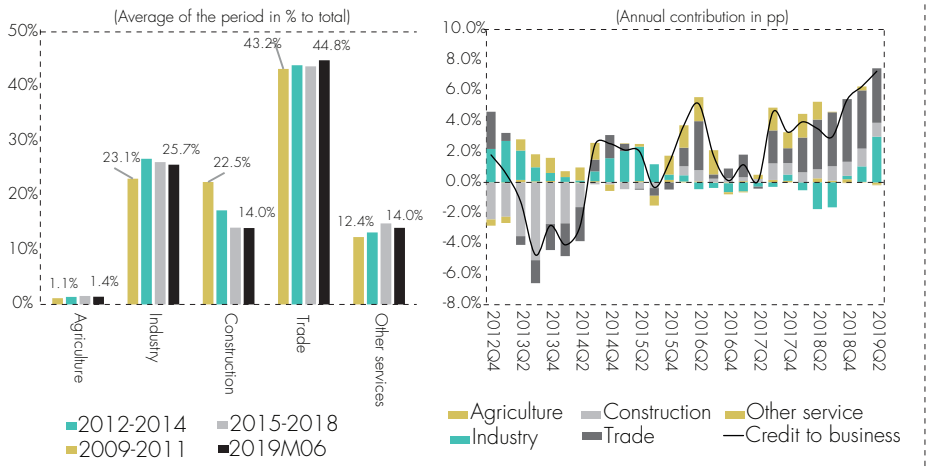
Source: Bank of Albania.

Improvement of loans to enterprises has reflected an increase in credit to trade and industry sectors.

Improvement of loans to enterprises in 2019 Q2 was supported by a growth in funding to the industry sector (12%, y-o-y) and trade (8% y-o-y). Unlike in Q1, growth of credit to this sector has been channelled mainly to investments, squaring with the high contribution from credit for liquidity in the previous quarter. Notably, the sub-branch of "Electricity, gas, steam and air conditioning supply" attracted more bank funds. Beyond these developments, credit to agriculture contracted and the growth pace of credit to construction slowed down. These sectors registered a reduction by -9% and an increase of 6.5 %, respectively, in the second quarter.

From a long-term perspective, the banking sector has financed mainly firms operating in the trade, hotels and restaurants sector. In June 2019, credit to this sector accounted for around 45% of total loans to enterprises, showing a steady performance over the years. Within this sector, in recent years, credit to the sub-branch of hotels and restaurants has increased, on the back of the upsurge in tourism in Albania. On the other hand, agriculture remains the least credited sector by banks. Credit to this sector accounts for a minor share in total loans to enterprises, at 1.4%, dictated by both structural problems in this sector related to access to finance, and the banks' reluctance to credit it.

Chart 3 Loans to enterprises by sector*



Source: Bank of Albania.
*Trade represents the sector of trade, hotels and restaurants.

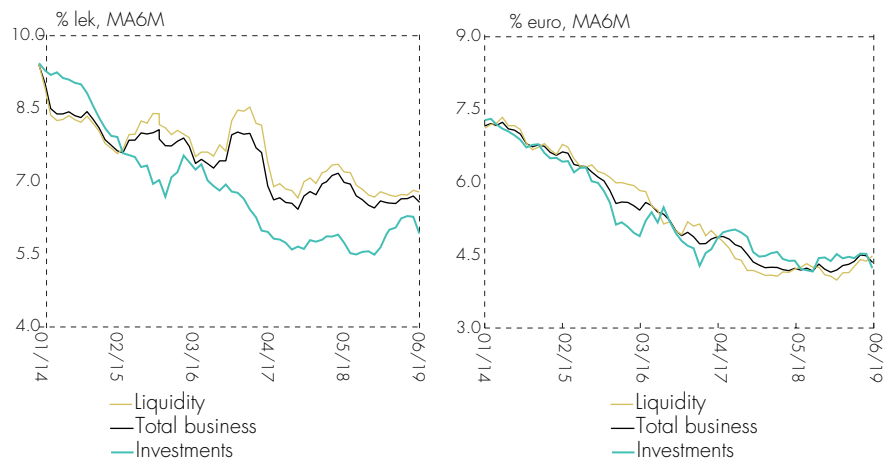
The structure of the credit portfolio has shown significant changes in the share of credit to construction and industry sectors. Bank financing to firms operating in the construction sector has declined significantly since 2008, from 22.5% at the start of the decade to 14% currently. Conversely, during this period, financing to the industry sector has surged. The share of credit to this sector in total credit has risen to 26%, from 23% at the start of the decade. This structural shift in financing has reflected the credit demand from these sectors, the credit risk profile for firms operating in these sectors and the banks' risk appetite.

Interest rates on loans to enterprises fell in 2019 Q2, whereas other credit conditions were tightened slightly.

The average interest rate on loans to enterprises in 2019 Q2 fell to 6.4% from 6.8%, on average, in the previous quarter and in the previous year. Monthly interest rates on loans to enterprises continue to be determined by interest rates on overdraft loans and loans for working capital. In this quarter, this category was unchanged from the previous quarter and showed a slight downward trend from the average rate recorded in 2018. This was a positive factor contributing to the lowering of total interest rates on loans to enterprises, which mainly reflected a reduction in the category of loans for investments (equipment and real estate purchase). The latter are often subject to preferential terms applied by certain banks, therefore adding to interest rate volatility in this segment. The interest rate on loans for investments was 5.2% in this quarter[4], from 6.6% in the previous quarter, and 5.7% in 2018. Meanwhile, interest rates on loans for liquidity remained at 6.8% in these three months, similar to the previous quarter, but slightly lower than their average in 2018 (7.0%).

[4] *The average interest rate for this category in this quarter was driven also by the average interest rate in June, which reflected a preferential interest rate applied by one bank for a specific entity. Yet, the average interest rate for investments in June, excluding this bank (5.5%) resulted close to the quarter's average (5.2%).*

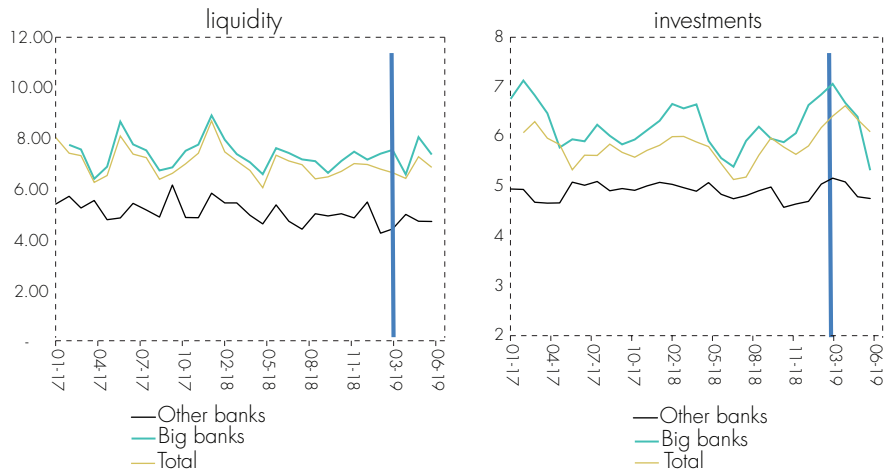
Chart 4 Interest rates on loans to private enterprises



Source: Bank of Albania.

Analysis of interest rates by bank size shows that the group of smaller banks applies, on average, lower premia than the group of larger banks for loans to enterprises for liquidity purposes; by contrast, in this quarter, the larger banks have lowered the required premia for loans for investment purposes.

Chart 5 Interest rates on loans to enterprises, in lek, by bank size

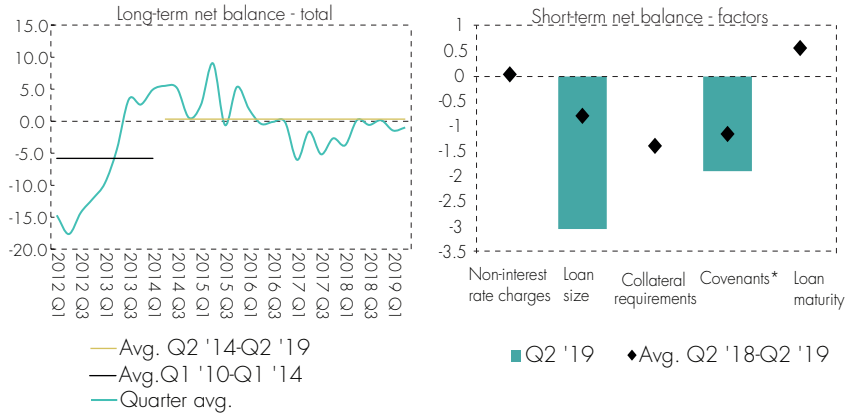


Source: Bank of Albania and staff estimates.

Interest rates on euro loans to enterprises fell in this quarter, reflecting the performance of interest rates for both liquidity and investment loans. Rates on liquidity loans to enterprises, however, stand slightly higher than their average in 2018. The average interest rate on euro loans to enterprises was 4.0% from 4.7% in the previous quarter and 4.2% in the previous year. By purpose of use, interest rates on overdraft loans, although down from the previous quarter, show a slight upward trend compared to 2018. Unlike overdraft loans, interest rates on loans for working capital and for investments fell, compared to both the previous quarter and the previous year.

For 2019 Q2, banks reported somewhat tighter non-price terms for new loans to enterprises. The general balance **of non-price conditions for loans to enterprises** in this quarter was assessed as below the average of the last five years. Despite the improving long-term trend, however, this indicator remains slightly on the tightening side, which implies a small tightening of credit terms and conditions through non-price instruments for loans to enterprises.

Chart 6 Non-price terms and conditions on loans to enterprises



Source: Bank of Albania.

*: *Values represent net balances between positive and negative responses, according to the BLS questionnaire in Albania, revised in 2018 Q2, by including new factors as part of non-price terms and conditions. Non-price terms and conditions include non-interest rate charges, loan size, loan maturity, collateral requirements and loan covenant.*

The slight tightening of credit terms and conditions - determined by non-price factors in this quarter, as presented in Chart 6, right - was reflected in the form of reduced loan size, and higher restrictions established in loan covenants. Both balances, which have led to the slight tightening of credit terms conditions for enterprises, have registered higher negative values than their respective average values registered in the previous year. Other non-price conditions for loans to enterprises - commissions, collateral requirements, and loan maturity - were assessed as unchanged from the previous quarter.

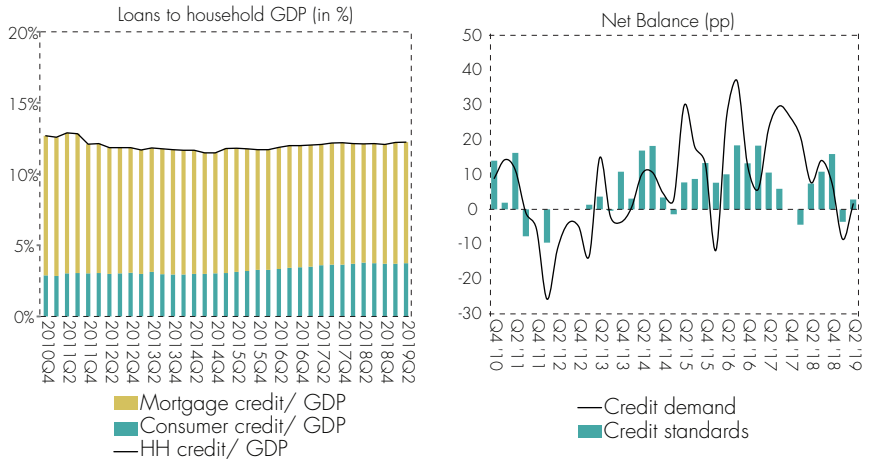
2. LOANS TO HOUSEHOLDS[5]

Loans to households maintained similar growth rates to the previous quarter.

The ratio of loans to households to GDP was assessed at around 12.2% at the end of 2019 H1. This ratio has hovered around similar values over the past three years, confirming a relatively stable performance of this portfolio vis-à-vis growth in economic activity in Albania. The expansion of loans to households is broadly supported by the positive performance of mortgage loans, which have accelerated their pace of growth, especially in the last two years. The improvement is in line with the improvements in the housing market and in the labour market over this period. From the supply-side perspective, it reflects the continuous easing of credit terms and conditions for this segment.

[5] *The data for loans to households are adjusted for written off loans and exchange rate fluctuations.*

Chart 7 Loans to households



Source: Bank of Albania

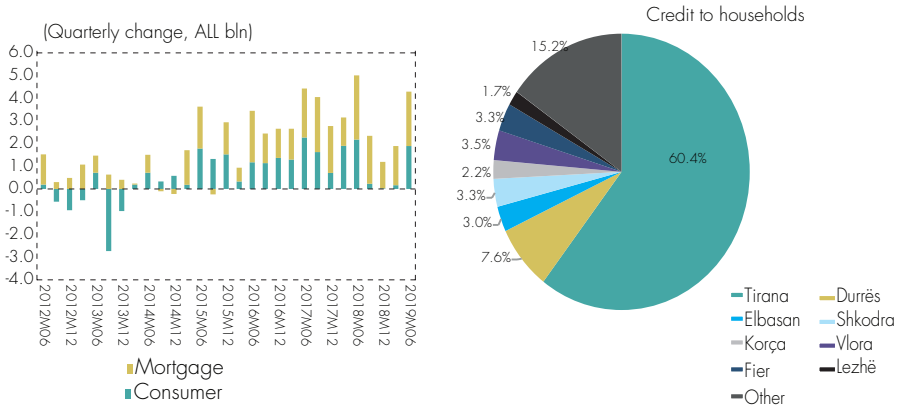
From the short-term perspective, loans to households registered similar growth rates to the first quarter. They have generally pursued a decelerating trajectory over a year. In 2019 Q2, loans to households grew at around 6.4% annually, compared with 6.7% in Q1. Quarterly changes in the outstanding credit show a higher contribution of consumer credit in this quarter, picking up from the sluggish performance registered over the three previous quarters. However, it slowed down in annual terms, on account of the effect of the high comparative base in the same quarter of the previous year. In the meantime, the portfolio of mortgage loans continued to expand at a steady pace, dominating the growth of total loans to households. Consumer credit and mortgage loans account for around 10% and 24%, respectively, of outstanding credit to the private sector[6] as at the end of 2019 H1. The performance by currency confirms that loans to households are given mostly in the domestic currency. This portfolio accounts for around 64% of outstanding loans to households as at the end of June, increasing this share by around 2.4 percentage points from the previous year.

Loans to households are concentrated most in the Region of Tirana.

Broken down by region, the analysis shows that loans to households are most concentrated in the Region of Tirana, accounting for 60%. By portfolio, this behaviour is most notable in the segment of mortgage loans (around 67.4%), which reflects the highest concentration of credit demand for house purchase in this Region as well as a faster urban and demographic development of this area. Conversely, the geographic distribution of consumer credit appears more even, with only 46.3% of credit in this segment concentrated in Tirana. The expansion of the consumer credit portfolio in recent years reflects, among other things, improvements in the labour market and relations with banks, hence easier access to the banking system for households.

[6] *These portfolios account for around 31% and 69% of total outstanding loans to households.*

Chart 8 Loans to households

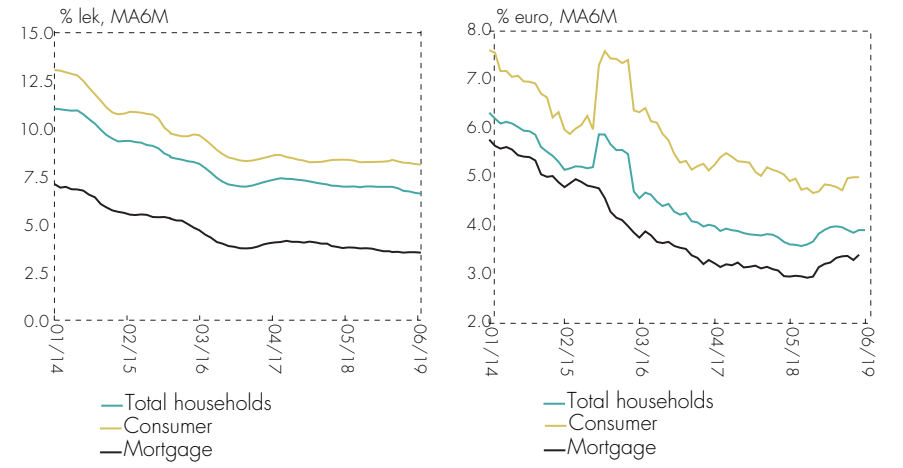


Source: Bank of Albania

Interest rates on loans to households remained unchanged in 2019 Q2. Other credit conditions remain on the easing side.

Interest rates of lek loans to households in 2019 Q2 did not change from the previous quarter. In this quarter, the average interest rate on loans to households was 6.6%, unchanged from the previous quarter. In the meantime, interest rates applied on loans to households were lower than in the second half as well as the average of the previous year, thus confirming the slight downward trend of interest rates in this segment in this period. By purpose of use, in this quarter, interest rates on consumer loans continued to decrease marginally, while on mortgage loans they increased slightly. In line with expectations, the analysis of interest rates by size of banks confirms that the group of larger banks applies, on average, lower premia than the group of smaller banks for both categories of loans to households. However, the interest rates of smaller banks on mortgage loans in these last three months have shown a downward trend, approaching those of larger banks.

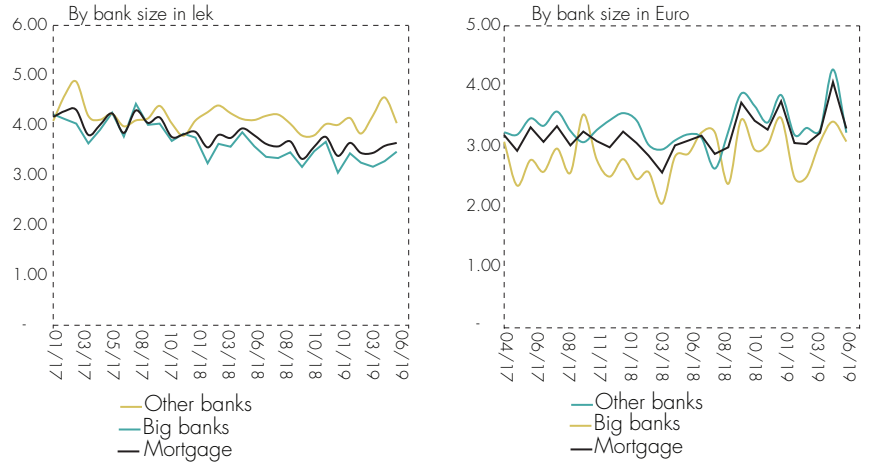
Chart 9 Interest rates on loans to households



Source: Bank of Albania.

In this quarter, the average interest rate on euro loans to households increased to 4.1%, from 3.7 % in the previous quarter. Interest rates on euro loans in these three months stand above the levels recorded in the previous year as well. By purpose of use, interest rates increased especially on loans for financing the purchase of durable and non-durable goods, but remained at similar levels on overdraft loans. Interest rates on mortgage loans returned to an increase again in this quarter, after a period of unchanged rates. The level of interest rates for this category, nevertheless, is above the average level of 2018, reflecting an upward trend of interest rates applied by banks in financing house purchase in euro. Like interest rates on loans in lek, the group of larger banks in this segment shows, on average, lower interest rates than the other banks. However, it must be noted that a downtrend is confirmed in interest rates applied by smaller banks in this quarter.

Chart 10 Interest rates on mortgage loans (in %)

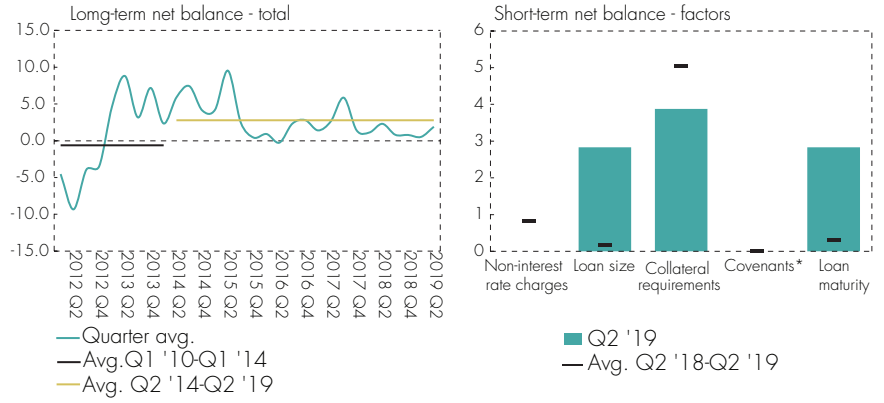


Source: Bank of Albania and staff estimates.

Non-price credit terms and conditions for households were perceived as improving in 2019 Q2. In this quarter, the general balance approached the average level for the period 2014-2019. From a longer-term perspective, a slight improvement was noted in factors that determine credit terms and conditions for households, but do not form the credit price directly.

For the second quarter, banks reported the following drivers to the improvement of non-price credit terms and conditions for loans to households: reduced collateral requirements; increased loan size; and longer maturity. The balances of the last two factors in the second quarter were higher than the respective average over a one-year horizon. Other factors included also in the general balance of non-price conditions - restrictions from the loan covenant, and commissions - remained unchanged from the previous quarter.

Chart 11 Non-price terms and conditions for loans to households



Source: Bank of Albania.

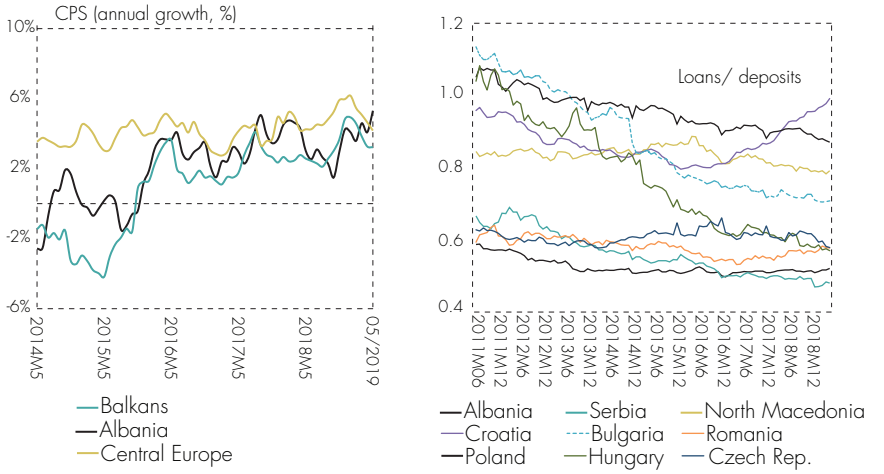
*: Values represent net balances between positive and negative responses, according to the BLS questionnaire in Albania, revised in 2018 Q2, by including new factors as part of non-price terms and conditions. Non-price terms and conditions include non-interest rate charges, loan size, loan maturity, collateral requirements and loan covenant.

3. TRENDS IN LENDING IN THE COUNTRIES OF THE REGION

Credit developments in CESEE[7] countries show lending continued to register moderate growth rates.

Credit to the private sector in the CESEE region remained at moderate levels. From a long-term perspective, the annual average growth rate of credit in this region has hovered around 4% over the last three years. Overall, growth has been fuelled by faster credit growth in Central Europe, broadly sustained by the households segment. Contributions from increased credit demand and constantly improving credit terms and conditions in this segment have exerted a positive impact on these developments.

Chart 12 Credit to the private sector and intermediation ratio* in CESEE countries



Source: Respective central banks, authors' estimates.

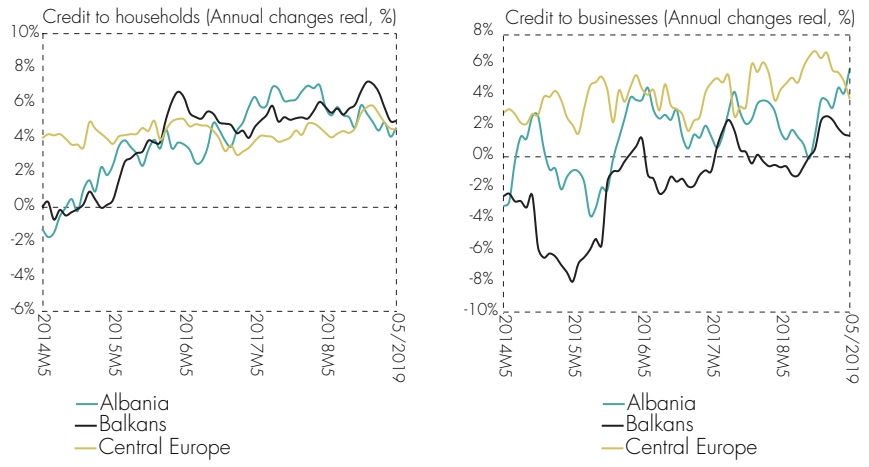
*The intermediation ratio is measured as the ratio of intermediated credit to the private sector to total deposits.

[7] CESEE countries in this analysis include, Albania, Bulgaria, Romania, Croatia, Hungary, the Czech Republic, Serbia, North Macedonia.

During the period April-May 2019, the portfolio of credit to the private sector registered 4.1% growth, from 5.3% recorded in the first quarter. According to the CESEE Bank Lending Survey[8], banks and subsidiaries of foreign banks in this region continue to report an increase in demand for bank credit. Meanwhile, supply is reported as tightened, hence widening the gap between demand and supply. About 40% of foreign banking groups report that they continued some restructuring activities during 2013-2018, via sales of assets and/or branches in the countries of this region.

Across the economic agent spectrum, growth of credit to the private sector shrank, manifested both in loans to enterprises and loans to households. Outstanding loans to enterprises expanded by 3.4% on average, in annual terms, around 1.4 percentage points lower than in the first quarter of the year. This behaviour appears almost uniform across the board, both in the Balkan region and in Central Europe. Growth in loans to enterprises in Albania picked up pace. From a long-term perspective, both in Albania and in the region, these loans have been relatively unstable over time. The recovery of low rates - even negative rates in Balkan countries - in this portfolio over the last five years has been associated with large fluctuations, beyond the common business cycles, especially in the Balkan region.

Chart 13 Credit in the countries of the region, by economic agent



Source: Respective central banks, authors' calculations.

The slowdown of credit rates in annual terms affected the portfolio of loans to households as well. Thus, in the period April - May 2019, loans to households registered an annual growth of 4.6% on average, compared to 5.6% recorded in the first quarter of the year. Yet, over time, the performance of loans to households is relatively more stable than that of loans to enterprises. Even in terms of geographical breakdown, the annual rates of loans to households are steadier. The portfolio of loans to households dominates credit to the private sector in the CESEE region, except for Albania, Romania and Bulgaria.

[8] *The CESEE Bank Lending Survey is available on: https://www.eib.org/en/infocentre/publications/all/cesee-bls-2019-h1.htm.*