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

"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 conditions based on the Bank Lending Survey. In addition, Trends in Lending includes an overview of the most recent credit developments in various Central, Eastern and South Eastern European (CESEE) countries.

Trends in Lending takes into account the following key statistics: a) data on bank lending activity in the resident sector of the economy; b) qualitative data from the Bank Lending Survey; c) statistics on credit interest rates in both lek and euro; d) 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 the Republic of North Macedonia (RNM).

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 analysis of the loan portfolio is based on the adjusted lending data on the impact of the exchange rate and on loans written-off banks' balance sheet, a process which banks have undertaken based on the Decision No 50, dated 30.3.2015 "On amendments to the Regulation "On Credit Risk Management".

The analysis covers data available as at 23 July 2021, which include information for monetary and financial data as at June 2021, and data from the Bank Lending Survey 2021 Q2. Data on credit in regional countries are as at May 2021.

OVERVIEW OF RESULTS

Lending activity developments in the second quarter of 2021 show that:

- *Credit to the private sector maintained the growth rates of the first quarter. The improvement of the growth rates in loans to households has offset the slowdown in loans to enterprises, by preserving, overall, the positive incentive of lending activity. The easing of credit standards from banks and the upward financing demand from private sector drove the expansion of the loan portfolio.*

- *Loans to enterprises reflected the slowdown in loans for liquidity, given the improvement of economic activity in Albania and the payments received from the Government. Meanwhile, loans for investments have maintained the positive path recorded since the end of 2020. By currency, this performance drove loans in lek to enterprises slowing down and the growth rate of loans in foreign currency remained stable.*

- *Loans to households have accelerated the growth pace, mainly reflecting the improvement of credit growth rates for house purchase. The latter have shown expansion in the demand for loans and easing of credit standards by banks for some quarters. Also, consumer loans have shown a moderate improvement.*

- *Interest rates for new loans in lek declined in the second quarter of 2021, to both enterprises, and on mortgage loans to households, in reflection of the accommodative monetary policy and the reduction of risk premia related to the expected performance of the economy.*

- *Banks have eased the lending terms and conditions applied on loans to households, while have kept them unchanged on loans to enterprises in the second quarter of 2021. This performance reflects both the reduction of risk premia and the increasing tolerance to take risk.*

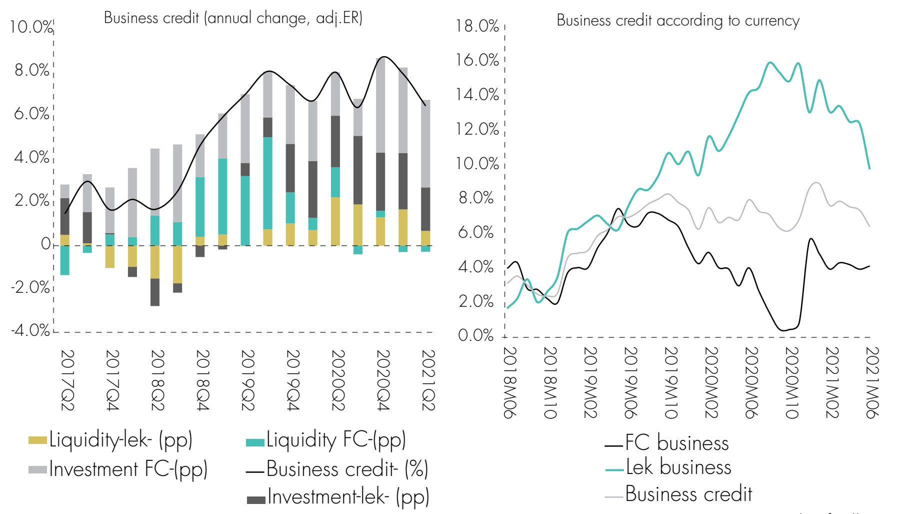
- *In April and May 2021, credit to the private sector in the CESEE region has reduced in annual terms. The contraction of credit portfolio in the Central Europe mainly highlighted the developments across the CESSE region. This contraction has affected loans to enterprises, while loans to households continue to expand.*

1. LOANS TO ENTERPRISES

Loans to enterprises showed a slowdown of the growth rates, reflecting the lower demand of enterprises for loans to finance liquidity needs. Given the return of economic activity towards normality and the increasing payments by public sector, the financing needs of enterprises have mainly been for loans for investments. Banks have eased credit standards on loans to this group, by supporting the financing demand from enterprises, given that both price and non-price conditions remain favourable.

Loans to enterprises showed lower growth rates, averaging 7.1% in the second quarter of 2021, or 1.1 percentage points lower than in the previous quarter. The second quarter of the year is characterised by the improving economic activity and confidence, and lower risk premia, driven by the lifting of pandemic-related restraining measures and its management. These positive developments, on one side, have reflected the increase in the financing demand of enterprises from banks - mainly to support investments and with long-term maturities - and, on the other hand, have sustained the improvement of enterprises' liquidity - by decreasing their demand for financing. Hence, loans for investments increased by 11.6%, over this period, and retained a similar growth rate to the first quarter. Meanwhile, loans for liquidity slowed the growth rates further, down to 1.4%, from the 3.5% average in the first quarter. This dynamic was determined by the good performance of enterprises' deposits, related to the VAT refunds by the Government.

Chart 1 Lending to enterprises by purpose of use and currency



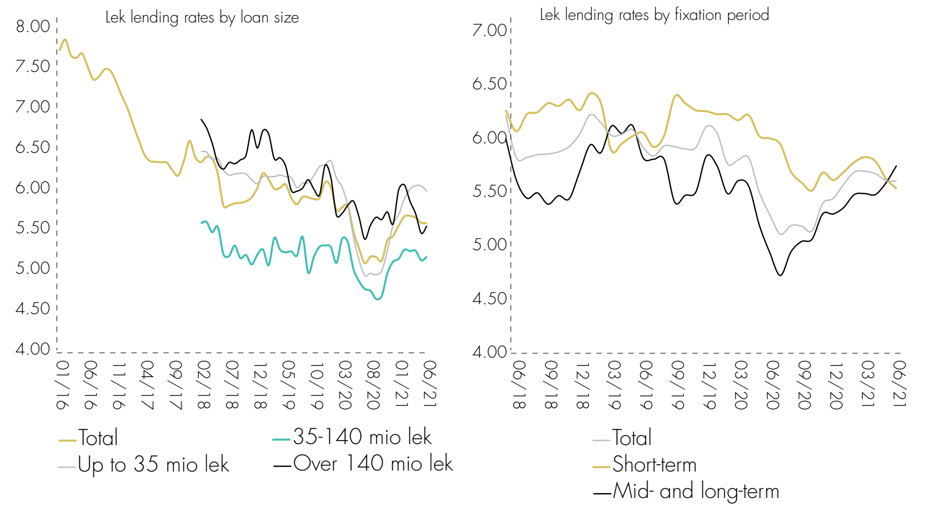
Source: Bank of Albania.

By currency, the good performance of loans for investments - dominated by lending in foreign currency - has sustained the stable growth of this portfolio by 4.1% yoy. While, lending in lek has slowed down to 9.8%, reflecting the reduction of lending to cover needs for liquidity. In addition, this portfolio reflects the lower benefit from the supportive measures taken by the Government, whose largest effect was recorded in the second quarter of 2020, with the pandemic spread. At end of June, loans to enterprises are dominated by foreign currency loans, at 57.6%. Nevertheless, this rate is 1.6 percentage points lower than in the previous year, reflecting the shift of portfolio towards the domestic currency, in response to the accommodative financial conditions, which were eased further at the outbreak of the pandemic.

Interest rates on loans to enterprises in lek have declined in the second quarter of 2021, in reflection of the reduced uncertainties for the future and a more positive approach of banks towards financing to the private sector. Also, the interest rates on loans in euro have retained the low levels recorded since the first quarter of 2021.

In the second quarter of 2021, enterprises have benefited financing at low interest rates from banks, after the increase recorded in the two previous quarters. The average rate applied on loans to this segment was 5.4%, from 5.8% and 5.6%, respectively in the first quarter of 2021 and in the fourth quarter of 2020. The reduction of interest rates was particularly present in the segment of loans larger than ALL 140 million. The average interest rate on these loans stood at 5.2% in the second quarter of 2021, from 5.9% in the first quarter of 2021, and 5.6% in 2020. Also, the interest rates on small loans-up to ALL 35 million - have also reduced. These loans are mainly granted to small and medium-sized enterprises. The average interest rate for these loans stood at 5.8%, from 6.2% in the previous quarter. This rate remains higher than the 5.4% average level in 2020. Interest rates on medium-sized loans have remained stable for the third consecutive quarter, at 5.2%, and close to the average level of 2020.

Chart 2 Interest rates on lek loans to private enterprises

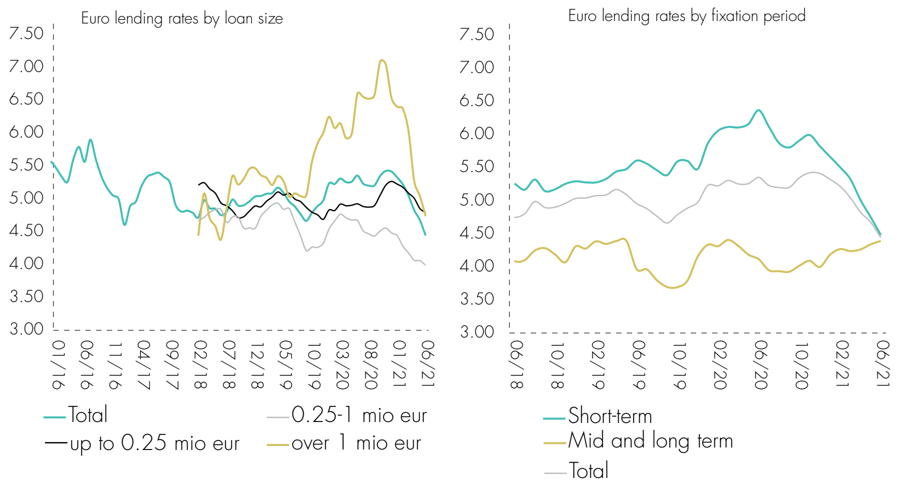


Source: Bank of Albania.

Current interest rates on loans to enterprises are close to the average in the first three quarters of 2020 (5.3%). In this period, the interest rates were considerably low due to the implementation of the sovereign guarantee schemes. Unlike the previous year, the decline in interest rates reflects, already, a more positive approach of banks towards lending and a more complete monetary policy pass through, given the reduction of uncertainties and the positive expectations for the future.

The impact of monetary policy in supporting lower interest rates on loans to enterprises is clearly reflected in the analysis by interest rate fixation period[1]. The short-term interest rate - either variable or fixed for the first year of loan - which carries more clearly the monetary policy pass through impact, in view that credit risk does not change, dropped to 5.3% in 2021 Q2, from 5.7% in 2021 Q1, and in the last three quarters of 2020. Since the mid-2018 up to the end of March 2020, prior to the reduction of policy rate, its average level was 6.2%2. On the other hand, fixed interest rate for a medium-or long-term period - which in addition to the forward guidance on the monetary policy stance, bears a set of risks, was recorded at 5.8%, remaining close to the level in the first quarter of 2021, and higher than in 2020.

Chart 3 Interest rates on loans to enterprises in euro



Source: Bank of Albania.

Interest rates on loans to enterprises in euro were stable in the second quarter of 2021, at 4.5%, from 4.4% in the first quarter of 2021, considerably lower compared to the 5.4% average in the previous year. By loan size, interest rates continued to decline, in the quarter under review, for loans larger than EUR 1 million, while it stopped for both small loans and medium-sized loans. The fall, by fixation period, was driven by fixed interest rates up to one year, while fixed interest rates for longer- term horizon showed a slight increase during this year.

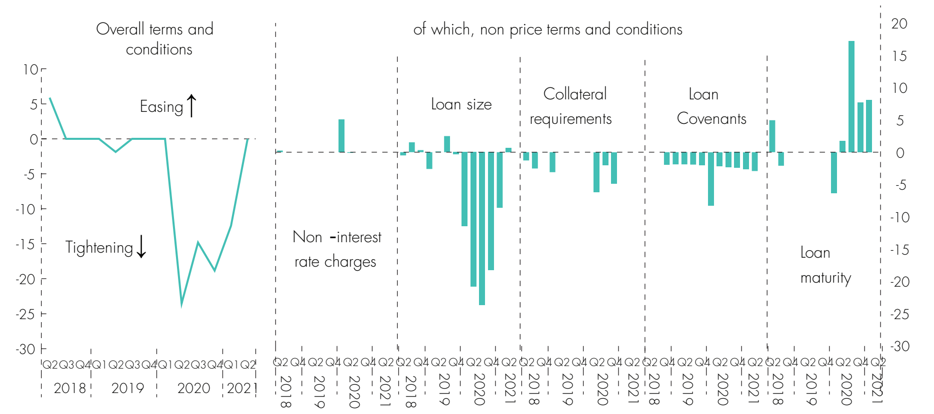
Non-price terms and conditions to enterprises remained unchanged, for the first time, after some quarters of tightening.

[1] *Fixed-term implies the period in which the loan's interest rate is fixed and doesn't change. A loan may be granted: a) with variable interest rate, b) with some period fixed and others variable or c) fixed throughout until its maturity. For the purposes of this analysis, the interest rate for loans granted with variable rates and those with fixed rate up to a year is called short-term rate, that for loans granted with over a year and up to 5 fixed rate is called medium-term rate, that for loans granted with fixed rate over 5 years is called long-term rate. Thus, the concept short-term/long-term is related with the period in which the interest rate is fixed, and not with the maturity of the loan.*

[2] *This period coincides with the policy rate at 1.00%.*

The improved macroeconomic framework in Albania has been also reflected in the lending policies of banks. Hence, banks have adopted a more positive behaviour related to the overall terms and conditions for new loans to enterprises, in the second quarter of 2021. The lifting of restricting measures and the increase of vaccinations in Albania, appears to have somewhat set off the uncertainties related to the pandemic. In turn, banks have become more pro-active in lending in Albania. Banks reported unchanged lending terms and conditions in the second quarter of 2021, following their tightening over the course of one year.

Chart 4 Non-price terms and conditions for new loans to enterprises



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 staff estimates.

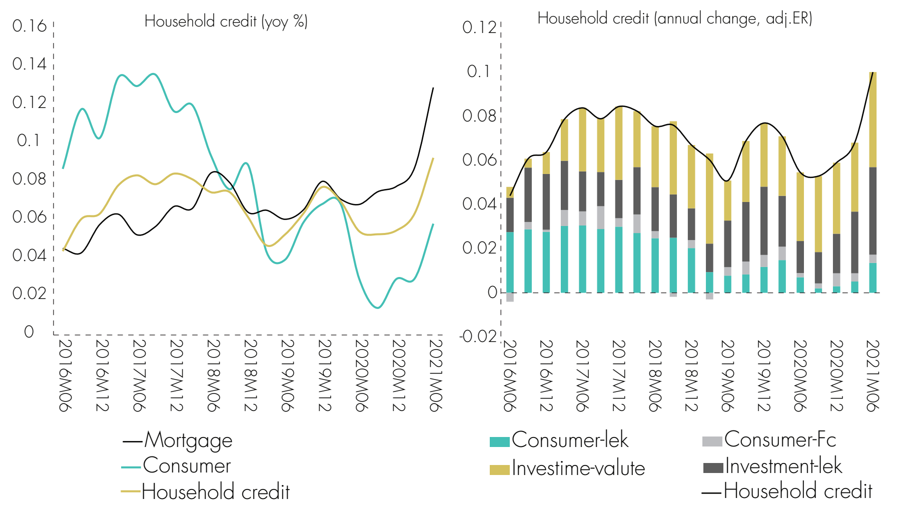
Related to the determination of margins, banks continue to compel a prudential behaviour towards riskier loans, which in turn has counterbalanced the easing on average loans. In non-price elements group the increase of loan size to enterprises seems to have offset the tightening effect due to higher restrictions in loan agreements. Other non-price elements: commissions; collateral requirements related to the granted loan; and maximum maturity on loans; remained unchanged from the previous quarter.

2. LOANS TO HOUSEHOLDS

Loans to households showed improved growth rates, reflecting the considerable expansion of loans for house purchase. In addition, consumer loans increased as well, reflecting the improved loan supply, financial conditions and demand from households.

Loans to households grew by around ALL 9 billion in the second quarter of 2021, showing an acceleration of growth rates, at 8.7% on average terms. This expansion reflects a complete recovery of the growth pace, similar to those in pre-pandemic period. The positive developments in loans to households have reflected both the improvement of households' confidence for the current situation and the future, in view of economic activity normalisation, and the increase in housing market. Alongside these factors, banks have continued to ease loan supply to households, in both segments: consumer loans and mortgage loans. The increase of bank competition in this segment is reflected also in the lower credit costs to households - particularly on mortgage loans - by supporting credit growth.

Chart 5 Lending to household by purpose of use



Source: Bank of Albania.

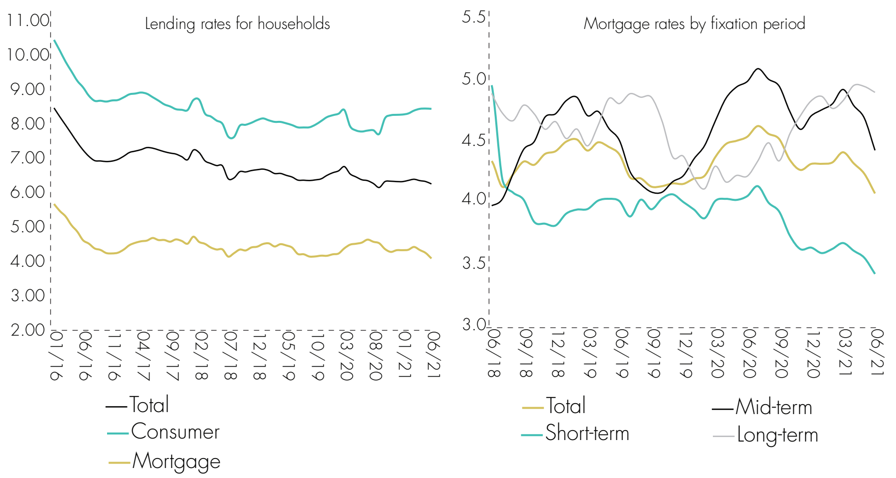
By currency, both lek and euro loans have been improved. The growth rate of lek and euro loans improved at 10.3% and 5.9%, respectively[3]. The expansion of lek loans for more than five years dominates the growth of credit portfolio to households. The accommodative monetary conditions and the continuous fall of interest rates have particularly sustained the rapid expansion of lending in lek for house purchase for some quarters. Also, the active policies applied from banks in lowering the households' exposure to the exchange rate risk have continued to support the shift of loan portfolio to households towards lek. In June 2021, these loans accounted for around 65% of portfolio, compared to 64% a year earlier.

Households have benefited financing at lower interest rates for consumer loans, both in lek and euro. Interest rates on consumer loans appeared stable.

The average interest rate on loans to households in lek declined in the second quarter of 2021. It averaged at 6.0%, from the steady average of 6.5% that has prevailed in the last two years. Their fall was entirely affected by the interest rates on mortgage loans. The latter recorded low levels in the second quarter of 2021, averaging at 3.5%, from 4.7% in the first quarter of 2021, and 4.4% in 2019 and 2020. By the interest rate fixation period, the decline of rates was mainly present on loans with fixed interest rate applied for a short-term horizon (up to one year) and medium-term horizon (1-5 years). On the other side, fixed interest rates for longer terms continue to fluctuate at a higher interval, reflecting the uncertainty that materialises in their fixation. Nevertheless, the share of loans to this segment in the new mortgage loans is low[4].

3 In 2021 Q1/, each portfolio recorded an average growth of 7% and 4.5%, respectively.
4 On average, only 15% of mortgage loans are granted at fixed interest rate in a time horizon over 5 years.

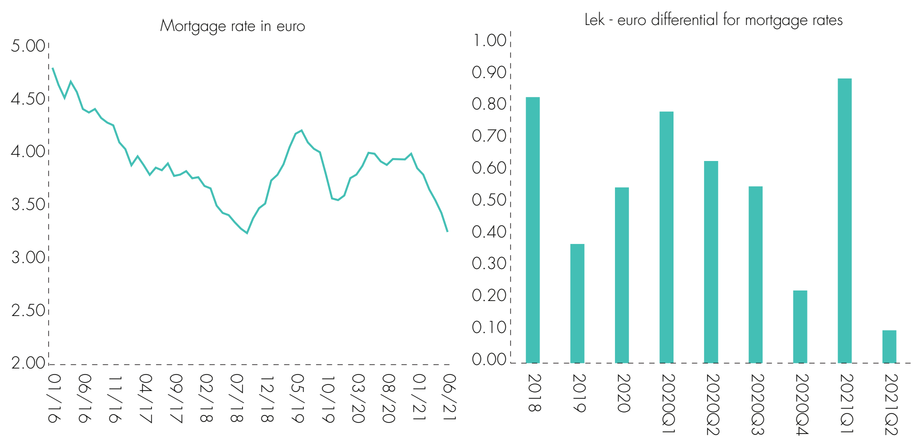
Chart 6 Interest rates on lek loans to households



Source: Bank of Albania.

The interest rate on consumer loans was stable, standing at 8.4% in the second quarter of 2021, unchanged from the first quarter of 2021, and close to the average of 2020[5].

Chart 7 Interest rates on loans to households in euro



Source: Bank of Albania.

The average interest rate on mortgage loans[6] to households in euro stood at 3.2% in 2021 Q2, close to the level recorded in 2021 Q1. In 2021, this rate has been considerably lower than the relatively stable average of 4.0% in the two previous years. The spread between lek and euro interest rates for mortgage loans narrowed at a minimum of 0.1 percentage points in the first quarter of 2021, from the average of 0.6 percentage points in the last years.

[5] *If April is excluded in the calculation of the average for this year, where the interest rate on consumer loan was considerably low, affected by the loans of a bank in the system.*

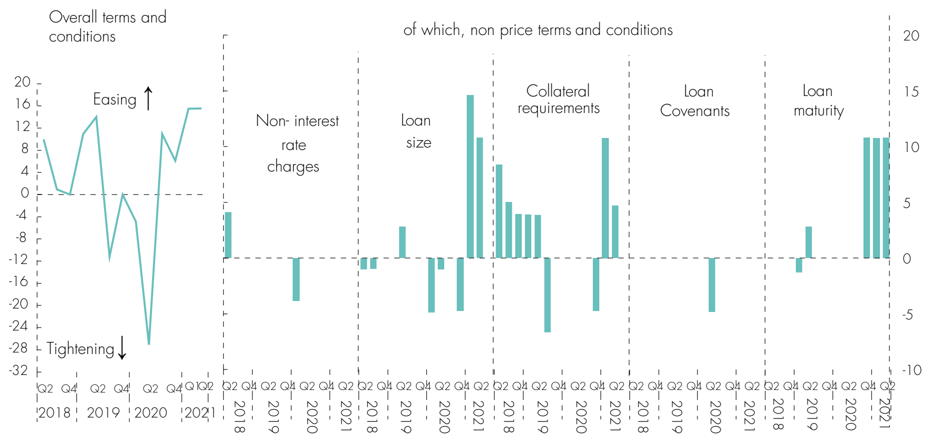
[6] *Mortgage loans are dominant in loans to households in euro, for that reason the analysis focuses only on this segment.*

Lending terms and conditions for new loans to households were further eased

Banks' overall terms and conditions for new loans to households continued to ease in the second quarter of 2021. The approach of banks towards lending to households, unlike to enterprises, was easier since the third quarter of 2020. Banks have continued to perceive low risk, and be more tolerant to the risk on loans to households, thus determining the overall easing of lending terms and conditions for loans to households.

Non-price elements of loans to households were eased through: (i) increasing the size of the loan required; (ii) extending the maximum maturity of loans; and (iii) the lower collateral requirements related to the granted loan. On the other hand, commissions and restrictions in loan agreements remained unchanged from the previous quarter.

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



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 staff estimates.

3. TRENDS IN LENDING IN THE COUNTRIES OF THE REGION[7]

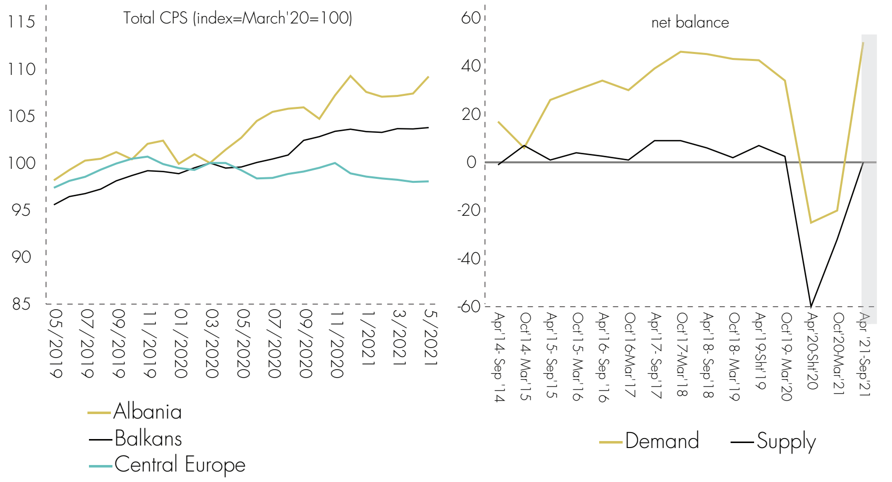
In April and May 2021, credit to the private sector in the countries of the CESEE region reduced in annual terms. The developments across the CESSE region were mainly driven by the contraction of credit portfolio in the Central Europe. This contraction has affected loans to enterprises, while loans to households have continue to expand.

Annual rates on loans to private sector across CESEE countries have entered into negative territory since March 2021. In April and May 2021, this portfolio contracted by around 0.4% in annual terms, on average, compared to the average fall of 0.1% in the first quarter of 2021 Q1. Notwithstanding

[7] *In this analysis are included 9 countries of the Central, Eastern and South-eastern Europe: Albania, North Macedonia, Croatia, Serbia, Bulgaria, Romania, the Czech Republic, Poland and Hungary. The credit to the private sector stock is adjusted for the impact of inflation and exchange rate.*

the perception for improved loan demand in the regional countries lending survey 8 (October'20-March'21), the loan supply was reported tightened. Based on this survey, the situation in global markets and non-performing loans of international banking groups retain their negative impact on the supply side. In more geographical details, credit has continued to contract in the region of Central Europe. This portfolio has been shrinking since the outbreak of the global pandemic (Covid-19), affecting the performance of loans in the segment of enterprises. Meanwhile, the expansion rates of loans in the region of Balkans have retained the positive trajectory after the outbreak of the pandemic. The regional positive developments during this period, overall, are related to the successful measures undertaken by the governments, central banks and other regulatory authorities in the framework of tackling the pandemic.

Chart 9 Credit to the private sector in the CESEE region



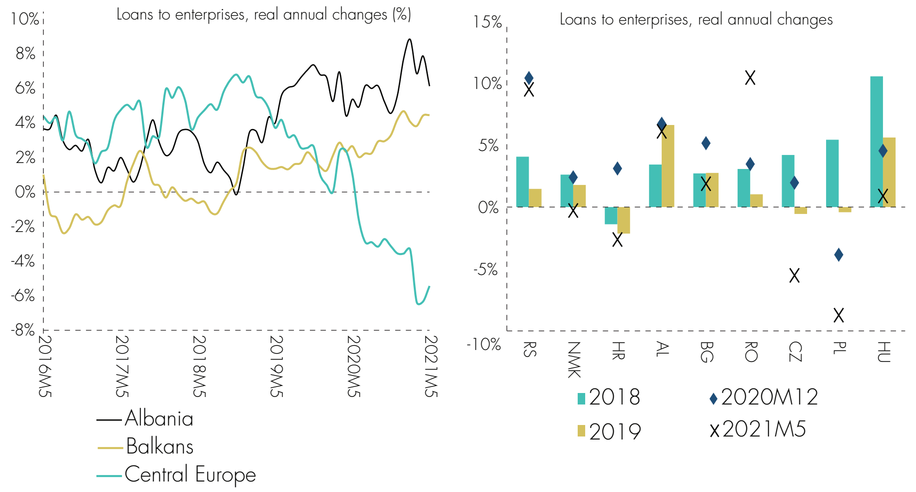
Source: Source: Bank of Albania; Banks of regional countries; EIB Bank Lending Survey in CESEE, authors' calculations.

Loans to enterprises continues to be the portfolio with a negative contribution on the performance of credit to private sector in the CESEE region, reflecting its contraction in the countries of Central Europe. In April and May 2021, this portfolio registered a growth rate of 2.8%, in annual terms, on average, compared to the decline of 2.4% in the first quarter of 2021. According to the Bank Lending Survey in the countries of CESEE region, credit standard tightened on loans to corporates and SMEs, and are expected to remain unchanged over the next six months. The contraction of portfolio to enterprises in some of these countries relates - among others - to the measures taken by the government in view of the pandemic, where in countries, as in Poland, the demand for funding from banks has declined compared to the pre-pandemic period.[9] On the other side, credit portfolio to enterprises in the Balkan region has recorded improving growth rates. The increase in the demand for loans as reported from enterprises in the last regional BLS, in both segments, SMEs and corporates, appears to have been mainly recorded in this region.

[8] *The results of the Bank Lending Survey of EIB are detailed at: https://www.eib.org/en/publications/cesee-bls-2021-h1*

[9] *In some regional countries, the supporting measures taken by the government have been perceived in the form of direct payments to enterprises.*

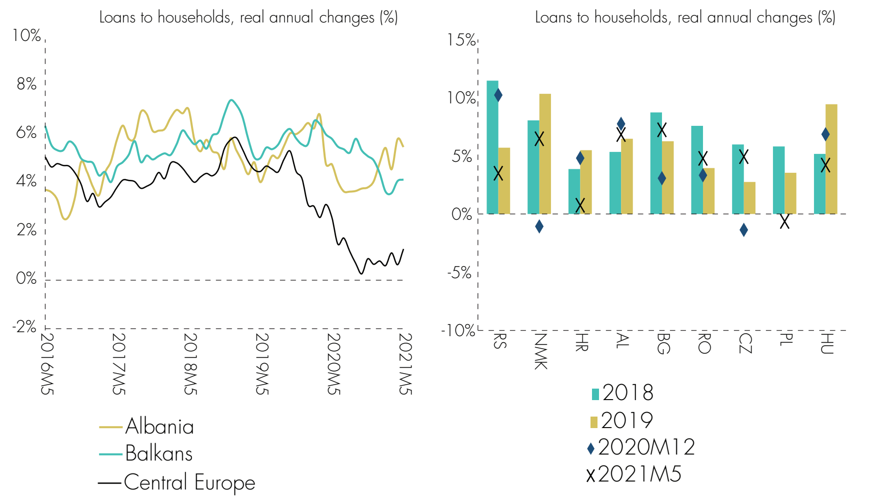
Chart 10 Loans to enterprises in the CESEE region



Source: Source: Bank of Albania; Banks of regional countries; EIB Bank Lending Survey in CESEE, authors' calculations.

Loans to households show a more stable performance compared to the portfolio of loans to enterprises. It continues to remain in positive territory, recording an annual growth of around 1.5%, on average, in April and May 2021, from 1.3% in the first quarter of 2021. The expansion of loans to households in this region is driven by the Balkan countries. Meanwhile, this portfolio records slowing growth rates in the countries of Central Europe. According to BLS in CESEE countries, the increase on the demand for funding from households is concentrated in the segment for house purchase, while lending terms and conditions were reported tightened on loans for both consumption and house purchase.

Chart 11 Loans to households in the CESEE region



Source: Source: Bank of Albania; Banks of regional countries; EIB Bank Lending Survey in CESEE, authors' calculations.