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. 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 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 impact. 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 24 January 2018, which include information for monetary and financial data as at December 2019[1], and data from the Bank Lending Survey 2019 Q4. Data on credit in regional countries are of November 2019.

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

OVERVIEW OF RESULTS

Developments of credit activity in 2019 Q4 show that:

- *Credit to the private sector has slightly improved its growth rate. This performance was mainly determined by the expansion of lending in lek, as well as to enterprises.*

- *The growth rates of loans to enterprises are slightly higher than in 2019 Q3. This performance has been positively affected by the increase of lending to large enterprises. Broken down by sector, credit to the services and trade sector showed the best performance during this quarter.*

- *Interest rates of loans to enterprises in lek have reduced for the liquidity segment, but have recorded a slight increase for investment loans compared to 2019 Q3.*

- *Loans to households showed an improvement of growth rates in 2019 Q4. The expansion of loans to households continues to be supported mainly by mortgage loans. Tirana District dominates the loan portfolio in terms of geographic distribution.*

- *Interest rates for loans to households in lek have been relatively stable, with a slight increase only in the segment of consumer loans.*

- *According to banks, lending performance is supported by the easing of lending standards, which have reflected the increase of competition between banks, as well as the improvements in their balance sheets. Meanwhile, they report a reduction in credit demand both for enterprises and households.*

- *Credit to the private sector activity in the CESEE region recorded moderate growth rates over this period.*

- *The credit stock in CESEE is dominated by loans to households, both in terms of their share to the total and in terms of annual growth rates. On the other hand, the performance of loans to enterprises continues to appear volatile and uneven in geographical terms.*

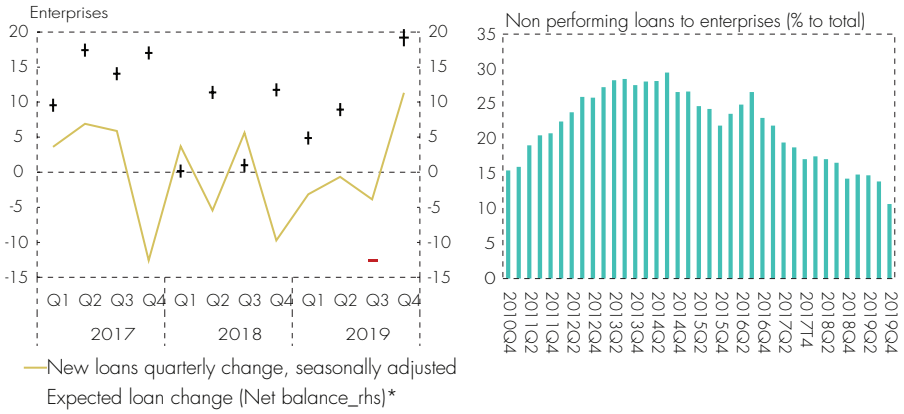
1. LOANS TO ENTERPRISES[2]

Loans to enterprises recorded higher growth rates in 2019 Q4, driven mainly by improved credit supply.

In 2019 Q4, loans to enterprises increased by ALL 6.5 billion, recording a slight improvement of the annual growth rate, to 8% on average. This growth has been driven by the easing of lending standards by banks, as also shown by the latest results of the Bank Lending Survey3. Increased competition in the banking system, driven mainly by the revival of lending activity by banks undergoing ownership changes, has been one of the main factors that has induced the easing of lending standards. Also, banks' favourable situation in terms of liquidity and well-capitalisation has helped them to pursue more eased lending policies for enterprises. The further contraction of non-performing loans against the total appears to have affected positively banks' policies on lending. At the end of 2019, non-performing loans of enterprises against the total were 10.7%, the lowest level in the last ten years. The decline of this ratio by 16 percentage points during this period reflected the improvement of economic activity, legal framework and financial conditions, the decrease of exchange rate volatility risk, as well as the strengthening of bank-enterprises relationships. The writte-off of lost loans from banks' balance sheetshas also had a significant impact on this performance[4].

On the other hand, enterprises' demand for loans does not follow a sustainable growth rate trajectory, displaying some volatility among quarters. In 2019 Q4, credit demand was reported slightly lower from the previous quarter. Sluggish demand for loans, being mainly pronounced in small and medium-sized enterprises segment for investment purposes, is attributed largely to the perception on the macroeconomic situation and its outlook, as well as to the fall in business' confidence.

Chart 1 Quarterly flows of new loans to enterprises and non-performing loans.



**(+) implies that banks expect credit to be higher than in the previous quarter; (-) implies that banks expect credit to be lower than in the previous quarter.*
Source: Bank of Albania and staff estimates.

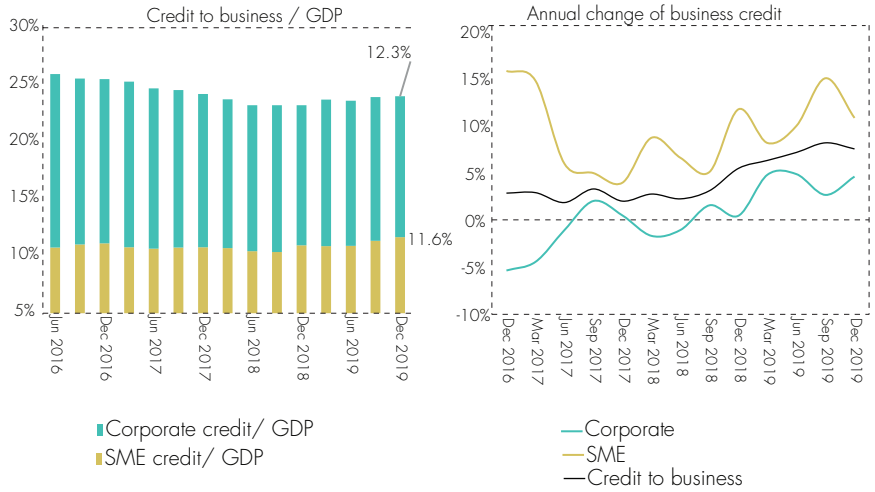
[2] *Data for loans to enterprises are adjusted for written-off loans and exchange rate volatility.*

[3] *For more detailed information please refer to the Bank Lending Survey section at: https://www.bankofalbania.org/Monetary_Policy/Surveys_11282/Bank_Lending_Survey/*

[4] *The writing-off of these loans started in 2015. Over 5 year period, the banks have written-off balance sheet around ALL 68 billion loans to enterprises.*

New loans to enterprises improved their growth rates in 2019 Q4. Thus, new loans flow for enterprises of ALL 52.7 billion, was significantly above the levels registered in previous quarters, reflecting seasonal behaviour as well. Adjusted for seasonality, this flow was 11.3% higher in quarterly terms. It was also 5.5% higher compared to previous year. The increase in new loans to enterprises in 2019 Q4, appears to be in line with the bank's expectations on lending demand, as expressed in the Bank Lending Survey[5].

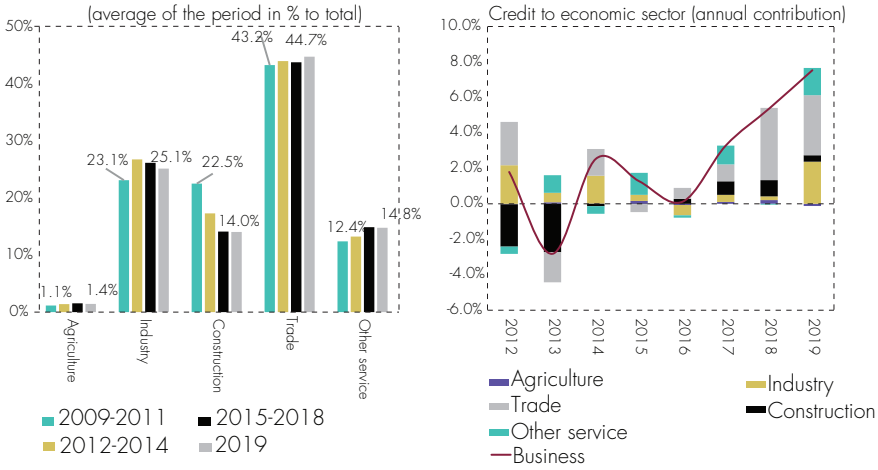
Chart 2 Structure of loans to enterprises by size



Source: Bank of Albania.

The positive developments of the portfolio of loans to enterprises were supported by lending to large enterprises. This portfolio registered an increase of 4.5%, or 2.5 percentage points more than the previous quarter. On the other hand, the increase of loans to small and medium-sized enterprises (SMEs) registered a slowdown, diverging from the upward trend up to 2019 Q3. The performance of the portfolio of loans to SMEs is affected positively by the easing of lending standards by banks, whereas their demand for funding is lower than in the previous quarter.

Chart 3 Structure of loans to enterprises by sectors of the economy



Source: Bank of Albania.

'Trade' (right Chart) represents trade, hotels and restaurants sector.

[5] *For more detailed information please refer to the Bank Lending Survey section at: https://www.bankofalbania.org/Monetary_Policy/Surveys_11282/Bank_Lending_Survey/*

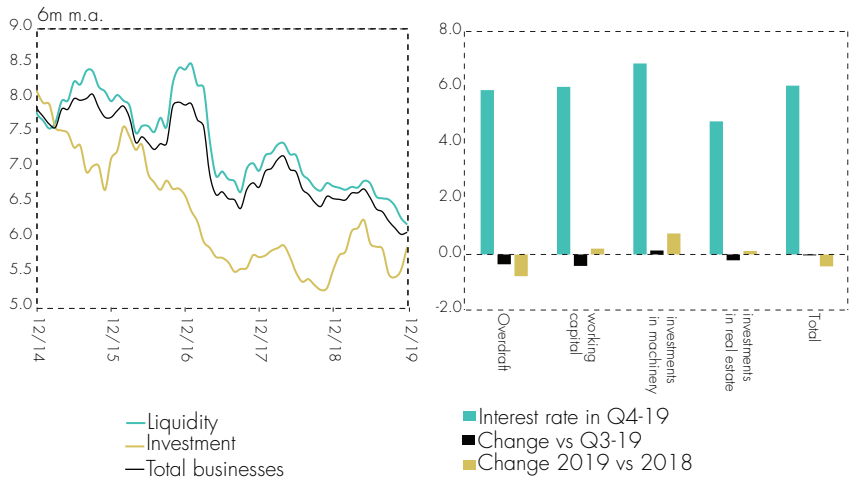
Due to the fragile nature of SMEs' economic activity, the impact of the November 26th earthquake may be higher for them. At the end of 2019, loans to SMEs accounted for 11.6% of GDP, or 0.7 percentage points higher than in the previous year. This ratio for loans to large enterprises was 12.3%, almost unchanged since 2018.

The analysis by sectors shows thatloans to enterprises in 2019 Q4 are supported by lending to services and trade sectors. The growth rates of loans to these sectors improved by 10.6% and 7.6%, respectively. Meanwhile, the portfolio of loans to the industry sector and to the construction sector remained almost unchanged from 2019 Q3. The growth rates of loans to these sectors slowed down to 9.7% and 2.5%, respectively. Agriculture is the only sector that registered a contraction of lending compared with the previous year, by around 7%. The contraction of this portfolio has been a phenomenon present throughout most of the year, thus affecting the reduction of the share ofloans to agriculture to the total to 1.4%. The construction sector also registered a reduction of its share to the total, to 14.0%, compared its share of 14.7% in the previous year. The contraction of credit share in these two sectors is accompanied by the expansion of the portfolio of loans to industry, trade and services sectors, which at the end of 2019 registered increase in their share to the total, to 25.1%, 44.7% and 14.8%, respectively.

Interest rates on new loans in lek to enterprises have decreased for liquidity loans, but have registered a slight increase in investment loans.

The average interest rate on lek loans to private enterprises was recorded at 6.1% in 2019 Q4, remaining unchanged from the previous quarter. By purpose of use, a further decline of interest rates for loans funding liquidity needs (overdraft and working capital) was recorded. The interest rate for liquidity loans registered at 6.1% on average in 2019 Q4, from 6.3% and 6.8%, respectively, in 2019 Q3 and 2019 H1. Overall, for 2019 it was 0.5 percentage points lower than in 2018, thus driving the decline of interest rates for enterprises in this period.

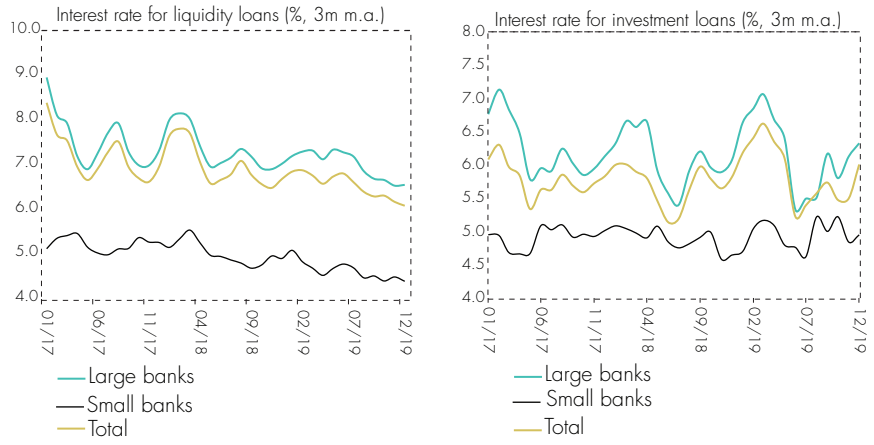
Chart 4 Interest rates on lek loans to private enterprises



Source: Bank of Albania.

The downward trend of interest rates for liquidity loans initially started by small banks of the system in 2018, and was further reinforced by large banks in 2019 H2. The latter systematically apply higher interest rates for this segment of lending compared to small banks, by around 2.4 percentage points.

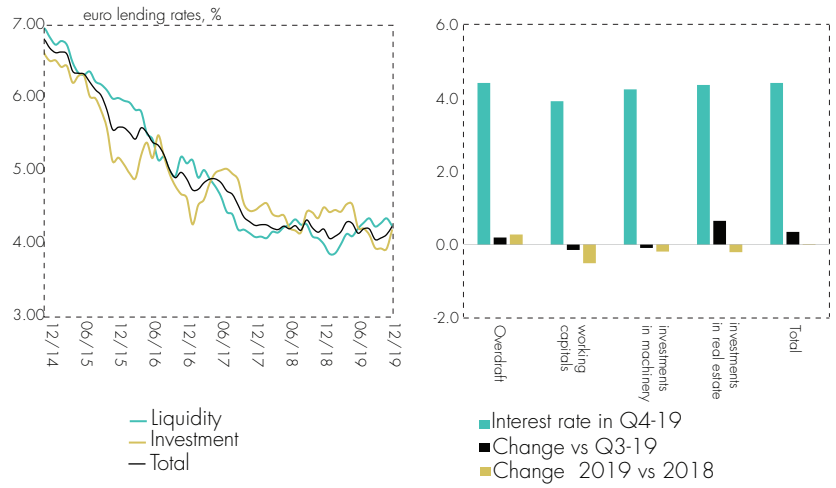
Chart 5 Interest rate of loans to enterprises by purpose and size of banks



Source: Bank of Albania.

The interest rate on investment loans increased again in 2019 Q4. It resulted on average at 6.0%, from 5.7% in the previous quarter. The increase of the interest rates in this segment reflected higher interest rates on funding for equipment purchase. However, in this quarter, this phenomenon was isolated in one bank of the system during November. Excluding this case, the average interest rates of investment loans appears steady, close to the rates of 2019 Q3. Overall, the interest rates on investment loans are characterized by high volatility, reflecting also the variation of risk level that these types of loans carry.

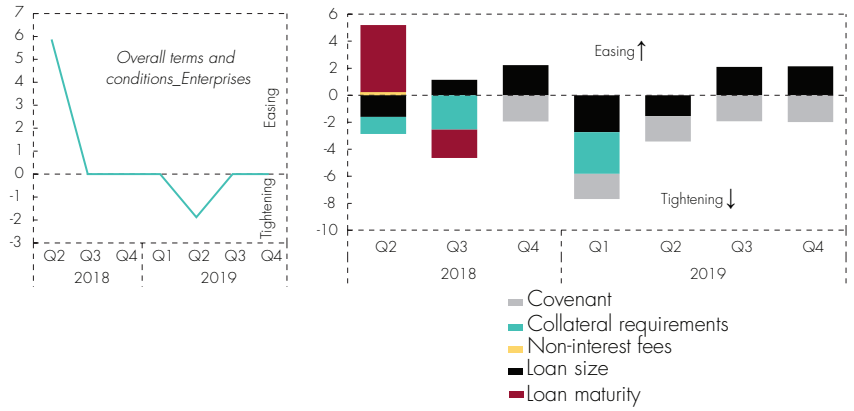
Chart 6 Interest rates on euro loans to private enterprises



Source: Bank of Albania.

Interest rates on euro loans to enterprises registered a slight increase in 2019 Q4. Average interest rates resulted 4.4% for this quarter, from 4.1% registered in the first three quarters of the year. The increase of interest rates was present mainly in the segment of investment loans for real estate, whereas interest rates for other types of lending did not undergo any substantial changes. Despite small fluctuations in these quarters, the interest rate on euro loans to enterprises has been relatively stable since 2017 H2, not deviating much from the average value of 4.2%.

Chart 7 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, staff estimates.

Lending terms and conditions together with non-price elements that form them (besides margins) are indicators obtained by the Bank Lending Survey. The value of each indicator represents net balances, derived as the difference between responses for terms and conditions very or somewhat eased, with those somewhat or tightened, adjusted for the weight of each bank in the credit stock. Technically these are qualitative values (i.e. non quantitative) and the higher is the value the more important is the direction they represent: if it is positive, negative, or unchanged.

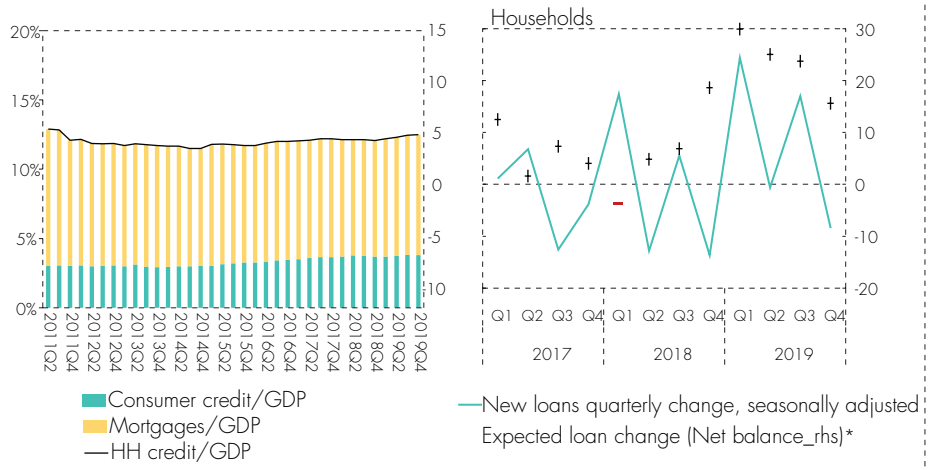
Overall terms and conditions for new loans to enterprises remained unchanged in 2019 Q4. From the non-price terms and conditions standpoint, -as one of the two pillars that constitute the overall terms and conditions-, the banking system considered as appropriate the use of two instruments to determine the overall terms and conditions on new loans. In 2019 Q4, banks reported that they increased slightly the size of the loans accorded to enterprises. On the other hand, banks loan covenants where higher in this quarter, offsetting thus the positive impact from the loan size on the overall terms and conditions for new loans. The other items of non-price terms and conditions remained unchanged from the previous quarter.

2. LOANS TO HOUSEHOLDS[6]

The growth pace of loans to households has improved in the last quarter.

The annual growth rate of loans to households accelerated on average to 7.5% in the last quarter, compared with 6.9% registered in 2019 Q3. Its expansion was supported largely by the positive developments in mortgage loans, while consumer loans appear more volatile over time. The analuysis by currency shows that the increase of loans to households has been mainly dominated by the domestic currency. The relatively stable expansion of loans to households in the last five years is driven by the continuous easing of terms and conditions on the supply side of the banking system. On the other hand, credit demand by households appears volatile, with a decline in the last quarter reported by the Bank Lending Survey[7]. According to banks' perception, this situation has factored in the impact of the November earthquake as well.

Chart 8 Loans to households against GDP and new loans flow



(+) implies that banks expect credit to be higher than in the previous quarter; (-) implies that banks expect credit to be lower than in the previous quarter.

Source: Bank of Albania.

As a ratio to GDP, the stock of loans to households in December is estimated at 12.5%, or around 0.4 percentage points higher than at the end of 2018. Despite the stable expansion of this portfolio in the last years, loans to households in Albania have remained at relatively low levels compared to the countries of the CESEE region[8]. Mortgages constitute the largest chunk of loans to households, at around 70%. As a ratio to GDP, mortgage loans are estimated at 8.7%, whereas consumer loans at around 3.8%.

In 2019 Q4 new loans flow to households was around ALL 15.6 billion, 4.2% lower from the previous quarter, adjusted for seasonality. The recent developments in loan flows to households were unexpected even by banks, which, in the previous quarter, forecasted a continuing quarterly growth rate of

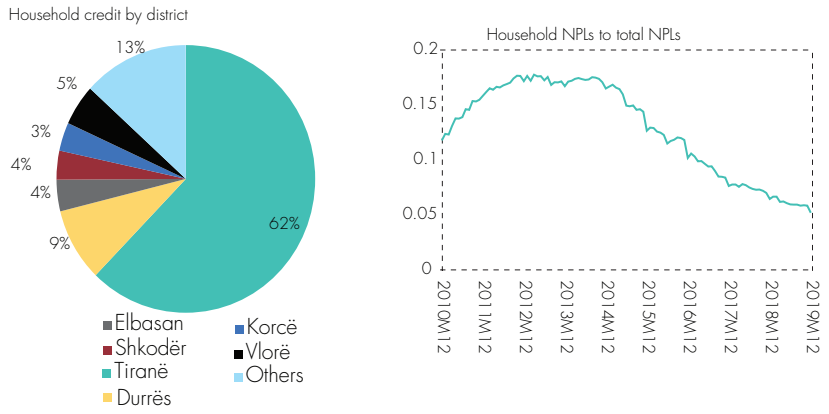
[6] *The data for loans to households are adjusted for written-off loans and exchange rate fluctuations.*

[7] *For more detailed information please refer to the Bank Lending Survey section at: https://www.bankofalbania.org/Monetary_Policy/Surveys_11282/Bank_Lending_Survey/.*

[8] *A more detailed analysis of the performance of lending in the countries of the region may be found in the last section of this material.*

new loans in the quarter ahead. However, it should be noted that new loans flow to households in 2019 Q4 was higher compared to previous years.

Chart 9 Geographical distribution of loans to households and non-performing loans to households



Source: Bank of Albania, authors' calculations.

The geographical distribution of the portfolio of loans to households shows a high concentration in Tirana District, with over 62% of the stock. Less than 10% of the stock of loans to households was distributed in the Durrës District, with the remainder distributed more evenly in the remaining districts. The domination of the Tirana District in the segment of loans to households, as well as to enterprises, has reflected the high concentration of economic activity and demographics in this district.

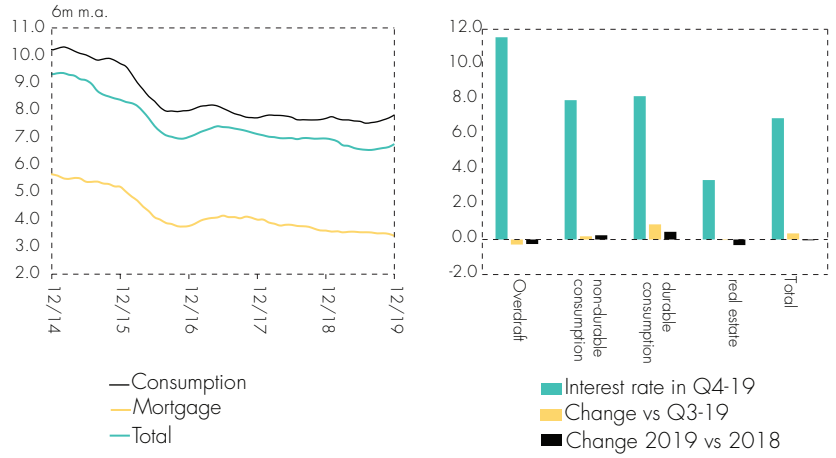
In terms of performance of the portfolio of loans to households, there has been a gradual decline of non-performing loans in the last five years. Among others, improvements in the labour market, the more cautious approach of banks to lending, coupled with increased awareness of this segment's exposure to exchange rate risks, have produced positive results in terms of improving credit quality. At the end of the year, non-performing loans in the segment of households constitute only 5.2% of this portfolio, declining by around 10 percentage points over a five-year period. This performance is also largely affected by the write-off process of non-performing loans from banks' balance sheets in the last five years[9].

Interest rates and non-price terms and conditions on loans to households were stable in 2019 Q4, with the exception of the slight increase of the interest rate on lek consumer loans.

The average interest rate on loans to households in lek registered an increase in 2019 Q4, to 6.9% from 6.6%, which was the average of the three previous quarters, due to the increase of the interest rate on consumer loans for durable goods. Overall, during 2019 the average interest rate on loans to households stood at 6.7%, or 0.3 percentage point lower than the previous year.

[9] *In the last five years, the banks of the system have written-off their balance sheets around ALL 14 billion.*

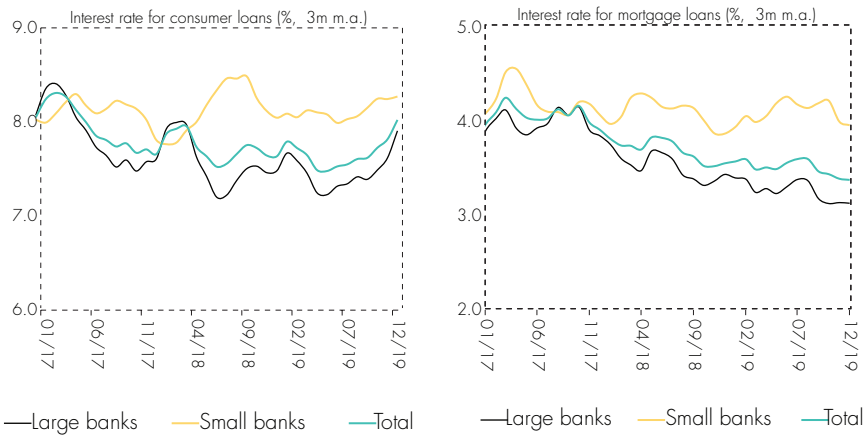
Chart 10 Interest rates on lek loans to households



Source: Bank of Albania.

The average interest rate on consumer loans increased to 8.0%, up by 0.4 percentage points from the three previous quarters. While the interest rates for households appear relatively stable for all types of credit in the first three quarters of the year, the increase of consumer loans interest rate in 2019 Q4 is mainly determined by the higher interest rates for this type of loans from large banks. The changes in the interest rates of loans to households in the other segments were marginal in this quarter. Average interest rates of loans for house purchase and overdrafts were recorded at 3.4% and 11.5%, respectively, remaining close to the averages registered throughout the year.

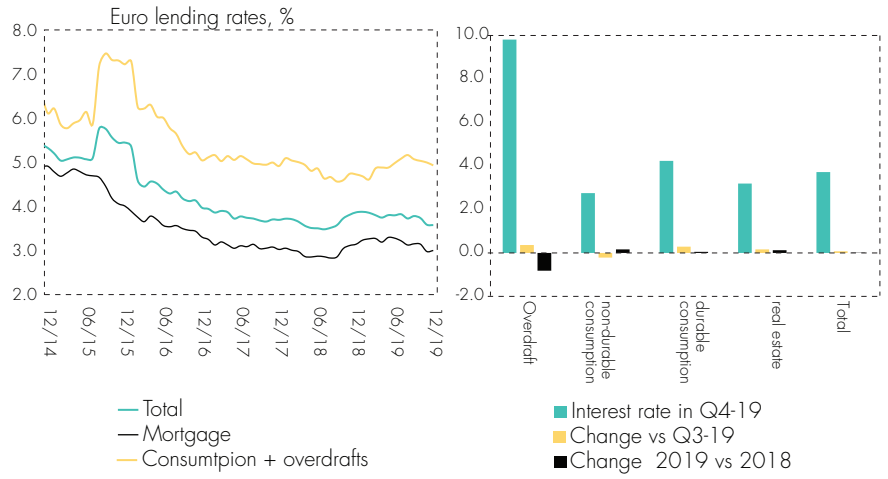
Chart 11 Interest rate on loans in lek to households by purpose and size of banks



Source: Bank of Albania.

The average interest rate of loans to households in euro appears to be stable in 2019 Q4. This rate was 3.6%, remaining close to the average of Q3 (3.7%). Interest rates appear stable for all types of credit. Apart from short-term changes, the interest rates of loans to households in euro have fluctuated around the average level of the last three years, att around 3.8%.

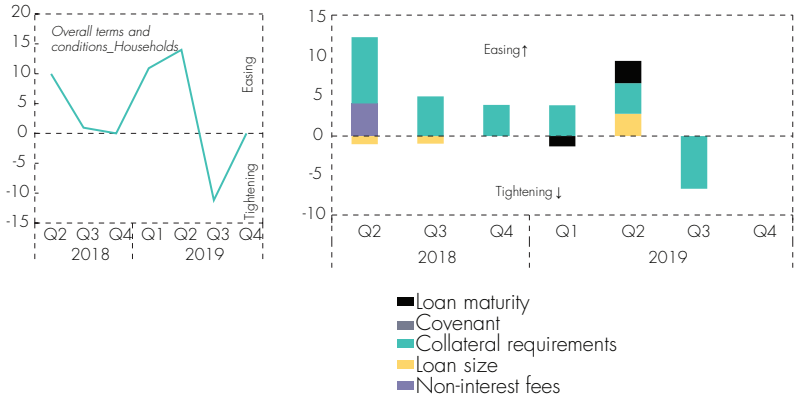
Chart 12 Interest rates on euro loans to households



Source: Bank of Albania.

Overall terms and conditions on new loans for households, as well as their non-price elements were perceived as unchanged in 2019 Q4. Thus, non-interest charges, loan size, loan maturity, collateral requirements and loan covenants remained unchanged from the previous quarter.

Chart 13 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, staff estimates.

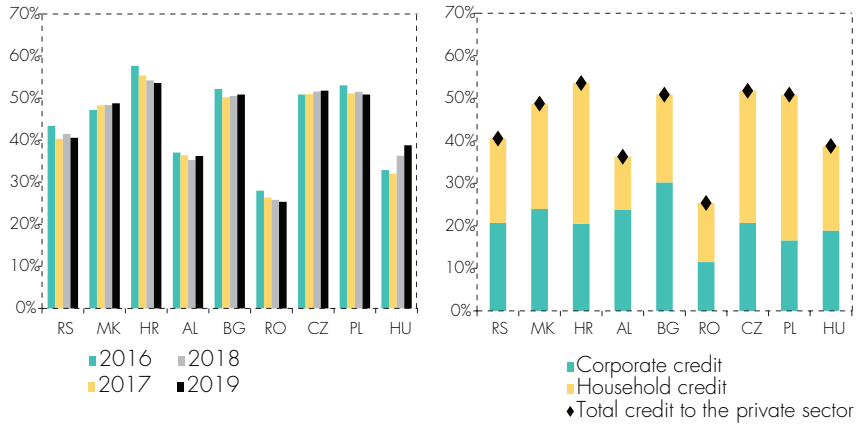
Overall terms and conditions on new loans are indicators obtained by qualitative data from the Bank Lending Survey. Each indicator is expressed as net percentage, which represents the difference between the responses indicating easing of overall terms and conditions with those indicating the tightening of overall terms and conditions, adjusted for each bank weight on credit portfolio. The positive values indicate eased credit terms and conditions, whereas negative values tightened ones. Technically, these are qualitative values (i.e. non quantitative) and more than the magnitude, the direction of the indicator is the one that matters, ie, if it is positive, negative or remains unchanged.

3. TRENDS IN LENDING IN THE CESEE REGION[10]

Lending activity in the CESEE region has expanded at a moderate pace throughout the year.

The lending activity in the CESEE region has expanded at a moderate pace throughout 2019. The ratio of credit to the private sector to GDP is estimated at around 44% on average. In geographical terms, this ratio fluctuated within a range of 25.4% in the case of Romania and 53.6% in the case of Croatia, the highest level for the CESEE region. This ratio has improved for five of the CESEE countries in the last three years. Among them, in the case of Albania this ratio is estimated at 36.5% as at end 2019, 1.2 percentage points higher compared to 2018.

Chart 14 Credit to the private sector in the countries of the region as a ratio to GDP



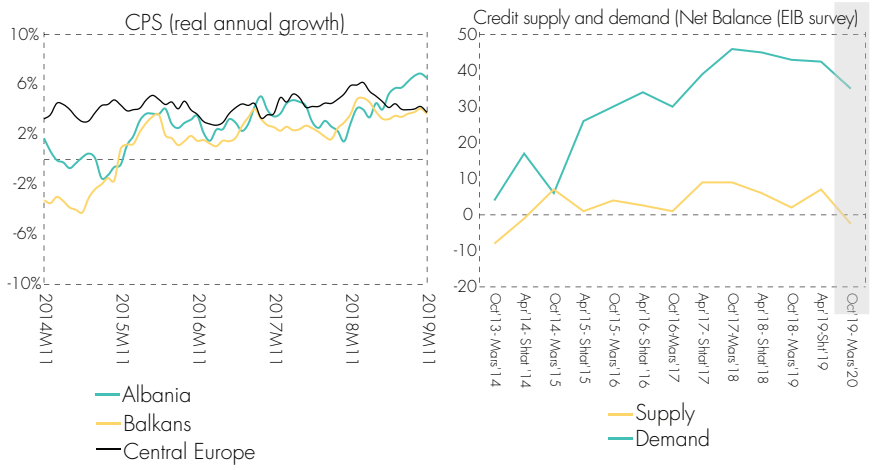
Source: Bank of Albania; respective central banks of countries in the region; IMF; authors' calculations.

In the last CESEE Bank Lending Survey[11], for the forecasted period October 2019 - March 2020, banks have predicted a slightly more moderate growth of demand by economic agents. At the same time, banks' expected a tightening of the supply conditions for the same period, affecting a further expansion of the demand - supply gap. These expectations appear to have materialized partially in the October – November period. During this time, the annual growth of credit to the private sector in the countries of the region was around 3.9%, similar to the previous quarter. The expansion of credit to the private sector hascontinued to be sustained by the stable performance of loans to the households segment. On the other hand, loans to enterprises show a relatively more volatile and uneven performance in geographical terms. Overall, the growth of this portfolio remains moderate and not yet stable.

[10] *This analysis includes 9 countries of the Central, Eastern and South-Eastern Europe: Albania, North Macedonia, Croatia, Serbia, Bulgaria, Romania, the Czech Republic, Poland and Hungary. The stock of credit to the private sector is adjusted for inflation and exchange rate effects.*

[11] *For more detailed information, please refer to the Bank Lending Survey in CESEE countries: https://www.eib.org/attachments/efs/economics_cesee_bls_2019_h2_en.pdf.*

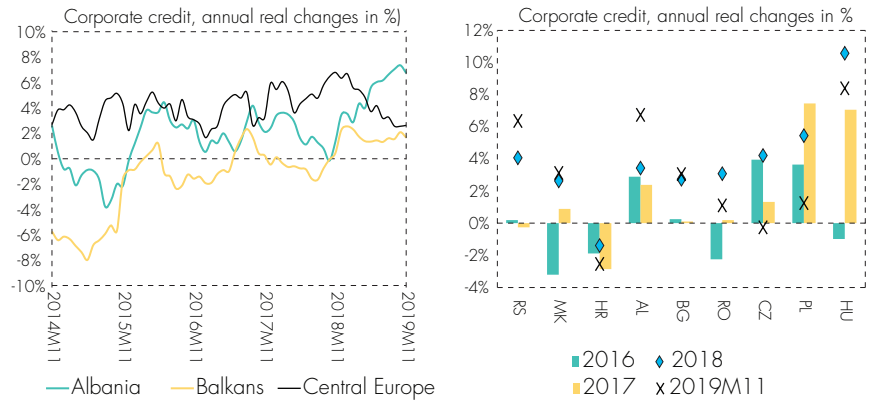
Chart 15 Credit to the private sector in the countries of the region



Source: Bank of Albania; respective central banks of countries in the region; authors' calculations.

The stock of loans to enterprises, compared to the third quarter, has recorded lower growth rates during October and November.. This portfolio expanded by around 2.3% in average annual terms, compared to 2.5% in 2019 Q3. The weak performance of this portfolio during 2019 - where annual growth rates have generally slowed down compared to the previous year - has led to a reduction of its share to the total. In November, the stock of loans to enterprises in the CESEE region constituted less than 40% of total credit to the private sector. The region of Central Europe is leading the growth rates of loans to enterprises, despite the slowdown in the annual growth rates of this portfolio over the last year.

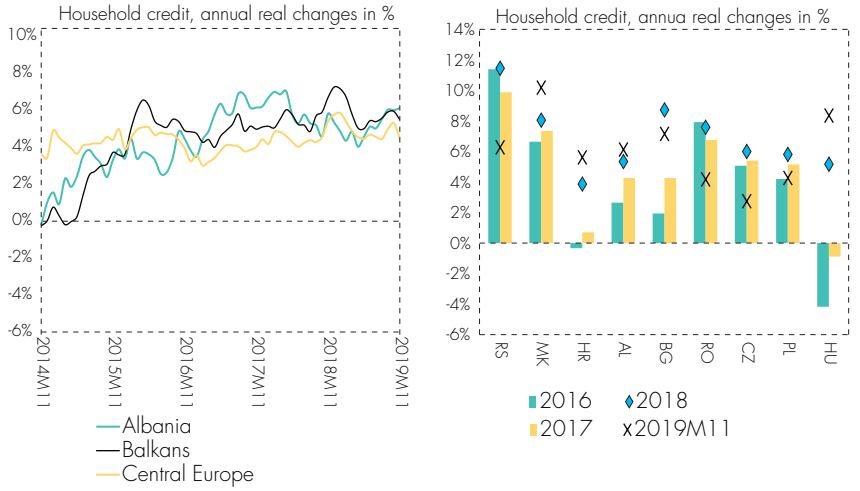
Chart 16 Loans to enterprises in the countries of the CESEE region



Source: Bank of Albania; respective central banks of countries in the region; authors' calculations.

The performance of loans to households is rather uniform over time, as wellas more balanced in geographical terms compared to the portfolio of loans to enterprises. Loans to households in the region constitute the majority of total credit, over 60%, compared to the share of only 35% of this portfolio to the total in Albania.

Chart 17 Loans to households in the countries of the CESEE region



Source: Bank of Albania; respective central banks of the countries in the region; authors' calculations.

The annual growth rate of loans to households accelerated slightly during October - November , to 5.0%, up from the 4.8% on average in 2019 Q3. Overall, the developments in this portfolio are in line with banks' expectations. In the last Bank Lending Survey in the CESEE region, banks said that, despite a small tightening of lending standards, in the consumer segment as well as in the mortgage segment, developments in loans to households have a positive inertia. The growth of loans to households is supported by the continuous contribution of positive factors,such as the high demand for consumer loans, consumer confidence and the positive outlook of the housing market.