



# CESEE Bank Lending Survey

H2-2014



# **CESEE Bank Lending Survey**

## H2-2014

The mission of the EIB's Economics Department is to provide economic analyses and studies to support the Bank in its operations and in its positioning, strategy and policy. The Department, a team of 30 economists and assistants, is headed by Debora Revoltella, Director of Economics.

## **CESEE Bank Lending Survey – H2 2014**

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The EIB wishes to thank the banks for their contribution and participation in the survey. Last but not least, it wishes to thank all Vienna Initiative and Steering Committee members for their comments and support in developing the survey.

### **Disclaimer**

The views expressed in this document are those of the authors and do not necessarily reflect the position of the EIB or its shareholders. The authors and administrators of the survey have endeavoured to ensure the quality of the analysis, representativeness of the survey and reliability of market players' assessment and expectations. However, they are not responsible for any errors or omissions in the responses to the survey or for the consequences of any such errors or omissions.

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# FOREWORD

The last fifteen years have witnessed many significant developments in the banking sector in Central Europe and South Eastern Europe (CESEE). From the late 1990s until 2008, the CESEE banking sector experienced an accelerated pattern of growth. A large number of international banks invested in the region and contributed to an inflow of capital and new banking practices. Lending growth was extraordinarily high, helping to close the region's financial penetration gap. On the flipside, it led to a build-up of imbalances and risks. The global financial crisis and EU sovereign debt crisis put a halt to the credit boom. Despite increased scarcity of capital and funding, the international banks' active in CESEE have remained committed to their CESEE growth strategy. The Vienna Initiative was crucial at the peak of the crisis. International banks formally undertook to provide capital and funding where needed to their subsidiaries, thus averting the risk of a disordered deleveraging. As the first acute phase of the crisis has faded, the CESEE banking sector continues to reshape. While there is still evidence of a financial penetration gap, a new banking model is emerging, with international banks calling for greater independence for their subsidiaries and a more balanced funding model, based on domestic resources. At the same time the recovery in lending has been slow, reflecting a mixture of demand and supply factors. Moreover, the international banks operating in the region have started to be more selective with regard to their CESEE strategies, clearly discriminating between countries and committing only to those markets that clearly offer long-term opportunities. Some of the international players have been subject to substantial restructuring at group level, with associated requests to reassess their own international position.

The Vienna Initiative (now known as "VI 2.0") has – via the Deleveraging and Credit Monitor – been monitoring the international banks' deleveraging process and related constraints on lending activity since the second quarter of 2012. In this context the EIB developed the CESEE Bank Lending Survey, which has been conducted on a semi-annual basis since October 2012 and investigates the strategies of international banks operating in CESEE as well as market conditions and market expectations, as perceived by the local subsidiaries/local banks. The survey seeks to disentangle the effects of demand and supply factors on credit developments, as well as the impact of national and international factors on demand and supply conditions. Results are key, to properly define policy actions.

The latest administration of the survey was finalised in September 2014. In the context of the AQR and Stress Tests conducted in the Euro area, international banks active in the region confirm they remain subject to restructuring and deleveraging at the overall group level. They remain generally committed to the region, but they clearly discriminate between countries. The crisis is taking its toll in terms of their assessment of local market potential, following several years of constrained profitability and heightened business risk. Some of the banks in the region are either located in unappealing markets (i.e. with low levels of profitability) or do not have, according to their owners, the right market positioning to exploit the value of operating in a particular country.

Both supply and demand factors are behind the slow recovery in lending. Still, banks seem to believe that demand will pick up, at a slightly faster pace than supply. It is interesting to note that funding does not seem to be a constraint on lending activity at the current very low levels of demand, as banks have switched from declining parent bank funding to new

domestic deposit taking and some new issuance in the local market. Credit quality, at both group and local level, is the biggest constraint on lending activity, together with regulation.

Looking ahead, important questions remain. If funding is not an issue at this level of demand, it might become a constraint in the event of a much stronger recovery. Developing local capital markets is key, as is finding the right balance to be able to still leverage the benefits of internationalisation for banking groups. With credit quality remaining a constraint on the supply side, more should be done to create the right incentives for banks to lend and to accelerate NPL management and disposal. VI 2.0 is a major step in this direction. Two major work-streams include a detailed analysis of the system of guarantee schemes, as a way to partially diversify the risk of lending to SMEs and a focus group on NPLs.

A handwritten signature in black ink, consisting of a stylized 'D' and 'R' followed by a horizontal line.

*Debora Revoltella*  
Director of the Economics Department  
European Investment Bank





# Survey Description

## Key statistics

- Developed in the context of the Vienna Initiative (VI) 2.0 as an additional instrument to monitor:
  - cross-border banks' deleveraging in CESEE
  - the determinants/constraints influencing credit growth in CESEE
  - market expectations of future developments.
- Target groups: international banks active in CESEE interviewed at group level and local banks/local subsidiaries of these groups interviewed at single-entity level:
  - 15 international groups
  - 90 local banks/subsidiaries.
- Average coverage: 50% of regional banking assets.
- Countries covered: Albania, Bosnia-Herzegovina, Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Macedonia, Poland, Romania, Serbia, Slovakia, Slovenia and Ukraine<sup>1</sup>.
- Periodicity: semi-annual (Sep/Oct and Mar/Apr). The first survey was conducted in October 2012.

## The CESEE Bank Lending Survey – technical note

The CESEE Bank Lending Survey was developed in the context of the Vienna Initiative 2.0 and has been endorsed by the various institutions participating in VI 2.0 as an instrument to:

- contribute to the monitoring of cross-border banking activities and deleveraging in CESEE;
- better understand the determinants/constraints influencing credit growth in CESEE;
- to gain some forward-looking insights into cross-border banks' strategies and market expectations regarding local financial conditions.

Taking into account the unique nature of the regional banking sector, with a large proportion of banks being foreign-owned, the survey investigates both the strategies of international banks active in CESEE and the market conditions and market expectations as perceived by the local subsidiaries/local banks. To that end, the

<sup>1</sup> Details for Estonia, Macedonia, Slovenia and Ukraine are not presented on a stand-alone basis, due to the relatively low coverage in terms of market share and/or number of banks.

survey covers the major international banks operating in CESEE and their subsidiaries in the region. At the same time, to gain a full understanding of local market conditions, an effort has been made to also include in the survey the relevant domestic players in a specific local market.

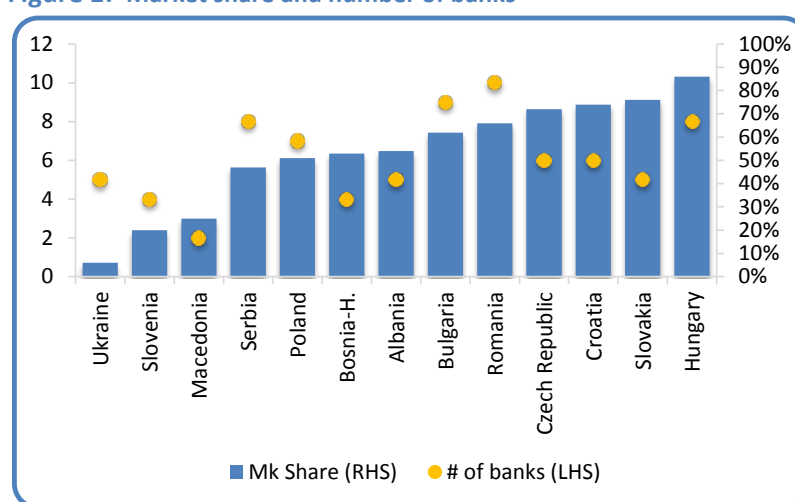
Given these features, the survey is a unique instrument for monitoring banking sector trends and challenges in CESEE. It complements domestic bank lending surveys by adding the value of comparability across countries and the unique feature of specifically addressing the parent/subsidiary nexus. It also complements information derived from BIS data concerning cross-border banks' exposure.

The survey is administered by the European Investment Bank, under a confidentiality agreement with the individual participating banks. It is addressed to senior officials of the banks involved and is conducted on a semi-annual basis in February/March and September. The first survey was carried out in September/October 2012. Most of the questions have a backward and a forward-looking component, covering the six months before and expectations over the following six months.

In terms of coverage, the latest survey involved 15 international groups operating in CESEE and 90 local subsidiaries/independent domestic players. It is highly representative of international groups active in CESEE and also of local market conditions, as it relates on average to 50% of local banking assets.

The countries currently included in the survey are: Albania, Bosnia-Herzegovina, Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Macedonia, Poland, Romania, Serbia, Slovakia, Slovenia and Ukraine. The coverage varies by country – Figure 1 presents the percentage of assets covered in each country and number of banks included.

**Figure 1: Market share and number of banks**



Source: EIB – CESEE Bank Lending Survey.

The detailed survey questionnaire is contained in the annex. The survey is divided into two sections, the first addressed to international groups, the second to domestic banks/subsidiaries of international groups.

The first section investigates international banks' strategies, restructuring plans, access to funding and deleveraging at the global and group level. It includes questions on the long-term strategic approaches adopted for CESEE, the level of profitability of CESEE operations and the groups' exposure to the CESEE region.

The second part of the survey is addressed to domestic/subsidiary banks operating in the CESEE region and investigates the main determinants of local banking conditions.

Among the supply conditions, attention is given to credit standards and credit terms and conditions, as well as to the various factors that may be responsible for changes to them. Credit standards are the internal guidelines or criteria that guide a bank's loan policy. The terms and conditions of a loan refer to the specific obligations included in a loan contract, such as the interest rate, collateral requirements and maturity. The survey includes a set of questions assessing the underlying factors affecting a bank's credit standards. Factors are clustered into domestic and international components. Examples of local factors are the local market outlook, local bank outlook and local bank access to funding, changes in local regulation, local bank capital constraints and local bank NPLs (non-performing loans). Among the international factors, the survey includes the group outlook and global market outlook but also EU regulation, group capital constraints and group NPLs.

Demand for loans is also investigated in terms of loan applications. Among the elements that may affect loan demand, various factors relating to financing needs in both the household and enterprise sectors are examined. For the enterprise sector, the survey includes fixed investment, inventories and working capital, corporate restructuring and debt restructuring. For the household sector, the survey considers the effects of housing market prospects, consumer confidence and non-housing-related consumption expenditure.

Most of the questions concerning demand and supply are classified according to two borrower sectors: households and enterprises. Further breakdowns are also considered. For example, the survey investigates developments in the SME and large corporate segments as well as different types of credit lines and loans in the household sector (e.g. consumer credit and loans for house purchases). In addition, maturity and currency dimensions are also explored.

The survey includes specific questions on credit quality and the funding conditions for banks in CESEE. Specifically it includes questions on NPL ratio developments, providing a breakdown between the retail and corporate subsectors. The survey investigates aggregate access to funding as well as funding conditions for an extensive list of funding sources. These include intra-group funding, retail and corporate funding, funding from international financial institutions (IFIs) and wholesale funding.

Most of the responses are illustrated in the following chapters of this report as net percentages, i.e. the percentage of positives minus negatives (excluding the neutral responses). For example, the percentage difference between responses reporting an increase in demand for loans and responses reporting a decrease – irrespective of the size of the increase or decrease. This is an oft-cited indicator, which has a barometer function. It helps to detect potential drifts and tendencies in the panel of respondents. Answers are not weighted by the size of the participating banks.

# Regional Overview

## 1. Summary – *Demand for credit has improved and supply conditions have stabilised. International banks are increasingly differentiating their strategic approaches to suit the individual countries of the CESEE region*

### International groups' views:

- **Global strategies:** Cross-border banking groups continued to restructure at the group level, primarily via sales of assets or branches. Capital market activities played a more prominent role than expected in the March 2014 survey, whilst capital injections from governments played no part. Deleveraging continues, in line with all previous releases of the survey.
- **Commitment to CESEE:** Operations in CESEE remain relevant for the global international groups' strategies. However, cross-border banks continue to discriminate in their country-by-country strategies. Roughly 33 percent of the groups expect to expand operations, while 33 percent may reduce operations in the region. Roughly 50 percent of the groups signal that they have been reducing their total exposure to the region (by reducing intra-group funding), while only 33 percent expect to continue to do so. The profitability of CESEE operations is emerging as a challenge. Expected returns on assets for these operations have been decreasing compared with overall group results. Banks are also reviewing their assessments of the potential of some of the region's markets. If confirmed, this trend might lead to some strategic refocusing over the medium term.

### Subsidiaries'/local banks' views:

- Banks report an **increase in credit demand and a stabilisation of supply conditions**, although levels of both remain low. Both supply and demand are expected to improve in the next six months.
- Banks expect an easing of **credit supply** conditions almost across the board. NPLs and regulation, at both the national and international level, remain the most cited factors constraining supply.
- **Demand for loans** improved substantially, mostly for debt restructuring and working capital needs, while investment demand remains very weak. Banks' optimism about demand is now close to the level of late 2012.
- **Access to funding:** Funding conditions are fairly favourable, with access to funding positive across all sources. A new funding model has emerged, with local bank funding playing a predominant role, substituting for decreased intra-group funding. Increased funding from IFIs is supporting the positive outlook.
- **NPL figures** deteriorated further and remain a key concern for the region's banks. NPL ratios in the corporate segment are expected to level off, while the retail segment is expected to deteriorate slowly. The rate of increase of NPLs is now at a much lower pace, signalling that a turning point may now be close.

## 2. Results of the Bank Lending Survey:

### 2.1 Parent banks

1. **Restructuring at the group level did not decelerate and is expected to continue, while slightly less than half the banking groups anticipate further deleveraging.** Cross-border banking groups have engaged in various forms of restructuring at the

group level and expect to continue this process

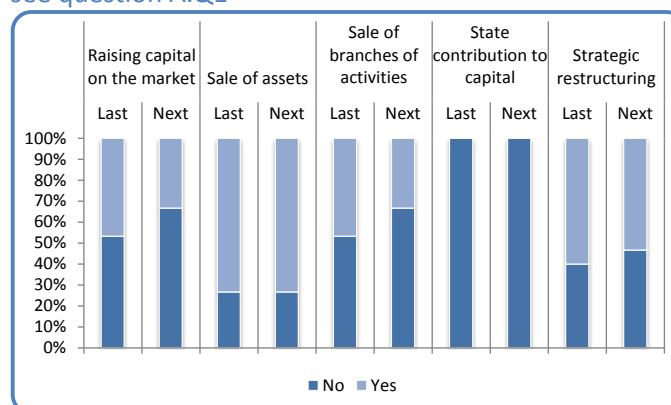
(Figure 1). Capital was raised primarily via the sale of assets, and there was no resort to capital provision from the state. Contributions to increased capital

ratios and to the strengthening of core activities also came from sales of branches, as foreshadowed in previous releases of this survey. The issue of new capital on the market played a significant role over the past six months. Looking at the next six months, contributions to balance sheet strengthening are again expected to come mainly from sales of assets, but also from sales of branches.

Capital market activities are expected to play a more limited role, while no government capital injections are foreseen for the first time since the inception of the survey. Deleveraging at the group level (not shown on these charts) is continuing,

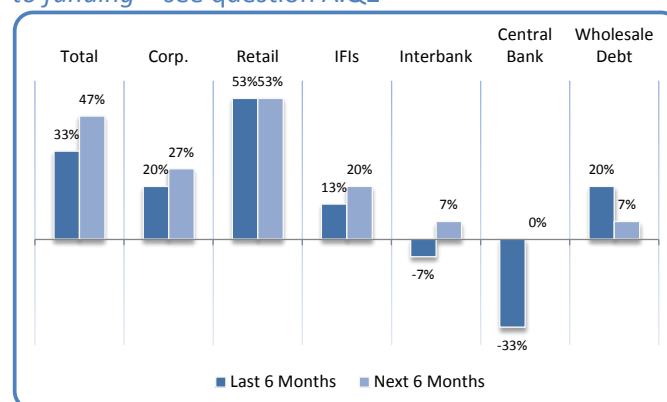
with still roughly half the groups expecting a decrease in their group-level loan-to-deposit ratios. These results show a generally stable picture compared to the March 2014 survey. Group-level access to funding continued to improve (Figure 2), although the extent of the improvement

**Figure 1: Strategic operations to increase capital ratio – see question A.Q1**



Source: EIB – CESEE Bank Lending Survey.

**Figure 2: Access to funding conditions – net percentages; positive values indicate increased access to funding – see question A.Q2**

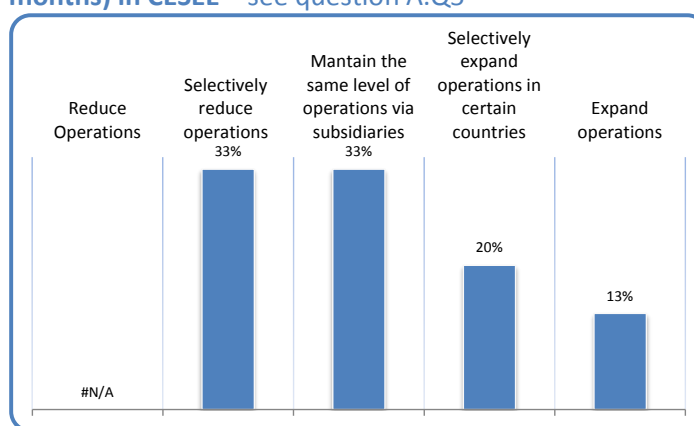


Source: EIB – CESEE Bank Lending Survey.

was smaller than in previous runs of the survey. This reflects protracted improvements in retail and corporate deposit funding, along with continued funding support provided from IFIs and some increased activity in the relatively small wholesale debt market. The interbank market, on the other hand, did not constitute an additional positive source of funding, and banks continue to reduce their recourse to central bank financing. Looking at the next six months, funding conditions are expected to remain fairly relaxed. Access to funding is expected to pick up even further as more funding is projected from the same sources as in the last six months. In addition, the interbank market is again expected to make a positive contribution, while parent bank access to the ECB's TLTROs may also relieve funding pressures.

2. **Cross-border banks continue to discriminate between the countries of operation in CESEE, reassessing their country strategies.** Operations in CESEE clearly remain part of the global strategies of a majority of the international groups operating in the region. CESEE operations also remain profitable. However, they deliver higher returns on assets than overall group operations for only roughly half of the groups. This is a pattern which has been confirmed over the several

**Figure 3: Group-level long-term strategies (beyond 12 months) in CESEE – see question A.Q5**



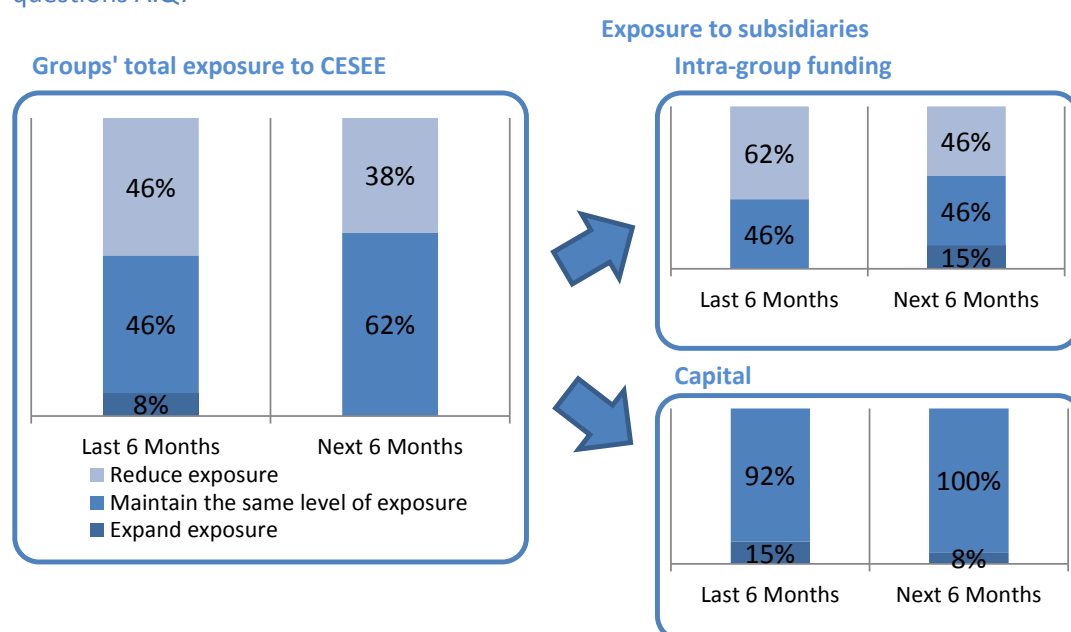
Source: EIB – CESEE Bank Lending Survey.

runs of the survey. As a result, cross-border banking groups continue to discriminate in terms of the countries in which they operate (Figure 3), reassessing their country-by-country strategies in relation to structural changes in individual countries' economic and political outlooks. Some 33 percent of the groups expect to expand operations, down from 46 percent in the March 2014 survey, while another 33 percent may reduce operations. In addition, the market potential and positioning differs robustly across countries (Annex A.5 and A.6). There has been a downward revision of assessments of the prospects for the regional market in general. Surveyed banks see the market potential (Annex A.9 for data on low market potential) as having deteriorated in Hungary, Bosnia-Herzegovina and to a lesser extent Albania, which now join Croatia as medium to low potential. Market prospects for Ukraine, Slovenia and FYR Macedonia are almost universally considered very poor. In the other countries of the region, relatively few banks see poor prospects, while most see reasonable market potential. In terms of market positioning, most banks in the majority of markets remain comfortable with their operations. Over 40 percent of the surveyed banks find their position in Hungary in the weak or niche category (Annex A.10 for data on weak positioning), and this is also the case in Bulgaria, FYR

Macedonia, Romania and Serbia, while in Ukraine this figure has risen to 70 percent. All in all, this is also reflected in the assessed profitability of the market in terms of ROA (adjusted for cost of risk) and ROE (adjusted for cost of equity), with rather differentiated prospects being depicted across countries (Annex A.7 and A.8).

3. **Just under half the groups signal that they have been reducing their total exposure to the region, and a smaller number expect to continue to do so over the next six months.** Almost all the decrease in exposure derived from reduced intra-group funding to subsidiaries. This is expected to continue over the next six months, although at a slower pace (Figure 4). Continuing weak local demand may have directly influenced the amount of intra-group funding needed to sustain local business activities, although other factors, including regulation affecting parent companies, may have also played a part. On the other hand, all parent banks report that they intend to maintain the current level of capital exposure to their subsidiaries, or even increase it – pending ECB asset quality review results and implications. On balance, increasing capital exposures seem to have partially compensated for decreased intra-group funding. In addition, the survey detected that the expansionary monetary policy operations announced by the ECB (primarily the TLTROs) may have some positive impact on groups' exposures to the CESEE region over the next six months<sup>1</sup>. The impact is expected to be primarily on intra-group funding exposure, while capital exposures are expected to remain unaffected.

**Figure 4: Groups' total exposure to CESEE – Cross-border operations involving CESEE countries – net percentages; positive values indicate increased access to funding – see questions A.Q7**



Source: EIB – CESEE Bank Lending Survey.

<sup>1</sup> Detailed data are not disclosed due to confidentiality reasons.

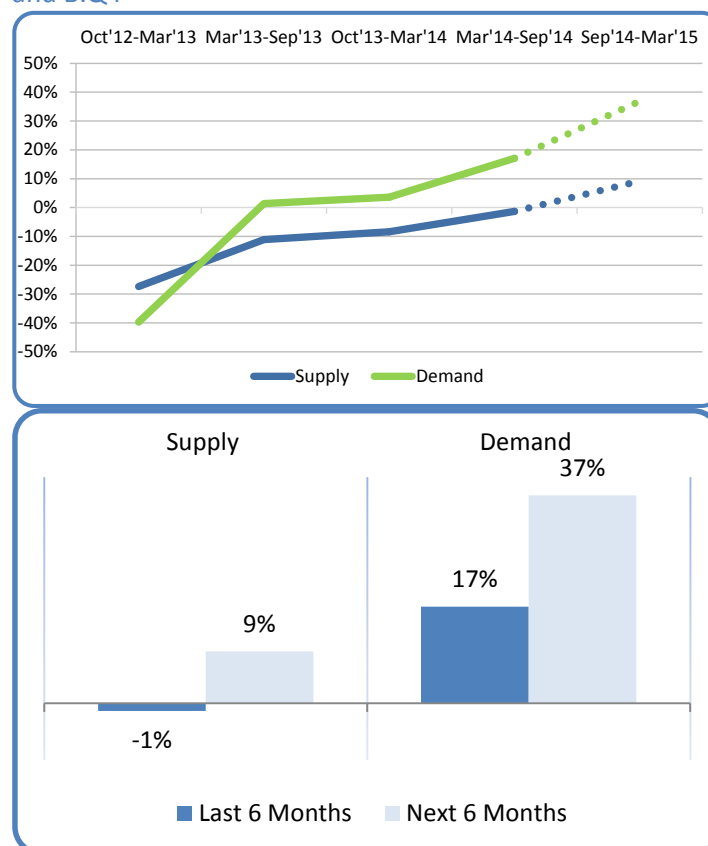


## 2.2 Local banks/subsidiaries

1. CESEE subsidiaries/local banks report an increase in demand for credit and a stabilisation in supply conditions, albeit at low levels. Both demand and supply are expected to improve in the next six months. In

the last six months, demand for loans and credit lines has been improving (Figure 5). This was the first significant improvement since the inception of the survey. This is mostly accounted for by debt restructuring and working capital requirements (see Annex A.1). On the other hand, demand for credit to finance investment has

**Figure 5: Total supply and demand, past and expected development – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



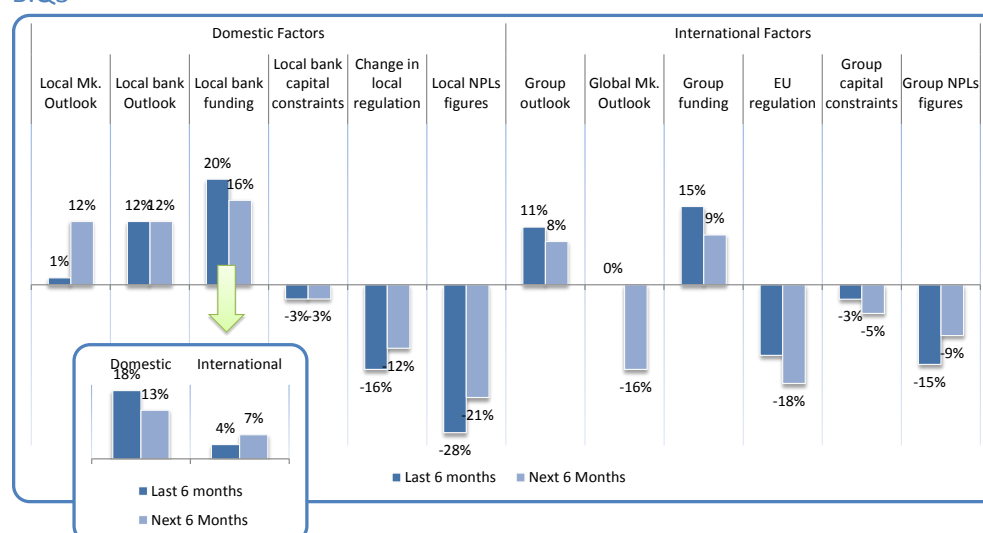
Source: EIB – CESEE Bank Lending Survey.

been very weak. Looking ahead, demand is expected to continue to increase. However, it should be noted that expectations have been overly optimistic compared to the actual outcomes over the recent past. Therefore the expected improvement may be exaggerated, particularly taking into account the lacklustre macroeconomic outlook. Supply conditions stabilised at the margin, in contrast to the still clear tightening pattern observed in the March 2014 survey. Across the client spectrum, supply conditions (credit standards) continued to ease for consumer credit, but tightened further in the large corporates segment. In the period ahead, banks expect a pick-up in credit demand and the start of an easing of supply conditions. On top of debt restructuring and working capital, consumer confidence and non-housing-related expenditures are expected to make a positive contribution to demand. For the first time, credit demand from enterprises (including SMEs) is also expected to rebound significantly (see Annex A.2). Aggregate supply conditions are expected to ease, with this being primarily driven by short-

term maturities and consumer credit (see Annex A.3). Easing is also expected in the SME segment of the market. General terms and conditions for loan supply to the corporate market segment are expected to start to ease; however, collateral requirements are expected to tighten further. A cumulative index, built on the demand and supply changes reported in Figure 5, hint at a widening gap between demand and supply situations, although growing optimism on the demand side, if confirmed, could be frustrated by the expected slow improvement of conditions on the supply side.

2. **NPLs and the regulatory environment, at both the domestic and group levels, continue to affect supply conditions negatively.** The cause of tightened supply (Figure 6) seems to be a few international and domestic factors, with the number of such factors mentioned decreasing over time. As in the previous surveys, access to domestic funding does not appear to be a constraining factor, and also international funding has started to ease. A smaller set of international factors plays a constraining role compared to the March 2014 survey. Group capital constraints, EU regulation and group-wide NPL levels are all mentioned as having a negative effect on credit conditions. At the domestic level, changes in local regulation and NPLs at the subsidiary level are the main constraining factors. Local bank capital constraints are still

**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**

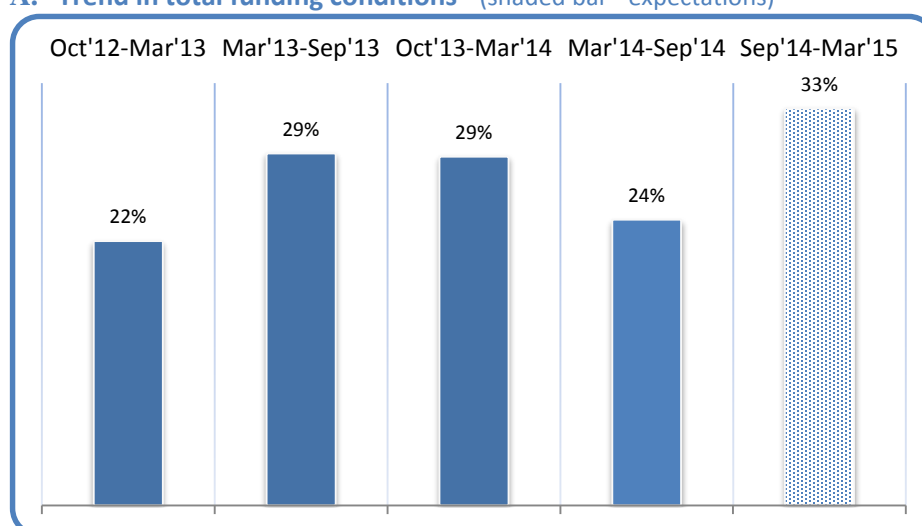


Source: EIB – CESEE Bank Lending Survey.

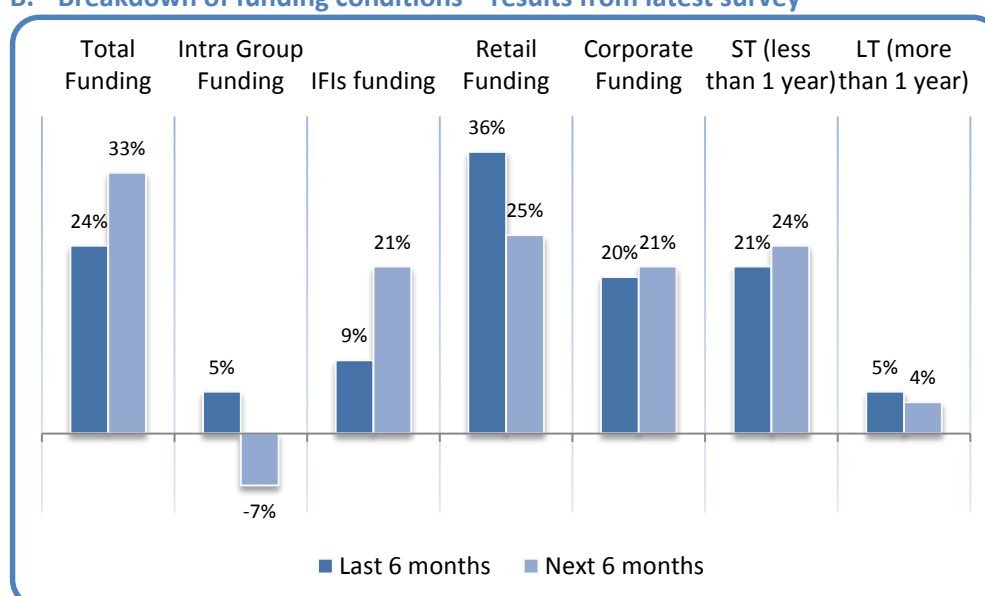
a limiting factor, but less so than in the previous survey. On the other hand, the local market and bank outlook, as well as funding, are easing factors.

**Figure 7. Access to funding by CESEE subsidiaries** – (net percentage; positive figures refer to an easing of access to funding) – see question B.Q7

**A. Trend in total funding conditions - (shaded bar - expectations)**



**B. Breakdown of funding conditions – results from latest survey**



Source: EIB – CESEE Bank Lending Survey.

- 3. CESEE funding conditions are fairly favourable, with access to funding being positive across all sources.** Easy access to retail and corporate deposits and increased funding from IFIs support a positive outlook (Figure 7). In addition, CESEE subsidiaries report easier access to short-term funding as making positive contributions to overall funding activities. For the second time in a row, longer-term funding conditions have slightly improved. This may allow a reduction of maturity mismatches and help boost banks' long-term funding ratios. Subsidiaries indicate that access to international and intra-group funding had a mild upturn over the past six months, thus breaking the continuous downward trend. However, banks also expected a decrease in intra-group funding over the next six months. This is also reported at the

group level, where a preponderance of parent banks also expect a reduced lending exposure to the region (see Figure 2).

4. **Credit quality continued to deteriorate, although expectations provide some signs of stabilisation ahead.** According to the survey results, the peak in NPL ratios has not yet been reached (Figure 6), although the speed of deterioration has been slower over the past six months than in the March 2014 survey. In absolute terms, less than 30 percent of banks continue to expect an increase in NPLs over the next six months (down from 40 percent in the March 2014 survey). The share of subsidiaries indicating an increase in their NPL ratios fell slightly below 50 percent over the past six months. All in all, the share of subsidiaries indicating either a stabilisation or decline in their NPL ratios increased. NPL ratios for the corporate segment are expected to start to decrease, whilst NPLs in the retail segment are still expected to increase marginally, providing more positive signals than in March.

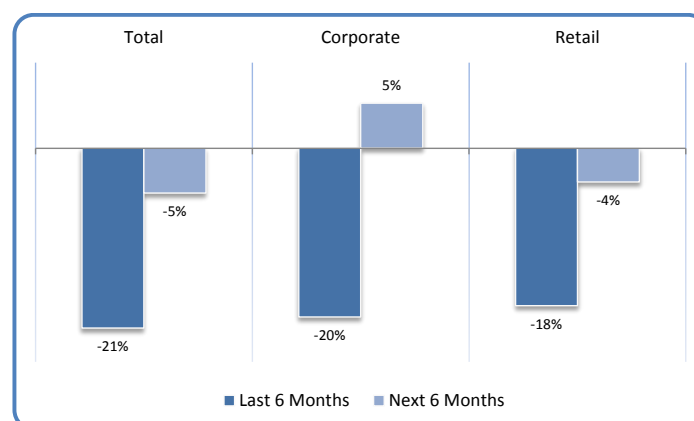
5. **Overall the survey highlights both an amelioration in regional lending conditions and some common risks.** Aggregate credit demand conditions

are turning positive, although some market segments remain very subdued, primarily those related to investment finance. Supply conditions are on an improving trend; however, tightened collateral

requirements seem to limit financing

possibilities in many cases. In addition, NPLs remain a drag on the supply of credit, and NPL ratios are expected to continue to increase over the next six months. Initiatives to tackle this problem therefore remain a high priority on the policy agenda. The resolution of NPLs is key to engineering a resumption of the healthy flow of credit into the economy to match the timid recovery materialising on the demand side of the market.

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.

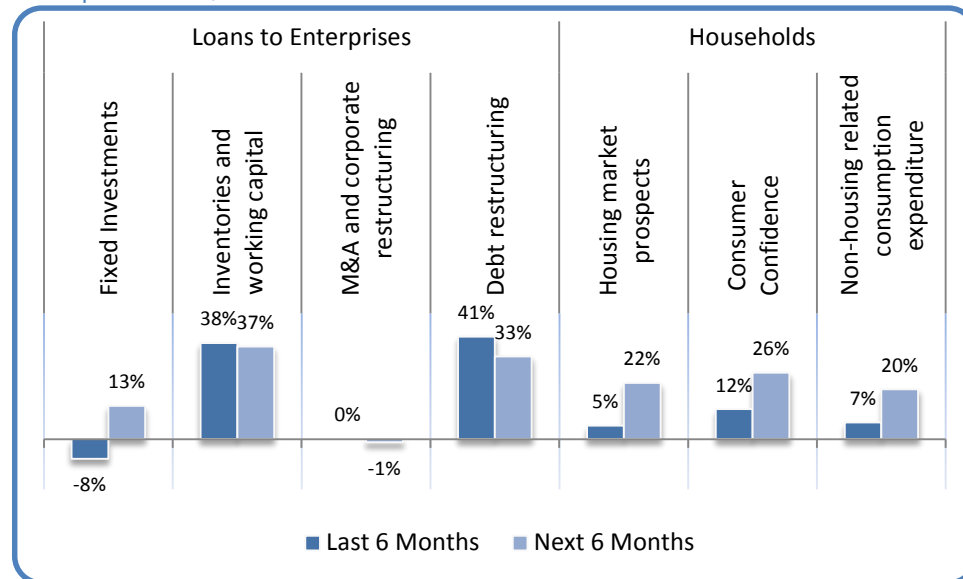
### 3. Annex

#### 3.1 Supporting charts

##### A.1 Factors affecting demand for credit

(net percentages; positive values indicate a positive contribution to demand conditions)

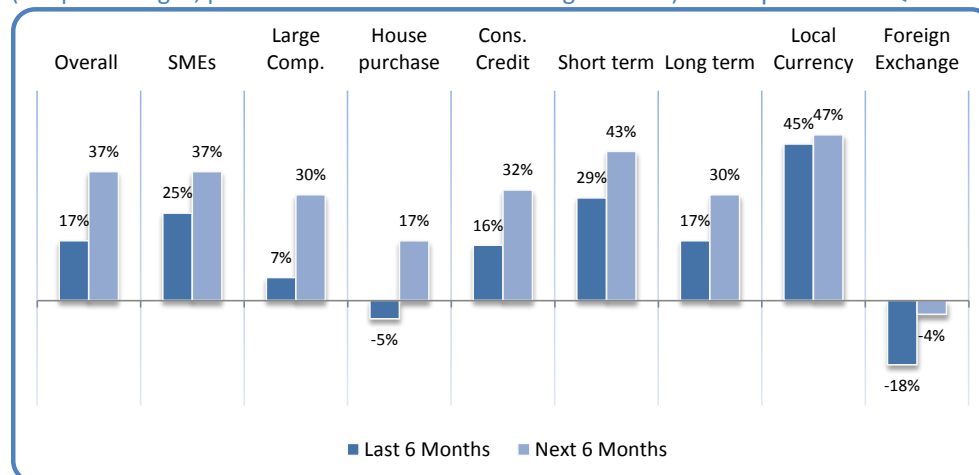
– see question B.Q5



Source: EIB – CESEE Bank Lending Survey.

##### A.2 Demand for loans or credit lines – client breakdown

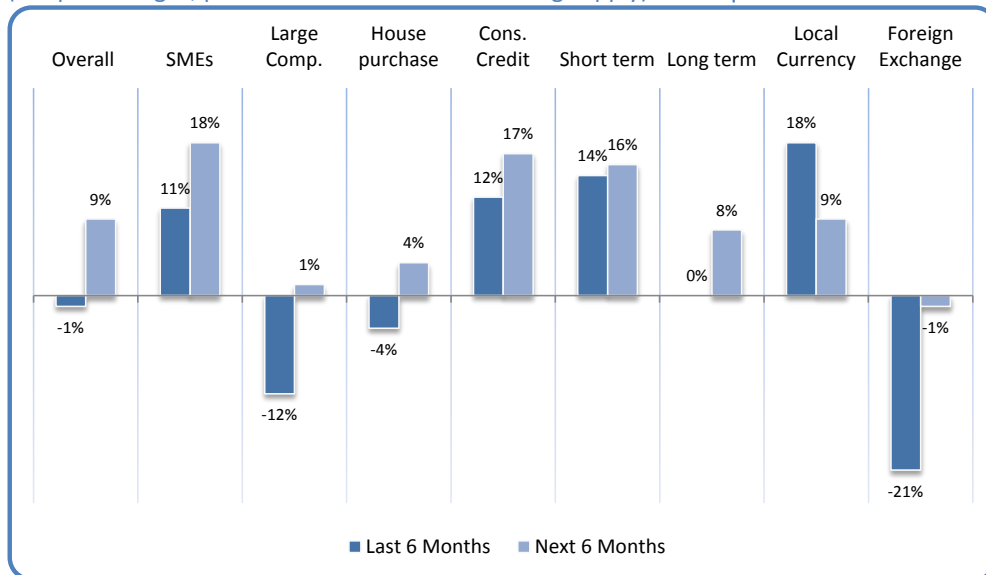
(net percentages; positive values indicate increasing demand) – see question B.Q4



Source: EIB – CESEE Bank Lending Survey.

**A.3 Credit supply (credit standards) – client breakdown**

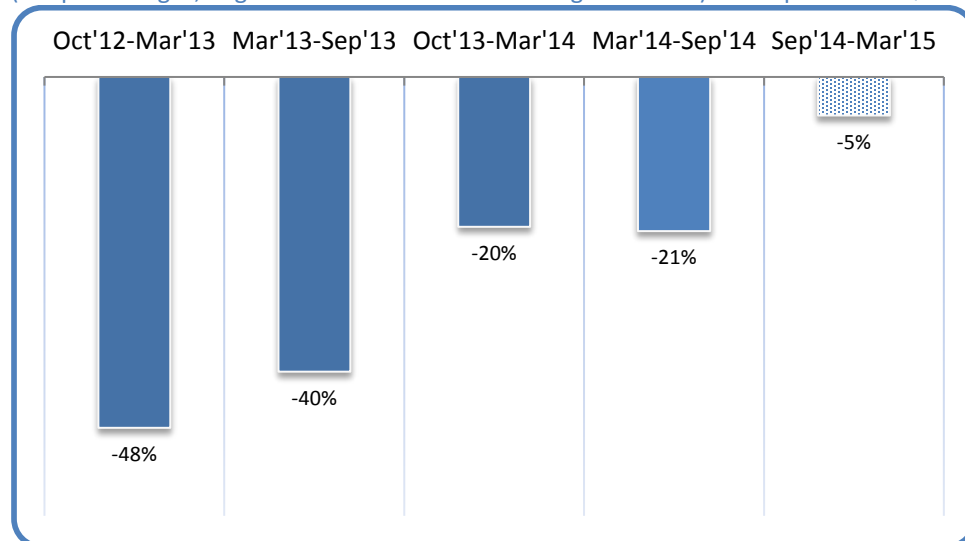
(net percentages; positive values indicate an easing supply) – see question B.Q1



Source: EIB – CESEE Bank Lending Survey.

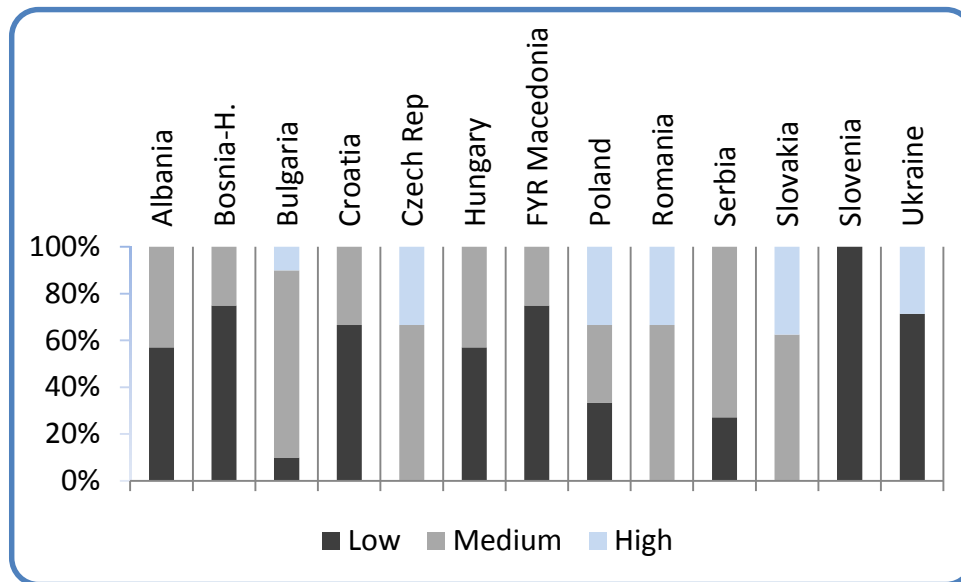
**A.4 NPL trend line**

(net percentages; negative values indicate increasing NPL ratios) – see question B.Q6



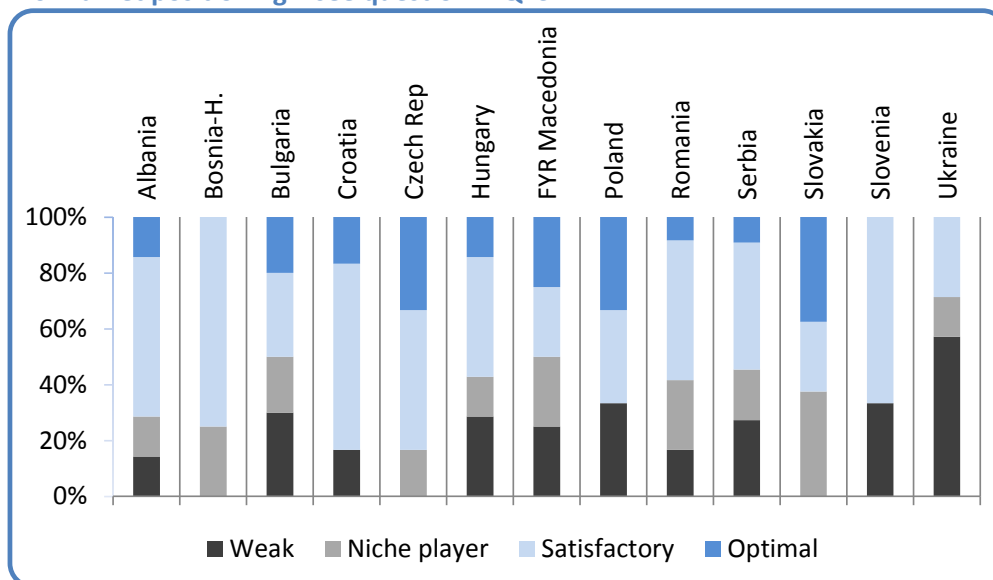
Source: EIB – CESEE Bank Lending Survey.

## A.5 Market potential – see question A.Q13



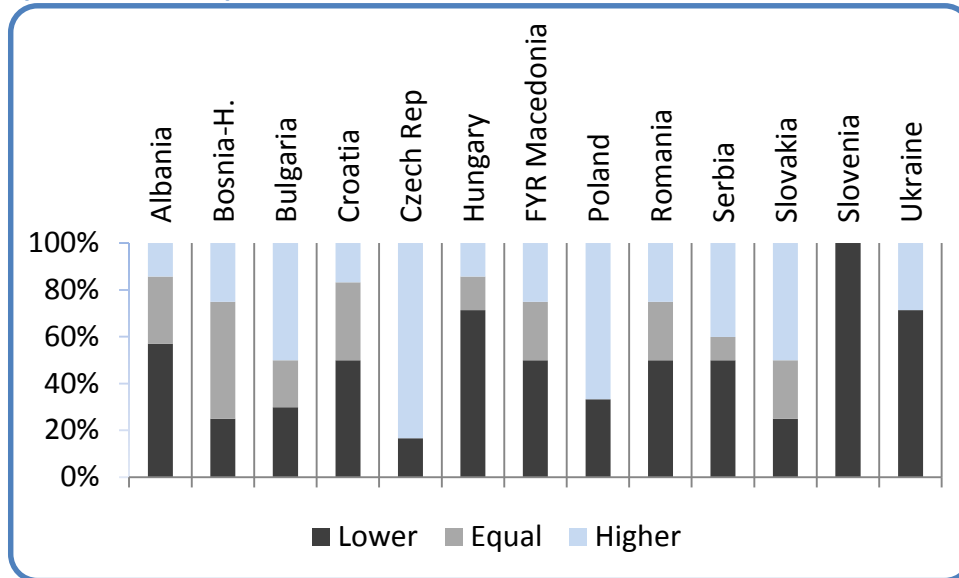
Source: EIB – CESEE Bank Lending Survey.

## A.6 Market positioning – see question A.Q13



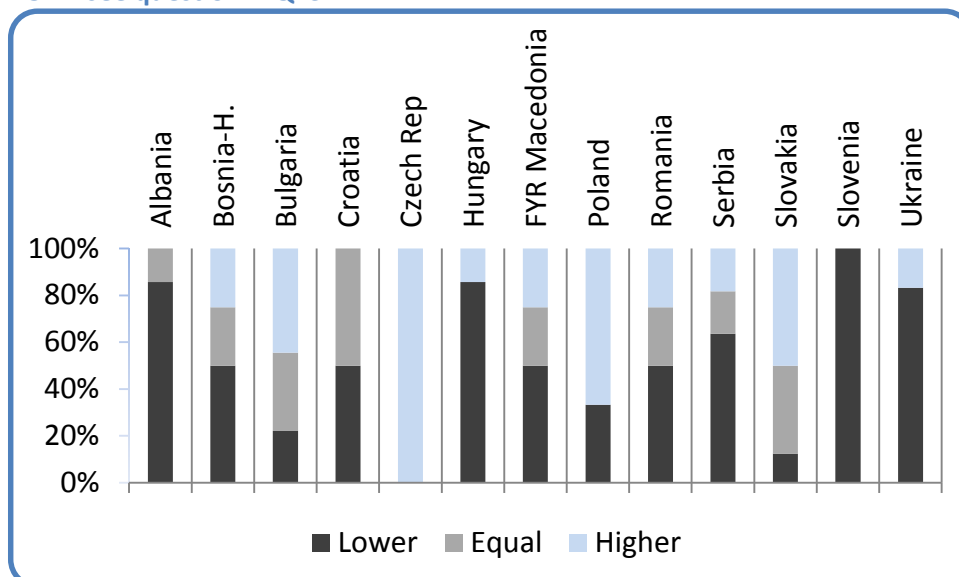
Source: EIB – CESEE Bank Lending Survey.

### A.7 Return on assets (adjusted for cost of risk) compared to overall group operations – see question A.Q13



Source: EIB – CESEE Bank Lending Survey.

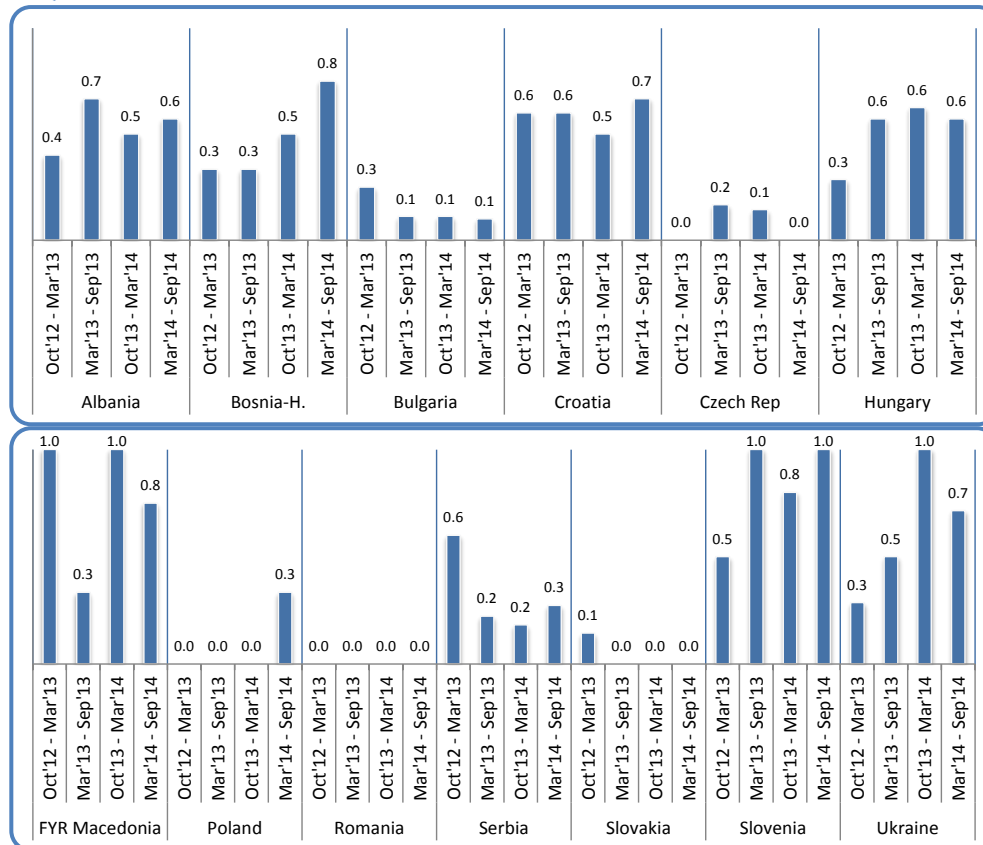
### A.8 Return on equity (adjusted for cost of equity) compared to overall group ROE – see question A.Q13



Source: EIB – CESEE Bank Lending Survey.

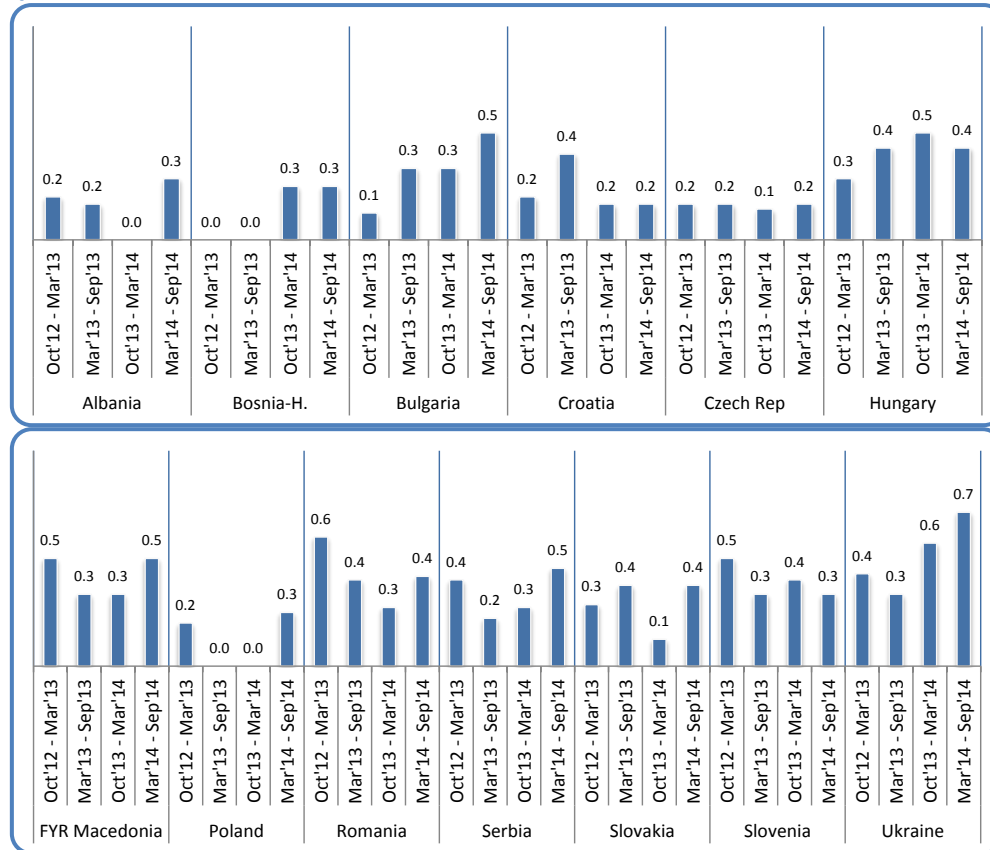


### A.9 Share (%) of parent banks indicating a “low” market potential – see question A.Q13



Source: EIB – CESEE Bank Lending Survey.

### A.10 Share (%) of parent banks indicating a “weak/niche” positioning – see question A.Q13



Source: EIB – CESEE Bank Lending Survey.

# Albania

## 1. Key statistics<sup>1</sup>

- Number of banks/subsidiaries participating in the survey: five
- Approximate share of assets covered (as proportion of total assets): 54 percent (Q2 2014)
- Current level of NPLs as proportion of total loans: 24.1 percent (Q2 2014)
- Latest credit growth (yoy): -1.8 percent (Q2 2014)
- Loan-to-deposit ratio: roughly 60 percent
- CAR: 18 percent (Q2 2014)

## 2. Key messages – *Economic recovery at risk, with NPLs and uncertainty being the key concerns.*

### International groups' views:

- **Group strategies:** International banks operating in Albania continue to engage in sales of assets. The deleveraging process has slowed down for these banks, but around a third of the groups indicate that they intend to reduce their group-wide loan-to-deposit ratios further.
- **Group assessment of positioning and market potential:** Groups continue to view Albania as a country with a relatively low market potential. Returns on equity and assets are lower than the CESEE average; however, there are signs of improvement in operational profitability.

### Subsidiaries' views:

- **Subsidiaries** operating in Albania report that **despite the easing demand conditions the supply conditions remain unchanged.**
- **Credit supply** has been stable on average. The conditions have eased for consumer non-mortgage credit and have tightened for the corporate sector, including SMEs and large enterprises. Banks are focusing more on short-term contracts, with no change in the long-term financing.
- **Demand for loans** has been increasing in consumer credit and decreasing in mortgages. The demand in the corporate sector is expected to pick up in the next months, albeit at a slower rate than the CESEE average.
- **Access to funding** has been easing in the context of negative lending growth. Most of the funding comes from central bank and local currency sources and is mostly short term. Access to long-term funding has been deteriorating.
- **NPL figures** have deteriorated in the last six months, but the rate of deterioration has slowed. Despite an improvement in economic conditions, credit quality is expected to deteriorate further in both corporate and retail sectors and thus remains the key concern for banks operating in Albania.

<sup>1</sup> Sources: The Bank of Albania and European Commission.

### 3. Relevant macroeconomic and banking conditions<sup>2</sup>

- **Growth:** Despite growth of 1.7 percent in the first three months of 2014, the Albanian economy contracted in the second quarter by 0.7 percent year on year. The main sources of contraction were net exports and industrial production. There are signs of a positive rebound in domestic private consumption, however.
- **Unemployment:** In the second quarter of 2014 the unemployment rate reached 17.7 percent. The proportion of employed was estimated at 48.5 percent. The labour market constantly suffers from the high prevalence of long-term unemployment and large gender differences in labour force participation.
- **Inflation:** Headline inflation was estimated at 1.9 percent in the first quarter and 1.6 percent in the second quarter of 2014. Prices continue on a decreasing trend from the previous year. This has allowed the Bank of Albania to cut the key interest rate to a historic low of 2.5 percent.
- **External and public sector balance:** In the second quarter of 2014, the current account deficit increased by almost 21 percent year-on-year, as a result of higher import figures. As of June 2014, the current account deficit rose to 11.6 percent of GDP. Public debt continued to rise in the last quarter of 2013, and stood at 70.5 percent of GDP, compared to 62.3 percent a year earlier. The fiscal deficit reached 2.2 percent of GDP in the first eight months of 2014, compared with a 6.5 percent target for the whole of 2014.
- **Banking sector:** Despite the cuts in key interest rates, the downward trend in lending continued in the first two quarters of 2014. However, in July 2014 the stock of loans grew by 0.5 percent year-on-year, signalling the first increase in twelve months. The level of capitalisation for the entire banking sector (CAR 18 percent Q2 2014) exceeds the required minimum. The loan-to-deposit ratio stood at roughly 60 percent in 2011. NPLs levelled off in the first two quarters of 2014 and reached 24.1 percent of all loans. This has brought the upward trend in NPLs over the last five years to a standstill; nevertheless, the stock of NPLs is still the major constraint on Albanian banks. Growth in local deposits has been fairly robust over the last three years, partially offsetting the reduction of cross-border assets allocated to Albania.
- **Rating:** Albania is currently rated by Moody's (B1, stable) and S&P (B, stable).

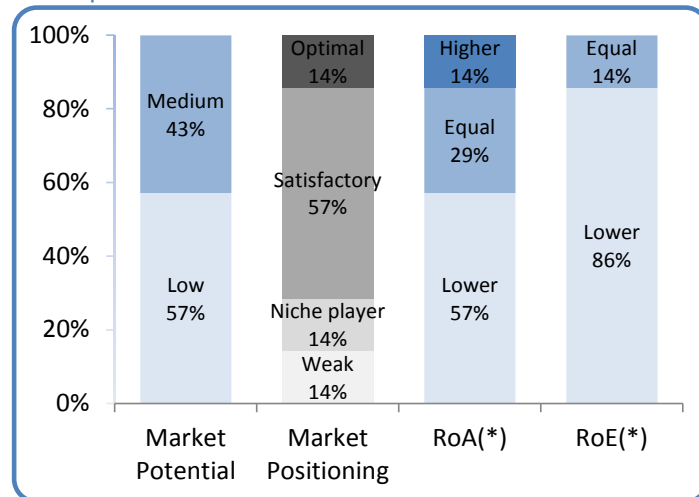
<sup>2</sup> Sources for the macroeconomic data: European Commission and Institute of Statistics (Albania). Sources for the banking data: European Commission and Bank of Albania.

## 4. Results of the Bank Lending Survey:

### 4.1 Parent banks<sup>3</sup>

1. The majority of parent banks operating in Albania report that their leverage has stabilised, with around a third of them indicating the need to decrease their group-wide loan-to-deposit ratios further. More than 80 percent of the parent banks indicate that they have engaged in sales of assets, compared to roughly 70 percent for the whole set of groups included in the survey. Compared to the March 2014 survey, a larger number of groups are willing to raise additional market capital or carry out strategic restructuring. None of the groups expect capital contributions from the state.

**Figure 1. Market potential and positioning, ROE and ROA**  
– see question A.Q13



Source: EIB – CESEE Bank Lending Survey.

(\*) Return on assets (adjusted for cost of risk) compared to overall group operations; return on equity (adjusted for cost of equity) compared to overall group ROE.

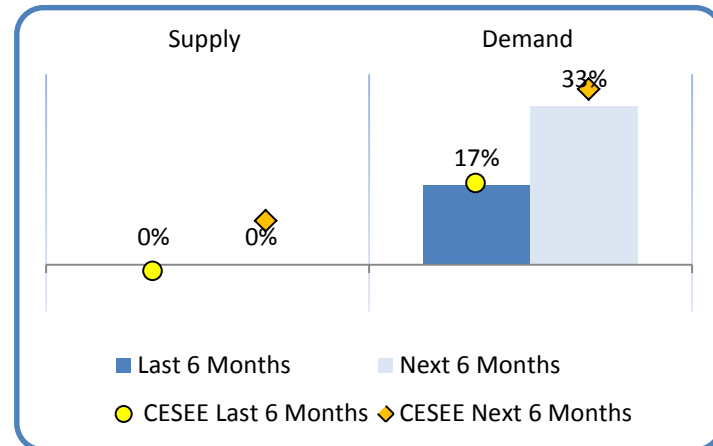
2. Albania is perceived by the parent banks as a market with medium to low potential. In addition, the majority of them have begun to view their market positioning as sub-optimal (Figure 1). Groups operating in Albania are generally more selective in their local strategies, however, and there are some signs of possible longer-term improvement. The returns on assets proved to be better for some parent banks operating in Albania, compared to overall group operations, and a small proportion of groups indicated their willingness to expand Albanian activities. About 50 percent of all the groups report that they intend to reduce their operations in Albania selectively; however, this proportion is less than in the March 2014 survey.

<sup>3</sup> In this subsection results refer to the views of parent banks. Results on market positioning and potential refer to questions addressing behaviours within a specific market, whilst the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents' views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a specific country.

## 4.2 Local banks/subsidiaries

- Against the background of negative credit growth in the first quarter of 2014, credit supply conditions in Albania remained unchanged. During the last six months the banks have not eased or tightened their credit standards, nor do they expect the situation to change in the coming six months. On the demand side, the Albanian banks have seen an improvement. Demand conditions have eased and they are expected to rebound more markedly in the coming months. The magnitude of the upswing is somewhat smaller than in the CESEE region as a whole (Figure 2).

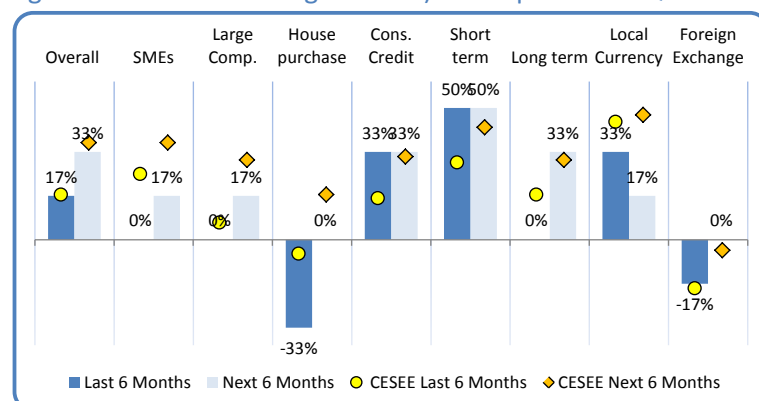
**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



Source: EIB – CESEE Bank Lending Survey.

- Against the background of the pick-up in economic activity and domestic consumption in the first half of 2014, the demand for loan applications has been improving and this trend is expected to continue over the next six months. The magnitude of the improvement is smaller than in the CESEE region as a whole (Figure 3). Demand in the next six months is expected to come mostly from the corporate side and consumer credit: this is generally in line with the credit dynamics of the region, but is smaller in magnitude as far as firms are concerned.

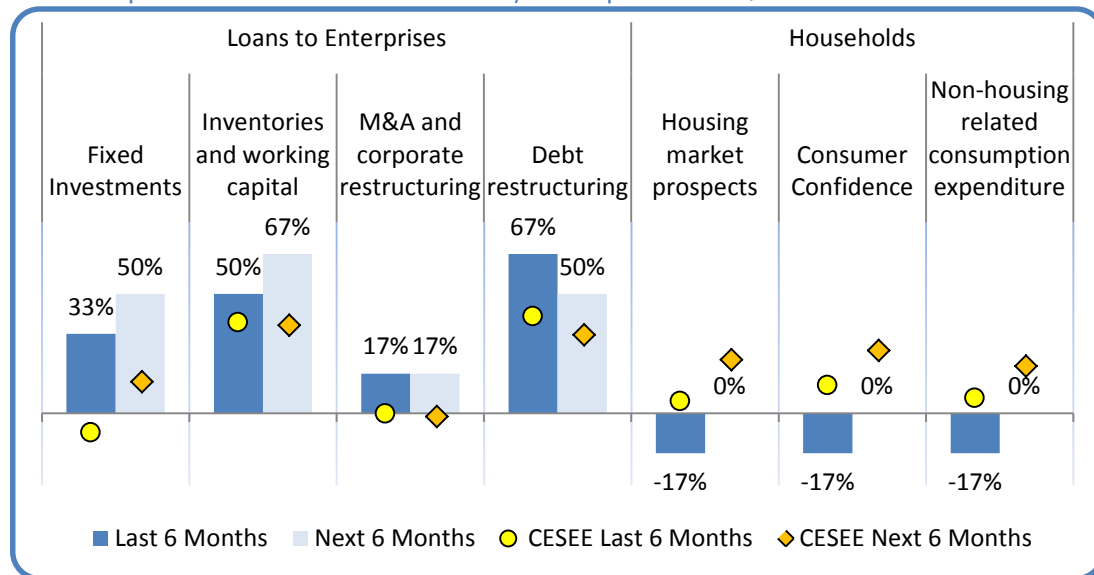
**Figure 3. Demand components - (net percentages; positive figures refer to increasing demand) – see question B.Q4**



Source: EIB – CESEE Bank Lending Survey.

- There has been a major improvement in demand conditions for the corporate sector in the last six months (Figure 4). This is expected to continue in the coming months. On the consumer side, demand has been deteriorating and is expected to remain stable in the next months.

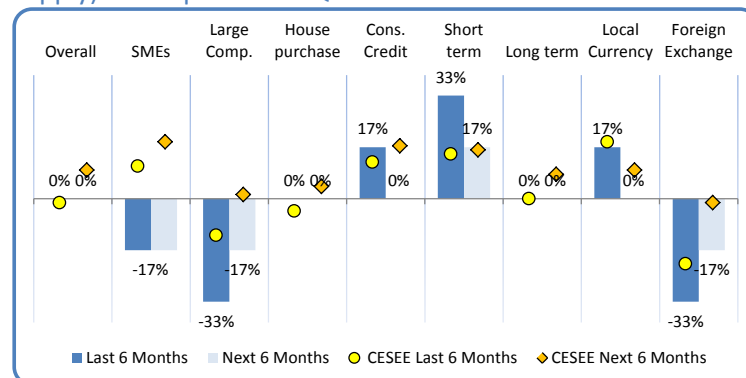
**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**



Source: EIB – CESEE Bank Lending Survey.

4. The overall supply components remained stable and are expected neither to improve nor deteriorate in the coming months. With a high share of NPLs, the Albanian banks increased the credit line requirements for the corporate

**Figure 5. Supply components – credit standards (net percentages; positive figures refer to a positive contribution to supply) – see question B.Q1**

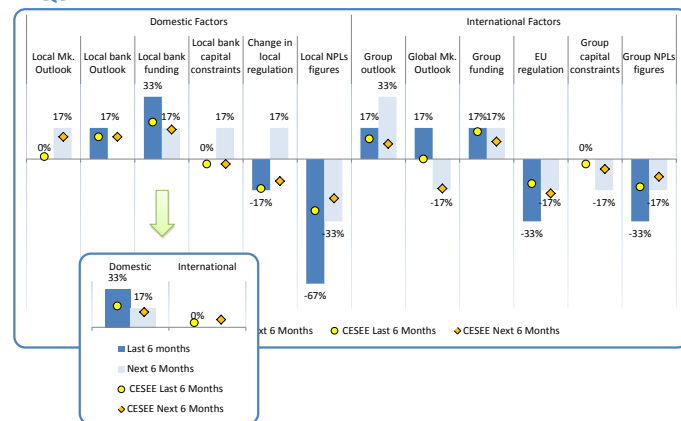


Source: EIB – CESEE Bank Lending Survey.

sector. Households benefited from alleviated supply conditions for non-mortgage loans. Banks have mostly targeted short-term lending and have refrained from foreign exchange loans. This is expected to continue over the coming six months. Supply conditions in the long-term segment have been stable and are expected to remain unchanged.

5. Both international and domestic factors affected credit supply conditions, being in line with the results from the March 2014 survey. The high levels of NPLs and changes in local regulations have been the biggest brakes on the domestic market (Figure 6). In the next six months both factors are expected to ease. All other domestic factors contributed positively to credit supply and are expected to continue to do so in the coming months. Similarly, on the international side group-wide NPL figures and changes in the EU regulations dampened supply conditions in Albania. In addition, group-wide capital requirements and a worsening global market outlook are expected to be important limiting factors in the near future.
6. Although the demand from SMEs is expected to rebound in the next six months, the restrained supply conditions are expected to influence credit for SMEs in the opposite direction. At the same time, loan size limits are expected to be increased for SMEs and decreased for the larger enterprises. Credit conditions are expected to ease for short-term loans.

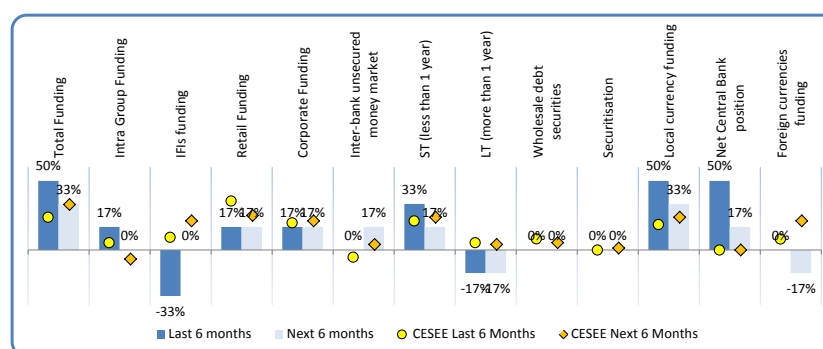
**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**



Source: EIB – CESEE Bank Lending Survey.

7. With the current negative credit growth, subsidiaries are not suffering from funding problems (Figure 7). The importance of central bank funding has increased as a result of recent monetary stimulus, and is mostly short-term. On the other hand, IFI and long-term financing have been limited. Of all sources of funding, retail and foreign currency funding have decreased significantly and are now below CESEE averages.

**Figure 7: Access to funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**

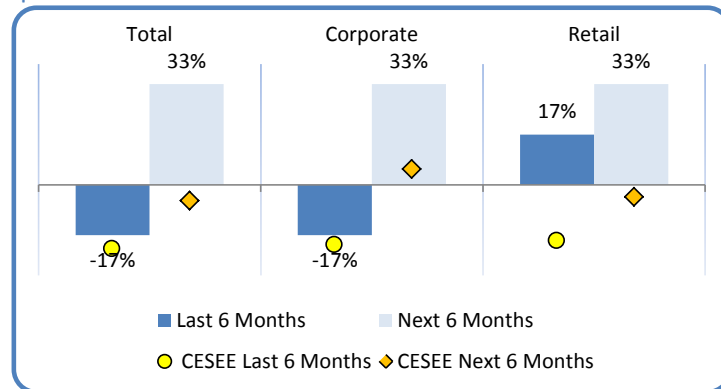


Source: EIB – CESEE Bank Lending Survey.



8. NPL figures have continued to deteriorate over the last six months (Figure 8), albeit at a slower rate than reported in the March 2014 survey and compared to the CESEE average. Although the recent aggregate figures also indicate that the proportion of NPLs stabilized at 24

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.

percent of gross loans, banks expect NPL figures to increase in the coming six months for both the corporate and retail segments. NPLs therefore remain a key issue for the Albanian banking sector.



# Bosnia-Herzegovina

## 1. Key statistics<sup>1</sup>

- Number of banks/subsidiaries participating in the survey: four
- Approximate share of assets covered (as proportion of total assets): 50 percent
- Current level of NPLs as proportion of total loans: 15.5 percent (Q2 2014)
- Latest credit growth (yoy): 3.7 percent (Q2 2014)
- Loan-to-deposit ratio: 111.8 percent in Q2 2014
- CAR: 17.3 percent (Q2 2014)

## 2. Key messages – *Deterioration in bank balance sheet ameliorated*

### International groups' views:

- **Group strategies:** Compared with the universe of groups active in the CESEE region, those active in Bosnia-Herzegovina signal a greater need to raise further capital in the market. However, they see less need for strategic restructuring, although they are equally likely to sell assets. The process of deleveraging seems to have stabilised for these groups and operational profitability is expected to increase.
- **Group assessment of positioning and market potential:** Groups operating in Bosnia-Herzegovina view it as a country with a relatively low market potential. Operational profitability, in terms of RoA and RoE, has slightly deteriorated compared with the outcomes from the last survey; nevertheless none of the groups expects to reduce its operations in Bosnia-Herzegovina.

### Subsidiaries'/local banks' views:

- Credit growth remains positive despite **unchanged supply conditions and tightened demand** for credit. Macroeconomic turbulence is expected to be temporary and credit conditions are predicted to ease on both the supply and demand sides.
- **Credit supply** has remained unchanged over the last six months. It is expected to rise in all market segments in the near future. **The largest positive effects are to be found in consumer credit for short and long-term lending.**
- **Demand for loans** has been deteriorating over the last six months. Nevertheless, it is expected to ease in the near future in all segments. The largest improvement is to be observed in lending to large companies and in the short-term market.
- **Access to funding:** Subsidiaries in Bosnia-Herzegovina report that their access to funding has generally improved, but remains, and is expected to remain, below the CESEE average.
- **NPL figures** have improved over the last six months, mostly in the retail sector. They outperformed the expectations from the last survey.

<sup>1</sup> Sources: European Commission, Central Bank of Bosnia and Herzegovina, and IMF.

### 3. Relevant macroeconomic and banking conditions<sup>2</sup>

- **Growth:** The economy grew in 2013 and this continued into 2014. In the first quarter of 2014 growth was estimated at 2.7 percent. Heavy spring floods have adversely affected output since then.
- **Unemployment:** Unemployment is a major problem for the Bosnian economy, amounting to over 43.8 percent in July 2014. Around two thirds of unemployment is long-term. The youth unemployment rate is close to 60 percent.
- **Inflation:** Against a background of weak domestic consumption, the deflationary trend that started in August 2013 continued in the first two quarters of 2014, with the price index showing 1 percent deflation in August.
- **External and public sector balance:** In the four quarters to June 2014 the current account deficit increased to 6.9 percent of GDP, reversing the trend of the previous year. The budget showed a slight surplus in the second quarter of 2014, reaching 0.3 percent of the full-year GDP. Public debt reached 44.5 percent of GDP in 2013.
- **Banking sector:** The profitability of the banking sector decreased slightly in the first half of 2014. In the second quarter of 2014, the return-on-assets and return-on-equity ratios were 0.45 percent and 3.5 percent, respectively. Banks remain well capitalised, with the capital adequacy ratio at 17.3 percent. The proportion of NPLs deteriorated in the first two quarters of 2014 to reach 15.5 percent of total loans and is expected to further increase in the aftermath of the spring floods. The loan-to-deposit ratio has decreased to 111.8 percent, following accelerated deposit growth. Average credit growth was modest at roughly 3.7 percent in the second quarter of 2014. Retail lending markedly rebounded to 6.5 percent in the second quarter of 2014.
- **Rating:** Bosnia is currently rated by Moody's (B3, stable) and S&P (B, stable).

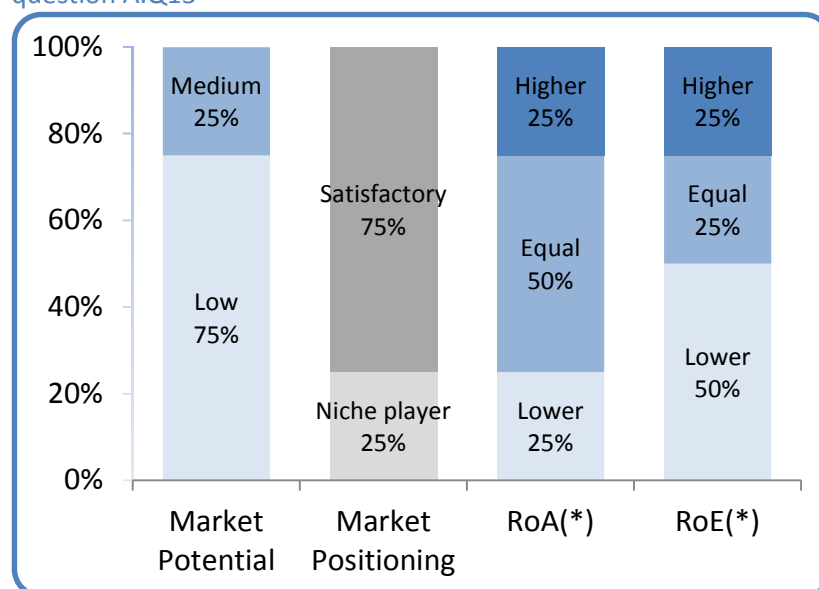
<sup>2</sup> Sources for the macroeconomic data: European Commission and Central Bank of Bosnia and Herzegovina. Sources for the banking data: European Commission and CBBH data.

## 4. Results of the Bank Lending Survey:

### 4.1 Parent banks<sup>3</sup>

1. All the parent banks report that their deleveraging process has stabilised, confirming the results from the March 2014 survey. More of the groups active in Bosnia-Herzegovina have signalled that they plan to raise additional capital on the market in the coming months than groups in the region as a whole. Nevertheless, the majority of the parent banks indicate that they have engaged in sales of assets and would like to continue such activities in the next six months. A smaller share of groups signal plans to strategically restructure their operations than is the case for the region as a whole.

**Figure 1. Market potential and positioning, ROE and ROA – see question A.Q13**



Source: EIB – CESEE Bank Lending Survey.

(\*) Return on assets (adjusted for cost of risk) compared to overall group operations; return on equity (adjusted for cost of equity) compared to overall group ROE.

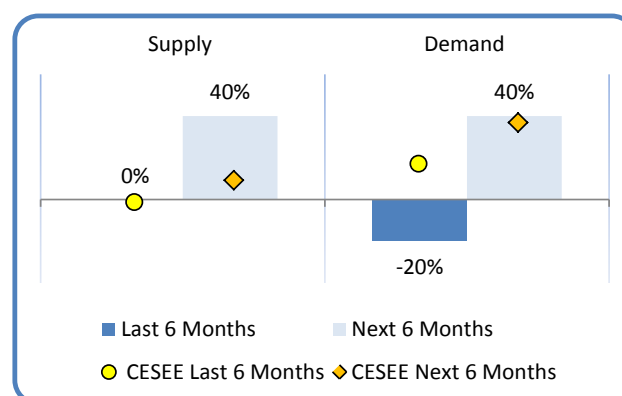
2. The majority of parent banks view Bosnia-Herzegovina as a market with a relatively low potential compared to other CESEE countries. None of the groups consider their market positioning as optimal, with the majority of parent banks describing it as satisfactory. The groups' profitability has deteriorated, compared to the March 2014 survey, bringing the RoA and RoE in Bosnia-Herzegovina for some parent banks below the CESEE averages (Figure 1). This may be a short-term effect of the spring floods, as the groups expect their profitability to increase over the next six months. Their published long-term strategies for Bosnia-Herzegovina show expansionary plans, with none of the groups intending to reduce their operations in the country.

<sup>3</sup> In this subsection results refer to the views of parent banks. Results on market positioning and potential refer to questions addressing behaviours within a specific market, whilst the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents' views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a specific country.

## 4.2 Local banks/subsidiaries

- Subsidiaries operating in Bosnia-Herzegovina report that they have experienced unchanged supply and tightened demand conditions over the last six months, which is below what was expected in the March 2014 survey. Demand conditions have weakened more than in the overall CESEE region. However, the poor performance of credit conditions is likely to be a temporary phenomenon, as both supply and demand are expected to rebound markedly in the coming six months, outperforming the CESEE averages (Figure 2).

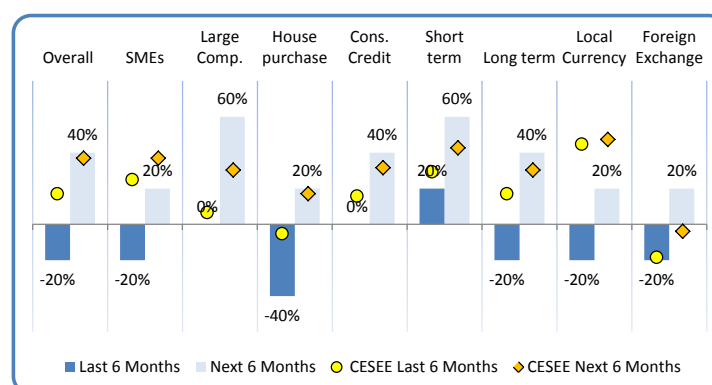
**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



Source: EIB – CESEE Bank Lending Survey.

- Subsidiaries report a tightening of demand conditions in almost all market segments. Only for short-term lending have demand conditions improved somewhat over the last six months, although they remained below the CESEE average (Figure 3). Nevertheless, demand is expected to ease in the coming months in all market segments. The largest improvement is expected in lending for large companies and in the short-term market. At the same time, an improvement is also expected in consumer credit and long-term lending.

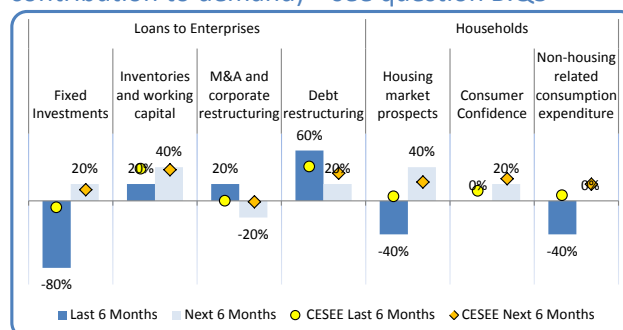
**Figure 3. Demand components – (net percentages; positive figures refer to increasing demand) – see question B.Q4**



Source: EIB – CESEE Bank Lending Survey.

3. The decline in lending for fixed investment has the biggest negative impact on corporate demand; all other demand components have made a positive contribution to corporate credit demand over the last six months, with debt restructuring being the most prominent element (Figure 4). The subsidiaries expect a limited improvement in corporate credit demand in the coming months, mostly in line with the CESEE averages. Housing market prospects together with non-housing-related consumption were the largest brakes on the consumer demand side. Banks expect a rebound in the next six months, albeit below the CESEE average.

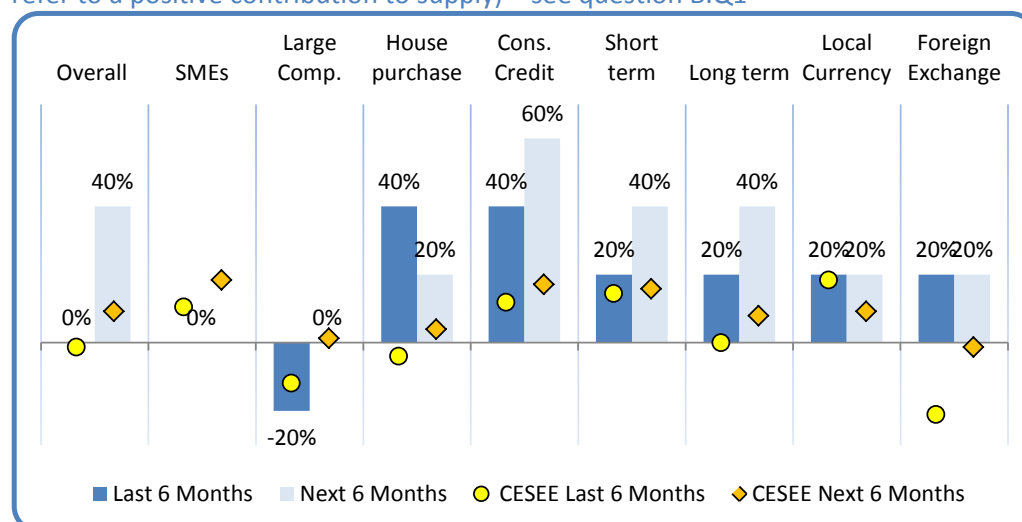
**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**



Source: EIB – CESEE Bank Lending Survey.

4. On the supply side, only the credit conditions for large companies have been

**Figure 5. Supply components – credit standards (net percentages; positive figures refer to a positive contribution to supply) – see question B.Q1**

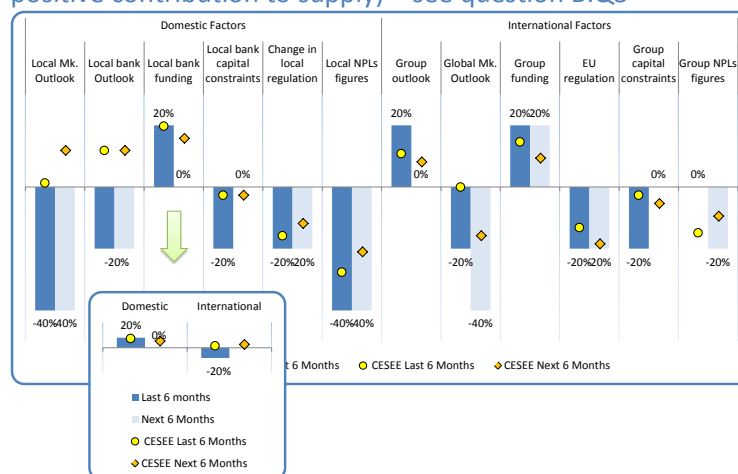


Source: EIB – CESEE Bank Lending Survey.

tightened (Figure 5). All the other supply components have been eased to a greater extent than in other CESEE countries. Supply conditions are expected to ease further in the coming six months, with consumer credit being the main driver behind the improvement. Compared with the last six months, the supply conditions for house purchases are expected to improve further. Access to funding is expected to be alleviated in both short-term and long-term markets. Similarly supply is expected to ease for both local and foreign currency loans.

5. Both domestic and international factors have affected supply conditions. Among the former, the local market outlook as well as the NPL figures were the major obstacles to credit supply. Both factors are expected to have similar negative supply effects in the coming months (Figure 6). Local bank funding has alleviated supply conditions; however this effect is predicted to disappear in the next six months. As far as international factors are concerned, the largest supply constraints come from the poor global market outlook, group-wide capital constraints and EU regulations. Those factors, together with group-wide NPL figures, are expected to have a negative impact on credit supply in Bosnia-Herzegovina in the coming months.

**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**

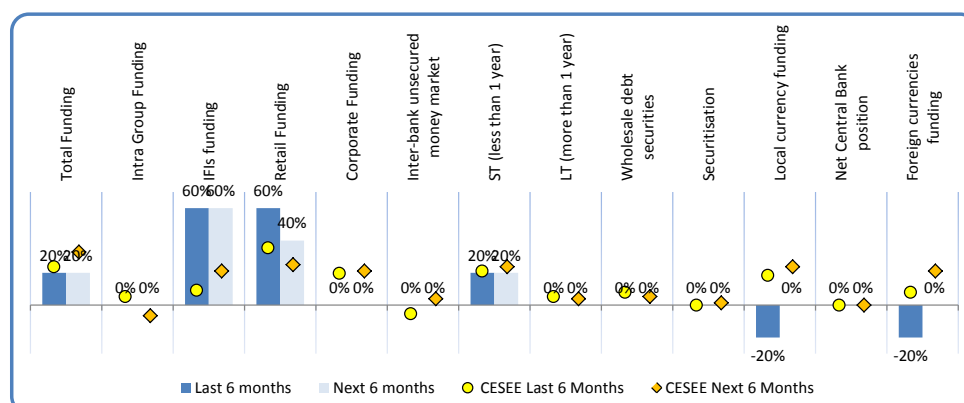


Source: EIB – CESEE Bank Lending Survey.

6. Credit supply conditions for SMEs have not changed nor are they expected to change in the coming months. Credit demand from the SME sector has been declining over the last six months but is expected to rebound in the near future. The terms and conditions for loan approvals are going to tighten for SMEs in terms of collateral requirements, average loan size and margins over the interbank interest rate.
7. Subsidiaries in Bosnia-Herzegovina report that their access to funding has generally improved but not by as much as the CESEE average. Banks have observed very positive funding contributions from IFI and retail funding over the last six months. Both sources are expected to continue to improve in the near future, particularly funding from IFIs. In terms of the maturity structure, we can observe easier access to short-term funding, in line with the regional trend (Figure 7).



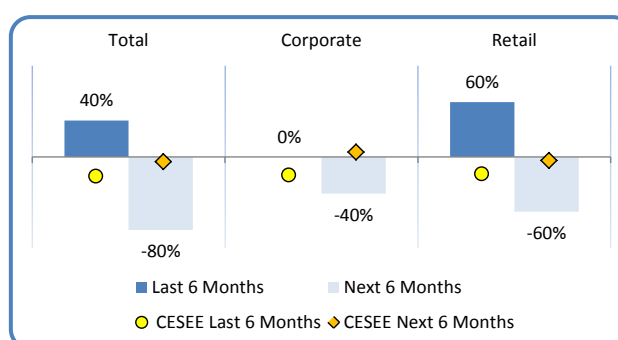
**Figure 7: Access to funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**



Source: EIB – CESEE Bank Lending Survey.

8. Although the aggregate proportion of NPLs increased in the second quarter of 2014, the subsidiaries' NPL figures have improved over the last months (Figure 8), mostly in the retail sector, outperforming expectations from the March 2014 survey. NPLs in the corporate sector remained unchanged.

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.

The situation is expected to deteriorate in the coming six months, with banks expecting a substantial deterioration in both sectors.



# Bulgaria

## 1. Key statistics<sup>1</sup>

- Number of banks/subsidiaries participating in the survey: nine
- Approximate share of assets covered (as proportion of total assets): 62 percent
- Current level of NPLs as proportion of total loans: 16.4 percent
- Latest credit growth (2014 Q2 relative to 2013 Q2): 2.1 percent
- Loan-to-deposit ratio: 89.1 percent
- CAR: 21.17 percent (Q2 2014)<sup>2</sup>

## 2. Key messages – *Continued decline in demand for investment, spillover effects of June-2014 large deposit withdrawals minimal.*

### International groups' views:

- **Group strategies:** The restructuring efforts of parent banks operating in Bulgaria have been in line with the full sample of parents included in the survey.
- **Group assessment of positioning and market potential:** Divergence of views about the market outlook in Bulgaria appears to be more pronounced than the regional average. There is a substantial improvement in groups' assessments of subsidiaries' profitability, with nearly half of respondents seeing profitability above their group's average.

### Subsidiaries'/local banks' views:

- **Credit supply** conditions have remained broadly stable and are expected to ease in the near future due to both domestic and international factors. As in the previous survey round, local bank and group NPLs are seen as major constraints on supply conditions. Over the next six months EU regulation and group NPLs are expected to be a significant constraint on credit supply.
- **Credit demand** fell significantly. By institutional sector, the largest declines came from SMEs and housing loans. In the next six months, both corporates and households are expected to increase their demand for loans. Loans for fixed investment have been most sluggish.
- **Access to funding** has improved over the past six months due to strong domestic retail and corporate funding and is expected to improve further, despite the negative impact of intra-group funding.
- **NPL figures** were reported to have deteriorated over the past six months but are expected to improve slightly in the near future.

<sup>1</sup> Sources: Bulgarian National Bank, Unicredit/Bank Austria, IMF and Bankscope.

<sup>2</sup> Does not include Corporate Commercial Bank group data.

### 3. Relevant macroeconomic and banking conditions<sup>3</sup>

- **Output:** GDP growth accelerated to 1.6 percent in 2014 Q2 relative to 2013 Q2. Both domestic demand and net exports contributed to this increase. Growth is projected to strengthen to 1.7 percent in 2014 and 2 percent in 2015, as domestic demand recovers and complements the positive contribution of net exports.
- **Unemployment:** The unemployment rate in Bulgaria appears to have peaked at around 13 percent in 2013, and employment rates stabilised and started to increase in the first half of 2014. The labour market is expected to stabilise further in 2014 but to remain generally weak, with the unemployment rate projected to decline to 12.5 percent in 2015.
- **Inflation:** Consumer prices, as measured by HICP, have been declining with only a few interruptions for the past 18 months. In August 2014 the level of HICP was 3 percentage points below its level in March 2013, which amounts to an average annual deflation of 1.6 percent. HICP is expected to start increasing again moderately in 2015.
- **External and public sector balance:** General government debt stood at 18.9 percent of GDP at the end of 2013 and ranks as the second-lowest in the EU. It is projected, however, to increase to about 24 percent by the end of 2014, as the general government deficit is expected to exceed 3 percent in 2014. The current account balance turned positive in 2013 (2 percent) and continued to grow in the first half of 2014. It is expected to decline gradually to zero by the end of 2015.
- **Banking sector:** Return on equity at the end of Q1 2014 stood at 8.3 percent. The profitability of Bulgarian banks has been stymied by the decreasing share of loans at the expense of a rising share of lower-interest-bearing assets, thus reducing the margin between funding costs and interest-based income. A high ratio of non-performing loans (about 16.5 percent) still imposes large, albeit declining costs on the banking system. NPLs are well provisioned and the regulator estimates that the banking system could absorb even higher NPL ratios without major negative consequences for the system as a whole. Putting Corporate Commercial Bank and its local subsidiary, Victoria Bank, into receivership has not caused negative spillovers in the banking system, as withdrawn deposits from the three most affected banks in June 2014 have returned to the banking system. The other bank that suffered mass withdrawals, First Investment Bank, was stabilised with liquidity support from the government that will be renewed later this year. The final resolution of this crisis is nevertheless an important test for Bulgarian authorities.
- **Rating:** Bulgaria is rated BBB- by Fitch, Baa2 by Moody's and BBB- by S&P.

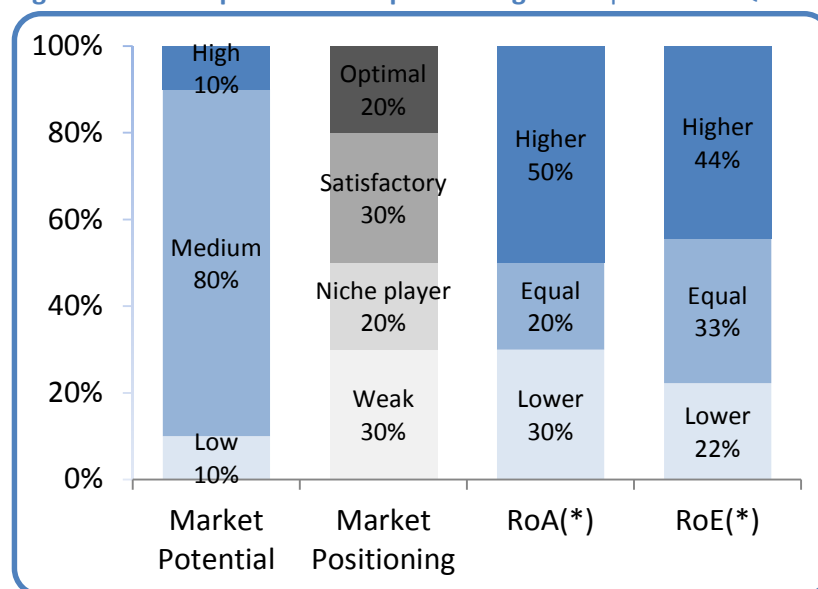
<sup>3</sup> Sources for the macroeconomic data: European Commission. Sources for the banking data: European Commission, Unicredit/Bank Austria and Bulgarian National Bank data.

## 4. Results of the Bank Lending Survey:

### 4.1 Parent banks<sup>4</sup>

1. Parent banks operating in Bulgaria have continued to restructure their businesses at the global level over the past six months and expect to continue to do so over the next six months, like the full sample of parent banks operating in the region and considered in this survey. About half of the banking groups with operations in Bulgaria plan to implement strategic restructuring measures over the next six months and about 40 percent intend to raise capital on the market. These figures are broadly the same for the full sample of parent banks included in the survey.

**Figure 1. Market potential and positioning – see question A.Q13**



Source: EIB – CESEE Bank Lending Survey.

(\*) Return on assets (adjusted for cost of risk) compared to overall group operations; return on equity (adjusted for cost of equity) compared to overall group ROE.

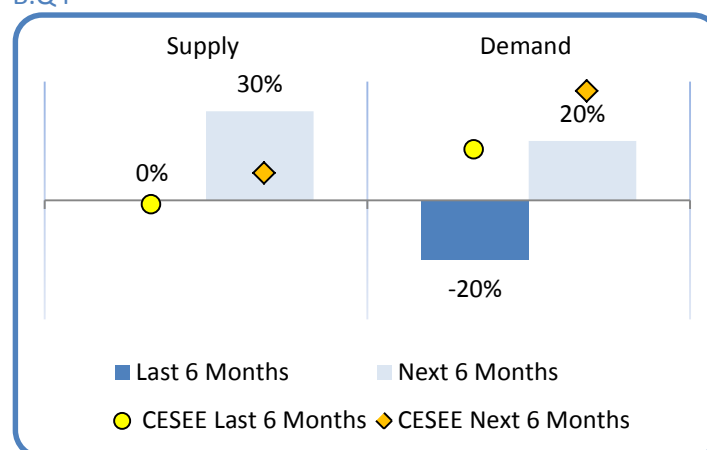
2. The restructuring of parent banks has also had an impact on operations in the CESEE region. For instance, a third of these banks intend to reduce operations selectively, while a third intend to expand operations. This divergence of views is even bigger in Bulgaria, where 40 percent intend to selectively reduce operations and 50 percent intend to expand. Such a divergence is underlined by two additional facts. First, 90 per cent of parent banks with operations in Bulgaria assess the local market potential as medium or low (Figure 1, first bar). Second, one half of parent banks report that risk-adjusted returns from their operations in Bulgaria are higher than those for group operations as a whole (Figure 1, last two bars).

<sup>4</sup> In this subsection results refer to the views of parent banks. Results on market positioning and potential refer to questions addressing behaviours within a specific market, whilst the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents' views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a specific country.

## 4.2 Local banks/subsidiaries

- As in the previous rounds of the survey, subsidiaries operating in Bulgaria describe supply conditions (credit standards) as broadly stable over the past six months but expect them to ease somewhat in the near future. This expectation of improvement is higher than the average in the CESEE region. Aggregate demand for loans and credit lines was seen as declining by a net 20 percent of subsidiaries over the past six months, while it is

**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**

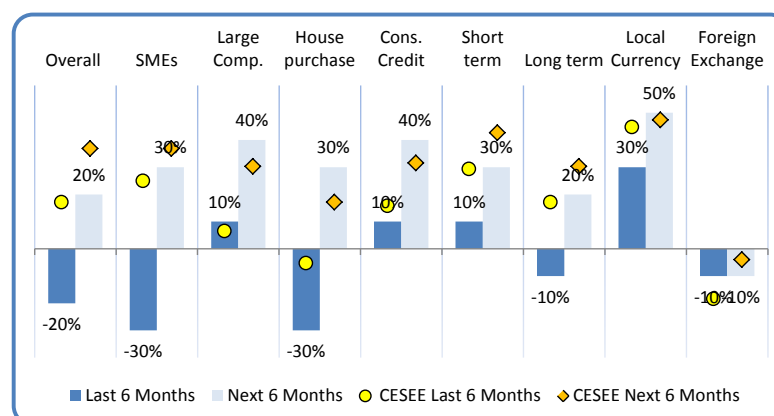


Source: EIB – CESEE Bank Lending Survey.

- expected to increase somewhat in the near future (Figure 2). Across the region, on average, demand has been improving and local banks expect it to continue to do so even more over the next six months. The difference between Bulgaria and the region as a whole is most likely due to heightened political uncertainty.

- Weak credit demand in Bulgaria stems from deterioration in both the corporate and household sectors (see Figure 3). A net 30 percent of banks reported declining demand from SMEs and declining demand for housing loans, while demand from large corporates and for consumer credit was seen as broadly unchanged. The

**Figure 3. Demand components – (net percentages; positive figures refer to increasing demand) – see question B.Q4**

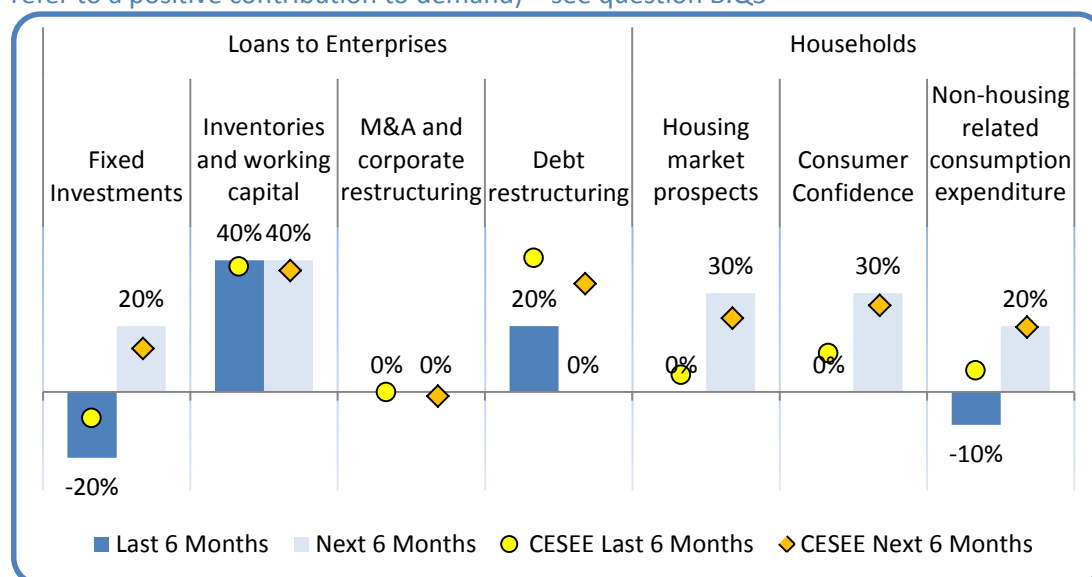


Source: EIB – CESEE Bank Lending Survey.

maturity structure of demand continued to tilt towards the short term as indicated also in the previous survey round. Banks expect that credit demand will pick up over the next six months in the corporate and household sectors, as well as across maturities.

3. Demand for loans for fixed investment continued to be the biggest drag on demand as in the previous survey round, while it picked up for loans for working capital and to a lesser extent for debt restructuring (Figure 4). These developments are broadly consistent with those in the rest of the CESEE region. Household demand factors are seen as broadly speaking unchanged. Looking ahead, credit demand for fixed investment and working capital is expected to increase in Bulgaria in line with developments across the region. Factors behind household credit demand are also expected to evolve favourably.

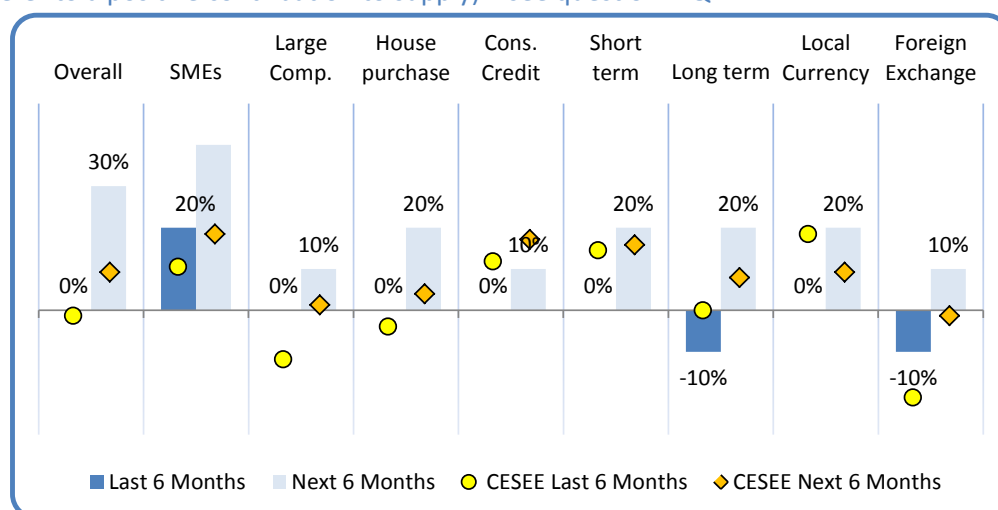
**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**



Source: EIB – CESEE Bank Lending Survey.

4. Overall supply (credit standards) has remained unchanged over the past six months in Bulgaria, despite the perceived easing for the SME segment. Stable supply conditions in Bulgaria are in line with average CESEE developments (Figure 5). Aggregate credit standards are expected to ease over the next six months, especially for SMEs and house purchases. Easing credit supply is expected for both short and long maturities as well as for local and foreign currency loans. Overall supply in Bulgaria is expected to improve more than the CESEE average and the factors with the most significant contributions are the expected decline in the margin of banks over the interbank rate and the expected easing of collateral requirements.

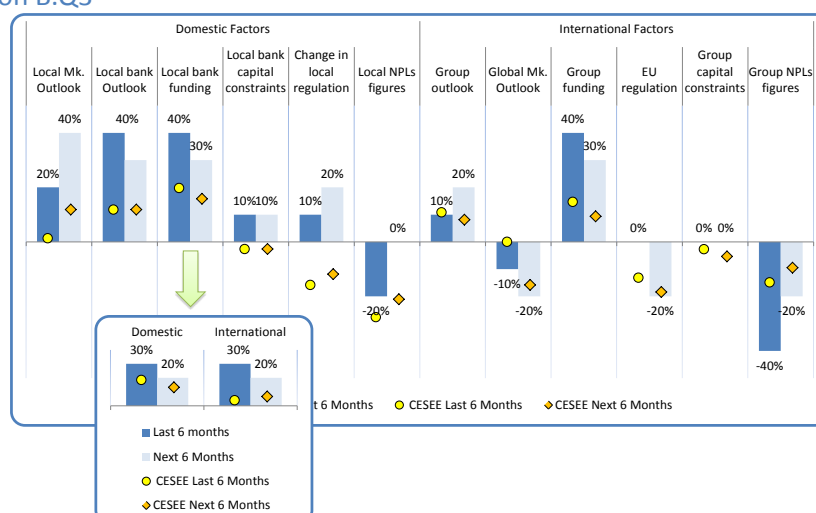
**Figure 5. Supply components – credit standards** (*net percentages; positive figures refer to a positive contribution to supply*) – see question B.Q1



Source: EIB – CESEE Bank Lending Survey.

5. Both domestic and international factors made an important contribution to determining supply conditions (Figure 6). As in the previous round of the survey, local bank funding and local bank and market outlooks contributed to easing credit conditions, whereas local NPL figures pulled in the opposite direction. Among international factors, the widely perceived positive influence of group funding was largely offset by the drag of group NPLs. Both positive and negative forces were stronger than the CESEE average. Looking ahead, the negative contributions of local and group NPLs are expected to decline. EU and local regulation are expected to have opposite effects on credit supply, with changes in local regulations expected to produce positive effects.

**Figure 6. Factors contributing to supply conditions (credit standards)** – (*net percentage; positive figures refer to a positive contribution to supply*) – see question B.Q3

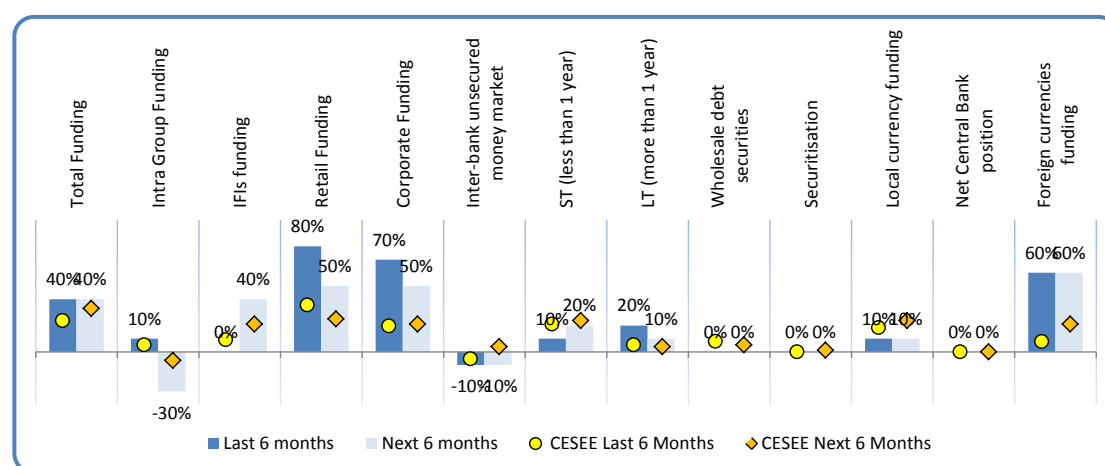


Source: EIB – CESEE Bank Lending Survey.



6. Credit supply conditions for SMEs have improved over the past six months slightly more than the regional average. Narrower margins and easier collateral requirements contributed to the easing. Credit demand from SMEs was perceived as very weak, in contrast to the regional average. It is expected to start recovering over the next six months. Supply conditions are also expected to further improve.
7. Access to funding has improved during the past six months in line with the CESEE regional average, as was the case also in the previous survey round. Retail and corporate deposits have contributed the most to the improved access, as well as foreign-currency funding (Figure 7). It is possible that the positive contribution of domestic deposits can be explained by the massive withdrawals of funds from two domestically owned banks. This may be partly correct, but it should be noted that retail and corporate deposits made a similar contribution during the previous round of the survey. Looking ahead, access to funding is expected to improve further, driven by the same underlying factors.

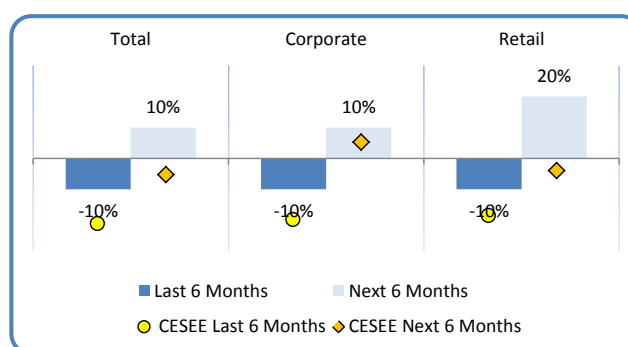
**Figure 7: Access to funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**



Source: EIB – CESEE Bank Lending Survey.

8. NPL ratios are reported to have remained broadly the same, on average, over the past six months, in both the corporate and retail sectors (Figure 8). On average, NPLs are expected to change little, if at all, over the next six months.

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.



# Croatia

## 1. Key statistics<sup>1</sup>

- Number of banks/subsidiaries participating in the survey: six
- Approximate share of assets covered (as proportion of total assets): 75 percent
- Current level of NPLs as proportion of total loans: 16.4 percent (Q2 2014)
- Latest credit growth (yoy): -2.0% (Q2 2014)
- Loan-to-deposit ratio: 117.8 percent (Q1/Q2 2014)
- CAR: 21.1 percent (Q1 2014)

## 2. Key messages - *NPLs are still perceived as a major constraint. Prolonged economic contraction limits credit expansion.*

### International groups' views:

- **Group strategies:** Global groups operating in Croatia are generally more positive than the overall sample of international banks included in the survey. They are less likely to engage in additional deleveraging at the global level. However, they expect to increase their efforts to strengthen the balance sheets.
- **Group assessment of positioning and market potential:** Groups operating in Croatia do not plan to reduce their operations in CESEE. However, market prospects in Croatia are deteriorating, with almost 70 percent of the groups reporting low market potential. Many parent groups also expect returns on assets and equity to be below group levels. Nevertheless a large majority of groups are satisfied with their current market positioning.

### Subsidiaries'/local banks' views:

- Croatian banks report that while **demand conditions stabilised and supply conditions were neutral**, credit growth was negative in the last six months.
- **Credit supply** conditions were neutral and are expected to remain so. The main influences on supply standards were domestic – on the positive side, domestic funding and changes in regulations, and on the negative side, NPLs, local banks' capital constraints and local market prospects. Little improvement is expected.
- **Demand for loans** started to stabilise for the first time. Debt restructuring was the only supportive factor whilst all other components of demand turned from negative to neutral. Looking ahead, demand is expected to expand.
- **Access to funding:** Funding conditions have been improving, with corporate and retail funding having a positive effect. Funding conditions are expected to remain unchanged over the next six months.
- **NPL figures:** All subsidiaries continue to report increasing NPLs.

<sup>1</sup> Sources: IMF, Croatian National Bank and Unicredit/Bank Austria.

### 3. Relevant macroeconomic and banking conditions<sup>2</sup>

- **Growth:** The Croatian economy has been in recession for five years. Real GDP fell by 1 percent in 2013, and continued to contract in the first and second quarters of 2014, leaving the country in recession. Increased net exports and steady domestic demand are expected to bring about a moderate recovery from 2015 onwards.
- **Unemployment:** The unemployment rate is high – about 21 percent at the most recent date. It is expected to remain at elevated levels over the next two years.
- **Inflation:** Inflation is expected to decline further due to weak domestic demand. The harmonised index of consumer prices rose 2.3 percent in 2013, but is expected to fall over 2014 as a whole.
- **External and public sector balance:** Low domestic demand resulted in a current account surplus of 0.5 percent of GDP in 2013, which is expected to increase further to 1.1 percent in 2014. On the fiscal side, however, the consolidation is slow: the deficit is expected to decline from 4.9 percent of GDP in 2013 to marginally below 4 percent in 2014. A pre-financing operation in late 2013 brought forward the increase in public debt, which will remain at just below 70 percent of GDP over the coming years.
- **Banking sector:** The Croatian banking sector is highly capitalised (CAR 21.1 percent in Q1 2014). Aggregate portfolio quality has been deteriorating in line with the recession. NPLs are relatively high at 16.4 percent and have been increasing recently. Lending growth turned negative around mid-2012, and total credit is still contracting (-2.0 percent Q2 2014). Partly as a consequence of the sluggish economy and the resulting low demand for credit, non-resident funding of the banking system had declined by 18 per cent by September 2013 on a year-on-year basis. Growth in domestic deposits, however, particularly from households, has been positive and has been gradually replacing foreign funding. This has also been supporting a continuing deleveraging process.
- **Rating:** Croatia is currently rated by Moody's (Ba1), Fitch (BB) and S&P (BB).

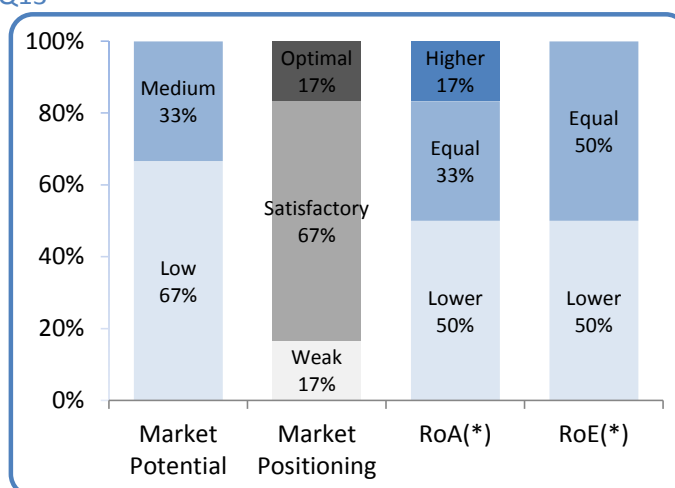
<sup>2</sup> Sources for the macroeconomic data: European Commission. Sources for the banking data: European Commission and Unicredit/Bank Austria based on CNB data.

## 4. Results from the Bank Lending Survey:

### 4.1 Parent banks<sup>3</sup>

- Parent banks operating in Croatia are generally more positive on their global operations than the overall sample of international banks included in the survey. They are less likely to engage in additional deleveraging at the global level over the next six months. However, they expect to increase their efforts to strengthen their balance sheets over the next six months, bringing them into line with the overall sample of international banks.

**Figure 1. Market potential and positioning – see question A.Q13**



Source: EIB – CESEE Bank Lending Survey.

(\*) Return on assets (adjusted for cost of risk) compared to overall group operations; return on equity (adjusted for cost of equity) compared to overall group ROE.

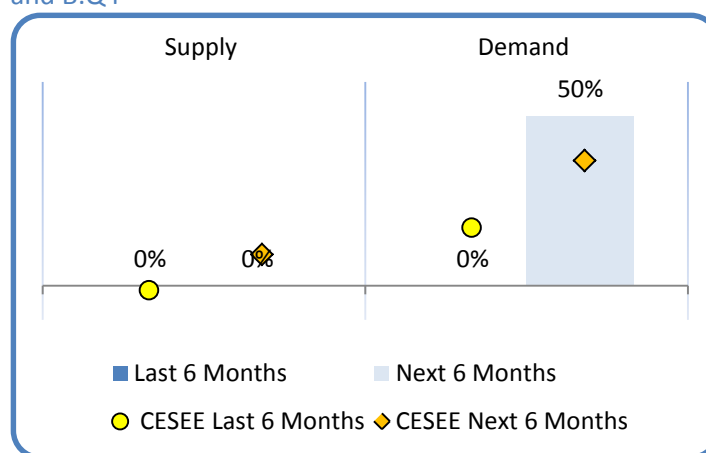
- Parent banks operating in Croatia do not plan to reduce their operations in CESEE over the coming months, as noted in the March 2014 Survey. By way of comparison, one third of the parent banks in the full sample are still planning to withdraw from selected activities at a regional level. In contrast to the previous Surveys, however, groups report a deterioration of market prospects in Croatia. Almost two thirds of the groups view Croatia's market potential as low (Figure 1). In line with this deterioration of prospects, half the groups describe the profitability (i.e. ROE and ROA) of Croatian operations as lower than that of the overall group operations (even when corrected for the cost of risk and cost of equity). These deteriorating views are counterbalanced by a more positive outlook on groups' positioning in the market. Two thirds of the parent banks consider their current market positioning to be satisfactory, and 17 percent assess their positioning as optimal.

<sup>3</sup> In this subsection results refer to the views of parent banks. Results on market positioning and potential refer to questions addressing behaviours within a specific market, whilst the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents' views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a specific country.

## 4.2 Local banks/subsidiaries

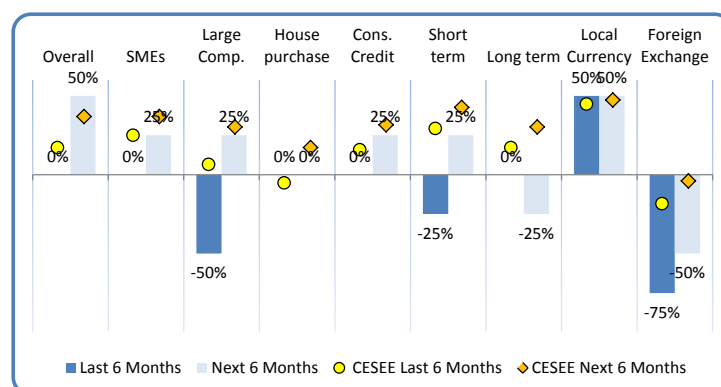
1. Subsidiaries operating in Croatia reported no change in the demand for loans over the past six months, while the broader CESEE region reported an increase. Supply conditions have also been unchanged over the past six months (Figure 2). No change is expected on the supply side over the next six months, while demand is expected to increase robustly.
2. Overall demand for loans has been rather stable, albeit at low levels. Some good news can be detected from the recent data. This is the first time that the Survey does not show an overall contraction in demand. In the corporate segment only credit demand from large companies has contracted, while it remained unchanged across all the other segments of the market (Figure 3). Demand for short-term loans was also marginally lower, although this was one of the few components of demand which was reported to have increased in the March 2014 Survey. The current downturn can be primarily related to the continuing contraction in household aggregate consumption. Looking ahead, demand for loans is expected to resume across the board, except for property-related lending. A protracted shift from foreign to local currency-denominated credit can be observed in Croatia, as elsewhere in the CESEE region.

**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



Source: EIB – CESEE Bank Lending Survey.

**Figure 3. Demand components - (net percentages; positive figures refer to increasing demand) – see question B.Q4**

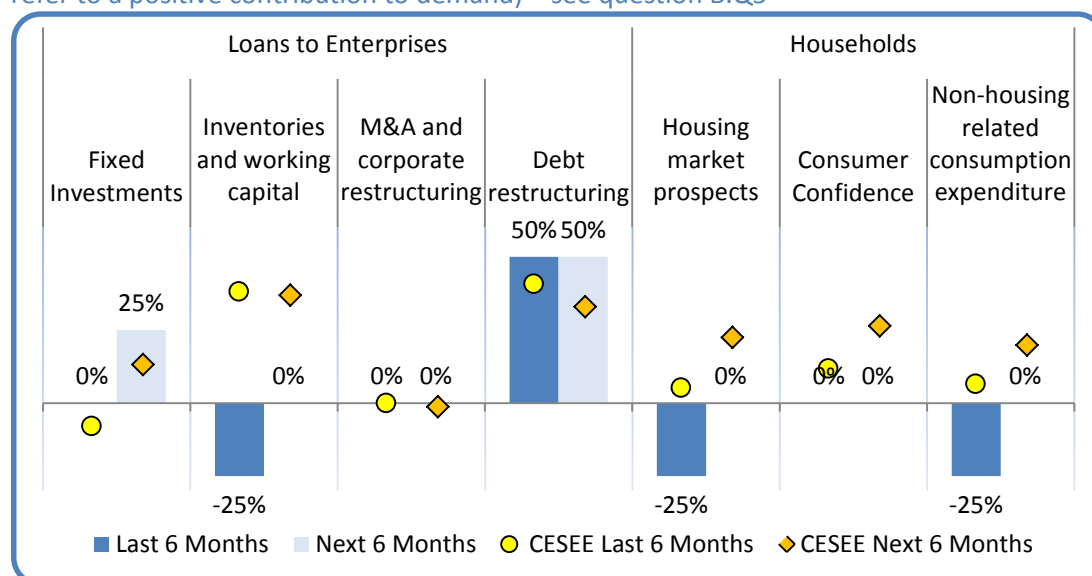


Source: EIB – CESEE Bank Lending Survey.

3. As for the factors behind credit demand, housing market conditions and other categories of household consumption have been a major drag over the last few months, whereas debt restructuring in the corporate sector has contributed positively (Figure 4). The protracted recession has had a strong negative impact

on housing market prospects and consumer confidence, accounting for the significantly lower household credit demand. This segment of the market is not expected to recover over the next six months and will remain less buoyant compared to elsewhere in the CESEE region, as noted in the March 2014 survey. Debt restructuring and investment are expected to support credit demand by the corporate sector in the period ahead.

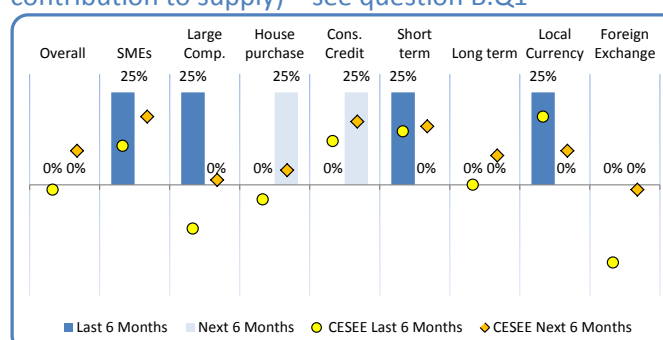
**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**



Source: EIB – CESEE Bank Lending Survey.

4. Credit supply factors have been positive on balance over the past six months (Figure 5). While the overall assessment has been one of little change, particularly in the consumer segment, there has been a loosening of standards on the corporate side (including SMEs). Credit standards for short-term and local currency lending have been relaxed. Over the next six months little change is expected for overall credit supply, but some easing of household credit standards is projected.

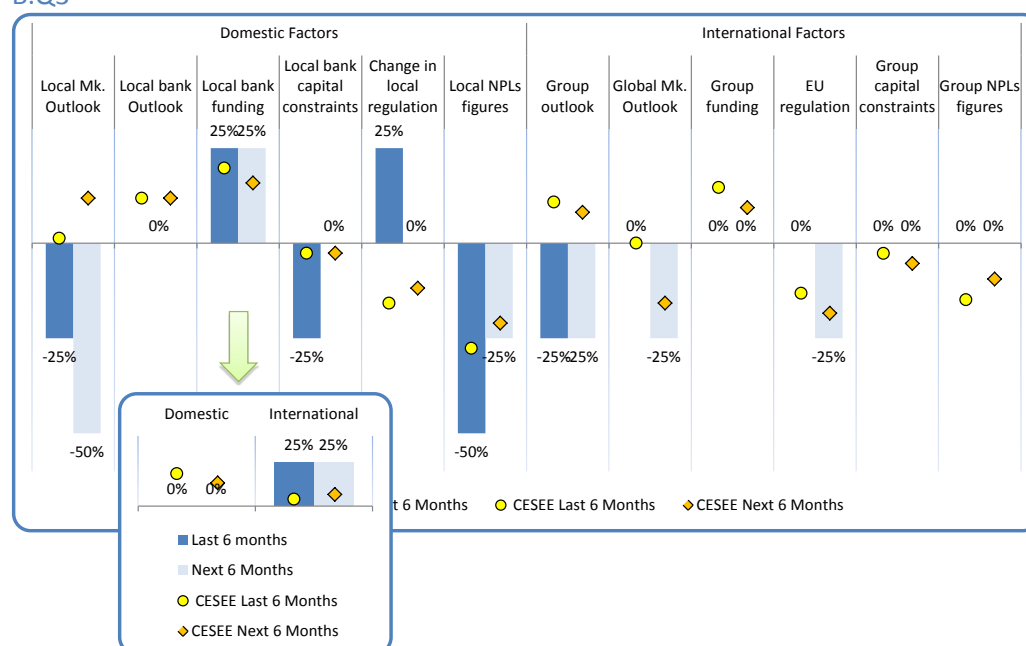
**Figure 5. Supply components – credit standards (net percentages; positive figures refer to a positive contribution to supply) – see question B.Q1**



Source: EIB – CESEE Bank Lending Survey.

5. While some domestic factors contributed positively to credit supply conditions in Croatia, others held them back (Figure 6). The local market outlook, local capital constraints and non-performing loans contributed to a significant tightening over the last six months, while local funding and local regulations helped to counteract this effect. Among international factors, the outlook for parent groups was the only constraining factor. In the period ahead most factors, both domestic and international, are expected to constrain credit supply. The funding of local subsidiaries, particularly their international funding, is expected to remain a positive element, while most other factors, including the local market outlook, local NPLs, the group and global market outlooks and EU regulations, are expected to constrain supply conditions.

**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**



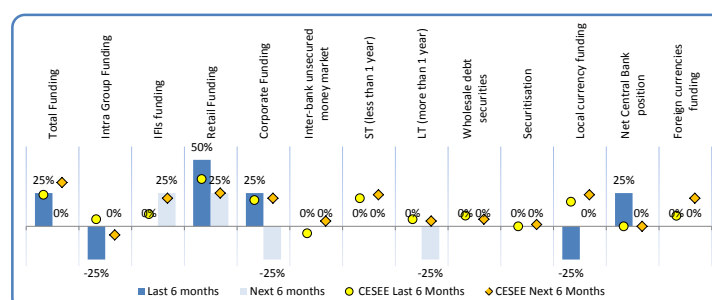
Source: EIB – CESEE Bank Lending Survey.

6. Subsidiaries in Croatia have reported an easing of credit standards for SMEs for the first time since the inception of the survey. However, this is not expected to continue over the next six months. On the other hand, demand for credit from SMEs is expected to pick up slightly over the next six months. This combination may indicate some credit rationing in this segment of the market. All in all, terms and conditions did not become more constraining for SMEs in the last six months, but this follows a prolonged period of tightening for this segment, particularly in terms of collateral requirements.



7. The overall funding situation of subsidiaries has improved over the last six months, primarily from increased retail and corporate funding, and central bank facilities (Figure 7). IFI funding is expected to exert a positive effect over the next six months in line with the regional trend. Intra-group funding, however, continued to exert a negative contribution.

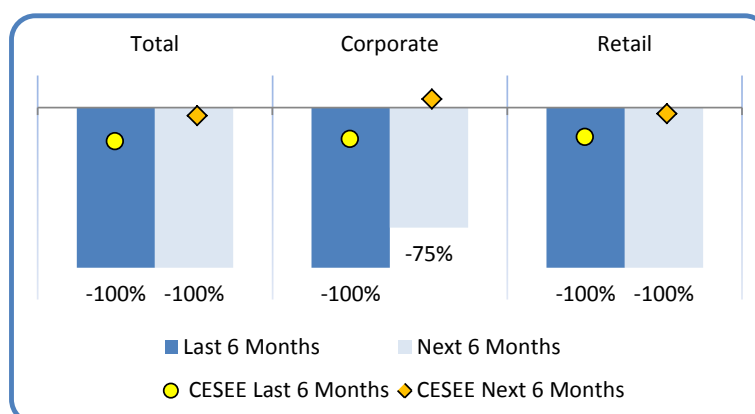
**Figure 7: Access to funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**



Source: EIB – CESEE Bank Lending Survey.

8. With regard to NPLs, the prolonged economic recession continues to weigh on banks' expectations, and the trend highlighted in the previous releases of the survey continued. All subsidiaries stated that NPLs had risen over the past six months – in both corporate and retail segments. In addition, although the level of NPLs is already relatively high, all subsidiaries think that it will rise further in the next six months (Figure 8).

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.



# Czech Republic

## 1. Key statistics<sup>1</sup>

- Number of banks/subsidiaries participating in the survey: six
- Approximate share of assets covered (as proportion of total assets): 70 percent
- Current level of NPLs as proportion of total loans: 6.3 percent (July 2014)
- Latest credit growth (yoy): 5.3 percent (July 2014)
- Loan-to-deposit ratio: 75 percent (July 2014)
- CAR: 16.5 percent (Q1 2014)

## 2. Key messages – *Perceived as a high-potential banking market with a gradual economic recovery under way.*

### International groups' views:

- **Group strategies:** The majority of international banks operating in the Czech Republic are not engaged in a restructuring process at group level. They present a more positive view in terms of group deleveraging than the overall sample of banks included in the survey.
- **Group assessment of positioning and market potential:** All the groups operating in the Czech Republic record higher profitability in CESEE than at the overall group level. They are also more inclined to expand operations in the CESEE region than other groups in the overall sample. They are satisfied with their positioning in the Czech market, and all of them regard the Czech Republic as having medium or high market potential.

### Subsidiaries'/local banks' views:

- **Credit supply:** Credit standards were broadly unchanged over the last six months and are expected to ease, mainly in the SME and large corporate segments, over the coming period. The positive impact on supply conditions of the local market and bank outlook is expected to be partly offset by local and international regulation, as well as by group capital constraints.
- **Credit demand:** Following the stagnation over the last six months, demand is expected to increase, particularly on the back of SMEs, consumer credit and demand for house purchase loans.
- **Access to funding:** Subsidiaries indicated stagnating funding conditions, as the deterioration in corporate funding was offset by improvements in retail and, to some extent, IFI and intra-group funding. Access to total funding is expected to improve, driven particularly by IFIs and intra-group funding.
- **NPL figures:** In contrast with the CESEE region, NPLs stagnated in the Czech Republic but are expected to deteriorate somewhat, in particular due to retail loans.

<sup>1</sup> Sources: The Czech National Bank.

### 3. Relevant macroeconomic and banking conditions<sup>2</sup>

- **Growth:** Following the contraction in 2012, the decline of economic activity continued but slowed down significantly in 2013. In fact, growth has been strengthening since mid-2013 and reached nearly 3 percent year-on-year in the first half of 2014. Real GDP is thus expected to rebound, with annual growth of around 2 percent in 2014. The contribution of domestic and external demand (both negative in 2013) is forecast to turn positive, with the latter mainly driven by the weakening of the koruna and accelerating economic activity in the main trading partners. Growth is expected to accelerate slightly in 2015, mostly due to strengthening domestic demand.
- **Unemployment:** The unemployment rate has been hovering around 7 percent over the last few years. Although the decrease in the labour force stemming from demographic changes will exert upward pressure on the unemployment rate, the strengthening of the economy is expected to result in a gradual decline in the unemployment rate over the medium term.
- **Inflation:** Sluggish economic activity contributed to the drop in inflation from 3.5 percent in 2012 to 1.4 percent in 2013. Despite the weakening of the koruna and stronger growth, inflation hovered around 0.5 percent in the first eight months of 2014 and is thus expected to turn out well below 1 percent in 2014, mainly as a result of declining administered and energy prices as well as indirect tax hikes dropping out of the calculation. Inflation is forecast to return to close to 2 percent in 2015, thanks to stronger domestic demand.
- **External and public sector balance:** The current account posted a slight deficit in 2013, while this is expected to decrease to close to zero in 2014-15 on the back of the weaker koruna, accelerating growth in the main trading partners and increasing absorption of EU funds. Following the fiscal consolidation that brought down the budget deficit to 1.5 percent of GDP in 2013, the fiscal stance is expected to be slightly eased in 2014. In 2015 further fiscal easing is expected, with the deficit increasing to around 2.4 percent of GDP. Public debt is just under 50 percent of GDP, and is expected to remain stable in the medium term.
- **Banking sector:** The capital adequacy ratio of the banking sector (16.5 percent in Q1 2014) comfortably exceeds the regulatory minimum. NPLs are around 6 percent, which is low compared with the rest of the region. The loan-to-deposit ratio (75 percent in July 2014) is very low in relation to the rest of the region. Credit growth is well below the pre-crisis level, albeit still positive (around 5 percent in mid-2014), with retail loans increasing at a slightly higher rate than corporate loans.
- **Rating:** The Czech Republic is currently rated A1 by Moody's, A+ by Fitch and AA- by S&P.

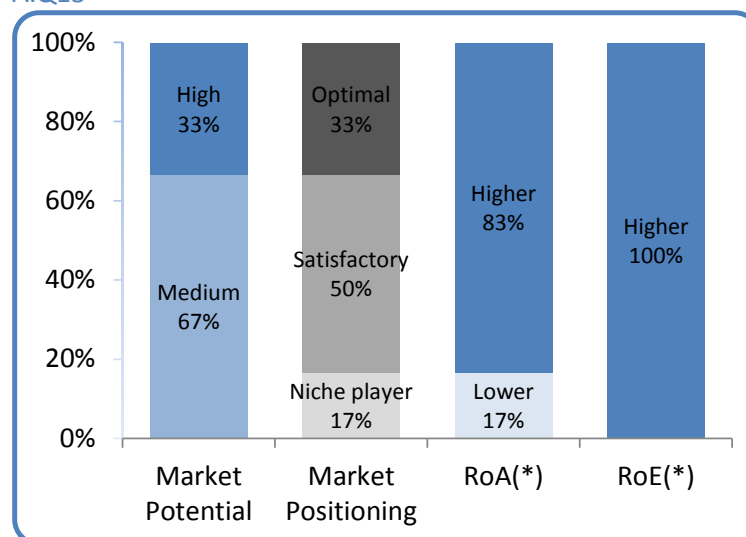
<sup>2</sup> Sources for the macroeconomic data: European Commission and the IMF. Sources for the banking data: European Commission and the Czech National Bank.

## 4. Results of the Bank Lending Survey:

### 4.1 Parent banks<sup>3</sup>

1. In several respects parent banks operating in the Czech Republic have a more favourable view than the overall sample of groups included in the survey. Half of parent banks (compared to 75% in the overall sample) are considering the sale of assets in the next six

**Figure 1. Market potential and positioning** – see question A.Q13



Source: EIB – CESEE Bank Lending Survey.

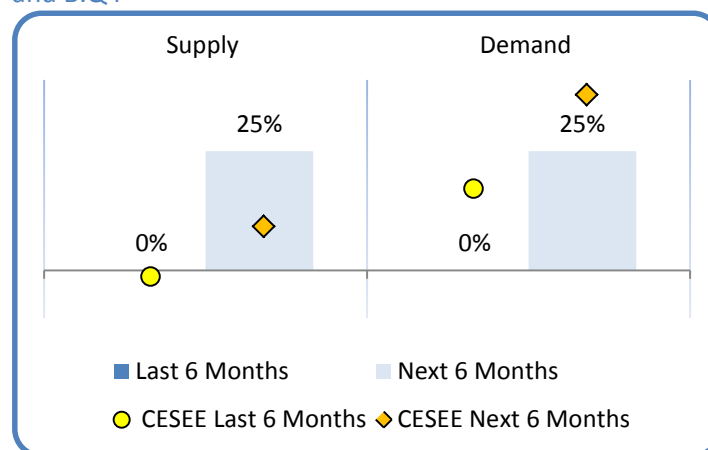
2. A vast majority of banks do not plan other strategic operations such as strategic restructuring, raising capital, selling branches or receiving capital from the government. Parent banks operating in the Czech Republic do not envisage further strong deleveraging, as reflected in the fact that three quarters of banks (compared to around 50% in the overall sample) expect their loan-to-deposit ratio to remain stable or increase over the next six months.
2. Groups operating in the Czech Republic remain strongly committed to the region. Three quarters of such banks intend to expand operations, while none of them plan to reduce their regional activity. Half of parent banks operating in the Czech Republic reported higher profitability in CESEE than at group level in the last six months, but three quarters expect higher profitability in the next half-year. Moreover, three quarters of banks expect either an unchanged or increasing contribution of activities in CESEE to the group level return-on-assets ratio over the next six months. Parent banks are satisfied with their market positioning, with 33 percent of respondents considering it to be optimal and 50 percent regarding it as satisfactory (Figure 1). Banks' overall assessment of market potential is also favourable since all surveyed banks consider it to be medium-to-high (Figure 1).

<sup>3</sup> In this subsection results refer to the views of parent banks. Results on market positioning and potential refer to questions addressing behaviours within a specific market, whilst the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents' views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a specific country.

## 4.2 Local banks/subsidiaries

- In line with the CESEE average, subsidiaries operating in the Czech Republic reported unchanged supply conditions over the last six months. In the next half-year supply is expected to increase markedly more in the Czech Republic than in the CESEE region (Figure 2). In contrast, demand has stagnated in the Czech Republic in the last six months, whereas it grew in the CESEE region. Looking forward, however, supply is expected to pick up more strongly in the Czech Republic than in CESEE countries on average.

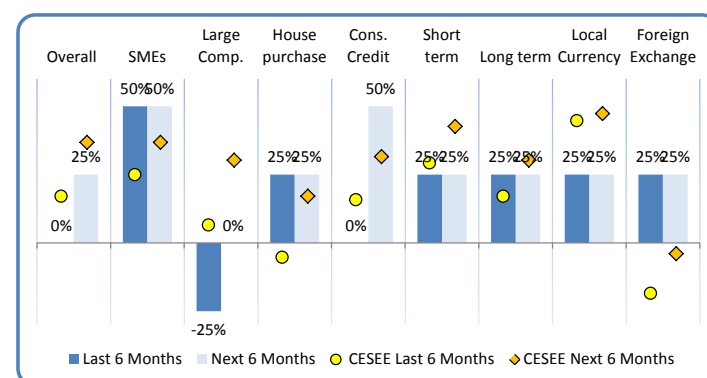
**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



Source: EIB – CESEE Bank Lending Survey.

- In the last six months demand has remained unchanged on balance as an increase in demand from SMEs and households was offset by a decrease in demand from large corporations. Looking ahead, a significant majority of banks expect an increase in overall credit demand. It is expected to be driven by SMEs, consumer credit and demand for house purchase loans, while credit demand from large firms is forecast to be largely unchanged. In terms of maturity and currency denomination, demand growth is expected to be even across all segments (Figure 3).

**Figure 3. Demand components - (net percentages; positive figures refer to increasing demand) – see question B.Q4**

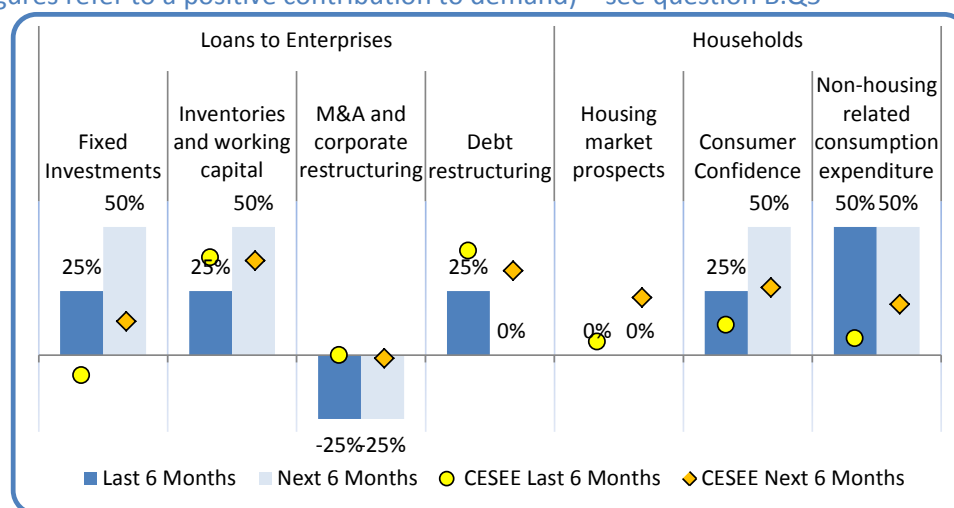


Source: EIB – CESEE Bank Lending Survey.

- In the corporate segment over the last six months demand was negatively affected by M&A and corporate restructuring, while fixed investments, debt restructuring as well as inventories and working capital had a positive impact on demand conditions. Looking ahead, demand is expected to increase thanks to the continuous positive contribution of investments in fixed and working capital

as well as inventories. In contrast, demand for debt restructuring is expected to stagnate and that for M&A and corporate restructuring to contract, which together will constitute a drag on the overall improvement in demand. In the household segment, demand was supported particularly by favourable non-housing-related consumption expenditures and to a lesser extent increasing consumer confidence. A similar pattern with an even stronger consumer confidence is expected in the next six months, way better than the aggregate CESEE outlook (Figure 4). However, housing market prospects are expected to improve somewhat in the CESEE region whereas they will continue to stagnate in the Czech Republic.

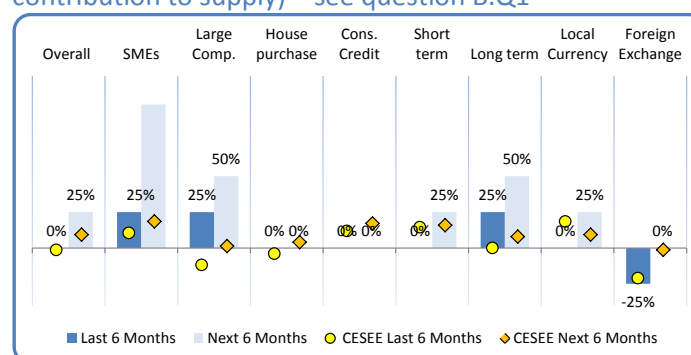
**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**



Source: EIB – CESEE Bank Lending Survey.

4. Supply conditions remained unchanged both in the Czech Republic and the entire CESEE region over the last two quarters. Subsidiaries operating in the Czech Republic expect credit conditions to ease over the next six months, primarily in the SME and, to a lesser extent, large corporate segments. The

**Figure 5. Supply components – credit standards (net percentages; positive figures refer to a positive contribution to supply) – see question B.Q1**



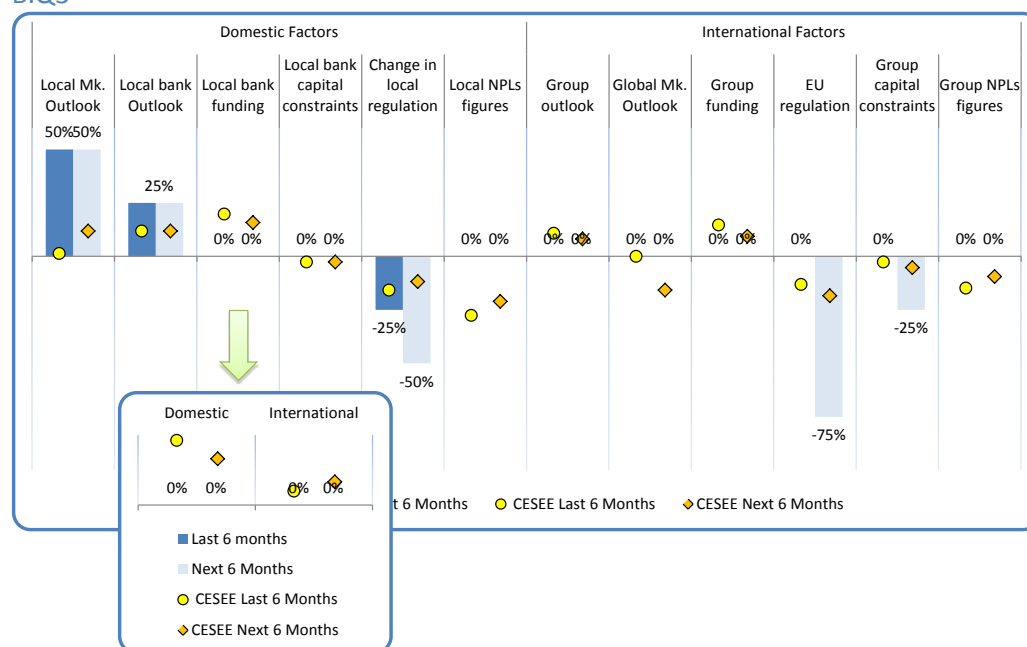
Source: EIB – CESEE Bank Lending Survey.

- The loosening of credit standards in these two segments should be significantly more pronounced in the Czech Republic than in the CESEE region as a whole (Figure 5).

5. Overall, both domestic and international factors made broadly neutral contributions to supply conditions over the last six months. In the case of

domestic factors, the local market and bank outlook pointed toward the easing of credit standards, whilst changes in local regulation contributed to a tightening of supply conditions. A similar trend is expected to continue over the next six months. However, changes in domestic and EU regulation, as well as group capital constraints, are likely to be a stronger constraint on easing credit standards (Figure 6).

**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**



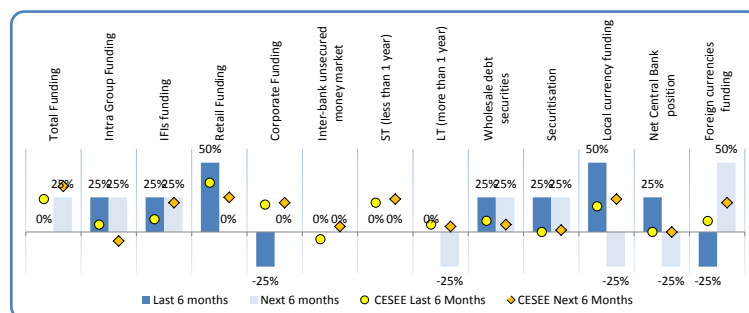
Source: EIB – CESEE Bank Lending Survey.

6. As regards SMEs, banks on balance reported some easing of credit standards in the last six months and a relatively more pronounced increase in demand. Looking ahead, demand is expected to strengthen further, broadly in line with the general developments in the CESEE region. All subsidiaries expect a further loosening of credit conditions in the Czech Republic, compared with only a slight majority expecting such a loosening in the CESEE region as a whole. Moreover, there are some differences regarding the components of credit standards. Specifically, interest rate margins, average loan size and other credit conditions are expected to loosen in the Czech Republic to a significantly larger extent than in the CESEE region as a whole.



7. With a loan-to-deposit ratio well below 100 percent, Czech banks generally had no pressing need to rely on intra-group funding to support credit growth. Subsidiaries reported stagnating funding conditions as the deterioration in corporate funding was counteracted by retail and, to a lesser extent, IFI and intra-group funding over the last six months. Broadly in line with the rest of the CESEE region, access to financing is expected to ease in the next six months. However, while the improvement will be driven particularly by IFIs and intra-group funding in the Czech Republic, in the CESEE region the tightening of intra-group funding will be offset by positive developments in other funding sources (Figure 7).

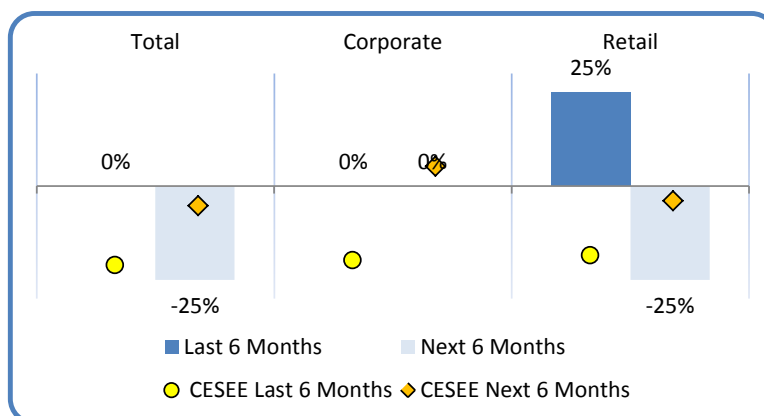
**Figure 7: Access to funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**



Source: EIB – CESEE Bank Lending Survey.

8. Corporate NPL ratios stagnated over the last six months and are expected to remain unchanged in the next two quarters. In contrast, NPL ratios decreased somewhat in the case of retail loans, but this decline is likely to be reversed looking ahead. In the CESEE region NPL ratios deteriorated in both segments and are expected to continue to rise, although at a much slower pace.

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.



# Hungary

## 1. Key statistics<sup>1</sup>

- Number of local banks/subsidiaries participating in the survey: seven
- Approximate share of assets covered (as proportion of total assets): 75 percent
- Current level of NPLs as proportion of total loans: 18.5 percent (Q3 2013)
- Latest credit growth, yoy: -4.8 percent (Q1 2014)
- Loan-to-deposit ratio: 103.5 percent (Q1/Q2 2014)
- CAR: 17 percent (Q2 2014)

## 2. Key messages - *Low profitability decreases the attractiveness of the Hungarian market, while no major impediments to supply and demand are detected at this stage.*

### International groups' views:

- **Group strategies:** Banking groups operating in Hungary are somewhat less likely to initiate restructuring processes at the global level than the full sample of banks included in the survey. Only 20 percent of the respondents envisage further deleveraging of their overall operations.
- **Group assessment of positioning and market potential:** Groups operating in Hungary remain committed to the CESEE region but see only medium-to-low potential in the Hungarian market. 70 percent of them consider the profitability of their Hungarian operations as lower than the group's other activities.

### Subsidiaries'/local banks' views:

- Hungarian banks report **improving demand for credit** and a **similar**, relatively positive outlook for **credit supply conditions**.
- **Credit supply** expectations are more optimistic than the CESEE average. Credit has been particularly accessible for SMEs, the sector targeted by the central bank's Funding for Growth initiative. Looking ahead, banks expect further easing of credit conditions for corporates and households. They regard some international factors and the domestic regulatory environment as potential drags on lending.
- **Credit demand** has been increasing in line with the strong rebound in economic activity after a prolonged recession and is expected to remain high.
- **Access to funding** from most sources is reported to be limited, suggesting that the central bank's funding scheme plays an important role in generating the optimistic credit supply expectations.
- **NPL figures** increased over the last period, but they are expected to stabilise.

<sup>1</sup> Sources: National Bank of Hungary, IMF, European Commission and Unicredit/Bank Austria.

### 3. Relevant macroeconomic and banking conditions<sup>2</sup>

- **Output:** After a modest increase of 1.1 percent in 2013, GDP growth in the second quarter of 2014 was the highest in the EU, at 3.9 percent. Fixed investment grew by an annual rate of 18.7 percent, driven mainly by large EU-funded infrastructure projects. Following a long period of contraction, domestic demand – strengthened by indirect fiscal measures and substantial monetary easing – has become the primary driver of growth.
- **Unemployment:** The participation rate increased and contemporaneously the unemployment rate declined to roughly 8 percent during 2014. Employment has been increasing, mainly as a result of the extension of the Public Work Scheme and the rising number of cross-border workers.
- **Inflation:** Cuts in regulated energy and utility prices, together with favourable global factors, contributed to a further fall in headline inflation to 0.4 percent in Q1 2014. Annual inflation was 0.1 percent in July 2014, back in positive territory for the first time since March 2014. Inflation is projected to increase gradually in 2015 as a result of the weaker exchange rate and the closing of the output gap.
- **External and public sector balance:** The 2013 ESA deficit stood at 2.2 percent of GDP and is expected to widen somewhat to 2.9 percent in 2014, as already programmed by the government. However the January-July budget deficit was 86.5 percent of the full-year target, down from 91.6 percent in the same period of 2013. Public debt is expected to remain at around 80 percent of GDP in 2014. The current account will continue to be in surplus, amounting to 3 percent of GDP in 2014.
- **Banking sector:** After two years of losses the banking system produced a positive, albeit small, profit in 2013 according to Hungarian accounting rules. However, on an IFRS basis the eight largest banks made a loss. Bank P&Ls are still heavily impacted by loan losses – the aggregate NPL ratio is 18.5 percent – and various policy measures (bank levy, transaction tax). Profits were further hit in Q2 2014. This was primarily caused by new loss provisions set aside by banks to cover expected losses from the July law ordering them to compensate borrowers for past foreign-currency consumer and mortgage loans. Capitalisation is adequate (CAR 17 percent in Q2 2014). The loan-to-deposit ratio fell from its early 2009 peak of 162 percent to around 103 percent (Q1/Q2 2014). Credit flows have been consistently negative since Q4 2008. The central bank's Funding for Growth initiative was intended to provide the corporate (mainly SME) sector with cheap funding, to slow down the decline in corporate credit. The foreign currency-denominated household credit portfolio remains a key vulnerability of the banking sector.
- **Rating:** Hungary's rating is BB+ (Fitch), Ba1 (Moody's) and BB (S&P).

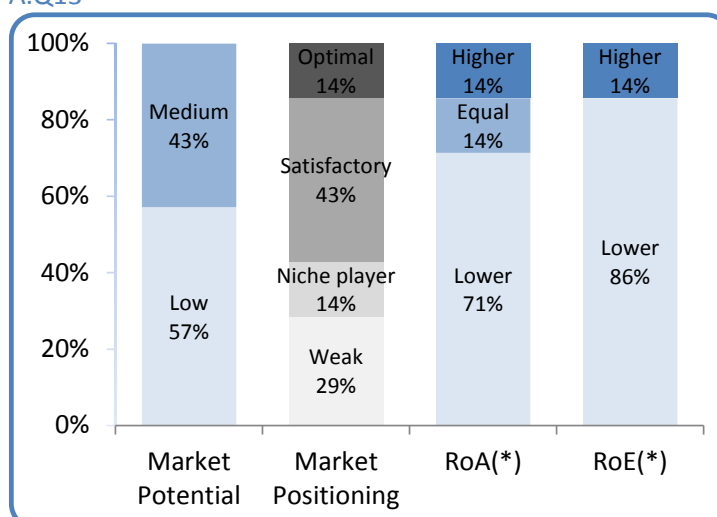
<sup>2</sup> Sources for the macroeconomic data: European Commission. Sources for the banking data: European Commission, Unicredit/Bank Austria and Raiffeisen Research based on NBH data.

## 4. Results of the Bank Lending Survey:

### 4.1 Parent banks<sup>3</sup>

- Banking groups operating in Hungary do not differ significantly on average from the overall sample of parent banks in terms of their global strategies. They are somewhat less likely to conduct strategic restructuring

**Figure 1. Market potential and positioning – see question A.Q13**



Source: EIB – CESEE Bank Lending Survey

(\*) Return on assets (adjusted for cost of risk) compared to overall group operations; return on equity (adjusted for cost of equity) compared to overall group ROE.

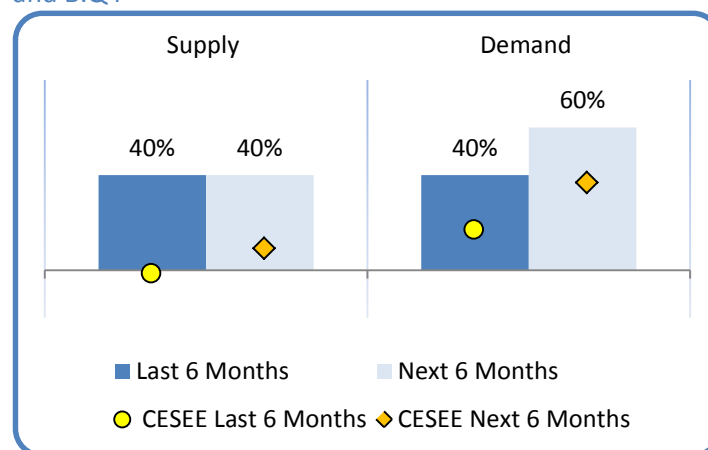
- However they signal a potential acceleration in sales of assets at the global level, in line with the whole set of international bank groups. As for deleveraging, they are less likely to reduce their current loan-to-deposit ratios at the global level in the near future, with only 20 percent of groups still expecting such a decrease.
- Groups operating in Hungary remain committed to their operations in the CESEE region, signalling their intentions of either maintaining or even expanding operations in the region. However the prospects for the Hungarian market are described as being rather gloomy. About 57 percent of respondents believe that the potential of the Hungarian market is 'low' (Figure 1). This confirms the results reported in the March 2014 Survey and indicates that the parents' view of the Hungarian banking market is less favourable than their perception of the other Visegrad 4 countries (Czech Republic, Poland and Slovakia). In addition, parents also stress that the profitability of the Hungarian operations has dropped quite dramatically, with roughly 70 percent reporting risk-adjusted returns on assets and equity in Hungary as being significantly lower than the overall group levels. This is most likely a result of the recent government measures, which imposed further losses on banks. As to market positioning, about half the parents believe it to be satisfactory or optimal.

<sup>3</sup> In this subsection the results refer to the views of parent banks. Results on market positioning and potential refer to questions about behaviour within a specific market, while the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents' views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a particular country.

## 4.2 Local banks/subsidiaries

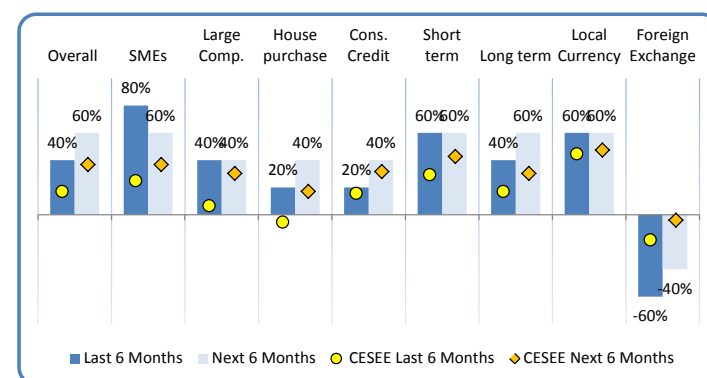
1. Hungarian subsidiaries and local banks generally reported high overall demand for credit. Survey participants also indicated a parallel, equally pronounced easing of credit standards. Both credit supply and demand exceed the overall CESEE results (Figure 2) and they are expected to continue to do so over the next six months.

**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



Source: EIB – CESEE Bank Lending Survey.

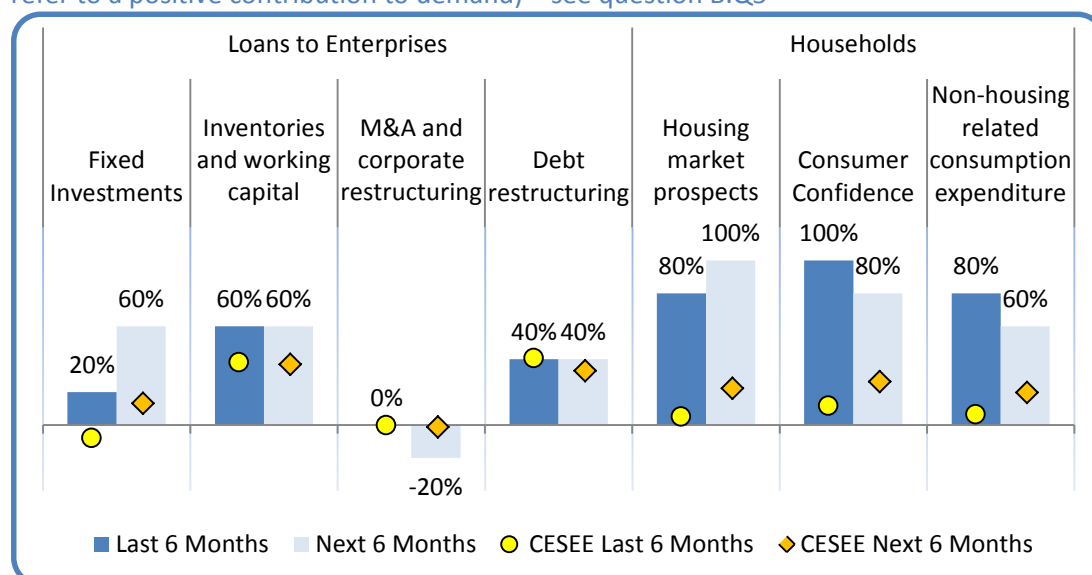
**Figure 3. Demand components (net percentages; positive figures refer to increasing demand) – see question B.Q4**



Source: EIB – CESEE Bank Lending Survey.

3. As for the factors behind credit demand, the household sector across all segments has contributed strongly to the aggregate increasing demand for loans. Working capital financing and corporate debt restructuring also contributed positively to demand increases. In addition, investment contributed rather robustly to demand, in contrast to the regional trend (Figure 4). Looking ahead, the same factors continue to play a positive role, with an even increased contribution from investment.

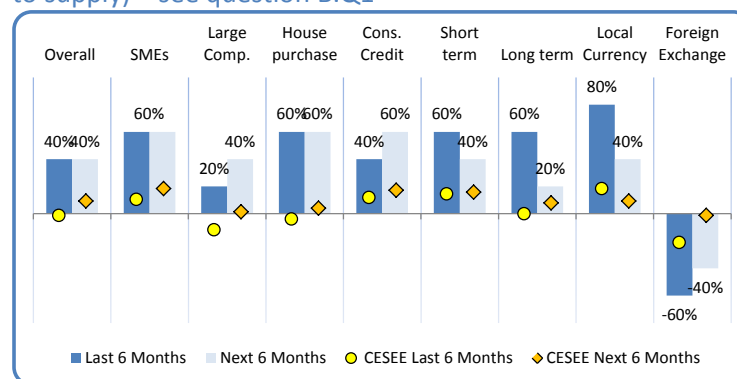
**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**



Source: EIB – CESEE Bank Lending Survey.

4. A marked easing in credit supply has been observed across most market segments in the last six months, and banks expect further easing of access to finance for corporates as well as households (Figure 5). The overall dynamics of credit supply conditions are significantly above the CESEE average. The significant monetary easing has probably influenced these supply developments. It was achieved through a series of cuts in the policy rate by the central bank and through unconventional measures, such as the successive phases of the Funding for Growth programme, providing subsidised funding to SMEs and mid-caps. Banks see maturity and collateral requirements as having been eased in particular. In this regard Hungarian banks report a marked improvement in customers' access to long-term finance and expect this trend to continue.

**Figure 5. Supply components – credit standards (net percentages; positive figures refer to a positive contribution to supply) – see question B.Q1**

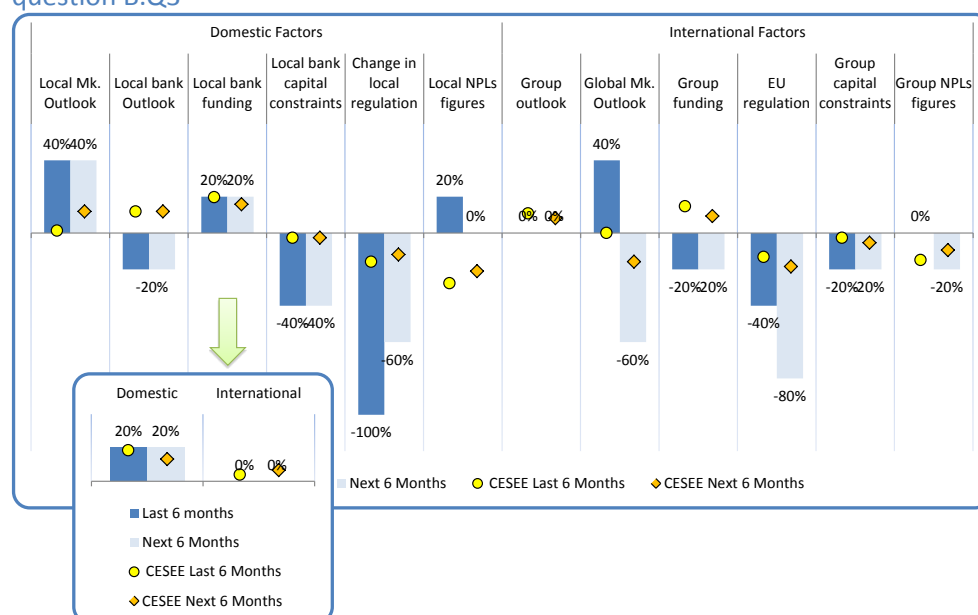


Source: EIB – CESEE Bank Lending Survey.

5. Unlike the results for the CESEE region as a whole, some international factors had a rather strongly negative impact on supply conditions, namely: EU regulation and group funding conditions. To a lesser extent, group NPLs are also expected to be impediments to credit growth (Figure 6) over the next six months. As for the domestic components, unpredictability of local regulation and local capital constraints are the two main factors that are expected to

continue weighing negatively on credit standards. On the other hand, the local market outlook and local bank funding played an easing role and are expected to continue to do so over the next six months. Constraints to supply derived from changes in local regulation continue to be much more evident in Hungary than in the CESEE region in general.

**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**



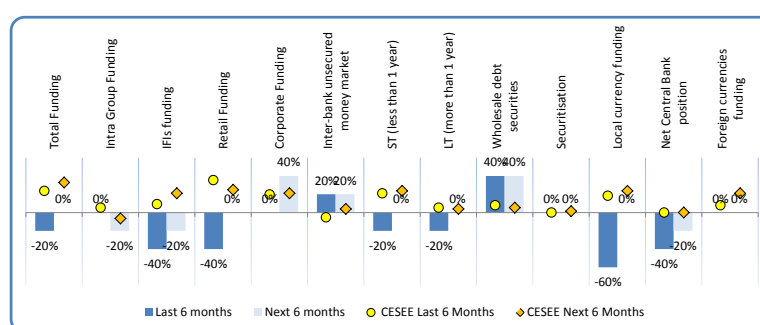
Source: EIB – CESEE Bank Lending Survey.

6. The SME sector recorded a rather pronounced easing in the conditions for credit supply. This is a result of the Hungarian central bank's Funding for Growth programme, targeted mainly at SMEs and mid-caps. As a consequence, the banking system was at least in large part able to match the increasing demand in this segment, and this is expected to continue, given that actual disbursements are still well below the total approved amount of the central bank facility.

7. While relatively optimistic about credit supply,

Hungarian subsidiaries and local banks are more concerned about funding than their CESEE peers (Figure 7). This is a trend already highlighted in the March 2014 release

**Figure 7: Access to funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**



Source: EIB – CESEE Bank Lending Survey.

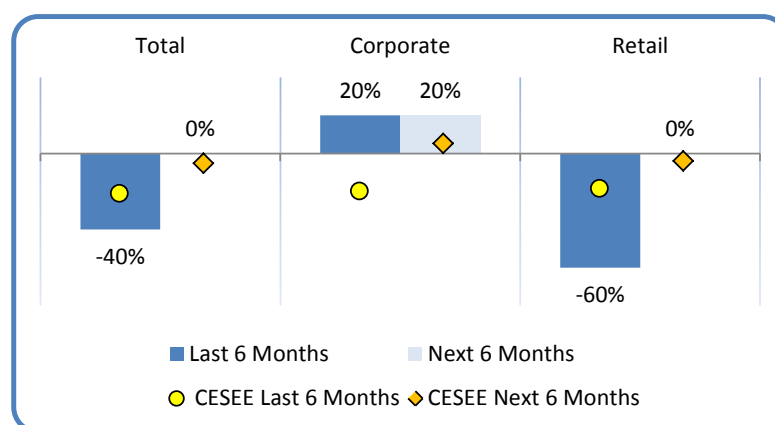
of the survey. At the same time, corporate and retail funding is also rather



subdued. Retail funding is perceived to be on the decline, probably as a result of increasing competition with the government for attracting domestic retail savings. The apparent difference between the funding outlook and the credit supply projection may be explained by the central bank's generous Funding for Growth programme, which may be used to address eventual shortfalls in funding if needed.

8. NPL ratios have continued to increase over the past six months. However, they are expected to stabilise over the next six months, in line with most other CESEE countries (Figure 8). NPLs in the retail sector have

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.

continued to increase rather sharply over the last six months, although banks do not envisage a further worsening in the period ahead.



# Poland

## 1. Key statistics<sup>1</sup>

- Number of banks/subsidiaries participating in the survey: seven
- Approximate share of assets covered (as proportion of total assets): 50 percent
- Current level of NPLs as proportion of total loans: 8.4 percent (Q1 2014)
- Latest credit growth, yoy: 4.4 percent (Q1 2014)
- Loan-to-deposit ratio: 104.6 percent
- CAR: 14.8 percent (Q2 2014)

## 2. Key messages – *Still a relatively attractive market, with strongly increasing demand for loans but somewhat slower improvement in supply conditions.*

### International groups' views:

- **Group strategies:** Groups operating in Poland tend to view their global operations as being generally in line with the overall set of groups included in the survey. In addition they seem to be less inclined to deleveraging.
- **Group assessment of positioning and market potential:** Groups operating in Poland show a strong commitment to the region and are less likely to reduce – and more likely maintain – their CESEE operations. Parent banks consider the Polish market to be among the most attractive within CESEE, although they have revised downwards their assessment of Poland's market potential. Risk-adjusted returns on equity and assets are believed to be among the highest in the region, and groups seem to be relatively satisfied with their current market positioning.

### Subsidiaries'/local banks' views:

- Polish banks report that credit **demand** has **increased**, whilst **supply** conditions remained in a **slight tightening phase**.
- **Credit supply** conditions have slightly tightened but are expected to ease in some segments. The supply of consumer credit is expected to remain strong, while for housing finance the conditions are unlikely to match the expected increase in demand. On the corporate side, however, larger corporates' increasing propensity to borrow is not reflected in increased bank willingness to lend.
- **Demand for loans** increased sharply and is expected to continue to increase significantly across both the corporate and retail segments over the coming months.
- **Access to funding:** Polish banks have not reported funding problems. They experienced a strong inflow of corporate and retail deposits.
- **NPL figures** have improved, especially in the corporate segment.

<sup>1</sup> Sources: The National Bank of Poland, Unicredit/Bank Austria and Raiffeisen Research.

### 3. Relevant macroeconomic and banking conditions<sup>2</sup>

- **Growth:** After a short-lived slowdown, the Polish economy has begun to regain strength since the second half of 2013. Real GDP increased by 1.6 percent in 2013 and accelerated to 3.3 percent in the second quarter of 2014. Domestic demand and investments again became the main drivers of real GDP growth.
- **Unemployment:** In parallel with the recovery, unemployment in Poland is expected to improve gradually from its 2013 level of 10.4 percent to around 10 percent in 2015. However, external political shocks may negatively affect this path.
- **Inflation:** Inflation declined rapidly to 0.8 percent in 2013 and continued to decline in the second quarter of 2014. Finally it turned negative in July 2014, for the first time in more than twenty years.
- **External and public sector balance:** The current account deficit contracted dramatically in the first half of 2014 and is expected to remain at around 1—2 percent of GDP over the next two years. On the fiscal side, Poland managed to reduce its budget deficit from 7.9 percent in 2010 to 3.9 percent in 2012. The deficit widened somewhat to 4.4 percent with the economic slowdown in 2013. In 2014 the asset transfer from pension funds to the government will result in a headline surplus of 5 percent, corresponding to a deficit of 3.8 percent without the one-off windfall revenues from the pension scheme. In 2015 a budget deficit of 2.9 percent is expected. Excluding cyclical factors and one-off revenues, the structural budget deficit is likely to improve by 1.2 percentage points between 2013 and 2015.
- **Banking sector:** The Polish banking system weathered the financial crisis well and remains profitable, well capitalised and liquid. The CAR in Q2 2014 stood at 14.8 percent, while ROE in Q1 2014 was 11.7 percent. Polish banks' average NPL ratio of 8.4 percent is still low relative to other CESEE countries. The orderly withdrawal of parent funding, reflected in the decline in the loan-to-deposit ratio, was offset by increasing domestic funding. As a result the credit flow remained consistently positive, declining to roughly 2.5 percent in 2013, and resumed more robust growth in Q1 2014. Regulatory action has contained foreign currency mortgage lending in Poland, but more than half of mortgages are still denominated in foreign currency, creating a potential vulnerability for the banking system.
- **Rating:** Poland is currently rated A- (stable) by S&P, A2 (stable) by Moody's and A- (stable) by Fitch.

<sup>2</sup> Sources for the macroeconomic data: European Commission. Sources for the banking data: European Commission and Unicredit/Bank Austria based on NBP data.

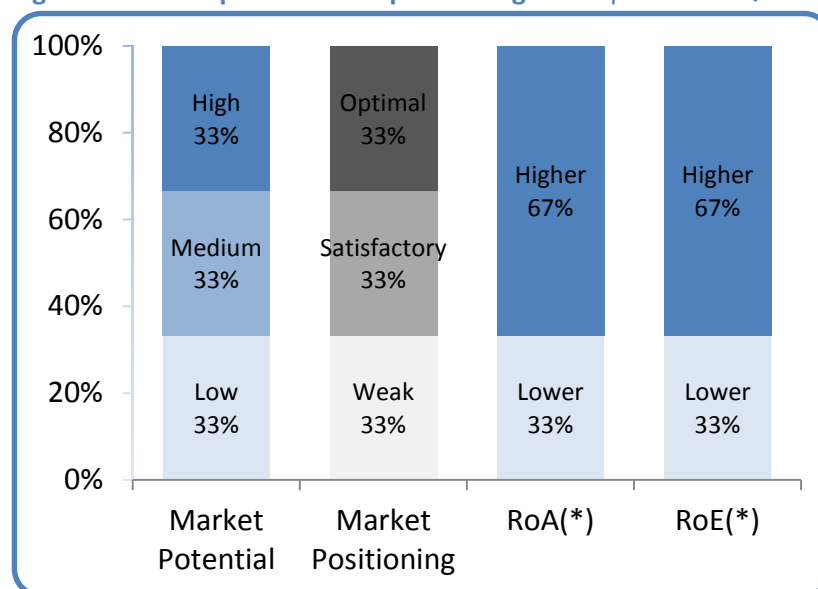
## 4. Results of the Bank Lending Survey:

### 4.1 Parent banks<sup>3</sup>

1. Groups operating in Poland tend to see their global operations as being in line with the overall set of groups included in the survey. In addition they seem to be less inclined to deleveraging, as the large majority of groups active in Poland signal that they intend to maintain a stable loan-to-deposit ratio over the next six months.

2. Parent banks operating in Poland show a strong commitment towards the region and are less likely to reduce – and more likely to maintain – their CESEE operations relative to the full sample. This is in line with the findings of the

**Figure 1. Market potential and positioning – see question A.Q13**



Source: EIB – CESEE Bank Lending Survey.

(\*) Return on assets (adjusted for cost of risk) compared to overall group operations; return on equity (adjusted for cost of equity) compared to overall group ROE.

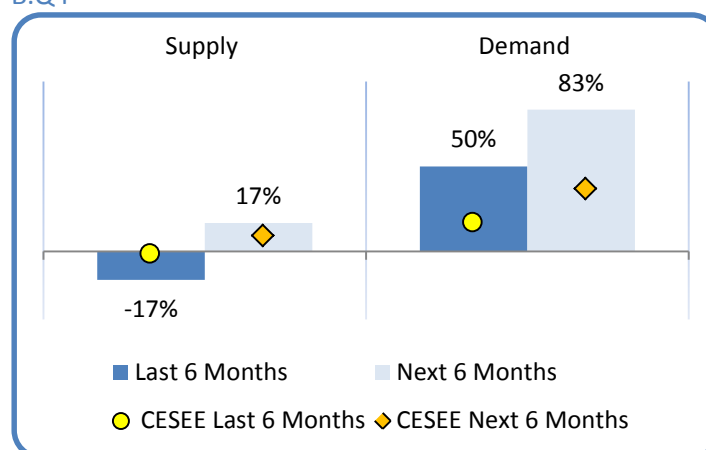
March 2014 survey. In addition, the majority of groups operating in Poland still consider their CESEE operations to be more profitable than their group's global operations. Parent banks consider the Polish market to be among the most attractive within CESEE, confirming the results of the previous surveys. Only 33 percent of the groups operating in Poland find that the country's market potential is low. This, however, represents a small downward revision of the assessment of Poland's market potential, in line with the overall trend in the region. Risk-adjusted returns on equity and assets are also believed to be among the highest in the region. Overall, parent banks operating in Poland seem to be relatively satisfied with their current market positioning (Figure 1).

<sup>3</sup> In this subsection results refer to the views of parent banks. Results on market positioning and potential refer to questions addressing behaviour within a specific market, whilst the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents' views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a specific country.

## 4.2 Local banks/subsidiaries

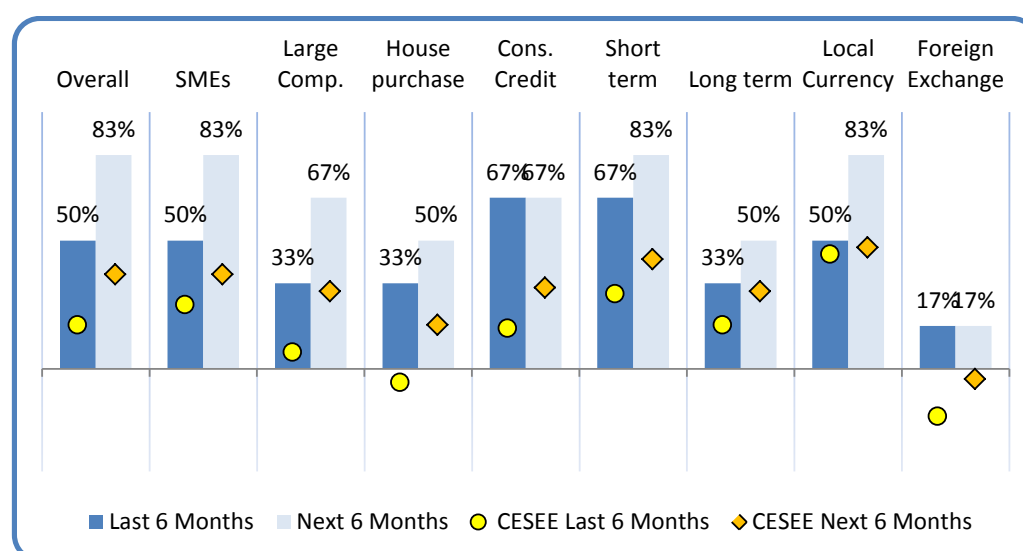
- The signs of economic recovery are reflected in the general view of Polish banks on future credit activity. The sluggish overall credit demand observed a year ago has been improving rather rapidly over the last six months and is likely to accelerate over the next six months by more than the CESEE average. Credit supply has still been in a mild tightening phase, and it is expected to ease in line with the CESEE region as a whole (Figure 2).
- Demand for credit picked up across the whole spectrum of products and segments over the last six months – including loans for house purchase.

**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



Source: EIB – CESEE Bank Lending Survey.

**Figure 3. Demand components – (net percentages; positive figures refer to increasing demand) – see question B.Q4**



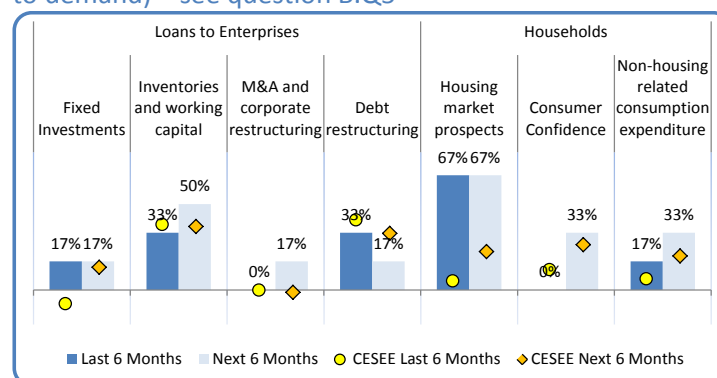
Source: EIB – CESEE Bank Lending Survey.

The reported increase has been much higher than the aggregate CESEE rebound. Looking ahead, financial institutions expect to face an even higher demand for credit across the board from wholesale clients, SMEs, consumer finance as well as loans for house purchases. The depicted trend in demand signals that the turning point in demand already announced in the March 2014 survey is becoming more solid and broadly based. As expected in the March 2014 release,

the survey also shows an increased demand for foreign currency-denominated lending – an important risk factor in CESEE in the past, especially in the case of loans granted to households or SMEs without offsetting incomes in foreign currency (Figure 3).

3. The individual factors contributing to credit demand provide stronger positive signals in Poland than in other economies within the CESEE region (Figure 4). In contrast to the CESEE aggregate, investments in Poland have been contributing positively to increases in demand

**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**

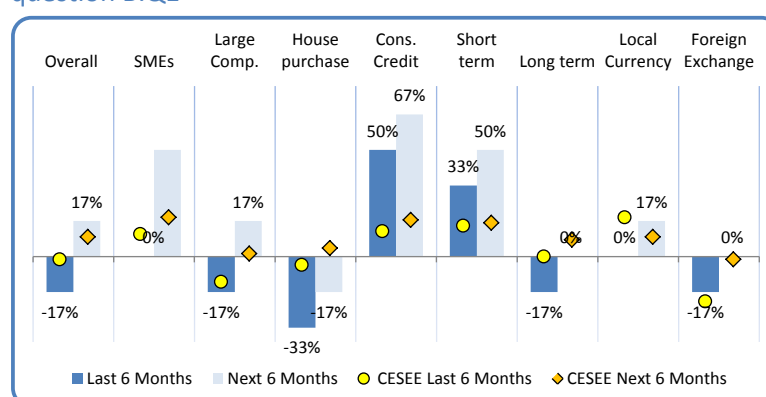


Source: EIB – CESEE Bank Lending Survey.

over the past six months. Working capital finance as well as debt restructuring have been and are expected to remain important drivers of corporate credit demand. The survey also highlights that borrowing for investment is becoming increasingly relevant. Household credit demand is likely to be largely driven by housing-related demand. The latter feature goes hand in hand with a rebound in demand for investment on the corporate side.

4. Credit supply conditions are also expected to ease in some segments, but to a lesser extent than demand conditions. As for households, the supply of consumer credit is expected to remain strong, while for housing finance, the conditions are unlikely to match the

**Figure 5. Supply components – credit standards (net percentages; positive figures refer to a positive contribution to supply) – see question B.Q1**



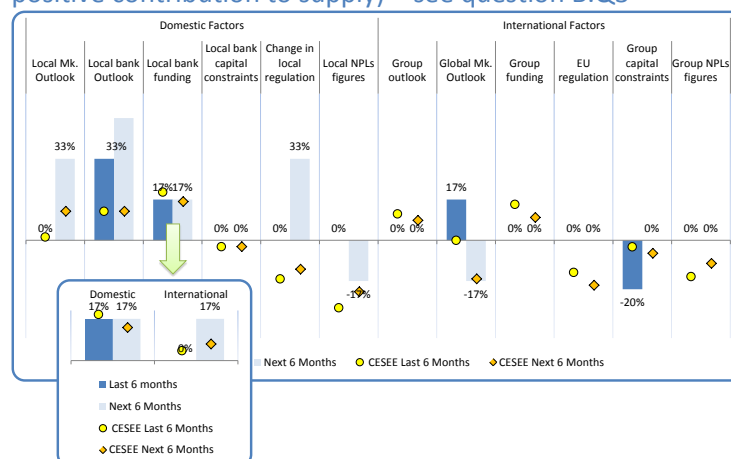
Source: EIB – CESEE Bank Lending Survey.

expected increase in demand. On the corporate side, however, the increasing propensity to borrow by larger corporates is not reflected in increased bank willingness to lend. Also, while banks expect the demand for longer-maturity

products to increase, this is unlikely to be matched by increased supply (Figure 5). The demand for foreign currency lending is projected to increase, but credit standards in this area are expected to be tightened.

5. Unlike many of their CESEE peers, Polish banks do not see international factors, such as EU regulation or group NPLs, as being an important impediment to credit supply. Group capital constraints are the only factor mentioned as a limitation to credit standards over the

**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**



Source: EIB – CESEE Bank Lending Survey.

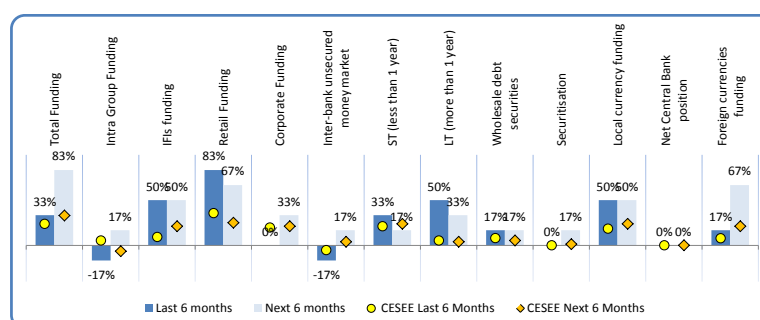
past six months (Figure 6). None of the domestic factors have created impediments to supply developments over the past six months. This signals the peculiarity of the Polish market compared to the CESEE region. Looking ahead, Polish subsidiaries remain rather optimistic. The local market and bank outlook, local funding and even local regulation are expected to exercise a positive contribution on supply. NPLs are expected to be contributing negatively to supply conditions, in line with the CESEE region.

6. SMEs faced slightly easier credit conditions than the corporate sector as a whole. However, the easing of supply constraints is unlikely to have fully matched the strong rebound in SME credit demand. In addition, some terms and conditions tightened in the segment, namely collateral requirements and the average size of the loans.



7. Funding has been in an easing phase and is expected to continue to be so (Figure 7). Banks indicate that they experienced strong inflows in the form of retail deposits and IFI funding. The

**Figure 7: Access to funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**

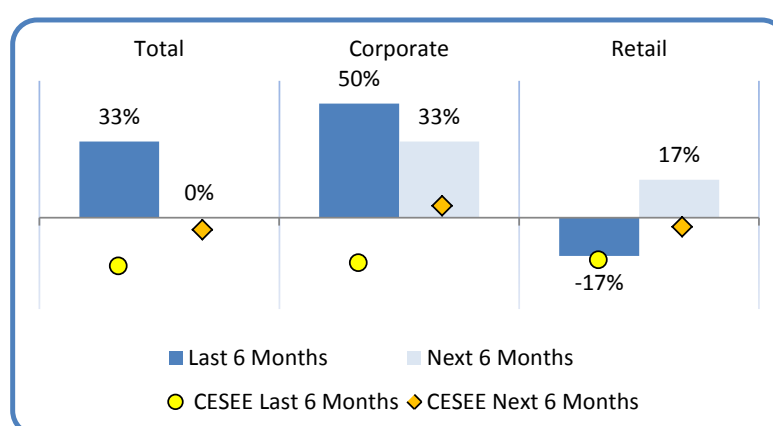


Source: EIB – CESEE Bank Lending Survey

increased access to funding covered the entire maturity spectrum, but a particularly large increase was evident at the long end of the maturity curve. Intra-group funding declined, despite parent banks' highly positive assessment of the Polish market. Banks also increased their foreign currency funding, most likely on the back of an increased demand for foreign currency-denominated loans.

8. NPL figures in Poland have been described as improving. This confirms a trend already highlighted in the previous release of the survey. NPLs improved significantly on the corporate side, while retail NPLs continued

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.

to increase slightly. Asset quality in the household segment is not expected to deteriorate further over the next six months (Figure 8). Overall, the improved trend on NPLs is expected to level off over the next six months.



# Romania

## 1. Key statistics<sup>1</sup>

- Number of banks/subsidiaries participating in the survey: ten
- Approximate share of assets covered (as proportion of total assets): 66 percent
- Current level of NPLs as proportion of total loans: 22.3 percent (Q1 2014)
- Latest credit growth (yoy): -7.2 percent (Q1 2014)
- Loan-to-deposit ratio: 94 percent (Q2 2014)
- CAR: 15.5 percent (Q4 2013)

## 2. Key messages – *Credit quality concerns while demand strengthens*

### International groups' views:

- **Group strategies:** Banking groups operating in Romania do not differ significantly in terms of their global strategies from the pool of parent banks in the survey. Banking groups in Romania are equally likely to restructure their operations in general and are only marginally more likely to sell assets or branches of activities and to engage in further deleveraging activities in the period ahead.
- **Group assessment of positioning and market potential:** Despite comparably low (current) profitability, groups operating have a positive view of Romania's market potential. A majority of banking groups active in Romania still consider their market positioning as satisfactory, although there has been a sharp decline in this figure since the March 2014 survey. The majority of groups remain – if somewhat more tentative in their assessment than the overall sample – committed to the region.

### Subsidiaries'/local banks' views:

- While a substantial majority of subsidiaries operating in Romania reported **increased credit demand** over the past six months, **credit supply** has only **eased slightly**.
- **Credit supply:** In line with developments in the CESEE as a whole, banks expect credit standards to ease a little in Romania in the next six months, primarily on the back of consumer credit. The positive impact of domestic factors is expected to dominate, although it will be somewhat counteracted by the less positive effect of local bank capital constraints and funding.
- **Credit demand:** The trend of broadly strengthening demand across all product categories and maturities for loans in local currency is expected to continue.
- **Access to funding:** Subsidiaries signal an improving funding situation across most funding sources, which should continue over the next six months.
- **NPL figures:** Credit quality remains a concern, with the NPL ratio rising, although the decline in credit quality is expected to moderate in the next six months.

<sup>1</sup> Sources: The National Bank of Romania, Unicredit/Bank Austria and Raiffeisen Research.

### 3. Relevant macroeconomic and banking conditions<sup>2</sup>

- **Growth:** An abundant harvest and strong exports helped boost real GDP growth to nearly 5 percent in the second half of 2013. Full-year growth thus accelerated to 3.5 percent. As the contribution of agriculture normalises again and demand starts to shift towards the domestic side, growth in real GDP is expected to slow down to 2.5 percent in 2014 and 2.6 percent in 2015. The forecast figure for 2014 corresponds to the actual performance of the economy in the first half of the year.
- **Unemployment:** Both total and youth unemployment remained roughly unchanged in 2013 (7.3 percent and 23 percent, respectively). Only very marginal declines in unemployment are expected in 2014 and 2015.
- **Inflation:** Inflation came in at 3.2 percent in 2013, as price pressures slowed partly due to the very good harvest and a reduction in VAT on certain food products. After declining to historical lows in the first eight months of 2014 (1.3 percent on average) on the back of falling food prices, inflation is forecast to decelerate significantly in 2014. In 2015, however, inflation is expected to return to levels above 3 percent as domestic demand strengthens, base effects fade and the increase in the fuel excise tax introduced on 1 April kicks in.
- **External and public sector balance:** In 2013 Romania's current account deficit dropped quite significantly to around 1.1 percent of GDP and is expected to increase only gradually this year and next. Fiscal consolidation has continued under the umbrella of the EU-IMF precautionary assistance programme. The fiscal deficit thus amounted to 2.3 percent in 2013 and should continue to improve slightly in 2014 and 2015.
- **Banking sector:** The situation of the banking sector in Romania is mixed. On the one hand, after a particularly poor year in 2012 banks' profitability turned positive again in 2013 and strengthened further in early 2014. Capitalisation of banks is also good (CAR: 15.5 percent in Q4 2013). On the other hand, withdrawals of parent funding in 2013 meant a substantial increase in the need for banks to rely on local funding. Also, asset quality is still poor (NPLs: 22.3 percent in Q1 2014). And, in addition, while the share of FX loans decreased somewhat recently, it remains a source of concern as more than two out of three loans are still denominated in a foreign currency.
- **Rating:** Romania is currently rated by Moody's (Baa3), Fitch (BBB-) and S&P (BB+).

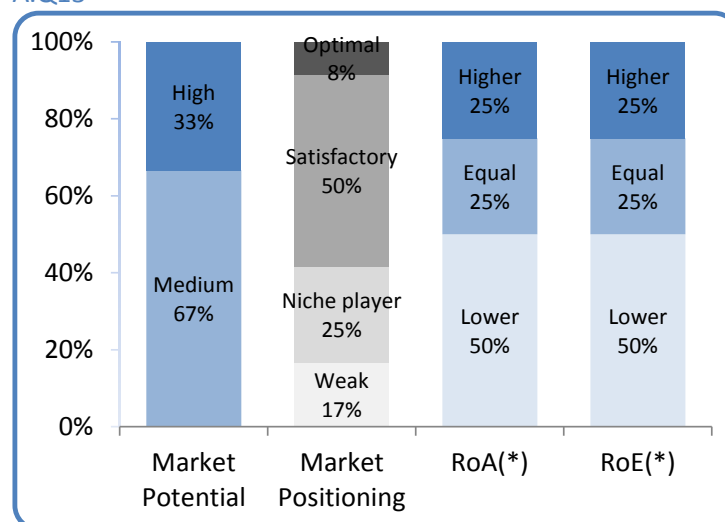
<sup>2</sup> Sources for the macroeconomic data: European Commission. Sources for the banking data: European Commission, Unicredit/Bank Austria and IMF.

## 4. Results of the Bank Lending Survey:

### 4.1 Parent banks<sup>3</sup>

- Banking groups operating in Romania do not differ significantly in terms of their global strategies from the pool of parent banks in the survey. While they are equally likely to restructure their operations in general, they are somewhat more likely to sell assets or branches of activities. But the differences are rather small. Also deleveraging activities in Romania correspond roughly to the overall sample, as 50 percent of banking groups operating in Romania expect reductions in their loan-to-deposit ratios over the next six months, compared with 47 percent for the international banks surveyed overall.

**Figure 1. Market potential and positioning** – see question A.Q13



Source: EIB – CESEE Bank Lending Survey.

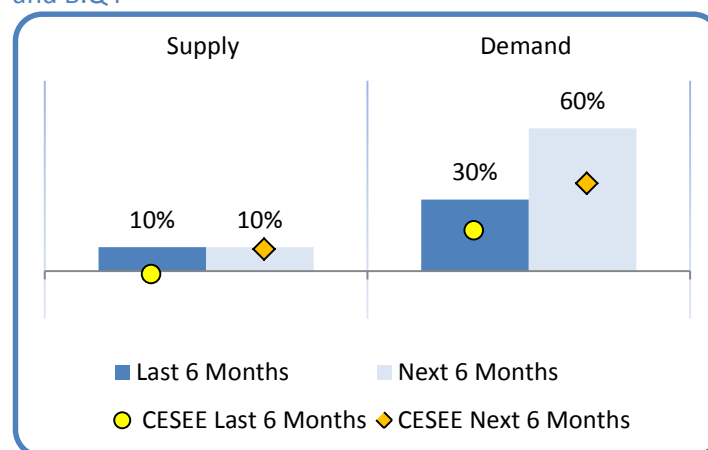
- Parent banks operating in Romania have a fairly positive view of the Romanian market: all believe that market potential is ‘high,’ or at least ‘medium’ (Figure 1). However, while in the last survey round three out of four banks considered their market positioning as ‘optimal’/‘satisfactory,’ currently it is less than 60 percent. This deterioration in satisfaction with their market position may be related to subpar profitability. For the past six months, 60 percent of parent banks active in Romania report lower profitability compared to their overall group profitability. This is a significantly higher proportion than for the CESEE region as a whole. Therefore, when it comes to plans about future activities, the picture differs from that in the CESEE region as a whole. In the latter, one third of banks plan to maintain, one third to expand (at least selectively) and one third to reduce operations selectively in the long run. In contrast, only 20 percent of parent banks operating in Romania plan to maintain the same level of operations, while half of the remainder will selectively reduce operations and the other half (at least selectively) expand them.

<sup>3</sup> In this subsection results refer to the views of parent banks. Results on market positioning and potential refer to questions addressing behaviours within a specific market, while the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents’ views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a specific country.

## 4.2 Local banks/subsidiaries

1. A significant majority of subsidiaries operating in Romania reported an increase in aggregate demand for loans over the past six months. Over the next six months, this positive trend is expected to continue, and even to gather momentum (mirroring similar, although less pronounced, developments at the CESEE level). As for credit supply, the subsidiaries reported a slight turnaround in the past six months to an easing phase which should continue at a hesitant pace over the coming six months (Figure 2).

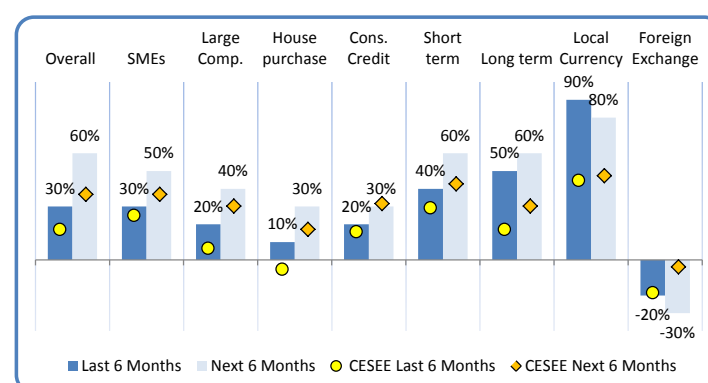
**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



Source: EIB – CESEE Bank Lending Survey.

2. Demand for loans has been on an upward trend across all the different products (Figure 3). On the side of corporate loans, a large perceived increase came from SMEs and to a slightly smaller extent from large corporates. In the retail sector, demand strengthened, particularly for consumer credit, while the increase has been less pronounced for mortgages. While there has not been a big difference in the increase in demand with respect to different maturities, in terms of currency denomination clients have been asking in particular for loans in local currency while demand for FX loans has weakened. The trend of broadly strengthening demand across all product categories and maturities for loans in local currency is expected to continue over the next six months.

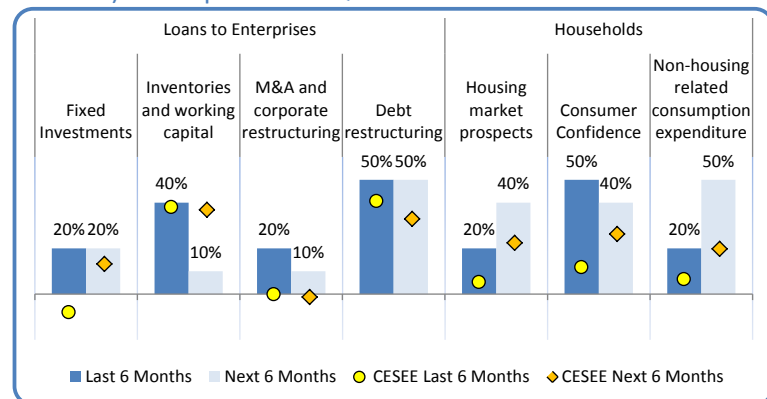
**Figure 3. Demand components – (net percentages; positive figures refer to increasing demand) – see question B.Q4**



Source: EIB – CESEE Bank Lending Survey.

3. In terms of the main drivers of credit demand, Figure 4 shows that all factors, in particular debt restructuring, inventories and working capital, have made a positive contribution to demand in the corporate sector in the last six months. Also on the household side, all factors (housing market prospects, non-housing-related consumption expenditure and particularly consumer confidence) contributed positively to the demand for loans. All drivers of demand in both the corporate and household segment are expected to continue to make a positive contribution in the period ahead. However, while the positive impact of inventories and working capital on corporate credit demand will weaken, in the household segment credit demand should rise even more strongly than thus far on the back of housing market prospects and non-housing related consumption expenditures.

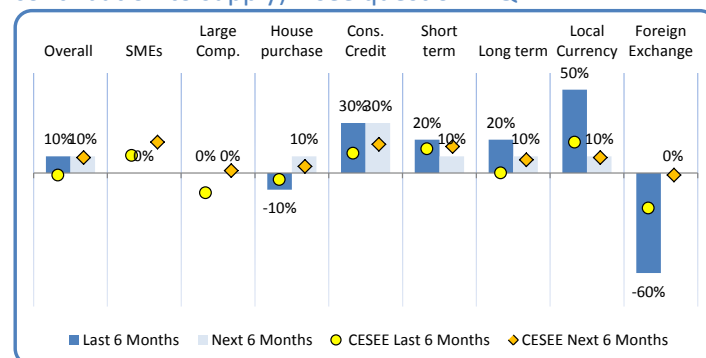
**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**



Source: EIB – CESEE Bank Lending Survey.

4. In line with expectations voiced six months ago supply (credit standards) in Romania turned from a tightening phase to slight easing over the past six months. This was mainly driven by consumer credits, for which the loosening of credit standards more than compensated some slight tightening in the mortgage area. It is also interesting to note that credit standards for FX loans have tightened significantly, which to some extent explains the decrease in demand for loans denominated in foreign currency. Looking ahead, in line with developments in the CESEE as a whole, in Romania too credit standards are set to ease a little in the next six months, again primarily on the back of consumer credits (Figure 5).
5. Both domestic and international factors played a role in determining supply conditions in the last six months, although the latter only marginally (Figure 6). Among the domestic factors, tightening pressures on credit standards exerted

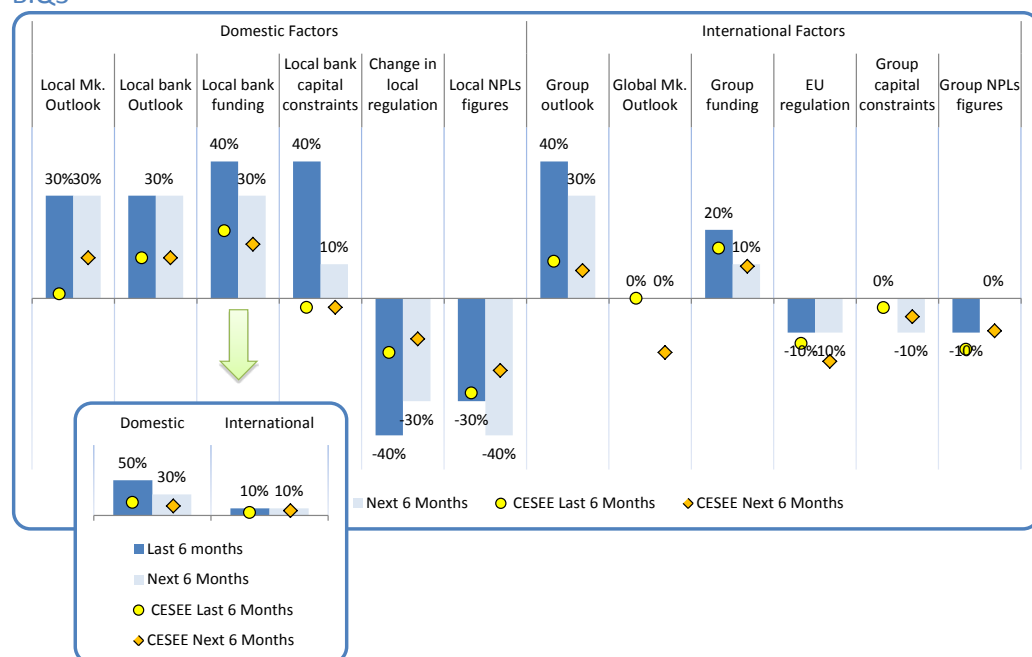
**Figure 5. Supply components – credit standards (net percentages; positive figures refer to a positive contribution to supply) – see question B.Q1**



Source: EIB – CESEE Bank Lending Survey.

by local regulation and NPLs were more than offset by the other factors, particularly local bank funding and capital constraints. Among the international factors, the easing effect exerted by group outlooks and funding was counteracted by EU regulation and group NPLs. Looking ahead, the picture is likely to remain broadly unchanged, although the positive impact of domestic factors is expected to weaken somewhat, particularly given the less positive effect of local bank capital constraints and funding. At the same time, local NPL figures are likely to weigh more on supply conditions.

**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**



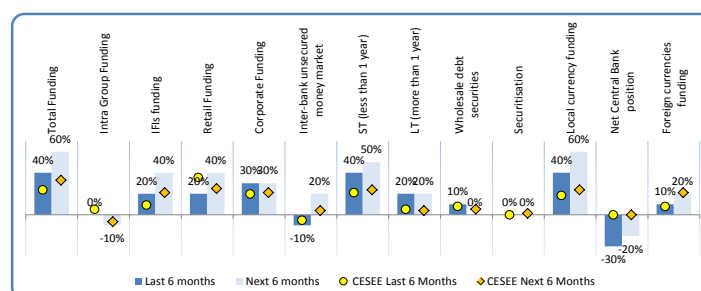
Source: EIB – CESEE Bank Lending Survey.

6. Supply and demand in the SME segment in Romania are roughly in line with the aggregate figures. While supply conditions have remained unchanged, credit demand has eased over the last six months. Looking ahead, supply conditions are set to stay stable for the SME sector in Romania, whereas they should ease somewhat in the CESEE region as a whole. In contrast, demand is expected to pick up rather strongly, in line with the aggregate. Margins charged on SME loans have stabilised recently but other conditions, including average loan size, maturity or collateral requirements, have improved. Looking ahead, almost all supply conditions for the SME segment are expected to remain unchanged, broadly in line with the CESEE aggregate.



7. Subsidiaries' access to funding has improved in Romania over the past six months, in line with the dynamics at the CESEE regional level. This has been driven primarily by improvements in corporate funding and, to a lesser extent,

**Figure 7: Access to Funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**



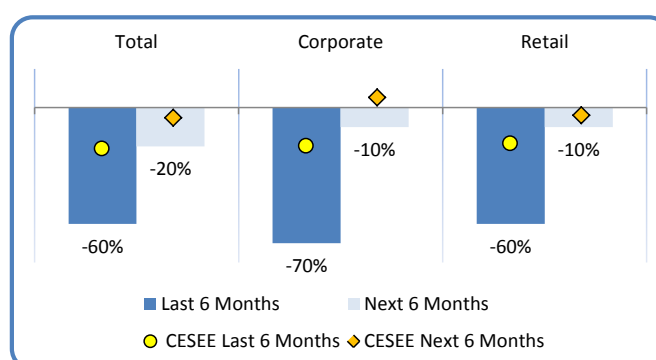
Source: EIB – CESEE Bank Lending Survey.

- Over the next six months access to funding is expected to ease across the board, except for intra-group funding, which is expected to contribute slightly negatively to aggregate access to funding.

8. NPL ratios are reported to have worsened again over the past six months – with a more pronounced deterioration in the corporate sector than in the retail sector (Figure 8). Over

the next six months, NPLs are likely to continue to increase, although the decline in credit quality is expected to moderate in both segments. For the CESEE as a whole a similar development is expected, although the overall NPL deterioration

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.

there is likely to be less pronounced than in Romania due to a slight improvement in credit quality in the corporate sector.



# Serbia

## 1. Key statistics<sup>1</sup>

- Number of banks/subsidiaries participating in the survey: eight
- Approximate share of assets covered (as proportion of total assets): 50%
- Current level of NPLs as proportion of total loans: 23% (Q2 2014)
- Latest credit growth (yoy): -2.8% (August 2014)
- Loan-to-deposit ratio: 134.3% (early 2014)
- CAR: 21% (end-June 2014)

## 2. Key messages - *Deteriorating market conditions and credit quality lead to a sharp tightening of supply conditions.*

### International groups' views:

- **Group strategies:** Cross-border banks operating in Serbia continue their deleveraging and report strategic restructuring plans and expected sales of assets at the global level in line with the whole sample of international banks.
- **Group assessment of positioning and market potential:** Groups show increased intentions to reduce operations in CESEE region. Market potential and positioning have been deteriorating in Serbia: fewer banks than in March 2014 are broadly satisfied with their current market positioning and more banks assess Serbia's market potential as low. A large number of groups describe the market as providing lower returns than the groups' other operations.

### Subsidiaries'/local banks' views:

- **Credit supply** has been tight over the past six months, primarily in the corporate sector (including SMEs) and with regard to loans for house purchases. Credit standards are not expected to change much over the next six months. Tight supply conditions are determined mainly by domestic factors, with the local market outlook and NPLs as key constraining factors. Group NPLs have also constrained credit standards.
- **Demand for loans** has rebounded. It is expected to continue to increase, albeit at a lower rate. Working capital and debt restructuring are described as the main positive contributors to credit demand conditions.
- **Access to funding:** Banks record access to funding as being on an easing trend and expect it to continue to ease. Long-term funding, however, has become harder to get
- **NPL figures** deteriorated further. However, a mild improvement is expected in the next six months.

<sup>1</sup> Sources: European Commission, National Bank of Serbia and Unicredit/Bank Austria.

### 3. Relevant macroeconomic and banking conditions<sup>2</sup>

- **Growth:** After a recession in 2012, a recovery started in 2013. However, the economy contracted in the first and second quarters of 2014 (-1.1 percent yoy) on the back of negative dynamics in household consumption and subdued government consumption – due to restrained government spending. Heavy floods had a negative impact on output dynamics in 2014. Investment also continued to contract (-6.3 percent yoy). In contrast, exports continued to support growth, driven by manufacturing and agricultural exports primarily to the EU. Real GDP is forecast to grow by roughly 1 percent in 2014.
- **Unemployment:** Unemployment continued to remain high and currently stands above 20 percent according to the Labour Force Survey. The employment rate continued to contract. In line with the bleak labour market situation, gross wages declined in real terms for the period January to May 2014 compared to the previous year.
- **Inflation:** Headline inflation was 2.1 percent yoy in May 2014, well below the central bank target. Dampened food prices and weak domestic demand are the main factors behind these subdued inflation developments.
- **External and public sector balance:** The current account deficit continued to fall in 2014. Exports denominated in euro increased at double-digit rates until early 2014, but have since decelerated rather abruptly. Imports continued to decline in response to weak internal demand. Public debt has been increasing and stood at 64 percent of GDP at end-July 2014. The fiscal deficit widened in the first half of 2014, against a 5.0 percent deficit reported in 2013.
- **Banking sector:** The banking system continued to be under stress. Bank profitability registered negative returns on assets and equity in 2013. However, the system turned profitable again in early 2014, while still remaining below average pre-crisis profitability levels. The level of capitalisation for the entire banking sector (CAR 21 percent end-June 2014) exceeds the regulatory minimum of 12 percent. NPLs have been increasing sharply and rose from 11.3 percent in 2008 to 23 percent in Q2 2014 – a new historical peak. The loan-to-deposit ratio stood at 134.3 percent in early 2014. Bank lending continued to deteriorate further, falling 2.8 percent yoy in August 2014, with corporate lending contracting most. Growth in local deposits has been rather robust over the last three years, and also continued in 2014, allowing significant deleveraging. This has partially offset the reduction of cross-border assets allocated to Serbian subsidiaries. The gross cross-border external position of BIS reporting banks vis-à-vis other banks and all sectors was negative in Q1 2014 and also in 2013.
- **Rating:** Serbia is currently rated by Moody's (B1, stable), S&P (BB-, negative)

<sup>2</sup> Sources for the macroeconomic data: European Commission. Sources for the banking data: European Commission, National Bank of Serbia and Unicredit/Bank Austria.

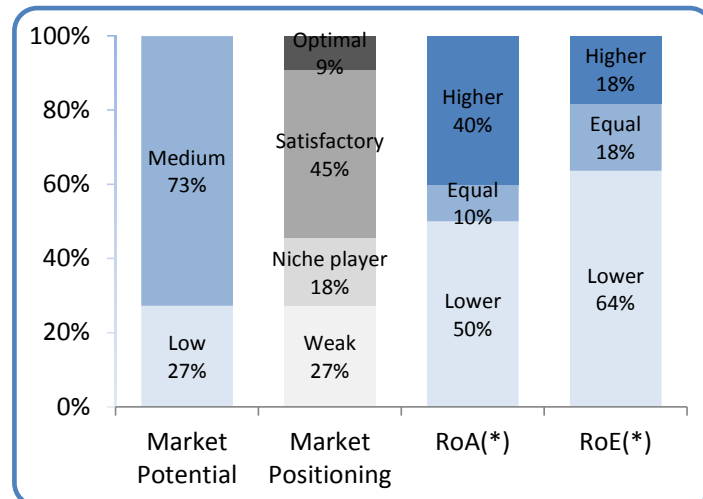
and Fitch (B+, stable).

## 4. Results of the Bank Lending Survey:

### 4.1 Parent banks<sup>3</sup>

1. The views of the parent banks operating in Serbia are in line with the overall sample of parents included in the survey, reporting similar intentions on strategic restructuring plans, as well as rather high activity in terms of current and expected sales of assets to increase their capital ratios at the global level. Groups operating in Serbia have also expressed the same likelihood of raising capital on the market as the whole set of groups included in the survey.

**Figure 1. Market potential and positioning – see question A.Q13**



Source: EIB – CESEE Bank Lending Survey.

(\*) Return on assets (adjusted for cost of risk) compared to overall group operations; return on equity (adjusted for cost of equity) compared to overall group ROE.

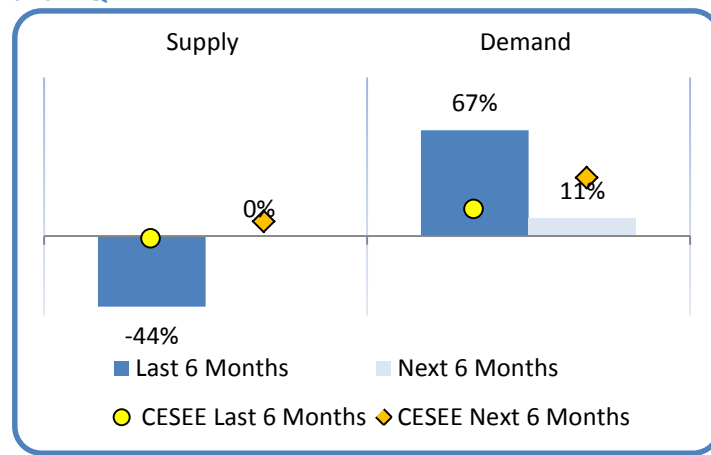
2. Groups operating in Serbia show rather clear intentions to reduce operations in CESEE compared to other groups operating in the CESEE region as a whole. Consistent with this, the profitability of groups operating in Serbia is expected to be lower at the CESEE level than the full sample of groups operating in the region. Roughly 50 percent of the banks operating in Serbia are fairly satisfied with their current market positioning (down from 75 percent reported in the March 2014 survey) and 73 percent regard the Serbian market's potential as medium. Last but not least, between 50 and 60 percent of the groups describe the market as having lower returns (i.e. ROA and ROE adjusted for the cost of capital and cost of equity) than the groups' global operations (Figure 1). All in all, this evidence suggests relatively lacklustre prospects for the Serbian banking sector.

<sup>3</sup> In this subsection results refer to the views of parent banks. Results on market positioning and potential refer to questions addressing behaviours within a specific market, whilst the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents' views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a specific country.

## 4.2 Local banks/subsidiaries

1. Supply factors were primarily behind the still negative credit growth over the past six months. Credit standards were described as being more restrictive than the CESEE aggregate (Figure 2). While supply conditions were described as still being in a tightening phase, demand for loans was reported to be rebounding, turning out more positive than the CESEE aggregate. Over the next six months demand conditions are expected to continue to increase, albeit at more contained levels, while supply is expected to take a neutral stance. This contrasts with an expected mild easing of credit standards at CESEE level.

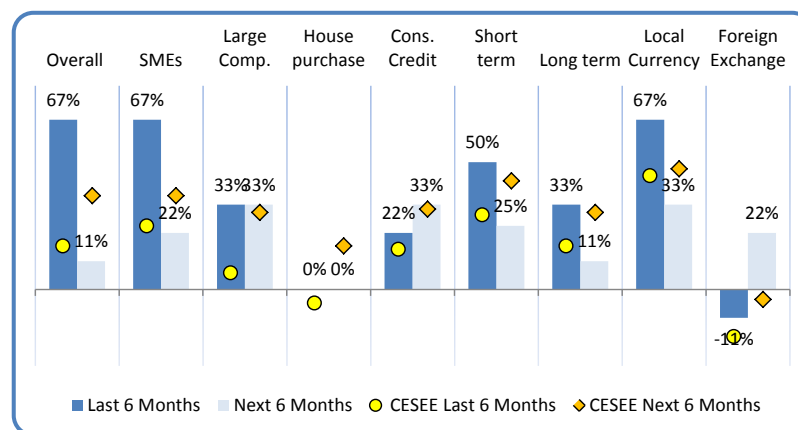
**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



Source: EIB – CESEE Bank Lending Survey.

2. Demand for loans has rebounded sharply (Figure 3), in line with the expectations reported in the March 2014 survey and also breaking a long trend of contracting demand conditions. It has turned positive across different products and maturities over the past six months, even more so than the whole CESEE region.

**Figure 3. Demand components - (net percentages; positive figures refer to increasing demand) – see question B.Q4**

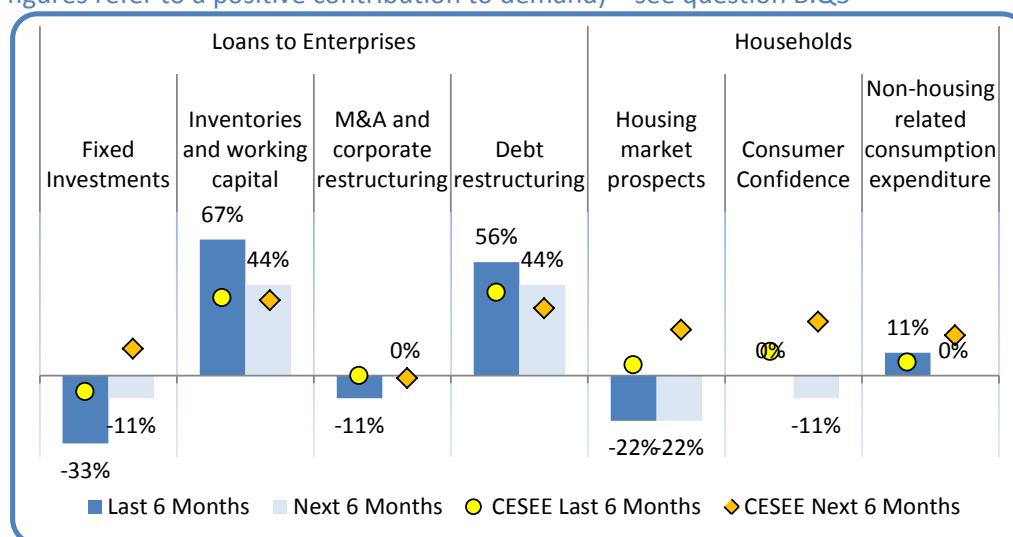


Source: EIB – CESEE Bank Lending Survey.

Demand from corporates (including SMEs) has been particularly strong. Demand for loans for house purchase has been rather subdued, in line with a gloomy employment situation and still contracting real salaries. Aggregate demand for loans is expected to continue to increase across different products and maturities over the next six months in line with the CESEE region – thus reporting lower increases in Serbia than over the past six months. On the other hand, demand for loans for house purchase is expected to remain limited.

3. Figure 4 shows that working capital and debt restructuring were the two main strong positive contributors to demand conditions over the past six months and that non-housing-related consumption made a mild positive contribution.

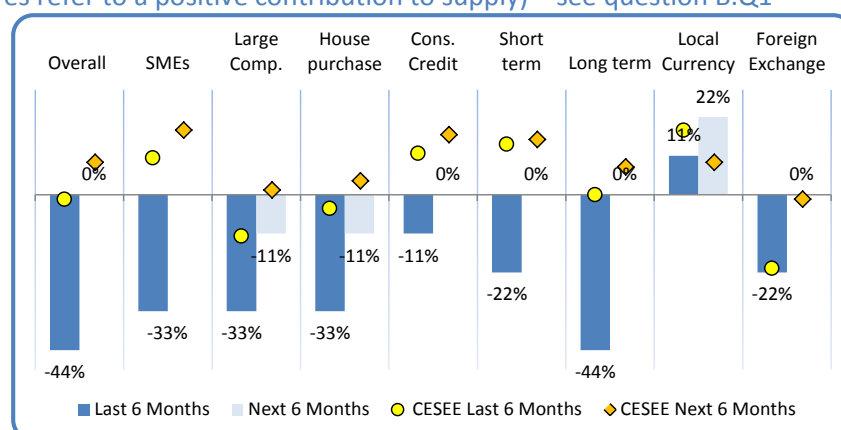
**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**



Source: EIB – CESEE Bank Lending Survey.

However, these were offset to some extent by the negative influence of housing market conditions and investment. Looking ahead, the same factors are perceived as exerting a positive or negative contribution to demand, with the consumer/household contribution to demand being assessed to be bleaker than in the CESEE region.

**Figure 5. Supply components – credit standards (net percentages; positive figures refer to a positive contribution to supply) – see question B.Q1**



Source: EIB – CESEE Bank Lending Survey.

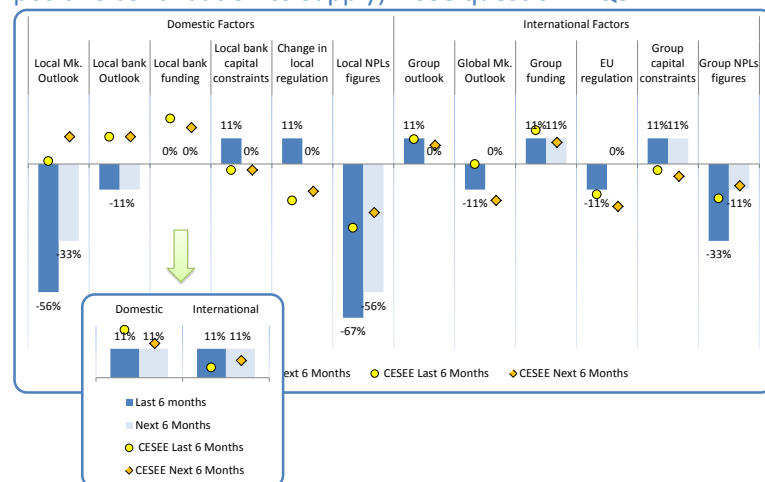
4. Credit standards have been tight over the past six months (Figure 5), contrary to positive expectations in the March 2014 survey. Supply conditions have

worsened over the past six months compared to a year ago. The gloomier supply conditions were linked to a tightening of standards, primarily in the corporate sector (notably the SMEs segment), and also with regard to loans for house purchase. Credit standards are not expected to ease over the next six months, in contrast to the trend expected for the broad CESEE region. These standards are expected to turn neutral for all segments, except for large corporates and house purchases, which should remain negative. Some banks' terms and conditions are expected to tighten further, especially collateral requirements for companies (including SMEs).

5. Both domestic and international factors have played a role in determining credit supply conditions in Serbia (Figure 6). Domestic factors seem to have had a more prominent role in limiting supply expansions than in the overall CESEE region.

The market outlook and local NPL figures were the key constraining factors, as in the March 2014 survey. NPLs in particular are reported as a key constraining factor in Serbia, even more so than for the CESEE aggregate. On the

**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**



Source: EIB – CESEE Bank Lending Survey.

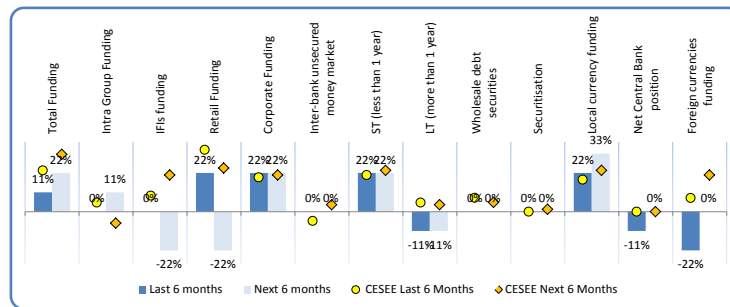
other hand, the regulatory environment does not seem to be perceived as a limiting factor, as already evidenced in the March 2014 release. NPLs at the group level are mentioned as the main international factor, with a clear negative effect on credit supply conditions over the past six months. Over the next six months all factors are expected to continue to exercise a similar impact as in the past on supply conditions, especially NPLs at the domestic level.

6. With regard to the SME segment, supply (credit standards) has been described as being in a robust tightening phase, whilst demand for loans has rebounded rather sharply. Looking ahead, demand is expected to continue to expand and supply is expected to turn neutral. Generally supply conditions for SMEs are expected to remain more restrictive than in the CESEE region. In particular, collateral requirements for SMEs have been tightening substantially in Serbia over the past six months.



7. Local funding was not reported as a constraining factor on supply conditions, so access to funding has been on an easing trend across the whole range of products and segments (Figure 7), albeit at more

**Figure 7: Access to funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**

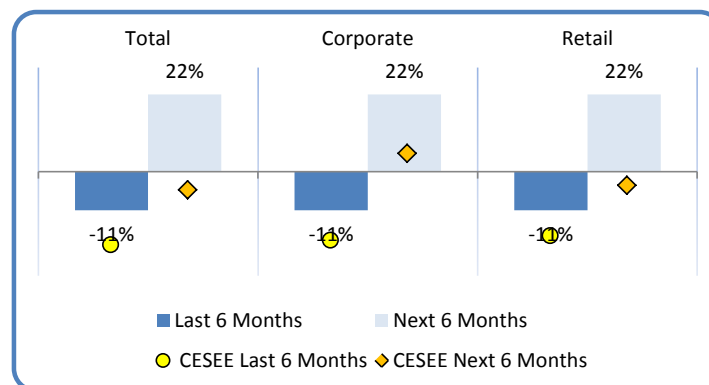


Source: EIB – CESEE Bank Lending Survey.

contained levels than the March 2014 release. Retail and corporate funding has been easing. On the other hand, long-term funding has been marginally decreasing, rolling back the upturn described in the previous releases of the survey. Intra-group funding did not decrease: this is in line with the information derived from the factors affecting supply, according to which intra-group funding did not exercise a negative contribution. Looking ahead, funding conditions are still described as easing, with most factors contributing positively, including intra-group funding. Retail and long-term funding are expected to be reduced over the next six months.

8. Aggregate NPL figures deteriorated further. NPLs in the household sector as well as in the corporate sector have followed the same negative trend over the past six months (Figure 8). A mild improvement is expected over the next six months.

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.



# Slovakia

## 1. Key statistics<sup>1</sup>

- Number of banks/subsidiaries participating in the survey: five
- Approximate share of assets covered (as proportion of total assets): 75 percent
- Current level of NPLs as proportion of total loans: 4.7 percent (July 2014)
- Latest credit growth (yoy): 7.9 percent (July 2014)
- Loan-to-deposit ratio: 94 percent (July 2014)
- CAR: 17.48 percent (Q1 2014)

## 2. Key messages – *Credit demand rebounding while supply conditions remain restrained*

### International groups' views:

- **Group strategies:** Banking groups operating in Slovakia are generally more positive concerning their group strategies than the overall sample of banks included in the survey. The majority of banks do not plan any additional strategic operations or further deleveraging.
- **Group assessment of positioning and market potential:** Parent banks operating in Slovakia remain strongly committed to the CESEE region, in which all banks see medium or high market potential. Some 60 percent of banks expect profitability in Slovakia to be higher than the average for group operations. Parent banks are generally satisfied with their current positioning in the market, although this view is not now held quite so strongly.

### Subsidiaries'/local banks' views:

- **Credit supply** has eased for SMEs and the large corporate segments over the last six months. The easing of credit standards was supported by domestic factors such as the local market and bank outlook, as well as local bank funding. In contrast, capital constraints and local regulation put a damper on supply conditions. Unlike much of the CESEE region, credit standards in Slovakia are expected to tighten across the board over the next six months, except for SMEs.
- **Demand for loans** increased broadly across all market segments, but particularly for consumer credit. Looking ahead, banks expect a further strengthening of demand led by consumer and SME credit.
- **Access to funding:** Subsidiaries reported an improvement in funding conditions over the last six months on account of better access to intra-group, retail and corporate funding. Access to funding is expected to ease further.
- **NPL figures** are rather low, but they have increased in both the corporate and retail sectors over the past six months. NPLs are expected to level off in both market segments in the next six months.

<sup>1</sup> Sources: National Bank of Slovakia, European Commission and Unicredit/Bank Austria based on NBS data.

### 3. Relevant macroeconomic and banking conditions<sup>2</sup>

- **Growth:** Economic growth slowed to 0.9 percent in 2013, mainly as a result of falling gross fixed capital formation and a decreasing, albeit still positive contribution from net exports. In the first six months of 2014 growth accelerated to just over 2 percent and is expected to be about 2 percent for 2014 as a whole. In 2015 GDP growth should speed up further to approximately 3 percent. In contrast with the past few years, when net exports were the main driver of the economy, growth is expected to rebalance towards domestic demand. Both private and public consumption are expected to make a stronger contribution to growth, while gross fixed capital formation is projected to increase in 2014, after declining substantially for two consecutive years.
- **Unemployment:** The unemployment rate has stabilised at above 14 percent in recent years. As structural factors such as gaps in education and lack of mobility have a negative effect on labour market developments, the unemployment rate is forecast to decrease only gradually, to just under 13 percent over the medium term.
- **Inflation:** As a result of weak economic activity, declining energy prices and moderating growth in food prices, inflation dropped from 3.7 percent in 2012 to 1.5 percent in 2013. In the first eight months of 2014 inflation hovered at or slightly below zero in light of weak domestic demand as well as falling food and energy prices. However, inflation is expected to return to moderately positive territory later in the year and to come out at around 0.5 percent for 2014 as a whole. In 2015 inflation is forecast to increase to around 1.5 percent due to stronger domestic demand.
- **External and public sector balance:** Since 2012 the current account has been posting a surplus that is expected to be around 2.5 percent of GDP in the medium term. The budget deficit was reduced from 7.5 percent of GDP in 2010 to 2.8 percent of GDP in 2013 and is expected to remain at around this level for 2014-15. Public debt was 55 percent in 2013 and is forecast to increase slightly in the medium term.
- **Banking sector:** The entire banking sector is relatively well capitalised (CAR 17.48 percent in Q1 2014). NPLs are relatively low, at 4.7 percent in July 2014 although up from 2.5 percent in 2007. The loan-to-deposit ratio stood at 94 percent in July 2014, up from 72 percent in 2006. Lending growth has been moderate in the last few years, but seems to be picking up recently.
- **Rating:** Slovakia is currently rated by Moody's (A2), Fitch (A+) and S&P (A).

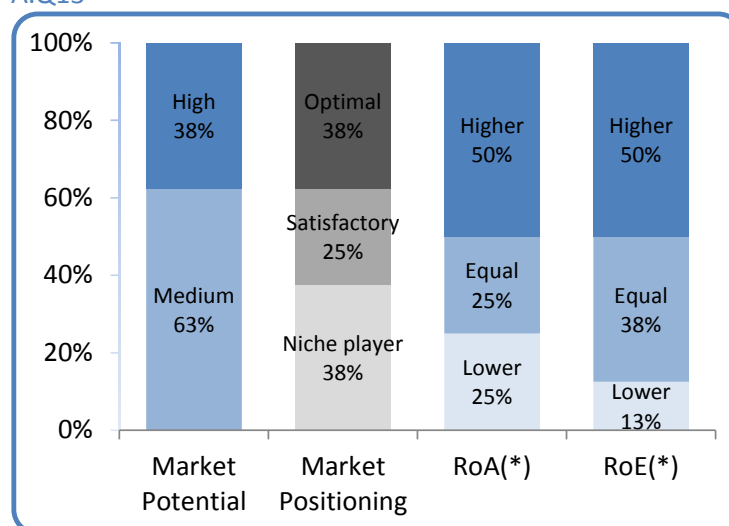
<sup>2</sup> Sources for the macroeconomic data: European Commission and IMF. Sources for the banking data: European Commission, National Bank of Slovakia and Unicredit/Bank Austria based on NBS data.

## 4. Results of the Bank Lending Survey:

### 4.1 Parent banks<sup>3</sup>

1. Parent banks operating in Slovakia are more positive than the overall sample of groups included in the survey. A large majority of parent banks are not planning additional strategic operations to raise capital. In general, banks do not expect further deleveraging at the group level, with 80 percent of them

**Figure 1. Market potential and positioning – see question A.Q13**



Source: EIB – CESEE Bank Lending Survey.

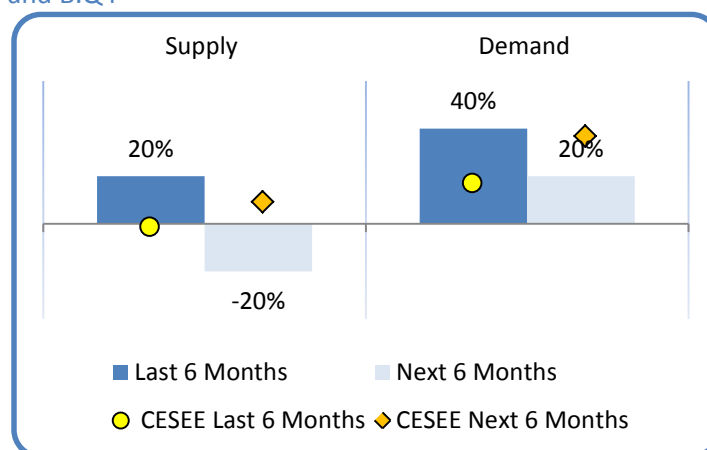
2. Parent banks operating in Slovakia remain strongly committed to the region, with none of them planning to reduce operations and 60 percent intending to expand business. Around 40 percent of banks reported higher profitability in the CESEE region than at the group level, but 60 percent expect higher profitability in the CESEE region in the next six months. Parent banks are satisfied with their market positioning in Slovakia, although their satisfaction has decreased quite significantly compared to the previous survey round. While in March 50 percent of banks indicated optimal positioning and a further 38 percent satisfactory positioning, most recently only 38 percent find their positioning optimal and 25 percent satisfactory (Figure 1). Nevertheless, banks maintain a positive view about market potential, with each bank reporting either medium or high potential (Figure 1).

<sup>3</sup> In this subsection results refer to the views of parent banks. Results on market positioning and potential refer to questions addressing behaviours within a specific market, whilst the other data (e.g. restructuring strategies, ROA, etc.) are derived results. These are obtained by filtering out from the parents' views for the CESEE region as a whole the views of those parents effectively operating in a particular country. This makes it possible to assess whether there is a divergent attitude of a sub-group of parents operating in a specific country.

## 4.2 Local banks/subsidiaries

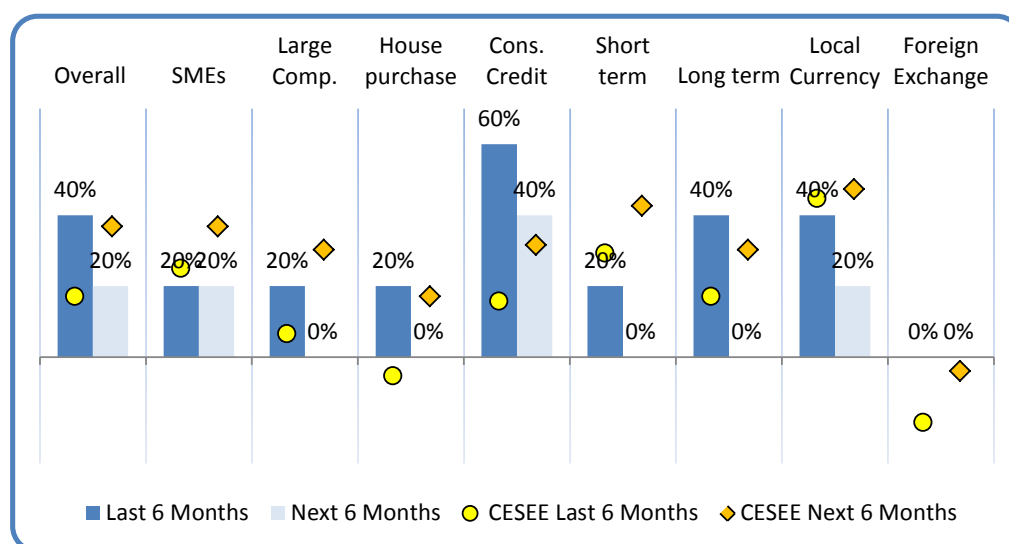
- Subsidiaries operating in Slovakia reported increasing demand and, to a lesser extent, also increasing supply over the last six months, which is a somewhat better development on both sides of the market than in the CESEE region as whole. Looking ahead, however, while the increase in demand is expected to continue – broadly in line with the expectations for the entire CESEE region – supply in Slovakia is predicted to tighten (Figure 2).

**Figure 2: Credit supply (credit standards) and demand conditions – net percentages; positive figures refer to increasing (easing) demand (supply) – see questions B.Q1 and B.Q4**



Source: EIB – CESEE Bank Lending Survey.

**Figure 3. Demand components - (net percentages; positive figures refer to increasing demand) – see question B.Q4**



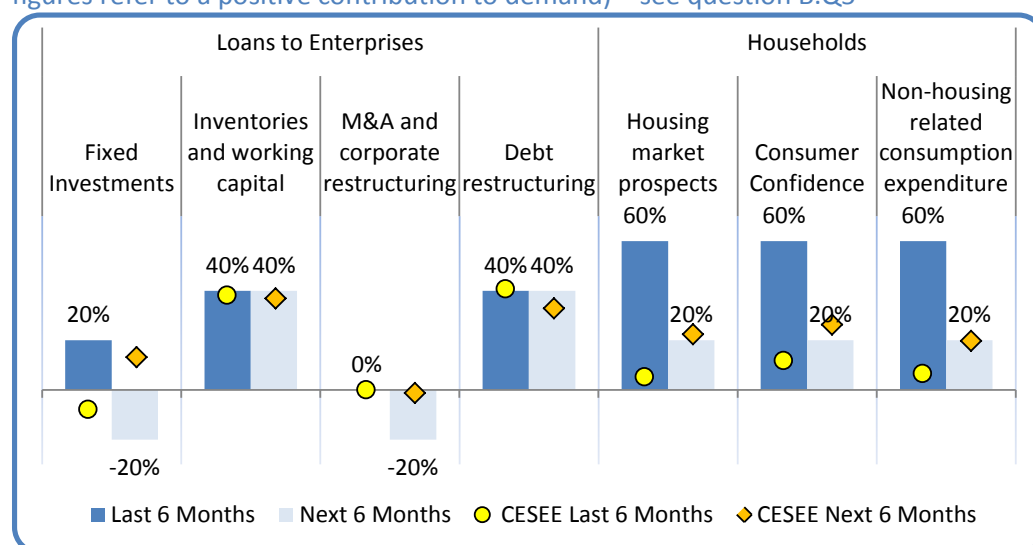
Source: EIB – CESEE Bank Lending Survey.

- The increase in overall demand was driven by all market segments but particularly by consumer credit. In terms of maturity and currency denomination, banks reported an increase in demand for short-term and local currency loans. Looking ahead, banks expect a further strengthening of demand led by consumer and SME credit. This is broadly in line with developments in the

CESEE region as a whole, although there the increase in demand is expected to be driven by all credit categories (Figure 3).

3. In the corporate segment fixed investment, inventories and working capital, as well as debt restructuring, contributed positively to demand. In contrast, M&A and corporate restructuring have made a neutral contribution over the last six months. Inventory, working capital and debt restructuring loans are expected to continue boosting credit demand over the coming period, while fixed investments, M&A and corporate restructuring will hold back demand for credit. In the household segment all factors contributed evenly to the support of credit demand and are expected to continue to do so in the six months ahead. The overall outlook in the household segment is similar to that of the CESEE region as a whole, while it is somewhat less favourable in the case of loans to enterprises (Figure 4).

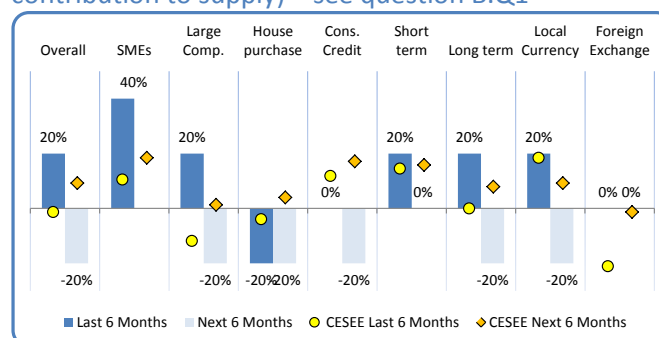
**Figure 4. Factors contributing to demand conditions – (net percentage; positive figures refer to a positive contribution to demand) – see question B.Q5**



Source: EIB – CESEE Bank Lending Survey.

4. Due to significantly eased credit standards for SMEs and large corporates, overall supply conditions also improved, despite some tightening in the household segment. This contrasts with the overall CESEE region, where credit standards have remained broadly unchanged over the last six months as a

**Figure 5. Supply components – credit standards (net percentages; positive figures refer to a positive contribution to supply) – see question B.Q1**

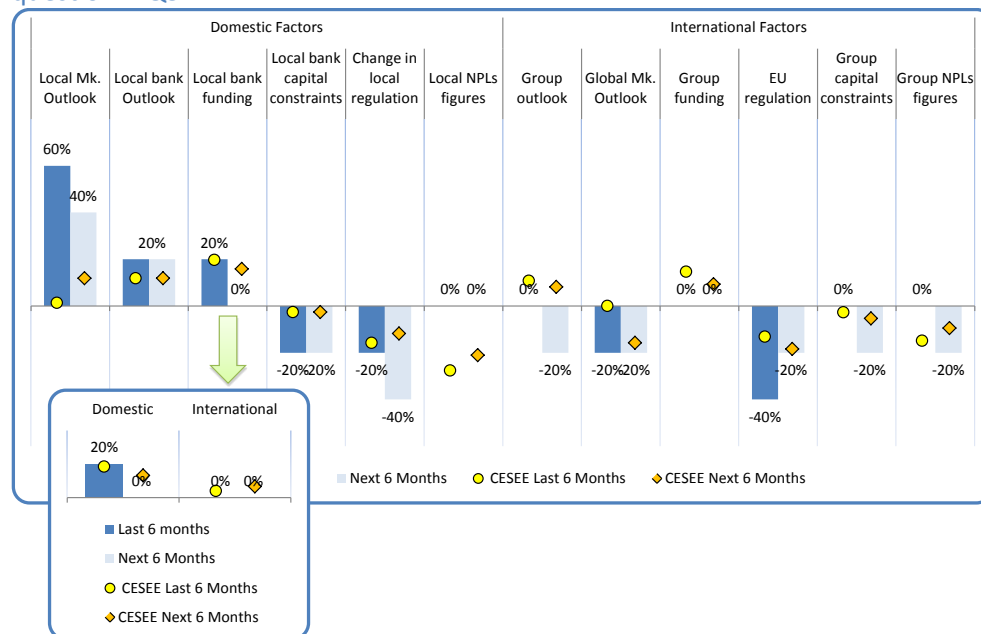


Source: EIB – CESEE Bank Lending Survey.

result of divergent developments in the SME and consumer credit segments on the one hand, and the large corporates and housing segments on the other. However, unlike in the CESEE region, credit standards in Slovakia are expected to tighten over the next six months, driven by all credit categories with the exception of SMEs, for which credit standards should be unchanged (Figure 5).

5. Standards for credit supply were supported by some domestic factors, such as the local market and bank outlook, as well as local bank funding. In contrast, capital constraints and local regulation put a damper on supply conditions. NPLs as well as international factors as a whole have played a neutral role over the last six months. Over the six months to come, a similar outcome is expected, not only for international but also for domestic factors. Regarding the latter, supportive development of the local market and bank outlook is expected to be counteracted by local regulation and capital constraints. While NPLs are not expected to contribute negatively to supply conditions in the coming months at the local level, they are set to do so at the group level. Indeed, most international factors are expected to constrain supply in the period ahead (Figure 6).

**Figure 6. Factors contributing to supply conditions (credit standards) – (net percentage; positive figures refer to a positive contribution to supply) – see question B.Q3**



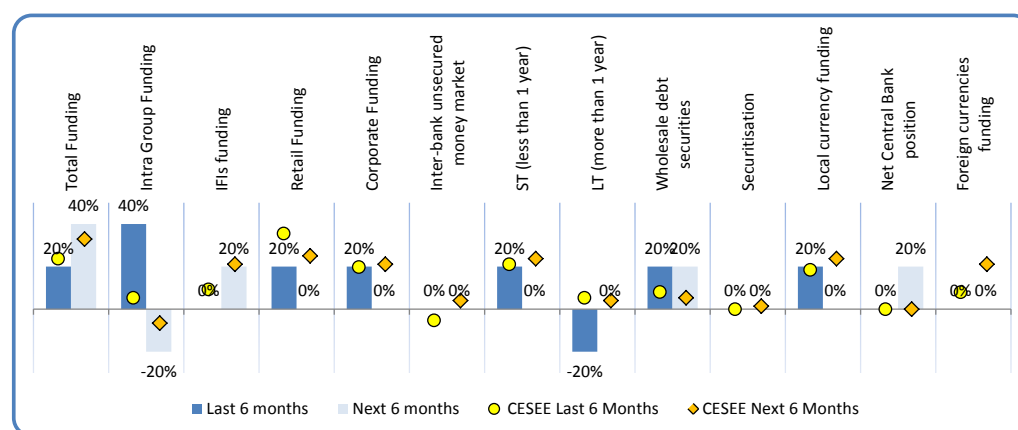
Source: EIB – CESEE Bank Lending Survey.

6. As regards SMEs, subsidiaries in Slovakia reported strengthening of demand and easing of credit standards over the last six months. Looking ahead, demand is expected to continue to increase, while basically all supply conditions, including interest rate margins, should remain unchanged and past and future demand developments are broadly in line with the CESEE region as a whole.



7. The overall funding situation of subsidiaries has improved in the last six months, mostly on account of better access to intra-group, retail and corporate funding. While conditions for short-term funding have eased, long-term funding became somewhat more difficult. Looking ahead, access to funding is expected to ease further, particularly as a result of IFI funding, although intra-group funding may become more problematic (Figure 7).

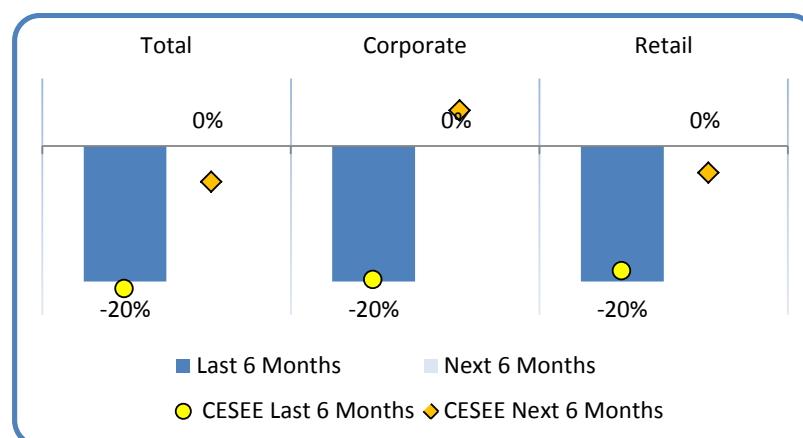
**Figure 7: Access to funding – (net percentage; positive figures indicate increasing access to funding) – see question B.Q7**



Source: EIB – CESEE Bank Lending Survey.

8. NPL ratios have continued to increase over the last six months, due to developments in both the corporate and retail sector. Looking ahead, NPLs are expected to level off in both

**Figure 8: Non-performing loan ratios – (net percentage; negative figures indicate increasing NPL ratios) – see question B.Q6**



Source: EIB – CESEE Bank Lending Survey.

loan segments, which is in contrast to the CESEE region as a whole, for which a slight majority of banks expect a further increase in NPLs in the next six months owing to deteriorating retail loans (Figure 8).



# The Questionnaire

**The questionnaire is divided into two parts:**

- **Part A addressed to parent banks**
- **Part B addressed to local/subsidiary banks**

## PART A

**A.Q1** - Strategic operations: Has your group conducted strategic operations to increase the capital ratio and/or will it be conducting strategic operations? If so, what type?

*(possible answers = yes; no)*

	LAST 6 months	NEXT 6 months
Strategic restructuring		
Sale of assets		
Sale of branches of activities		
Raising capital on the market		
State contribution to capital		

**A.Q2** - Group funding: Group's access to funding...

*(possible answers = decreased considerably; decreased somewhat; remained basically unchanged; increased somewhat; increased considerably)*

	<i>How has it changed over the last six months?</i>	<i>How do you expect it to change over the next six months?</i>
Total		
Retail (deposits and customer bonds)		
Corporate (deposits and customer bonds)		
Interbank market		
IFIs		
Wholesale debt securities		
Loans or credit lines from the central bank		
Securitisation		
Short-term funding (any source)		
Long-term funding (any source)		

**A.Q3** - Deleveraging – over the next six months, do you expect the loan-to-deposit ratio of your group to...

*(possible answers = decrease; remain stable; increase)*

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**A.Q4 – Longer-term strategic approach (beyond 12 months):** Looking at operations via subsidiaries in CESEE, your group intends to...

*(possible answers = reduce operations via subsidiaries; selectively reduce operations; maintain the same level of operations via subsidiaries; selectively expand operations via subsidiaries; expand operations via subsidiaries)*

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**A.Q5 - Profitability of the strategy in the CESEE region:** the contribution of activities in CESEE to total ROA of the group has/will...

*(possible answers = decreased considerably; decreased somewhat; remained basically unchanged; increased somewhat; increased considerably)*

	LAST 6 MONTHS	NEXT 6 MONTHS

**A.Q6 - Profitability of the strategy in the CESEE region:** ROA of your CESEE operations is higher than/lower than/equal to that for the overall group...

*(possible answers = lower; equal; higher)*

	LAST 6 MONTHS	NEXT 6 MONTHS

**A.Q7 - Group total exposure to CESEE: concerning cross-border operations in CESEE countries, your group did/intends to...**

*(possible answers = expand exposure; maintain the same level of exposure; increase exposure)*

	LAST 6 months	NEXT 6 months
Total exposure		
Exposure to subsidiaries - intra-group funding		
Exposure to subsidiaries – capital		
Direct cross-border lending to domestic clients, booked in the BS of the parent company		
MFIs - funding to banks not part of the group, booked in the BS of the parent		

**A.Q8 - How has FED tapering/emerging markets volatility impacted on your group's external exposure? How do you expect it to impact?**

	LAST 6 months	NEXT 6 months
Total exposure to emerging markets		
Total exposure to CESEE region		
of which:		
exposure to CESEE subsidiaries - intra-group funding		
exposure to CESEE subsidiaries - capital		
direct cross-border lending to CESEE domestic clients, booked in the BS of the parent company		
MFIs - funding to CESEE banks not part of the group, booked in the BS of the parent		

**A.Q9 - ECB measures:**

1) Will you have access (as a group) to the ECB-announced TLTROs?	
2) If answered yes to 1), do you expect to access the ECB TLTROs?	
3) If answered yes to 2), will you withdraw the full amounts allowed by your (group) collateral or only partially?	
4) Is the access to the two TLTROs able to satisfy your demand for long-term liquidity at group level?	
5) Do you expect that the TLTROs will be utilised to (multiple yeses or noes are possible)...	
...fund non-financial corporates' lending growth in jurisdictions where TLTROs access is available?	
...indirectly fund non-financial corporates' lending growth in jurisdictions where TLTROs access is NOT available (e.g. via intra-group funding)?	
...fund the investment/acquisition of bonds?	

**A.Q10 - How has the TLTROs announcement impacted on your group's external exposure? How do you expect TLTROs to impact?**

	<b>LAST 6 months</b>	<b>NEXT 6 months</b>
<b>Total exposure to emerging markets</b>		
<b>Total exposure to CESEE region</b>		
of which:		
exposure to CESEE subsidiaries - intra-group funding		
direct cross-border lending to CESEE domestic clients, booked in the BS of the parent company		
MFIs - funding to CESEE banks not part of the group, booked in the BS of the parent		

**A.Q11 - How have other ECB measures, excluding TLTROs (e.g. negative depo rate, stop to SMP sterilisation) affected your group's external exposure? How do you expect them to impact?**

	<b>LAST 6 months</b>	<b>NEXT 6 months</b>
<b>Total exposure to emerging markets</b>		
<b>Total exposure to CESEE region</b>		
of which:		
exposure to CESEE subsidiaries - intra-group funding		
Direct cross-border lending to CESEE domestic clients, booked in the BS of the parent company		
MFIs - funding to CESEE banks not part of the group, booked in the BS of the parent		

**A.Q12 - Conditions of your funding to your own subsidiaries in CESEE...**

	<i>How have they changed over the <b>LAST</b> six months?</i>	<i>How do you expect them to change over the <b>NEXT</b> six months?</i>
<b>Overall</b>		
Pricing		
Maturity		

**A.Q13 How do you assess in each country...**

Country	Market potential	Your subsidiary's current positioning	Return on assets (adjusted for cost of risk)	Return on assets (adjusted for cost of risk) compared to overall group operations	Return on equity (adjusted for cost of equity)	Return on equity (adjusted for cost of equity) compared to overall group ROE
Albania						
Bosnia-H.						
Bulgaria						
Croatia						
Czech Republic						
Estonia						
Hungary						
Latvia						
Lithuania						
Macedonia						
Poland						
Romania						
Serbia						
Slovakia						
Slovenia						
Ukraine						



## PART B

### B.Q1 - Credit supply: bank's (local subsidiary's) credit standards applied when assessing credit applications...

*(possible answers = tighten considerably; tighten somewhat; remain basically unchanged; ease somewhat; ease considerably)*

	<i>How have they changed over the last six months?</i>	<i>How do you expect them to change over the next six months?</i>
<b>Overall</b>		
Loans to small and medium-sized enterprises		
Loans to large enterprises		
Loans to households for house purchase		
Consumer credit (other than loans for house purchase)		
Short-term loans		
Long-term loans		
Local currency		
Foreign currency		

**B.Q2 - Credit supply: have bank's terms and conditions** (e.g. maturity, pricing, size of average loan, etc.) **for approving loans or credit lines changed/will they change?...**

(possible answers = -- tighten considerably; - tighten somewhat; 0 remain basically unchanged; + ease somewhat; ++ ease considerably)

Over the LAST 6 months					
	Overall	Loans to SMEs	Loans to large companies	Loans to households for house purchase	Consumer credit (other than loans for house purchase)
A) Your bank's margin over interbank rate (wider margin = --, narrower margin = ++)					
B) Size of the average loan or credit line					
C) Maturity					
D) Other terms and conditions					
E) Collateral requirements					
Over the NEXT 6 months					
	Overall	Loans to SMEs	Loans to large companies	Loans to households for house purchase	Consumer credit (other than loans for house purchase)
A) Your bank's margin over interbank rate (wider margin = --, narrower margin = ++)					
B) Size of the average loan or credit line					
C) Maturity					
D) Other terms and conditions					
E) Collateral requirements					

**B.Q3 - Factors affecting your bank's credit standards (credit supply).**

**Have the following domestic and international factors contributed to tightening (easing) your credit standards over the past six months, and do you expect them to contribute to tightening (easing) your credit standards over the next six months?**

*(possible answers = contributed considerably to tightening; contributed somewhat to tightening; contributed to remaining basically unchanged; contributed somewhat to easing; contributed considerably to easing)*

	Over the <b>LAST</b> six months	Over the <b>NEXT</b> six months
<b>Impact on credit standards</b>		
<b>A) Domestic factors - affecting your subsidiary</b>		
i) Local market outlook		
ii) Local bank outlook		
iii) Local banks' access to total funding		
iii.a) of which: domestic		
iii.b) of which: international/intra-group		
iv) Local bank capital constraints		
v) Change in local regulation		
vi) Competition		
vii) Credit quality (NPLs)		
<b>B) International factors - affecting your subsidiary</b>		
i) Group company outlook		
ii) Global market outlook		
iii) Overall group access to funding		
iv) EU regulation		
v) Group capital constraints		
vi) Global competition		
vii) Credit quality (NPLs)		

**B.Q4 - Loan applications: demand for loans or credit lines to enterprises and households (to your local subsidiary/branch)...**

*(possible answers = decrease considerably; decrease somewhat; remain basically unchanged; increase somewhat; increase considerably)*

	<i>How has it changed over the last six months?</i>	<i>How do you expect it to change over the next six months?</i>
<b>Overall</b>		
Loans to small and medium-sized enterprises		
Loans to large enterprises		
Loans to households for house purchase		
Consumer credit (other than loans for house purchase)		
Short-term loans		
Long-term loans		
Local currency		
Foreign currency		

**B.Q5 - Factors affecting clients' demand for loan applications...**

*(possible answers =*

*contributed considerably to lower demand; contributed somewhat to lower demand; contributed to basically unchanged demand; contributed somewhat to higher demand; contributed considerably to higher demand)*

**...Loans or credit lines to enterprises**

	<i>How have they changed over the last six months?</i>	<i>How do you expect them to change over the next six months?</i>
<b>A) Financing needs</b>		
Fixed investments		
Inventories and working capital		
M&A and corporate restructuring		
Debt restructuring		

**...Loans to households**

<b>A) Financing needs</b>		
Housing market prospects		
Consumer confidence		
Non-housing related consumption expenditure		

**B.Q6 - Gross non-performing loans ratio in your local subsidiary/branch (excluding extraordinary operations)...***(possible answers = decrease; no change; increase)*

	<i>Has the non-performing loans ratio changed over the last six months?</i>	<i>How do you expect the non-performing loans ratio to change over the next six months?</i>
Total		
Retail		
Corporate		

**B.Q7 - In terms of funding: has access to funding of your local subsidiary/branch changed over the past six months, or do you expect it to change over the next six months?***(possible answers = decrease considerably; decrease somewhat; remain basically unchanged; increase somewhat; increase considerably)*

	Over the <b>LAST</b> six months	Over the <b>NEXT</b> six months
<b>A) Total funding</b>		
<b>A.1) Intra-group funding</b>		
<b>A.2) IFI (international financial institutions) funding</b>		
<b>A.3) Retail funding</b> (deposits and customer bonds)		
<b>A.4) Corporate funding</b> (deposits and customer bonds)		
<b>A.5) Inter-bank unsecured money market</b>		
<b>A.6) Wholesale debt securities</b>		
<b>A.7) Securitisation</b>		
<b>A.8) Net central bank position</b>		
<b>B.1) Local currency funding</b>		
<b>B.2) Short-term (less than 1 year)</b>		
<b>C.1) Long-term (more than 1 year)</b>		
<b>C.2) Foreign currency funding</b>		

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**B.Q8 - How have the following factors affected your local subsidiary's funding conditions over the past six months, and do you expect this to change over the next six months?**

*(possible answers = considerably negative effect; somewhat negative effect; basically no effect – neither positive nor negative; somewhat positive effect; considerably positive effect)*

	Over the <b>PAST</b> six months	Over the <b>NEXT</b> six months
A) Exposure to sovereign debt		
B) Indirect exposure (via group company) to sovereign debt		
C) Value and availability of eligible collateral for repo transactions		
D) Intra-group funding restrictions (e.g. company-specific rules and home/host regulatory rules)		
G) Rating of group residence country		
H) Rating of parent company		
I) Rating of subsidiary		
J) Capital ratio of your subsidiary		
K) Capital ratio of your parent		









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