











Press Release

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Improved outlook for bank lending in emerging Europe as funding conditions stabilize and stocks of bad loans fall, new Vienna Initiative reports show.

The external positions of BIS reporting banks in Central, Eastern and South Eastern Europe (CESEE) have broadly stabilized, and post-crisis deleveraging seems to have been largely completed, while banks' strategies in the region have become more selective, according to two new reports from the Vienna Initiative. A third such report shows that levels of bad loans in the region declined in the year to mid-2016, but in several countries, they continue to have a negative impact on the local economy, and further action is needed to deal with them.

The Vienna Initiative, founded at the height of the global financial crisis of 2008/09 as a private-public sector platform to support banking sectors in CESEE, now works on specific financial sector problems in the region, including NPLs, the impact of regulatory reform, and capital market developments.

The latest Deleveraging and Credit Monitor¹ finds that, in the second half of 2016, BIS reporting banks modestly reduced their exposure vis-à-vis CESEE by about 0.5 percent of regional GDP (compared to 0.3 percent of GDP in the first half of 2016), a figure which drops to a mere 0.2 percent of GDP with Russia and Turkey excluded. This indicates that deleveraging has largely come to an end for the region overall. Substantial increases in foreign bank funding were reported for Albania, Bosnia and Herzegovina, and the Czech Republic, while the largest declines – mostly driven by reductions in claims on banks – were observed in FYR Macedonia, Moldova, and Ukraine.

Outside the Commonwealth of Independent States (CIS), credit continues to recover, while, credit growth in the CIS and Turkey, following a sharp slowdown, is stabilizing in low single digits. Deposits continue to grow robustly across the region, facilitating the gradual reduction in loan-to-deposit ratios, with the regional average standing at 103 percent in January 2017.

The latest CESEE Bank Lending Survey,² covering the period from October 2016 to March 2017, shows that international banks continued to discriminate among countries of operations

¹ A full report on developments in H2 2016 will be published on May 11, 2017 on the <u>Vienna Initiative webpage</u>.

² A full report, including country chapters, on the H1 2017 survey release will be published in May 2017 on the EIB website (http://www.eib.org/about/economic-research/surveys.htm) and on the Vienna Initiative webpage.

in response to relative returns, market potential, and positioning. Regional demand for credit, driven largely by investment, continued to increase, while supply standards did not ease, leading to a steadily widening demand-supply gap. Group asset quality, domestic capital, and changes in regulation weighed negatively on subsidiaries' supply stances. On the other hand, restrained supply may mean that most of the new credit is, on average, of better quality than in prior credit cycles.

Subsidiaries' non-performing loan (NPL) ratios continued to decline, as evidenced by the Vienna Initiative's latest semi-annual NPL Monitor: the NPL ratio in the CESEE region fell to 7.1 per cent as of 30 June 2016, down from 7.9 per cent a year earlier. Bad loans totalled €52.6 billion (down 8.2 percent year-on-year), around 4.3 per cent of GDP. The fall came mostly through NPL sales, which had amounted to €6.5 billion since June 2015, with stable market absorption over the last 18 months.

Three countries in the region (Hungary, FYR Macedonia and Slovenia), have managed to reduce their NPL ratio below the 10 per cent threshold since December 2015. However, NPL ratios remain persistently high, exceeding 10 percent, in seven of the eighteen CESEE countries monitored, and much work remains to be done. Impediments to NPL resolution and sales exist in many countries, and several structural reforms (*e.g.*, new out-of-court restructuring frameworks, strengthened enforcement and insolvency laws, removal of excessive tax disincentives to NPL write-offs) are still needed for deeper secondary markets in NPLs.