European Banking Coordination (Vienna 2) Initiative

Full Forum Meeting
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Bank Deleveraging in CESEE: An Update

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EBCI Vienna Initiative

European Commission · European Investment Bank · European Bank for Reconstruction and Development · International Monetary Fund · The World Bank

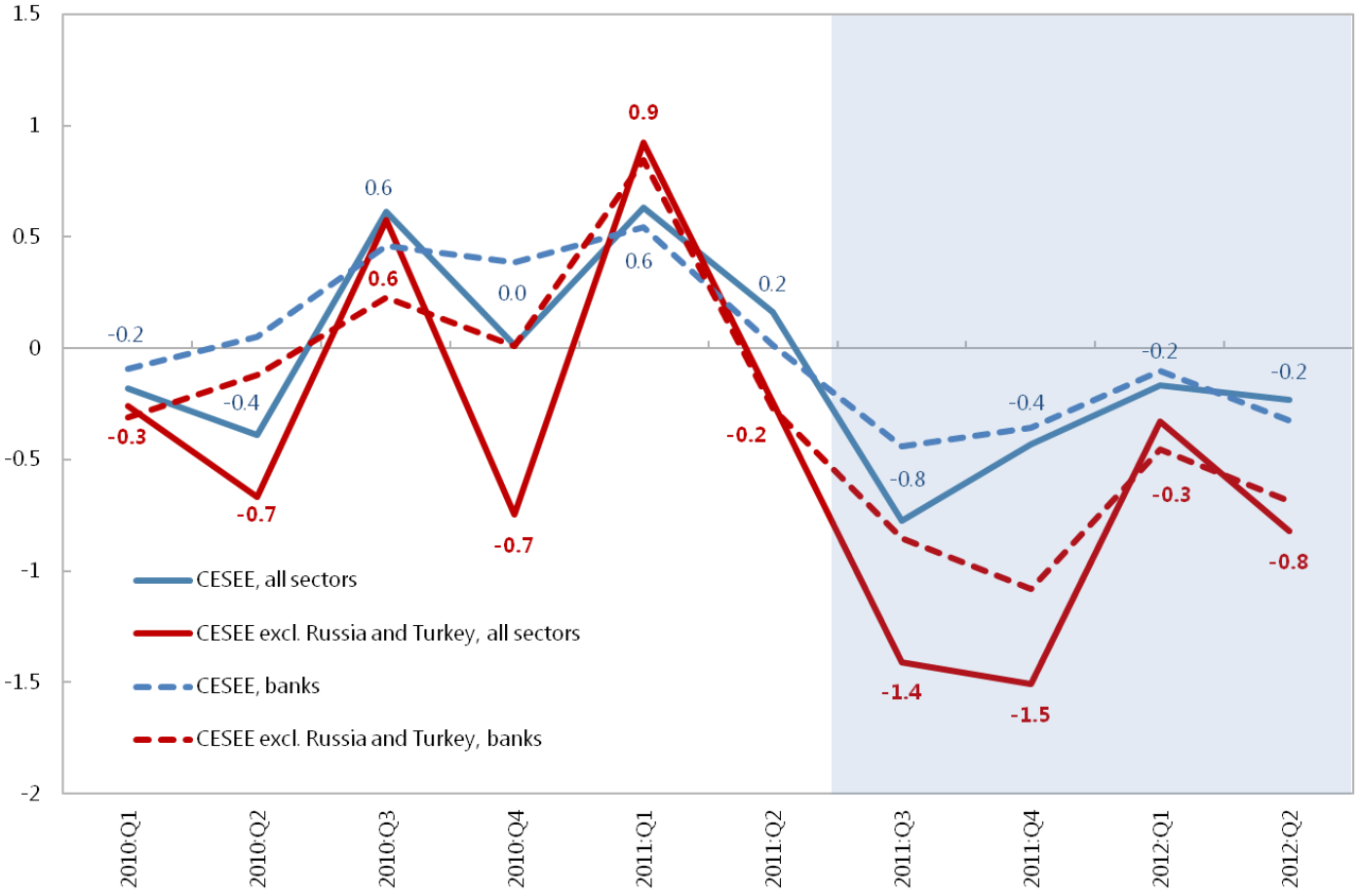
Second edition of the Steering Committee's quarterly *CESEE Deleveraging Monitor*

- **Recent developments**
  - Funding of CESEE by western banks according to BIS banking statistics through 2012:Q2
  - Likely developments since mid-2012 according to high-frequency indicators
  - Private sector credit growth in CESEE
- **Receding parent-bank funding and weak CESEE credit growth**
  - Which way does the causality run?
- **The EIB's CESEE Bank Lending Survey: preliminary findings**
  - The role of demand and supply conditions in credit growth
  - Key factors influencing demand and supply conditions
  - Longer-term strategies of cross-border banking groups for CESEE

The external positions of BIS-reporting banks fell moderately in 2012:Q2

CESEE: External Positions of BIS-reporting banks, 2010:Q1-2012:Q2

(Percent of GDP)

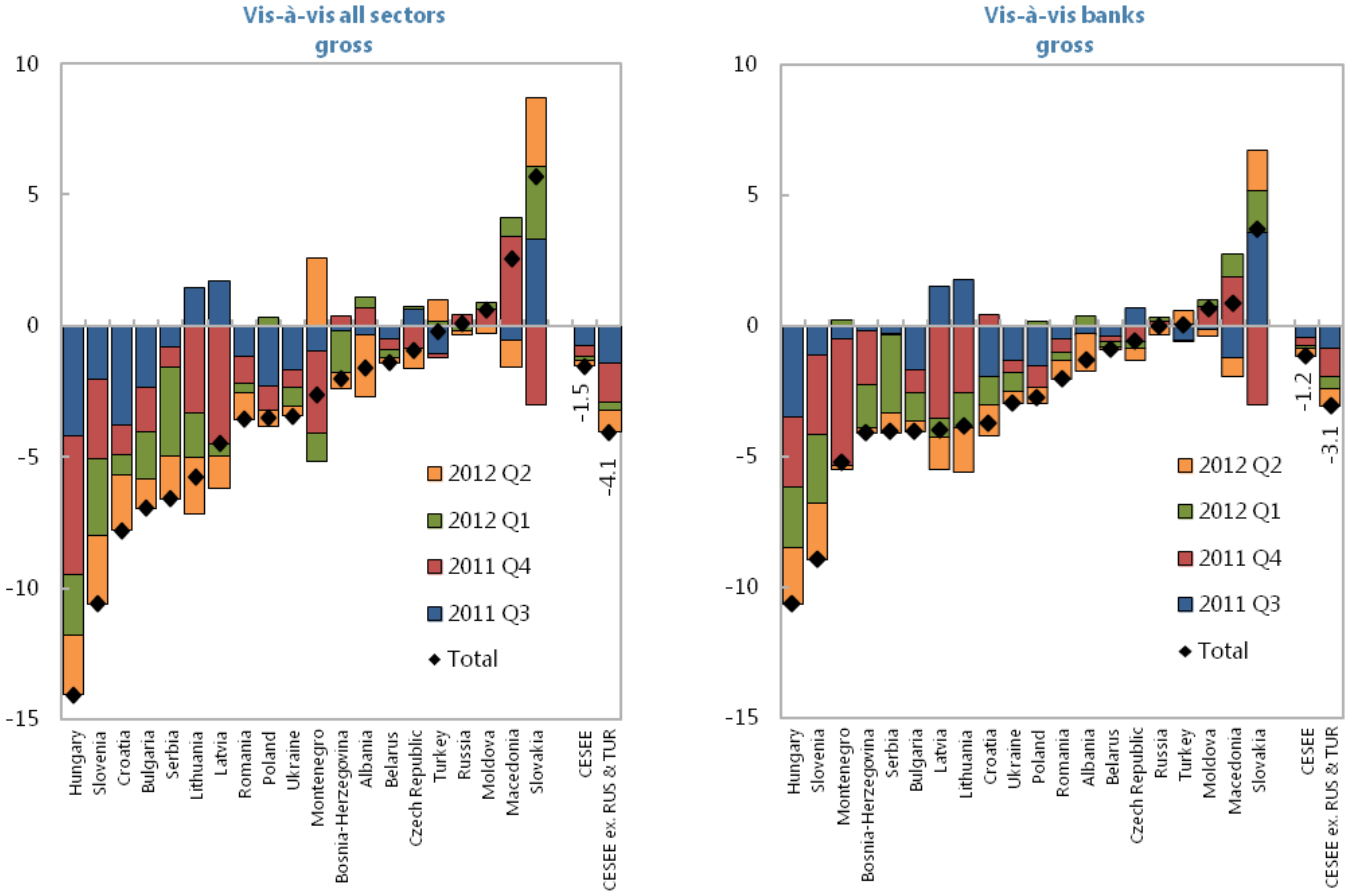


Sources: BIS, Locational Banking Statistics: and IMF staff calculations.

Nonetheless, cumulative fall of external positions since mid-2011 was large, particularly vis-à-vis some countries

CESEE: External Positions of BIS-reporting Banks, 2011:Q3 - 2012:Q2

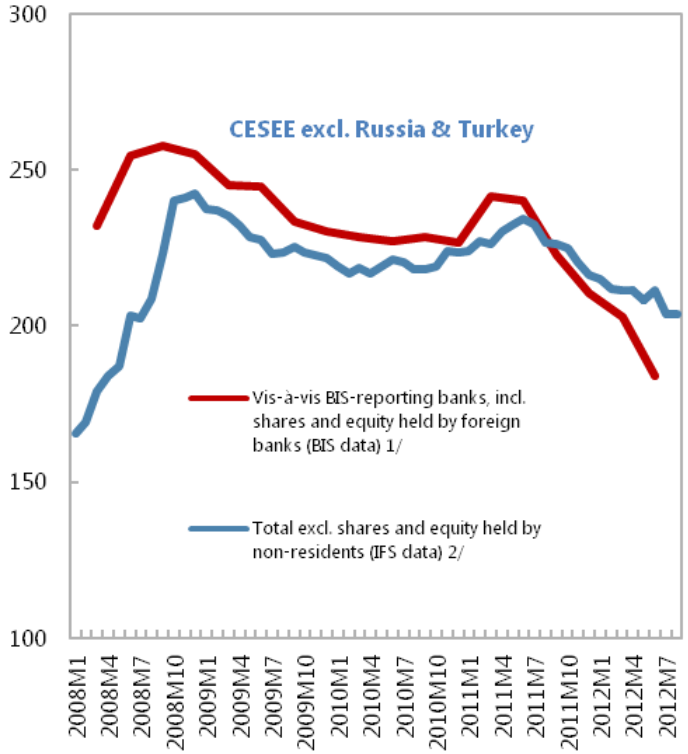
(Change, Percent of GDP*)



Sources: BIS, Locational Banking Statistics; and IMF staff calculations.
* Full year 2012 GDP.

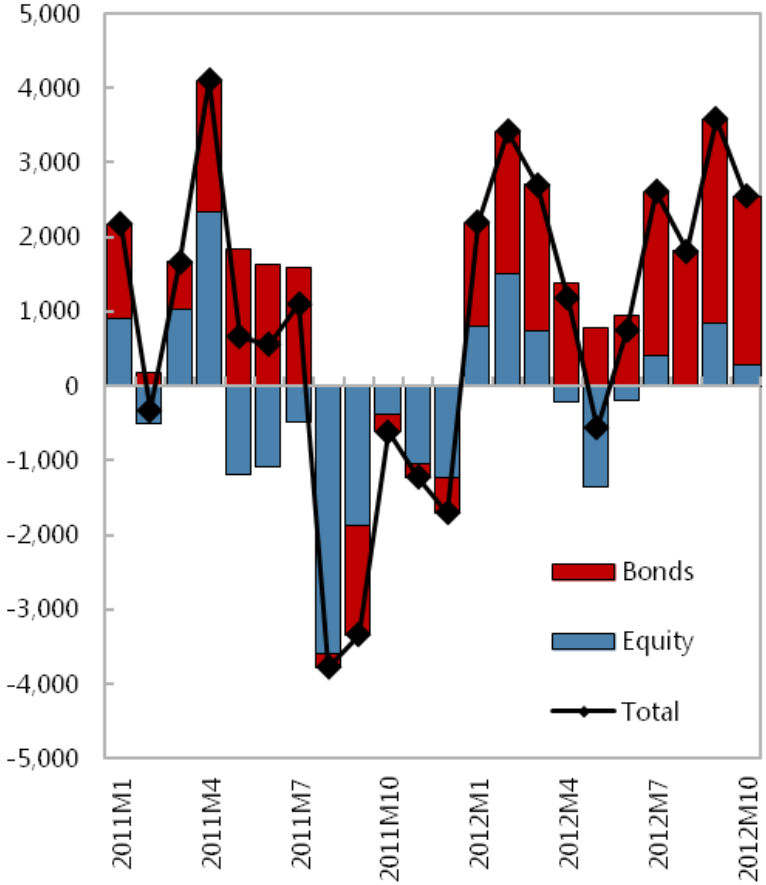
High frequency indicators point to limited changes of external positions since 2012:Q2

External Liabilities of Banks, 2008:M1-2012:M8
(Billions of US$)



1/ BIS-reporting banks' claims on banks in emerging Europe (exchange-rate adjusted).
2/ Other depository institutions' liabilities to non-residents (exchange rate adjusted).
Sources: BIS, Locational Statistics; IMF, International Financial Statistics (IFS); and IMF staff calculations.

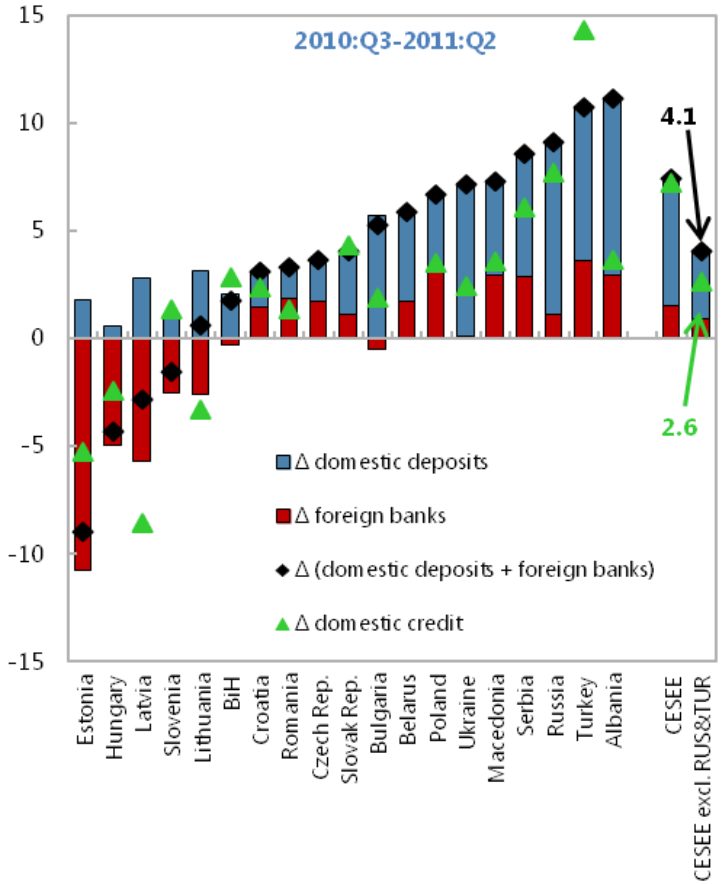
Emerging Europe: Flows into Dedicated ETFs and Mutual Funds, Jan. 2011 - Oct. 2012
(Millions of US$)

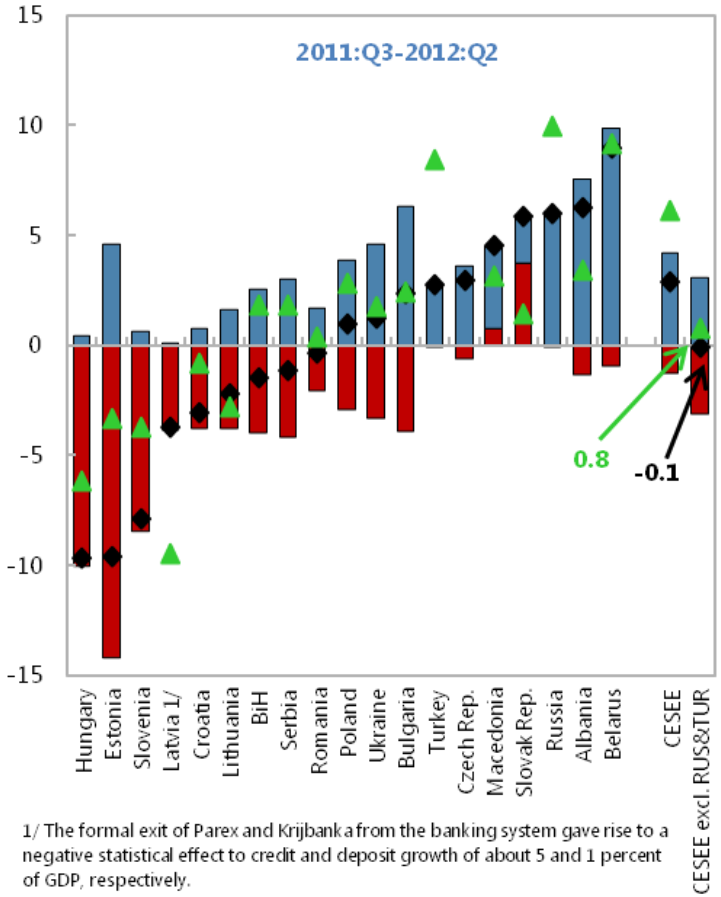


Source: EPFR, equity and bond country flows.

The reduction of external positions during 2011:Q3-2012:Q2 coincided with stalling CESEE credit growth

CESEE: Banks' Funding Sources and Credit Developments
(Percent of GDP, exchange-rate adjusted)





1/ The formal exit of Parex and Krijbanka from the banking system gave rise to a negative statistical effect to credit and deposit growth of about 5 and 1 percent of GDP, respectively.

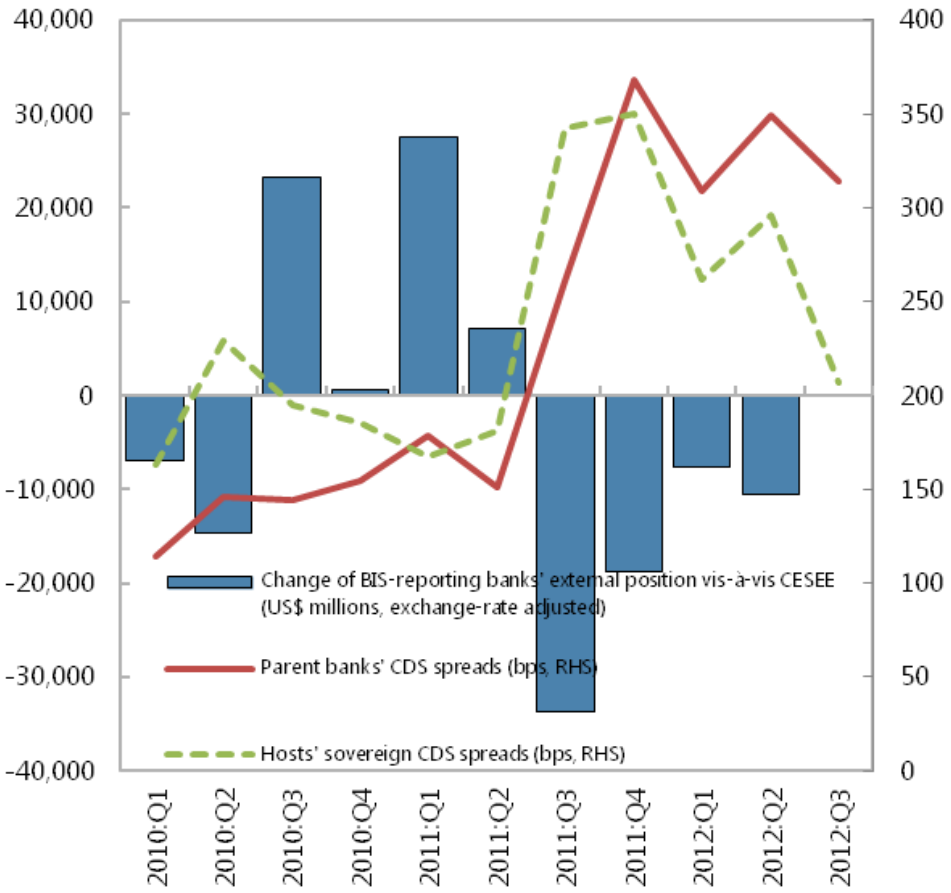
Sources: BIS, Locational Banking Statistics; IMF, IFS; IMF, WEO; national authorities; EBRD; and IMF staff calculations.

Receding foreign funding drives weak local credit growth or vise versa ?

- **Demand-side effects clearly important**
  - Soft regional (and global) economic outlook
  - Legacy of 2003-08 credit boom
- **Supply-effects should not be discounted**
  - Sharply higher funding costs of parent banks and CDS spreads of sovereign hosts made foreign funding much more expensive
  - Lending surveys show strong tightening of credit-supply conditions, but only moderate dampening effect on credit-demand conditions
  - Foreign banks with higher loan-to-deposit ratios have lower credit growth
- **Only modest interest rate movements since mid-2011 point to roughly balanced demand and supply side effects**

Sharply higher funding costs of parents and host CDS spreads made foreign funding much more expensive

CESEE: Funding by Western Banks and Their Funding Costs, 2010:Q1 - 2012:Q2



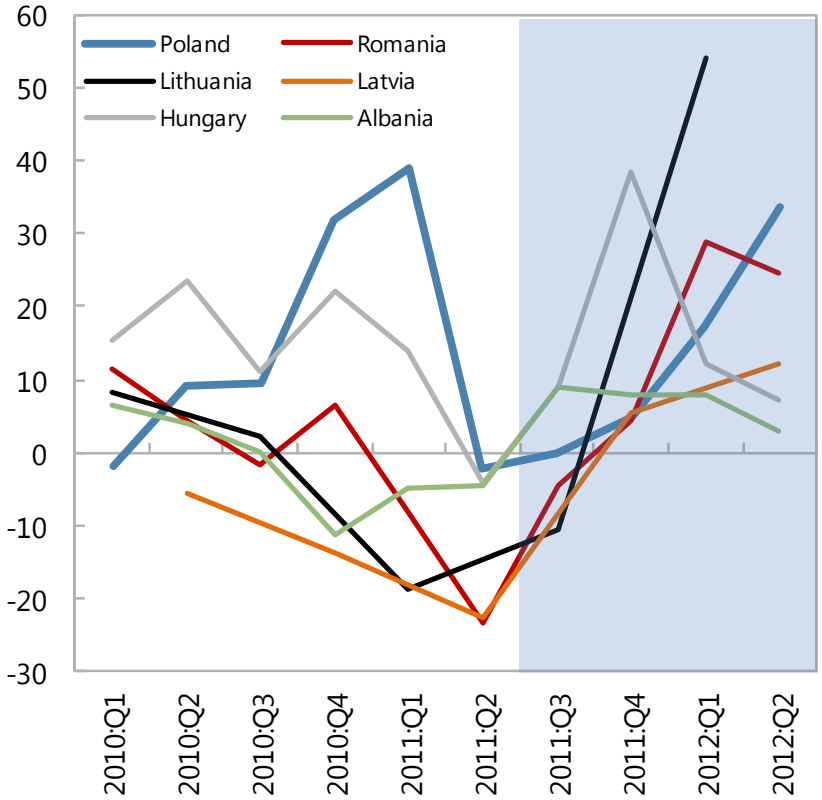
Sources: BIS, Locational Banking Statistics; Bloomberg; and IMF staff

Lending surveys: strong tightening of credit-supply conditions, only moderate dampened demand conditions

Selected CESEE Countries: Credit Supply and Demand Conditions, 2010:Q1 - 2012:Q2

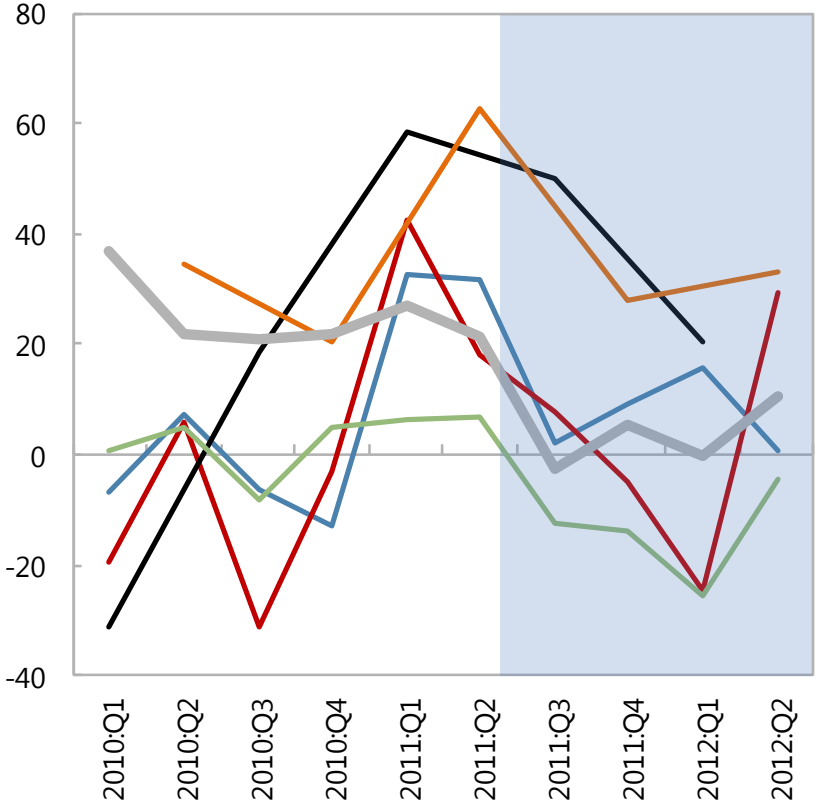
Supply Conditions

(Net percentage; positive values indicate tightening compared to previous period; average of conditions applied to enterprises and households)



Demand Conditions

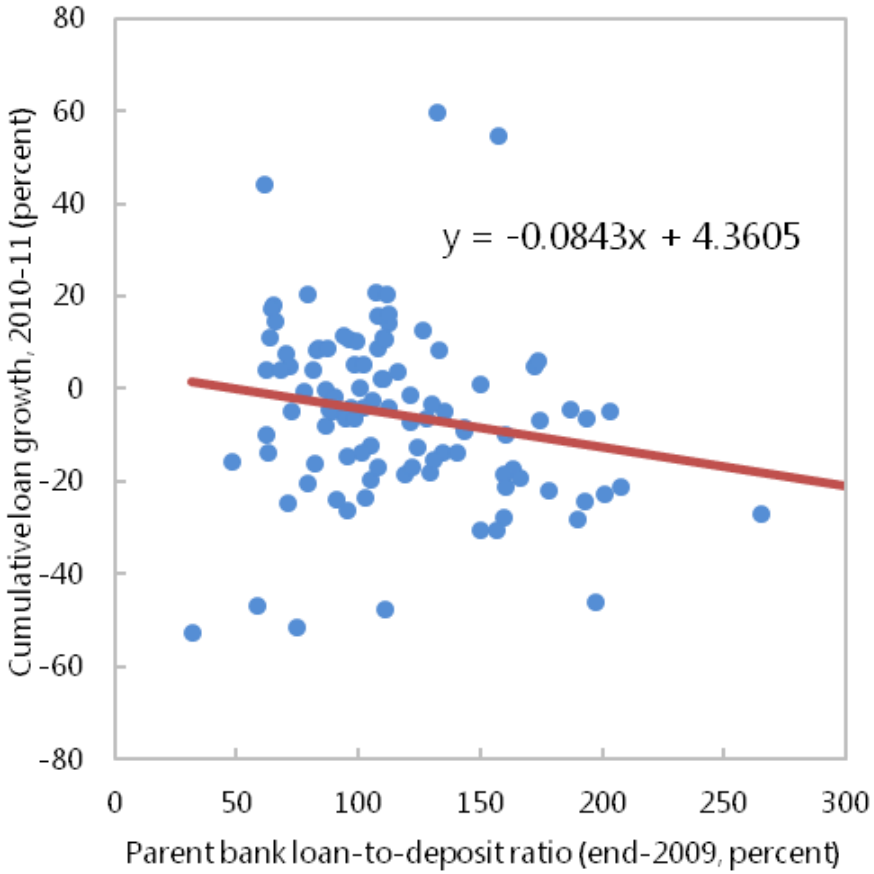
(Net percentage; positive values indicate higher demand compared to previous period; average of conditions applied to enterprises and households)



Sources: Lending surveys of central banks; and IMF staff calculations.

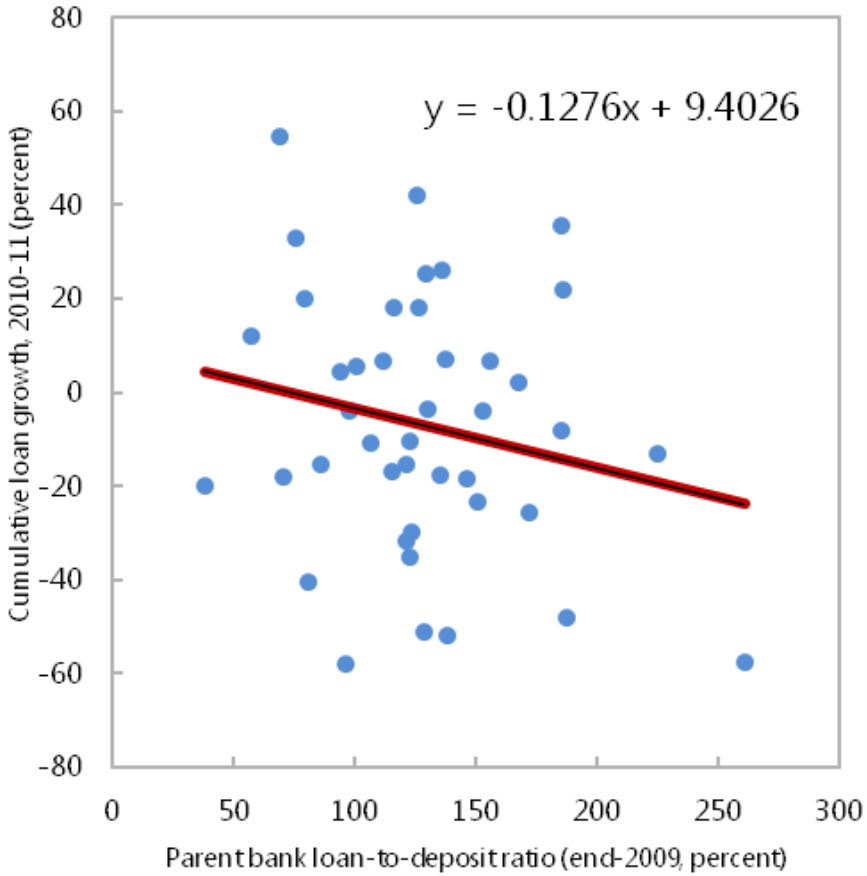
Foreign banks with higher loan-to-deposit ratios have lower credit growth

CESEE: Subsidiary Loan Growth and Subsidiary-level Loan-to-deposit Ratios



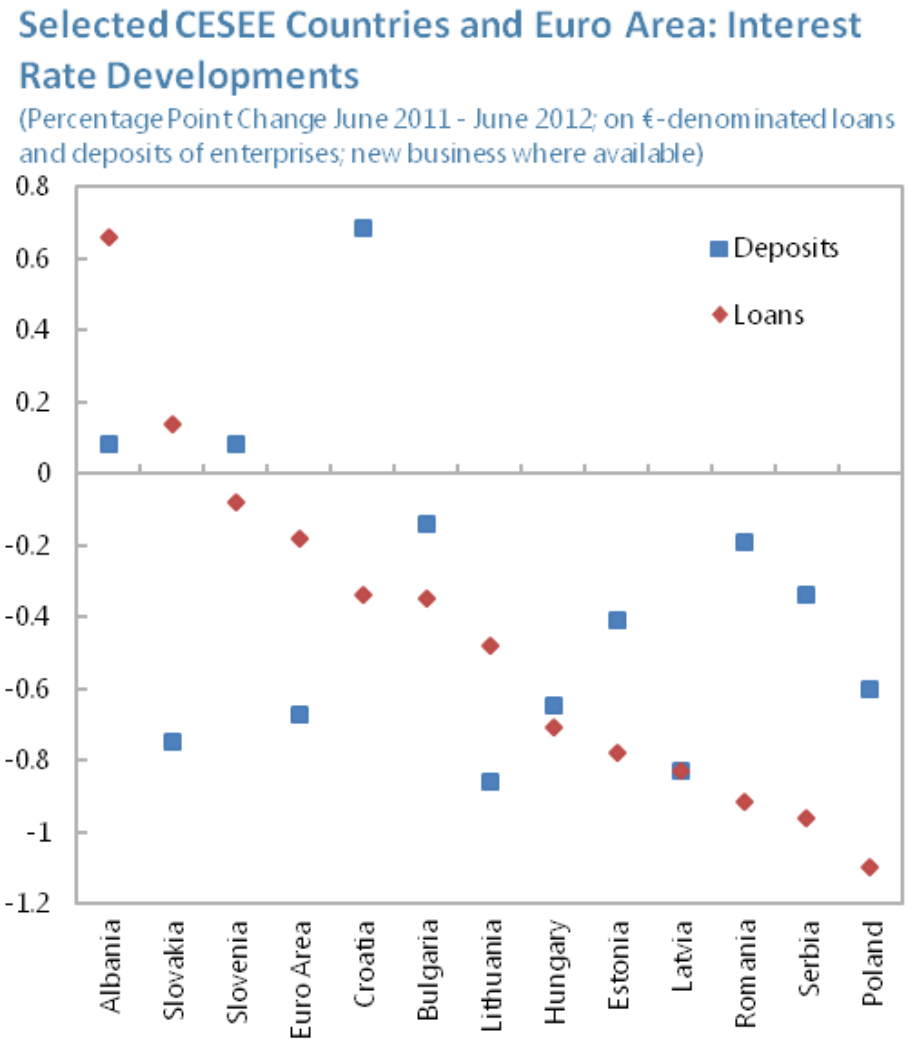
Sources: BankScope database, and IMF staff estimates.

CESEE: Subsidiary Loan Growth and Group-level Loan-to-deposit Ratios



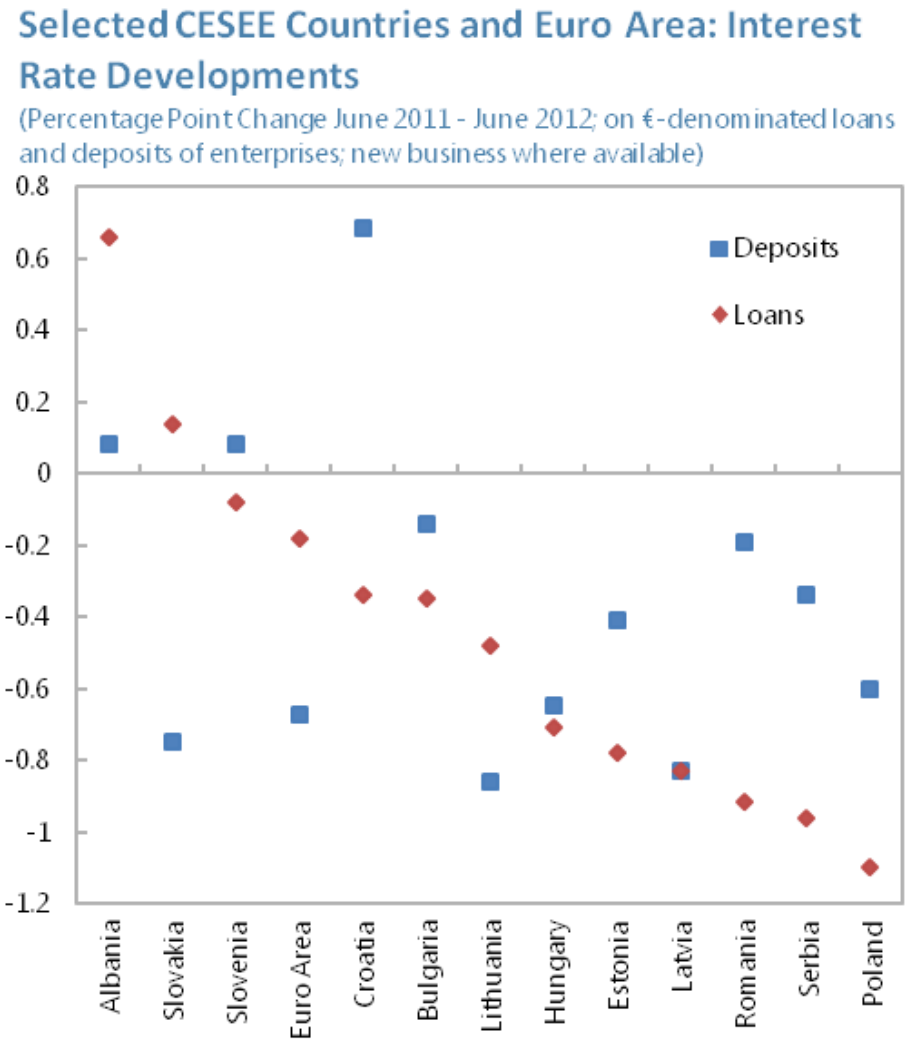
Sources: BankScope database, and IMF staff estimates.

Only modest interest rate movements since mid-2011 point to roughly balanced demand and supply side effects



Sources: National central banks; and Haver Analytics.

Only modest interest rate movements since mid-2011 point to roughly balanced demand and supply side effects



Sources: National central banks; and Haver Analytics.

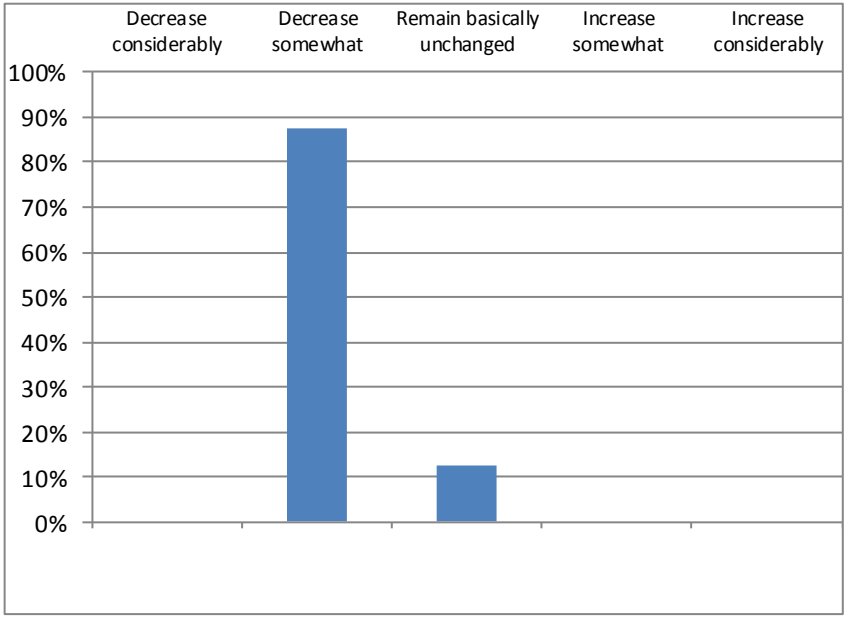
First results of EIB's CESEE Bank Lending Survey

- **Stalling credit in CESEE is a key concern – understanding the underlying factors is key for defining proper actions**
- **This survey disentangles**
  - Demand and supply factors
  - Domestic and international factors
  - Role of expectations
- **First run - October 2012. High participation: 8 groups, 42 banks, on average 40 percent coverage per country**
- **Next round, participation/coverage can be broadened by country and groups/banks:**
  - All the large groups
  - Baltic countries, Slovenia, Poland, Ukraine, and Russia

Results: group level

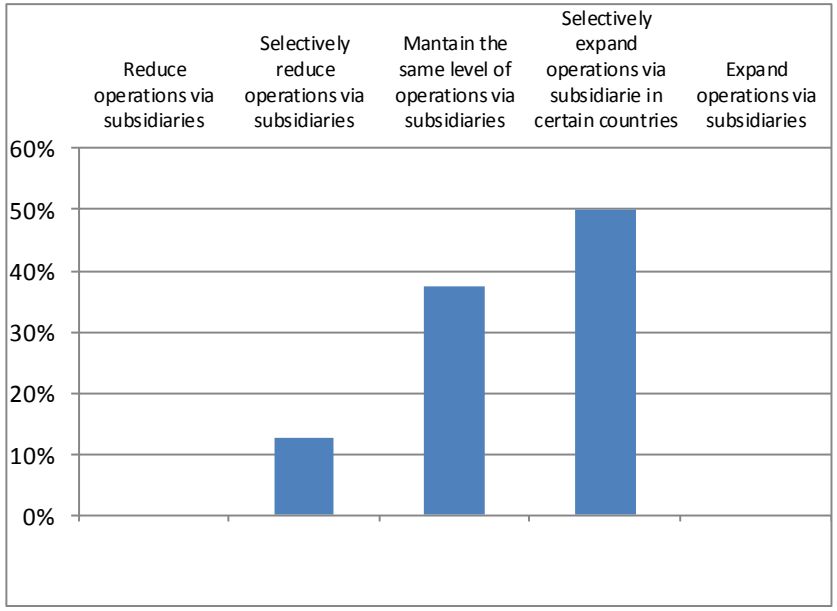
- All parents going through some sort of strategic restructuring
- At group level, some more deleveraging expected

Deleveraging —over the next six months, do you expect the loan-to-deposit ratio of your group to…



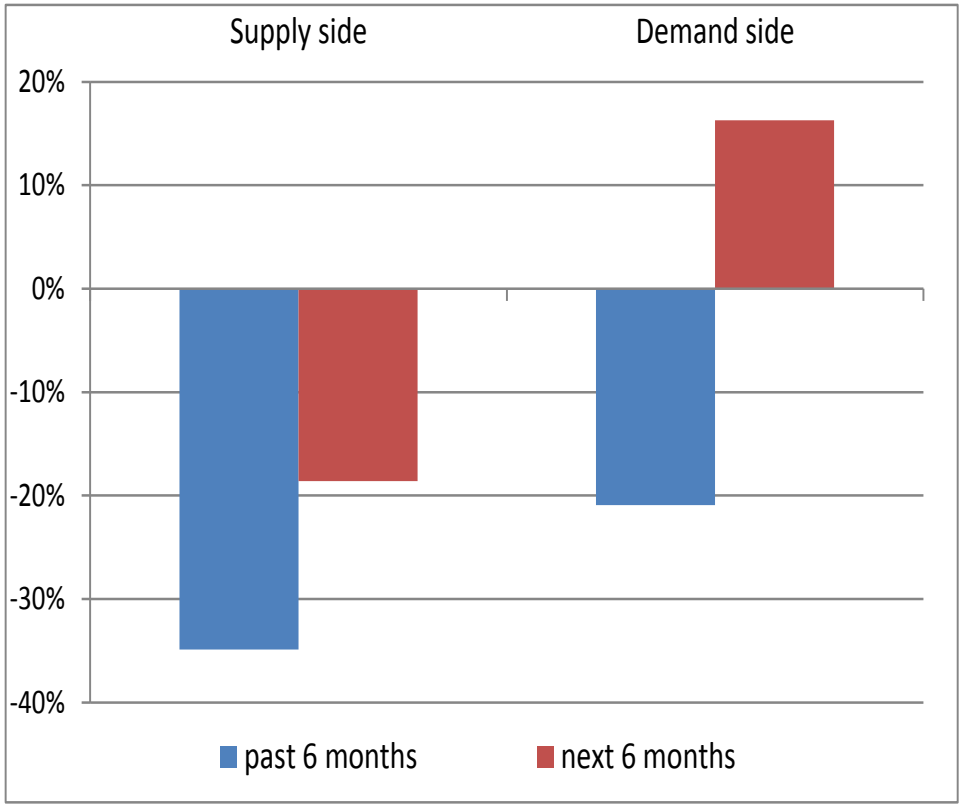
- Continued commitment to operations in the CESEE
- Being selective is the key strategic factor

Longer term startegies (beyond 12 months): Looking at operations via subsidiaries in CEE-SEE, your group intends to…



Results: subsidiary level

- **Demand and supply**
  - Past six months: both subdued
  - Looking ahead: demand more positive; supply tilted to the downside

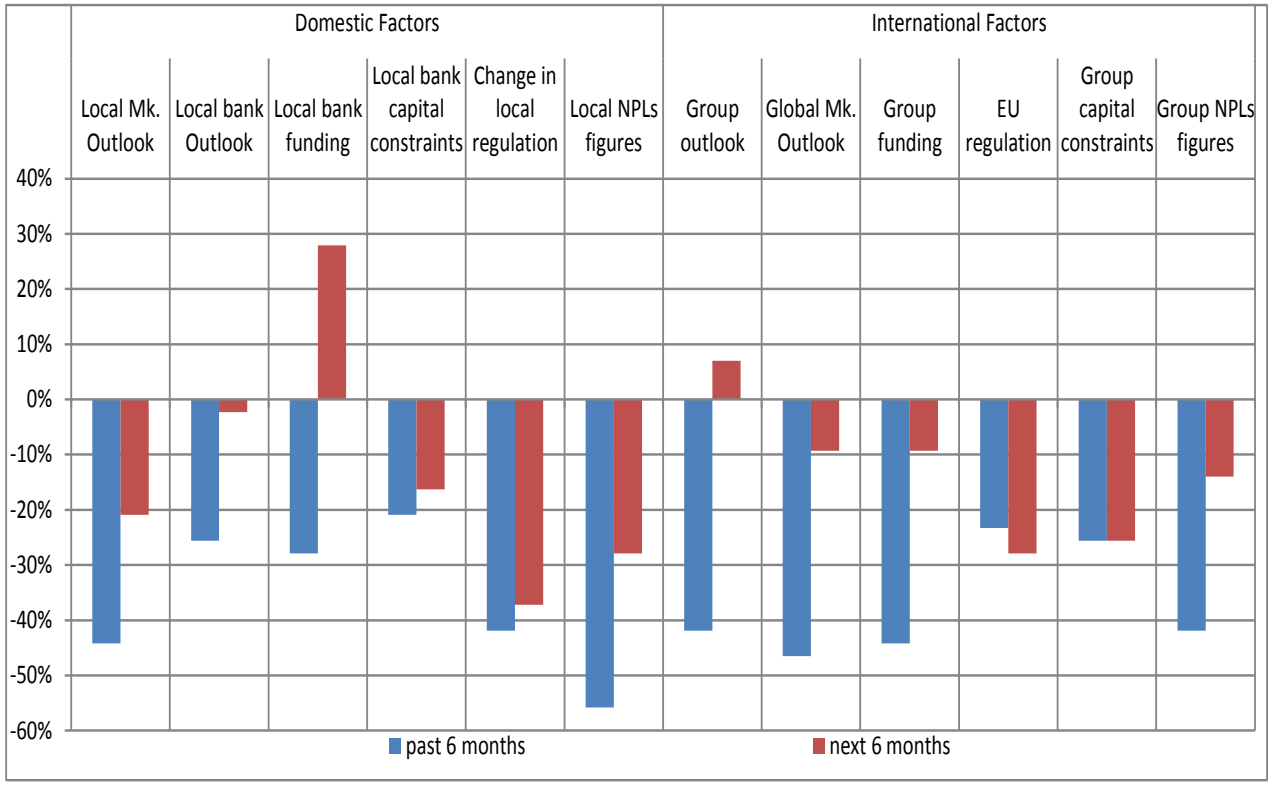


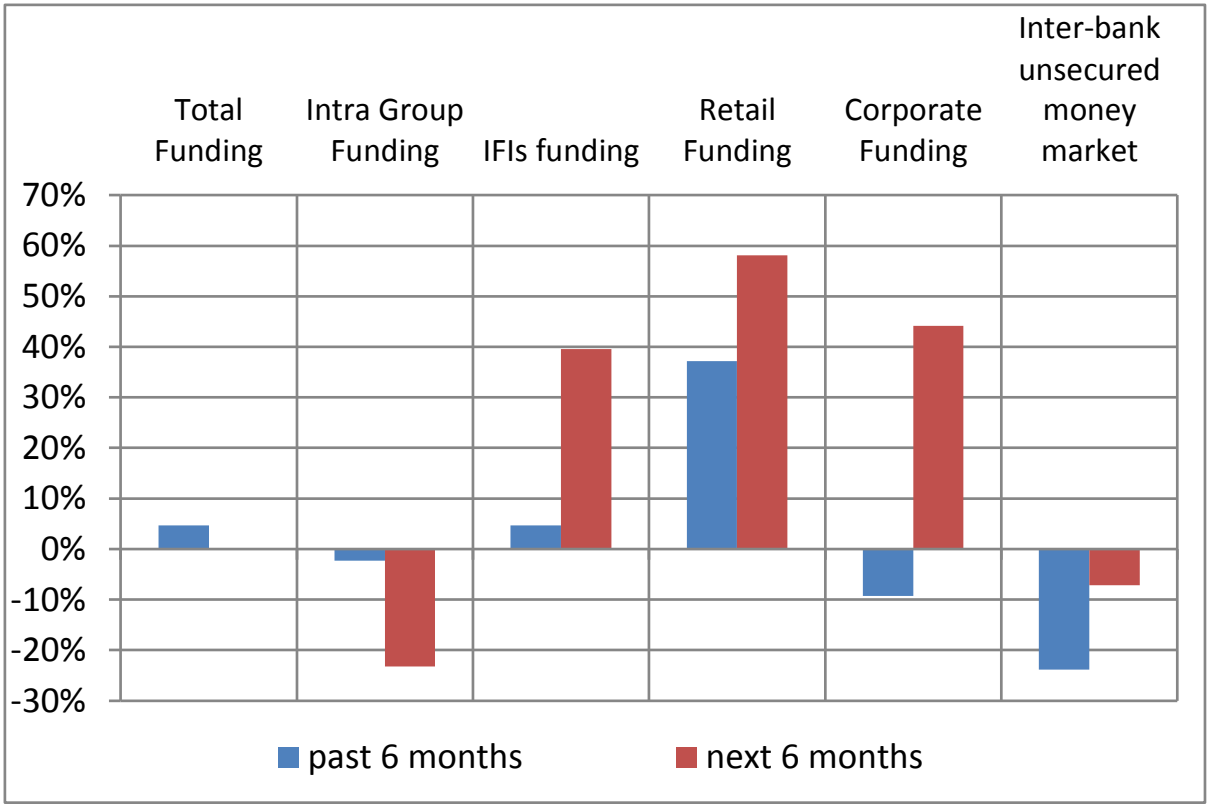
- **Among negative factors affecting past demand**
  - low consumer confidence
  - housing price prospects
  - subdued M&A activities
  - weak fixed investment

Results: subsidiary level (cont'd)

Domestic and international factors weight on supply tightening, signaling a shift toward a more self-sustainable banking model

- **Domestic**
  - local market outlook
  - local regulation
  - Compliance with local bank capital requirements
  - NPLs
- **International**
  - global market outlook
  - group funding
  - group capital
  - group NPLs



Results: subsidiary level (concluded)

- Toward a rebalancing of the banking model
- If demand recovers, funding constraints might become more binding, particularly in some markets