

ECRI Statistical Package 2017 - Lending to European Households and Non-Financial Institutions

Carolina Raquel Melches*, August 2017

The ECRI Statistical Package 2017 provides data on outstanding credit granted by monetary-financial institutions (MFI) to households and non-financial corporations (NFCs) in the period from 1995-2016. Credit volumes and annual growth rates are broken down by sector and credit type to enable detailed insights into credit market developments throughout time and across countries in the European Union and beyond. It has continuously been extended and improved and today comprises 42 countries including EFTA states, emerging economies and other countries as the US, Canada, Japan and Australia.

Key Findings of the Statistical Package 2017

The total outstanding credit from MFIs to households and NFCs in 2016 showed an increase of 0.7% in the EU28 compared to the previous year. Private credit to households has entered stable growth for the second consecutive year, which suggests that private credit markets are recovering from the implications of the economic and financial crisis in 2008.

Among credit types, consumer credit experienced the strongest annual growth, while housing loans remained on a slower but steady growth path. The country group of new member states that acceded in and after 2004 constitute an exception, with a housing loan growth more than 2.5 times higher than that of the entire EU28. Whereas private credit continues to grow across all loan types, the growth rate magnitudes are consistently smaller than the 2015 growth rates.

Diverging trends between private and corporate credit on European credit markets continue as credit to NFCs experiences a contraction for the eighth consecutive year, albeit with a smaller magnitude than in the previous year. Annual growth rates at country level show a much smaller variation on a range half as wide as in the preceding year, suggesting that credit markets for NFCs are stabilising and could soon enter recovery as well.

With the exception of Italy, the PIIGS continue to exhibit negative growth rates across all credit types.

Notwithstanding the signs of recovery conveyed by annual growth rates, outstanding amounts across all loan types continue to be well below pre-crisis levels, with the exception of housing loans.

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Are households driving Europe's economic recovery?

The year 2015 marked the first trend reversal since 2008 for private credit markets towards an expansion of credit volumes. In real terms, private and corporate total lending by monetary financial institutions (MFIs) continued to expand by a rate of 0.7% in the EU28.¹ Compared to the previous year, credit expanded 0.2 percentage points less as annual growth reached 0.9% in 2015. The positive trend is even more visible within the new member states² (NMS), which experienced a considerable expansion of total credit of about 2% for the third consecutive year (see Figure 1). The numbers confirm that European credit markets are recovering from the effects of the financial and economic crisis.

While the overall message is positive, the package reveals that growth rates are, on average, lower than in the previous year across countries and sectors. A number of factors impacted bank lending behaviour and private and corporate sector credit demand in 2016: the macro-economic and political climate; the Brexit-vote and ensuing exchange rate volatility; ongoing problems in the banking sectors of the PIIGS³ countries and the persistent low interest rate environment.

A more granular analysis of annual growth rates by lending sector and country groups lays bare a divergence between credit to households and credit to non-monetary financial corporations (NFCs). Growth rates by sector show that the expansion of total credit volume is driven solely by the growth of private credit granted to households, whereas credit to NFCs continues to contract for the 8th consecutive year, by -0.45% in the EU28 and even -0.97% in the Euro Area 19 (EA).⁴ In the NMS, credit to NFCs experienced a positive peak of almost 2% in 2015, but stagnated in 2016 with a contraction of -0.01%, in real terms. Particularly noteworthy is the fact that, apart from Italy, the PIIGS continue to record negative growth rates across all credit types.

Cumulative growth rates also reveal the diverging trend in credit to NFC as opposed to credit to households. Credit to NFCs has contracted by more than 19.1% in real terms in the EU28, while total credit to HH experienced a maximum contraction of 4.08% between 2009 and 2014.

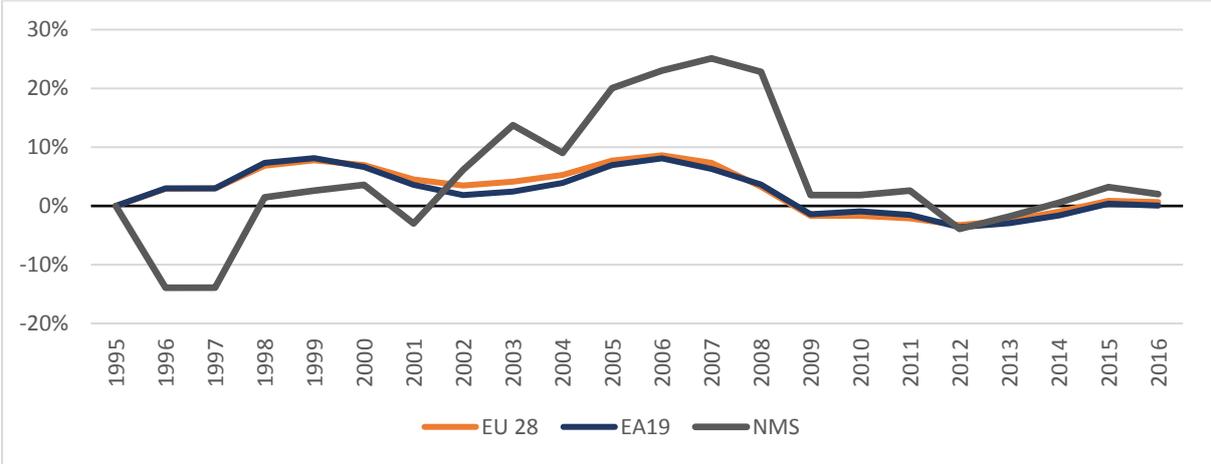
¹ The EU28 or EU encompasses the 28 member states of the European Union as of 1 January 2015, namely Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and the United Kingdom.

² NMSs are the 13 countries that joined the EU either as part of 2004 enlargement or subsequently. The group consists of Bulgaria, Croatia, Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, Slovenia and Slovakia.

³ The country group PIIGS comprises Portugal, Ireland, Italy, Greece and Spain.

⁴ The euro area comprises 19 member states as of 1 January 2015, namely Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain.

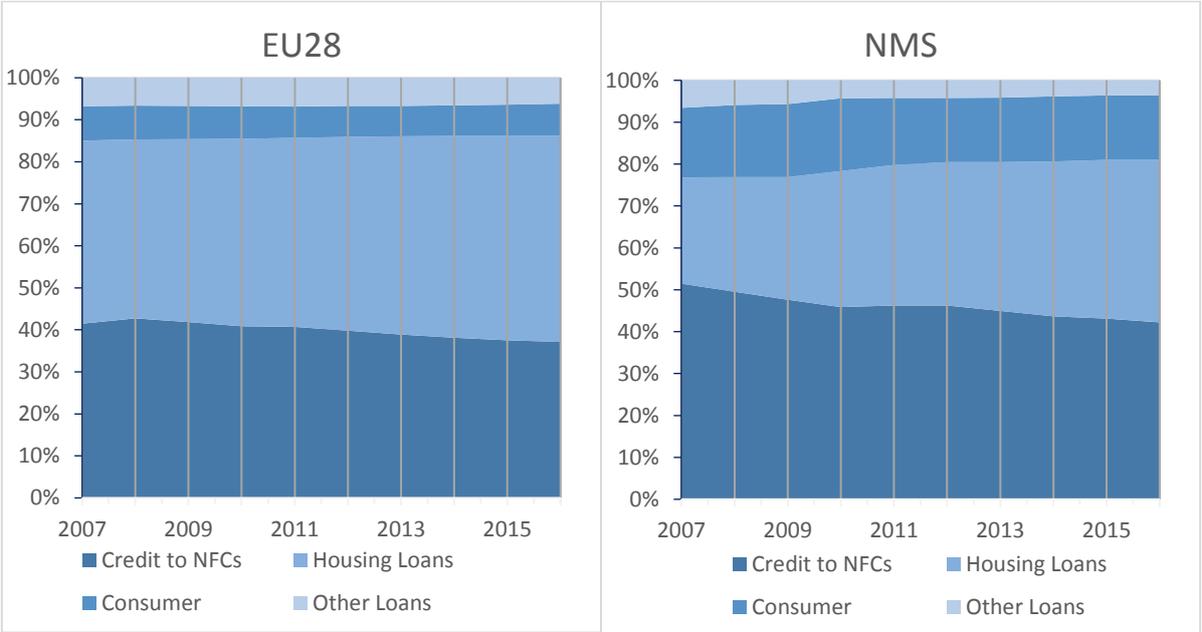
Figure 1: Annual growth rate of total credit market, by country group (2005-2016)



Source: ECRI Statistical Package 2017.

There are also positive signs coming from Europe’s GDP development, which increased by 2.6% in 2016 for the fourth consecutive year. In the NMS, real GDP growth even reached 4% in 2016. While the persistent correlation between credit and GDP growth emphasises the importance of credit for economic growth, the development of European credit markets suggests that growth due to credit has been mainly demand-side driven. Figure 2 illustrates the shrinking share of corporate credit as a percentage of total credit in the EU28 as well as the NMS. It also clearly depicts the gradual approximation of total credit composition of the NMS to the EU28.

Figure 2: Proportion of loans by type of total credit granted to households and NFCs in EU28 and NMS (2007-2016)



Source: ECRI Statistical Package 2017.

As indicated, the total credit figures mask two major divergent trends and considerable heterogeneity within loan categories and between countries. Furthermore, they raise the question of whether Europe is experiencing a demand-driven recovery or whether corporate investment has been financed

through alternative financing sources. To better grasp the dynamics of European credit markets, the following sections conduct a more granular analysis of the developments by sector and loan type.

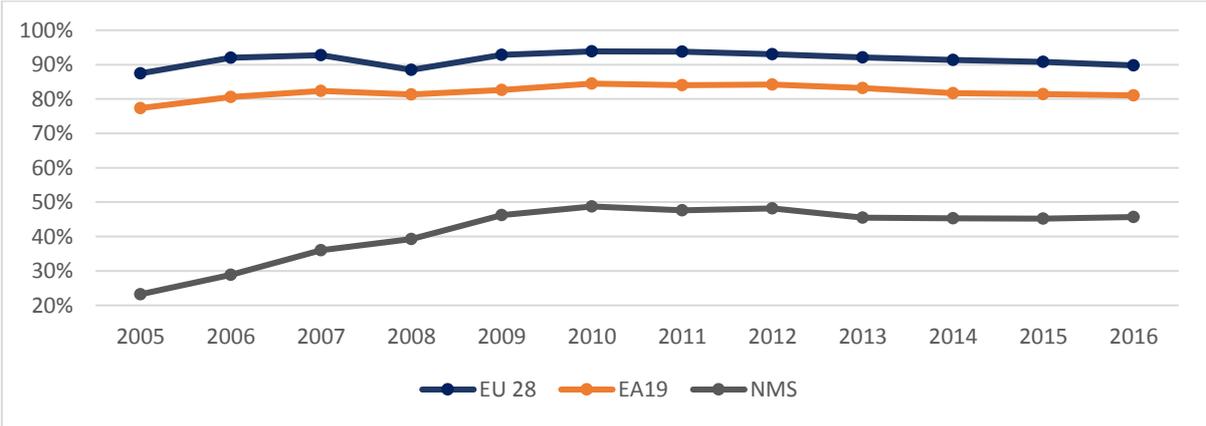
Private credit markets in the European Union

Total lending to households is composed of consumer credit, housing loans and other loans. In 2016, household lending made up more than 62.8% of total lending, a share that has increased by an average annual rate of 0.7% since 2009. In 2016, total credit to households increased by 1.4% in the EU28 (0.8% in the EA) and by 3.6% in the NMS in real terms. Looking at the composition of total credit to households in 2016, *consumer credit* experienced the most remarkable expansion of 3.13% in real terms in the EU28, with a magnitude of 0.2 percentage points more than in the previous year. Real growth rates for *other loans* continue to contract by -2.9% in the EU28.

Whereas growth rates have been positive for three consecutive years and imply credit ease across all country groups, only the NMS managed to return to and even exceed pre-crisis levels of total outstanding credit. In 2016, outstanding credit for the EU28 lay at 98.7% of 2010 levels, the year that marked the peak of outstanding consumer credit in absolute terms.

Although not equivalent, the ratio of outstanding credit to households as a percentage of disposable income can be seen as a proxy for the indebtedness of the household sector. Consequently, the more indebted a household, the less new credit it is going to take on. Theoretically, this translates into higher credit growth rates in country groups with lower debt-to-income ratios. As the data reveals, this is also the case in the EU, where the ratio of outstanding credit to disposable income in the EU28 lies at 89.1% (81% in the EA19) and 45.6% in the NMS. In addition, consumer credit growth rates were more than twice as high in the NMS as in the EU28 in 2016. Despite having slowed down considerably since 2010, these findings convey a positive message for the convergence process between the NMS and the rest of the EU, (see Figure 3).

Figure 3: Total credit to households as % of gross disposable income, by country group (2005-2016)

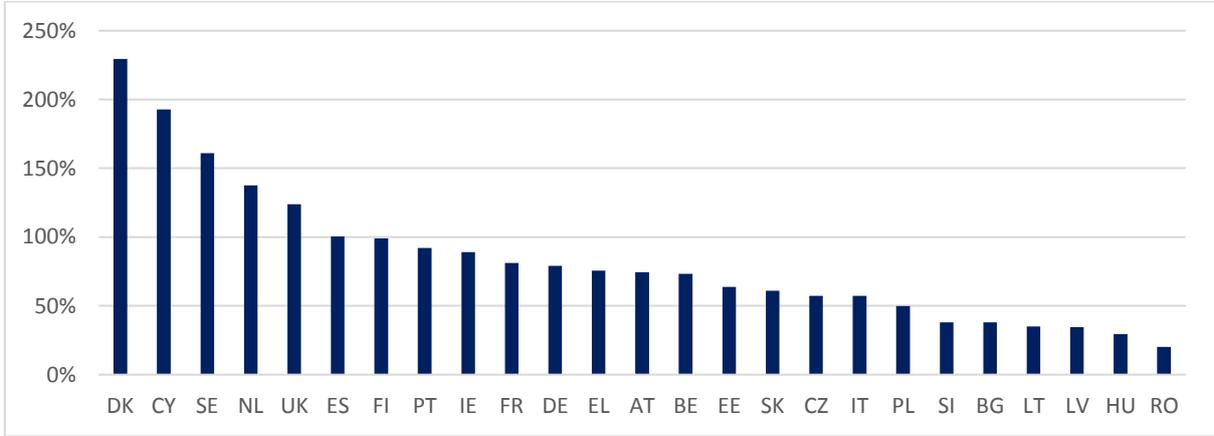


Source: ECRI Statistical Package 2017.

On a country level, there is considerable heterogeneity between countries in credit-to-disposable income ratios, which is reflected in a range of 209.2% between credit-to-income ratios. With 229.5%, Denmark records the highest credit-to-disposable income ratio throughout the EU, and Romania the lowest, with 20.24%. Yet, as Figure 4 highlights, the countries of the NMS are all among those with the lowest ratios. The exception is Cyprus, whose high ratio is the product of excessive credit growth and where the ratio is declining, with a decrease of more than 13.2% in 2016. Today, the main factors

influencing the declining stock of outstanding credit in Cyprus are the insufficient creditworthiness of the household sector, restrictive loan origination requirements and limited capital headroom.⁵

Figure 4: Total credit to households as a % of disposable income of households, EU28 (2016)



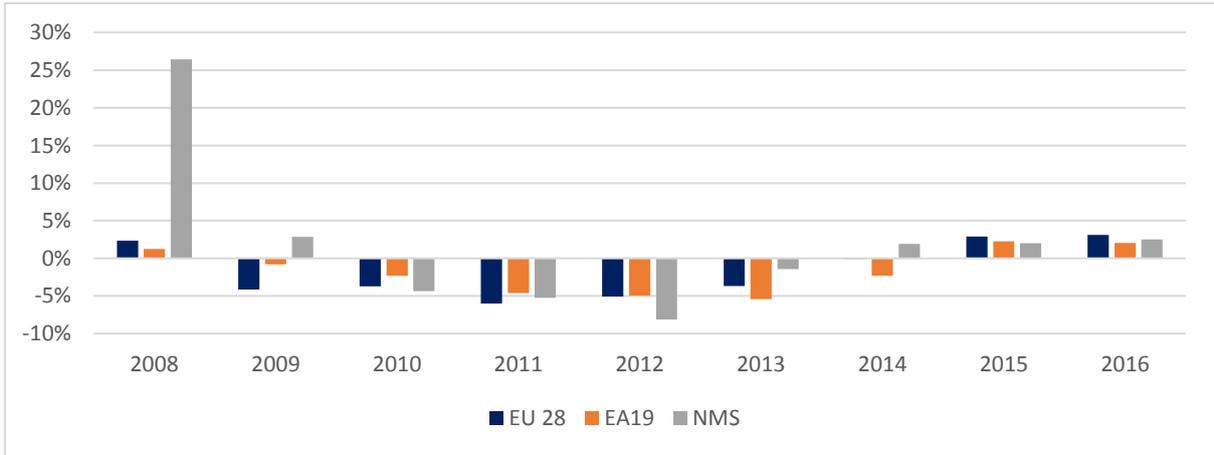
Source: ECRI Statistical Package 2017.

As a percentage of GDP, total credit to households showed no major change from the previous year and remains at 55.6% for the EU and 50.3% and 29.3% for the EA and the NMS respectively.

Consumer credit

Consumer credit comprises credit used for buying goods and/or services that are consumed by households individually. It constitutes 12.1% of total credit to households in the EU28 and EA and 26.8% in the NMS. Debt financing for consumption appears to play a greater role in the NMS than in the member states of the euro area and the EU28 as a whole. The difference in proportions is considerable and could be traced back to different credit cultures, as well as to differences in the indebtedness of the household sector.

Figure 5: Annual variation in outstanding consumer credit, by country group (2009-2016)



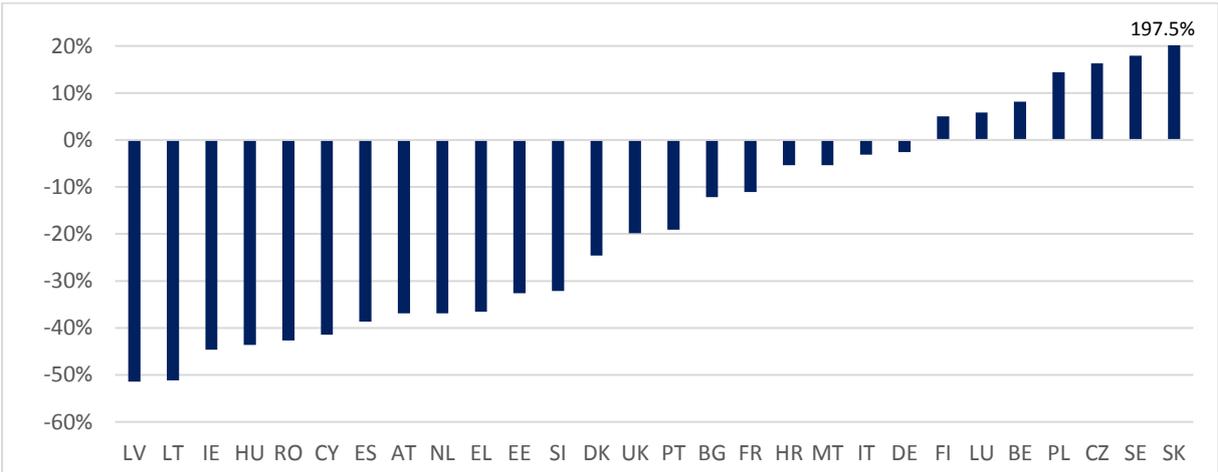
Source: ECRI Statistical Package 2017

⁵ For more information on the Cypriot banking sector development, see: European Commission (2017), Country Report Cyprus 2017 (SWD(2017)78 final).

Across all country groups, consumer credit exhibits positive annual growth rates with an increasing magnitude (Figure 5). In 2016, outstanding amounts increased by 3.1% in the EU28 and 2.5% in the NMS. Considering that credit for consumption does not include housing loans, the strong growth rates imply that households regained confidence in future economic development encouraging them to take on extra debt for consumption. In 2014, consumer credit reached its highest cumulative contraction since 2008 with a magnitude of -20.2% in the EU28. After two years of consecutive growth, it is now at 84% of the 2008 level. In the NMS, consumer credit returned to 91.4% of the peak outstanding amount in 2010. Hence, although increasing growth rates show that the EU has embarked on a recovery from the financial crisis, absolute amounts of outstanding consumer credit are still a comparatively long way from pre-crisis levels.

At country level, there is considerable variation in the growth rates, with few obvious patterns in terms of geographical distribution. In addition, Figure 6 shows that despite positive growth rates for two consecutive years, very few countries have so far managed to return to or exceed pre-crisis levels yet. With more than 10 percentage points' increase on the previous year, Portugal and Ireland experienced the highest increase in consumer credit to 2015. Considering their faltering recovery since the financial crisis in 2008, these developments are seen as positive and indicative of improved consumer confidence.⁶

Figure 6: Cumulative variation outstanding consumer credit in the EU, by country in euro (2008-2016)

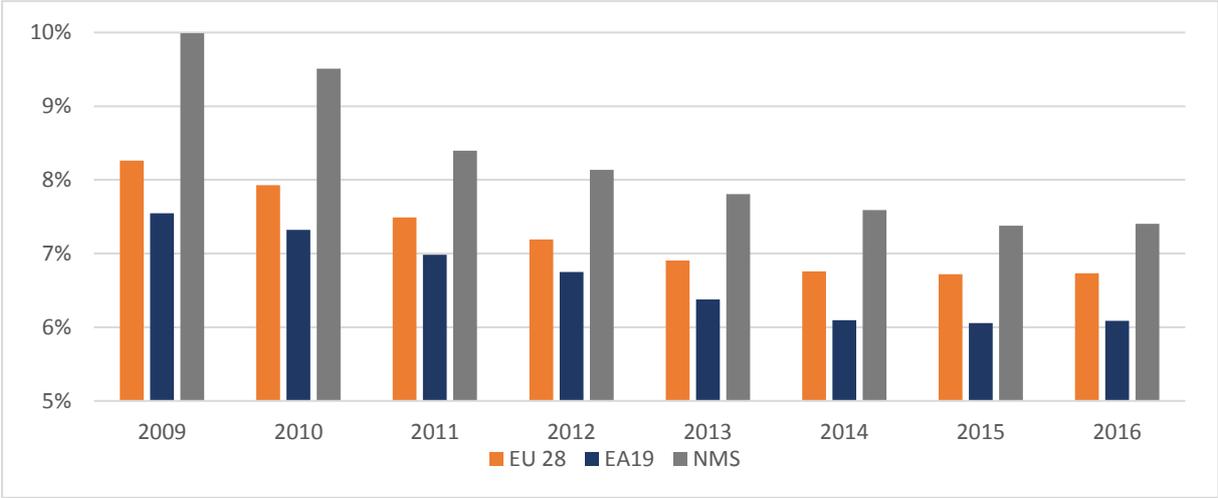


Source: ECRI Statistical Package 2017

In terms of percentage of GDP, the fraction remains steady. In the EU28, consumer credit accounts for 6.7% (6.1% for the EA) while in the NMS, it accounts for 7.4% (Figure 7). With more than 10% of GDP, consumer credit as a percentage of GDP is largest for Croatia, Cyprus, Greece and the UK and smallest for Lithuania, Latvia, the Netherlands and Luxembourg, with less than 3%.

⁶ For further information, see: European Commission (2017), Post-Programme Surveillance Report, Portugal. Brussels.

Figure 7: Annual percentage change of outstanding consumer credit as a percentage of GDP, by country group (2009-2016)



Source: ECRI Statistical Package 2017

Overall, consumer credit markets present a positive picture, recording increasing growth rates for the second consecutive year. Whereas total outstanding amounts have not yet reached pre-crisis levels, the trend suggests that consumer credit markets have embarked on the road to recovery.

Housing loans

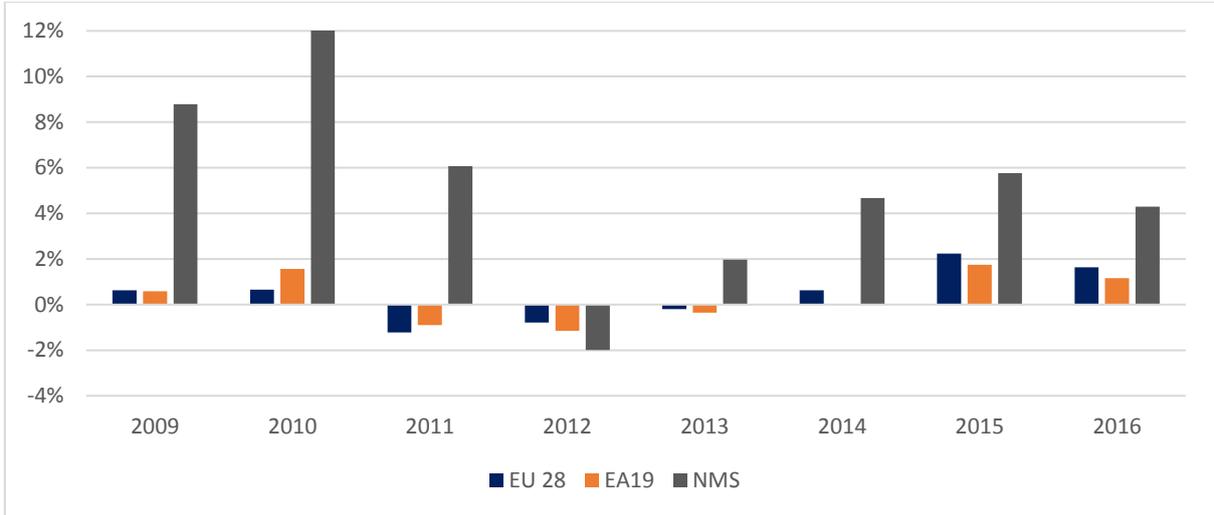
Housing loans are crucial to bank lending and historically constitute the largest share of credit to households in Europe. In 2016, housing loans in the EU28 accounted for more than 78% of total private credit (78.1% in the EA) and 49.1% of total credit to households and NFCs (43.2% in the EA). For the third consecutive year in the EU28, housing loans in the EU28 experience an expansion of 1.7% (Figure 8). Despite the implementation of the EU Mortgage Credit Directive (MCD) by March 2016, housing loans in the EU28 and the EA remained relatively stable. Due to their outstanding importance to households and therefore relative immunity to the economic situation, they only experienced a slight contraction of a magnitude between 1-3% during the crisis in the EU28 and Euro area and exceeded pre-crisis levels across all country groups.

In the NMS, housing loans make up a smaller fraction, with 38.72% of total loans and 67% of loans to households. In 2016, they experienced an annual growth rate of 4.3%, a magnitude of more than 2.5 times than in the EU28. Since the growth of outstanding housing loans turned positive again, cumulative growth rates between 2008 and 2016 are especially noteworthy for the NMS, as they experienced an increase in total outstanding housing credit of 54.3%, as opposed to the EU28 and the EA19, which experience a weak expansion of only 3.7% in the EU28. This difference could be the combined result of the convergence process between the NMS and the EU28, but also of the availability of credit through foreign banks.

At country level, cumulative variation between 2009 and 2016 has been very heterogeneous, with a range of 155.1%, with Slovakia experiencing the highest increase in housing loans of 117.3% and Latvia the lowest, at 37.7%. Latvia’s low cumulative growth is an aftermath of the Baltic housing bubble that burst in 2008, which is reflected in a contraction rate of -1.82% in 2016. Slovakia’s increase is accompanied by two-digit growth rates for the fourth consecutive year. While these numbers appear alarming at first, the rapid credit growth has not so far given rise to any economic imbalances as total

credit levels continue to be comparatively low (36.3% of GDP and 61% of total household credit to disposable income in 2016).⁷ In 2014, the National Bank of Slovakia introduced macro-prudential measures to address the excessive credit growth, but the data reveals that to the present day, these measures have not been successful. Up to now, the indebtedness of the Slovakian household sector increases by an average rate of 4.04% per year, which indicates that credit growth could eventually become a problem if it continues at the same pace.

Figure 8: Annual variation of total outstanding housing loans in 2016, by country group



Source: ECRI Statistical Package 2017.

Housing loans as a percentage of GDP remained relatively stable in the EA19 and NMA, with less than a 0.5 percentage point increase in the fraction, and fell slightly for the EU28. At country level, there is considerable variation in the housing loan as a percentage of GDP, with higher rates among non-NMS countries. In Denmark, outstanding housing loans constitute more than 102.9% of the GDP, followed by Cyprus (72.46%) and the UK (70.25%). The lowest numbers can be found in Romania (7.7%), Hungary (8.36%) and Bulgaria (9.46%).

There is thus a continuation of the trend depicted in 2016, with a slight but steady overall expansion of housing loans in 2016. Cumulative variation at country level reveals considerable heterogeneity between countries with a range of almost 200% in variation in outstanding housing credit since 2008.

Credit to Non-Financial Corporations

Whereas the development of the credit market for households conveys a positive signal for Europe’s recovery, credit to NFCs tells a different story, recording a contraction for the eighth consecutive year of -0.45% in the EU28 (Figure 9). This is particularly worrisome since 90% of NFC debt financing is intermediated through banks in the EU, as opposed to only 30% in the US. Assuming that lending by NFCs translates into investment, the development of outstanding credit to NFCs should be of utmost importance to the recovery of the EU and a strong indicator of the recovery of the market. Furthermore, it raises questions about the success of the efforts undertaken by the ECB to strengthen

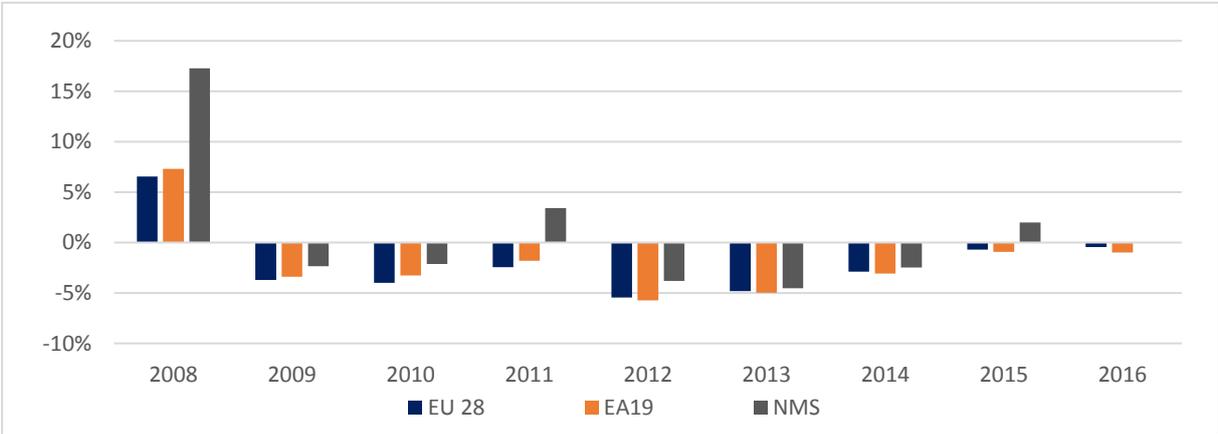
⁷ For more information, see: Harvan et al. (2015), “The Impact of Rapid Credit Growth on Slovakia’s Housing Market”, European Commission, Brussels.

liquidity and ease credit through lowering interest rates to the zero-lower bound and asset purchasing programmes.

Overall, credit to NFC has continued to decline for eight years in a row for the EU28 and the euro area and turned negative again after a positive peak in the NMS in 2015. Total outstanding loans to NFC are 19% lower in the EU28 and EA today than they were in 2009. In the NMS, outstanding loans are only -8.7% below their peak amount in 2011. Given the rising stocks of base money in the EU as well as the low interest rate environment, the continued contraction hints at a weak monetary transmission mechanism and continued tight credit standards for NFCs.

According to EIB findings, overdependence on bank lending in comparison to market-based financing can slow down the recovery process.⁸ This is well reflected in the data because, apart from the slow overall recovery, the European corporate sector exhibits a strong overdependence on bank lending and has still not entered recovery. It is particularly the case for the PIIGS that are, in addition to overdependence on bank lending, among the countries with the biggest banking sectors and record negative growth rates across all loan types.

Figure 9: Annual variation in outstanding credit to NFCs, by country group (2008-2016)



Source: ECRI Statistical Package 2017.

Also on a country level, 21 out of 28 countries record outstanding corporate credit levels well below the pre-crisis level, with a cumulative contraction of down to -56.45% for Slovenia and -71.7% for Ireland (Figure 10). Since 2015, Luxembourg has experienced the highest increase in loans to NFCs, with a real growth rate of 10.2%, whereas Ireland, Slovenia and Cyprus experienced the highest contractions with -9.3%, -10.7 and -14.4% respectively. Although negative, the contraction of -9.3% in Ireland constitutes a noticeable improvement compared to the contraction of -22.3% it experienced in 2015. While a move towards non-bank funding has been raised as one of the possible reasons for the Irish decline in outstanding bank lending, Ireland is particular due to its high share of multinational corporations. As they do not interact with the national financial system, debt levels of NFCs differ considerably on a national and international level.⁹

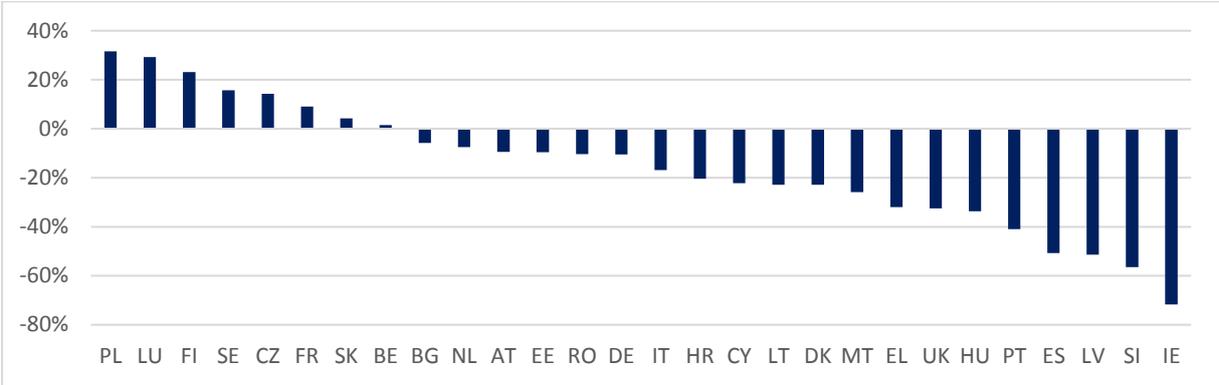
With a range of 24.6%, there is less inter-country variation in annual growth rates than in 2015, where the range was more than 52.3%. Credit to NFCs continues to contract, but at a slower pace than in

⁸ For further information, see EIB (2014), “Unlocking Lending in Europe”.

⁹ For more information, see: Irish Central Bank (2016), Quarterly Bulletin 02/April 16.

previous years. If the trend continues, aggregate growth rates for the EU28 might soon return to positive.

Figure 10: Cumulative variation in outstanding loans to NFCs by country (2009-2016)



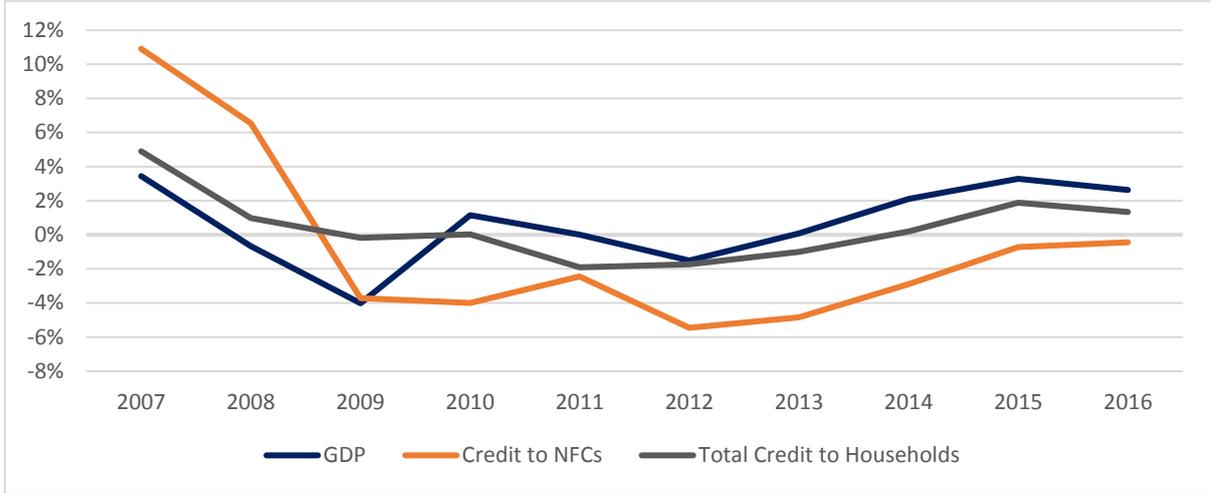
Source: ECRI Statistical Package 2017.

What is driving Europe’s recovery?

Credit markets in Europe have undergone diverging trends in the last year. Given the stable economic growth for four consecutive years, outstanding credit to NFCs is declining, which would translate into fewer investments and ultimately less economic growth. The fact that GDP is nonetheless increasing suggests two possible explanations.

First, it might be demand that is driving economic growth due to increased disposable income and household lending, a possibility backed up by the data released in the Statistical Package 2016. A second explanation hints at alternative ways of corporate debt financing through the market, whereby investment would be decoupled from bank lending and the annual variation of outstanding credit would no longer be a proxy for investment. Figure 11 illustrates that annual variation in GDP nonetheless correlates with both variation in household credit and corporate credit. Bank lending to NFCs seems to be hampered by various factors such as weak monetary transmission, low profitability and tight credit conditions. The persistent correlation between annual variation in NFCs and GDP shown in Figure 11 shows the importance of SME-investment to Europe’s recovery and considerable unleashed potential for further GDP growth once credit to NFCs starts moving again.

Figure 11: Annual growth rate of GDP, total credit to households and credit to NFC in EU 28 (2005-2016)



Source: ECRI Statistical Package 2017.

In sum, the findings of the ECRI Statistical Package 2017 are a positive sign for the recovery of credit markets for households across the EU countries and country groups. Credit to NFCs continues to be weak and recovery is slow, however. The magnitudes of annual growth rates show that 2015 represented a positive peak for household credit, as they continue to be positive but are weaker. The opposite is the case for credit to NFCs, where annual growth rates are negative but record a smaller magnitude in 2016. If the trends identified continue, Europe’s private and corporate credit markets might soon enter into full recovery again.