Banks in the CEE/SEE countries benefit from ample deposit funding and a strong liquidity cushion

22 September 2017

Intesa Sanpaolo
Research Department

International Research Network

Davidia Zucchelli
Economist

- Banks in the CEE/SEE countries benefit from ample deposit funding. The funding and the liquidity profile are strong and are expected to remain stable.
- The "deposits from the private sector/GDP" ratios strongly increased after the break of the financial crisis, growing from an average of 44% in 2008 to 53% in 2016 in the area (countries with ISP subsidiaries). This strong increase could be explained by growing uncertainties both in the household sector and in the corporate sector. Uncertainties in the labor market among families and lack of investments opportunities among corporates supported deposits hold for prudential reasons, despite low and decreasing interest rates.
- Bank deposits are playing a relevant role in bank funding. In all countries, with the only exception of Albania among countries with ISP subsidiaries, the weight of deposits in the total asset increased from 2008 to 2016, strongly in Slovenia and in Romania (by around 20pp).
- In all countries with ISP subsidiaries, deposits count for most of liabilities. The deposits/TA ratio is particularly high in Slovakia and in Albania, equal to 75% of total liabilities, while the lowest percentage refers to Hungary (48% as of December 2016), where foreign liabilities and liabilities from other financial institutions show relevant shares (more than 13% and 15%, respectively). Bonds and other funding products with longer maturity are missing in banking balance sheets.
- In 2016 and in the first part of the current year, foreign liabilities continued to record negative percentage annual changes despite better financial conditions for western European banks proving the underlying trend of rebalancing the financing of EE subsidiaries towards local sources. Similarly, their impact on TA further decreased, although with less intensity in the last few years. The Foreign liabilities/TA ratios declined by around 20pp from 2008 to 2016 in Slovenia, where particularly in 2014 banks repaid most of their European Central Bank borrowing, but also in Bosnia, Hungary and Romania.
- The LTD ratio offers a first indication. In the last few years, all countries with ISP subsidiaries showed a strong decrease in the LTD ratio from December 2008 to December 2016, with the only exception of Slovakia. In Slovenia and in Ukraine the decrease was particularly intense, by 82pp and 59pp respectively. In Romania, the LTD decreased by over 50pp as well. It was due to both the fall or the deceleration of lending activity because of the strong economic crisis and to the positive dynamic of deposits, which increased quite strongly in all countries in the same period.
- The fall of nominal interest rates on household deposits was particularly strong in Hungary (-7.6pp) from 2008 to 2016 among CEE countries and in Romania and Serbia (-10.4pp and -7.5pp respectively) among SEE countries.
- The asset management activity currently plays a limited role in Emerging Europe's banking systems. It remains a niche activity but its growth potential appears to be relevant. It is reasonable to believe that driven by increasing expected returns investments into CEE/SEE assets may grow in the near future but stronger financial systems are necessary. Capital markets remain in their infancy in the area, although they are growing slowly. The development of capital markets is being strongly supported by central authorities. Their clear policy message is that it is better to finance the real economy through several channels rather than relying on just one, banking.

Deposits still prevail among banking liabilities

In the financial development process – as shown in more mature economies – deposits represent the first fundamental step to satisfy liquidity purposes of clients, both corporates and households – like basic commodities – while other more sophisticated products can be used (such as securities, particularly government bonds, and asset management with mutual funds and pension funds) for saving purposes. The asset management activity[1] plays currently a limited role in the banking systems of the CEE/SEE countries[2]. It remains a niche activity but its growth potential appears to be relevant.

In the CEE/SEE countries, bank deposits still dominate among household assets[3]. This note is organized as follows. At first, the role played by deposits, with respect both to the GDP and the banking total asset, has been analysed; then, the composition of deposits is also studied to highlight the short-term component, the most volatile part of bank funding.

Funding: the growing role of deposits

The "deposits from the private sector/GDP" ratios strongly increased after the break of the financial crisis, growing from a average of 44% in 2008 to 53% in 2016 in the area (countries with ISP subsidiaries)[4]. This strong rise could be explained mainly by growing uncertainties in the labor market among families, which supported deposits hold for prudential reasons, and lack of investment opportunities among corporates, despite low and decreasing interest rates.

The increase in deposits was particularly strong in the countries where the deposits/GDP ratio was lower. It has been the case of Serbia, where the ratio increased from 29% at the end of 2008 to 46% as of December 2016, and in Russia (from 26% to 47%). In Croatia, the deposits/GDP ratio rose gradually from 56% to 73% in the period, both because of deposits' increase and the GDP decrease. In Hungary, the ratio declined in 2012 to 42.3% (from 43.4% at the end of the previous year) and further in the year ahead to 37.7% in 2014, growing again during the following years, to 40.2% in 2016.

In contrast, in Ukraine the ratio decreased from 33%, a low level, to 28% in 2016 because of the economic crisis and political tensions.

---

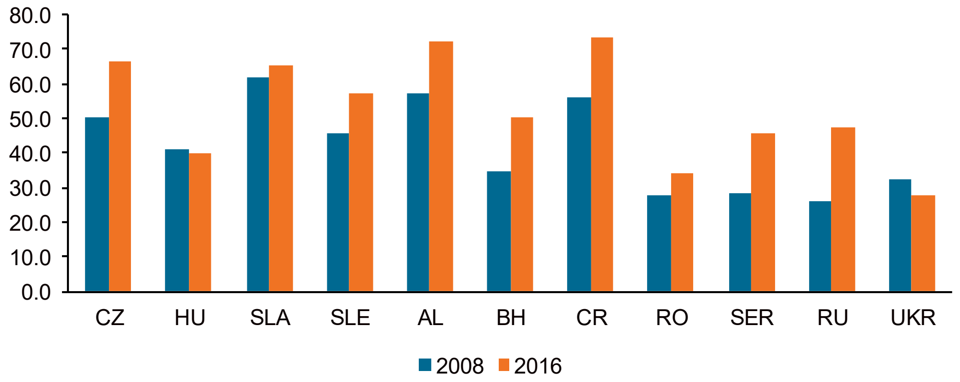
[1] The asset management activity refers to assets under management by banks and other financial institutions. Asset management companies recently built up in many countries – also called bad banks – to manage NPLs are not considered in this note. For example, in November 2014, the Magyar Nemzeti Bank (MNB) established the Magyar Reorganizációs és Követeléskezelo (MARK), an asset management company in order to help restore monetary transmission, credit growth, and economic recovery. Banks' participation is voluntary, market prices determine valuations, and MARK's lifetime is 10 years.

[2] In this note CEE/SEE countries with ISP subsidiaries have been considered.

[3] See on this topic, E. Beckmann, M. Hake, J. Urvova, Determinants of Households' Savings in Central, Eastern and Southeastern Europe, Focus on European Economic Integration Q3/2013, OeNB.

[4] Bank deposits are a household asset class strictly connected to savings. This connection appears to be still very strong in the CEE/SEE countries. Bank deposits depend not only on macroeconomic drivers (GDP, unemployment and income, inflation and interest rates, exchange rate and government budget balance) but also on financial structure (the financial deepening) and banking fundamentals (liquidity, ALM, profitability, and regulation). Saving rates vary considerably across countries and over time. In N. Loayza, K. Schmidt-Hebbel and L. Serven, What Drives Private Saving around the World?, World Bank, WP 2309, March 2000, an analysis of saving determinants can be found.

Deposits from the private sector/GDP (countries with ISP subsidiaries, %)

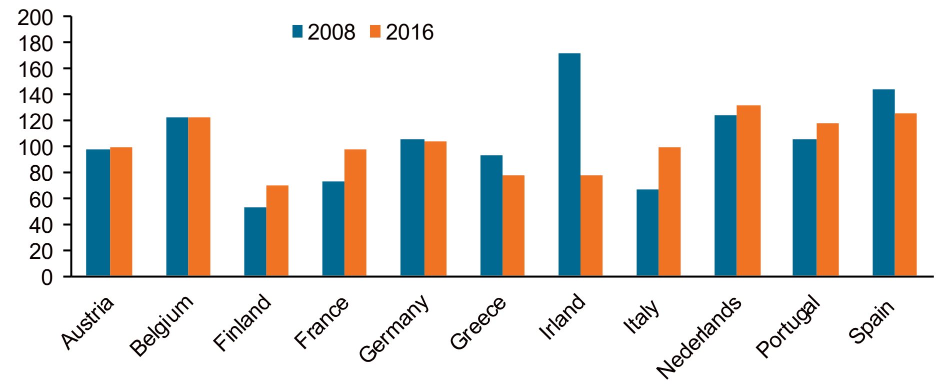


Source: ISP elaborations on central banks' data

The increase in the Deposits/GDP ratio is also connected to the convergence process of Emerging Europe to most mature European countries, which is gradually taking place in the area in all banking activities[5]. Despite its stop and go evolution, the trend towards a most homogeneous playing field is in progress.

Deposits are expected by IRN to increase gradually in the next few years, at higher rates than loans, but showing a slight deceleration from the recent highs, partially affected by stronger competition from investment funds[6].

Bank deposits/GDP (some Western European countries, %)



Note: customer deposits in the banking system (excluding deposits with other banks). Source: ISP elaborations on EIU data

The average of the "bank deposits/GDP" ratio among biggest Western European countries remained slightly over 100% in 2008 and in 2016. Nevertheless, the dispersion remains high

[5] In comparing the savings behaviour of market economies and transition economies, a very interesting paper (by C. Denizer, H. Wolf, The Savings Collapse during the Transition in Eastern Europe, World Bank, WP2419, Aug 2000) highlighted substantial similarities, except for a negative link between savings and GDP growth. The transition economies of Eastern Europe almost uniformly experienced a precipitous plunge in savings rates – from levels above 30 percent of GDP to levels about half that – early in the transition, before rebounding slightly. Involuntary savings – reflecting binding limits on consumption spending below desired levels – played a special role on that.

[6] See IRN Forecast Note, September 2017. Forecast on asset management is connected to private financial wealth. According to Boston Consulting Group, mentioned by I. Walter, The Industrial Organization of the Global Asset Management Business, CFA Institute Research Foundation, 2015, the private financial wealth is expected to growth at the average annual change of 10% until 2019.

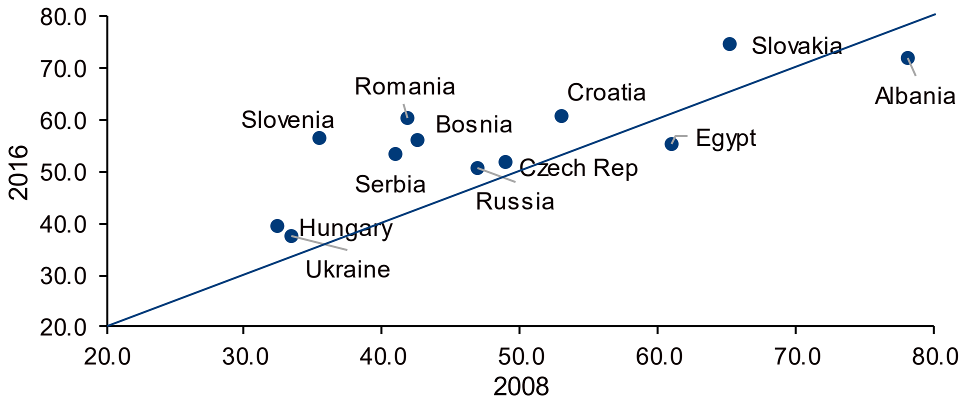
depending essentially on the prevailing banking business model (based on commercial banks or on capital markets) and on the diffusion of alternative saving products.

The gap between Western and Eastern European countries partly shows that there is still room for growth in this segment in the latter. At the same time, a still low level of financial deepening is evident[7].

Nevertheless, new room can be highlighted in the bank liabilities structure using bond or covered bond and other long-term securities first of all to reach a more adequate asset & liabilities mismatching. In fact, bank deposits are still playing a relevant role in bank funding, as shown by the **deposits of the private sector/TA ratio**[8].

In all countries, with the only exceptions of Albania and Egypt among countries with ISP subsidiaries, the weight of deposits in the total asset increased from 2008 to 2016, particularly in Slovenia and in Romania (by around 20pp).

Deposits from the private sector/TA (countries with ISP subsidiaries, %)



Note: in the left part of the chart there was an **increase in ratio**. Source: ISP elaborations of central banks' data

Still plenty of room for growth in bank accounts

Bank accounts count for the highest share among deposits (see table on page 11). The analysis of the diffusion of bank accounts and their utilisation (payment services vs savings) is useful to

[7] It is interesting to note that bank deposits and asset management, especially mutual funds and money market funds, are strictly interconnected. The roles of mutual funds as funding providers for banks appear to vary across instruments and developed countries. Mutual funds invest in long-term bank bonds (more in the United States than in other economies), but generally they are not the main holders of bank bonds whereas money market funds play a more significant role in short-term funding markets. See IMF, *The asset management industry and financial stability,* Global Financial Stability Report, April 2015.

[8] At the same time, the asset under management industry plays a very modest role in Eastern Europe currently. In the last Annual Report of the European Fund and Asset Management Association (EFAMA), only the Czech Republic and Hungary are included among the highest 15 European countries with a very modest market shares of the total asset under management in Europe (0.2% and 0.1% respectively at end 2015, but a quite significant AuM/GDP ratio 21% and 25% respectively). See EFAMA, Asset management in Europe, 9th Edition, Facts and figures, May 2017.

understand at first the actual level of financial inclusion[9] – that is the first basic step in the financial development process – and potential opportunities[10].

While access to financial services is reasonably high in more mature economies, it is not so good in CEE/SEE countries. In the latter case, financial access is also distributed unevenly[11]. Specifically, many women, young people and rural populations remain disconnected from the financial system. The reasons for such exclusion vary depending on the circumstances of the household or individual, with many young people being discouraged by onerous documentation requirements, while older people are often deterred by long distances to the nearest bank branch.

In many countries in the area, bank accounts are widely used by adults, especially in Slovenia (with over 97% of adults) and Croatia (86%), among the High Income (HI) countries, as defined by the World Bank[12], as well as in Serbia (over 83%) and Hungary (with 72.3% of adults) among the Upper Middle Income (UMI) countries. In contrast, in the other countries, the gap remains high. This is the case of Slovakia (77%) and particularly of Russia (67%) among HI countries, and for Albania (38%) and Bosnia (53%) among UMI countries. In this latter group, the gap between men and women is higher (around 4-5pp).

With regard to gender, it is interesting to note that in many High Income countries bank accounts are used more by women than men[13], contrary to the category average. This is the case for Slovakia, Croatia and Russia, as well as Hungary among Upper Middle Income countries.

Banks could find further business opportunities with young people (aged between 15 and 24 years old) which show a very diversified degree of distribution. In Slovakia and Croatia, bank accounts diffusion is very low, equal to 38% and 58%, respectively, well below the category average (84%). A similar result has been recorded in Hungary (50.7% compared to 58.1% in the respective income category). Such data – bearing in mind, however, any regulatory restrictions that may limit the opening of bank accounts based on age – point to significant growth potential for financial services to new customers[14].

The use of bank accounts is modest for the payment of bills, in the ISP countries, with the exception of Czech Republic, where it is 53.8%, compared to a category figure of more than 60%

---

[9] Interest in financial inclusion – which refers to the possibility of accessing financial services, first of all by holding a bank current account with adequate fees and charges – is spreading rapidly around the world due to its positive effects on the degree of economic and social development. According to the EIU, *Global Microscope 2016, The enabling environment for financial inclusion,* 2016, financial inclusion is now on the global agenda and is understood to be a critical foundation for the improvement of livelihoods, earning it a key role in the United Nations' 2030 Sustainable Development Goals.

[10] Many studies indicate that financial inclusion is not only positively correlated with growth and employment, but it is generally believed to causally impact growth. Safeguard savings (particularly in form of bank deposits) can help households and small enterprises manage cash flow spikes, and build working capital. See the numerous World Bank publications, available on the website.

[11] See EBRD, *Transition report 2016-17*, November 2016.

[12] See World Bank, *The little book on financial inclusion*, April 2015. For years, the World Bank has sought to monitor this issue due to its significant impact in terms of financial inclusion.

[13] The weight taken by women deserves to be considered, especially in view of the lesser degree of risk associated with them as clients, generally in emerging countries, as well as due to the higher return in terms of utilisation and investment of the financial resources at their disposal, more than likely intended for family, school, healthcare or for the creation of a more solid basis for future growth.

[14] Considering young people a target of financial products may seem like a marginal business, due to the modest capacity for savings and demand for credit, as well as the irregular transactions, but this must be viewed in a broader strategy of approach towards future families, as a means of gaining greater loyalty in customers and as a cross-selling opportunity (young people help parents use mobile devices).

(in HI countries). In UMI countries, the use is high in Hungary (32%), compared with a category average of 12.3%.

With regards to the **payments system,** the use of debit cards is significant in Slovenia, Hungary and Serbia, with percentages above the respective averages of the relevant categories. Furthermore, the figures referring to actual use show a higher use of **debit cards** than credit cards in all countries, revealing significant potential for growth in this latter area, particularly in Slovakia and Hungary (which generally show a higher level of distribution and use of these accounts). Bank accounts are used predominantly for saving purposes.

The **use of the Internet** to make payments, such as utility bills, appears to be modest, especially in the High Income countries examined, with percentages well below the category average (54%), especially in Russia (17.5%). By contrast, among the Upper Middle income countries, where the percentages are much lower, the use of the Internet in Hungary is much higher.

Bank accounts (%, 2015)

	High Income Countries						Upper Middle Income Countries						
	SLA	SLE	HR	CzRep	RU	High Income	HU	AL	BH	RO	SRB	Upper Middle Income	Europe & Centr. Asia
All Adults (% age 15+)	77.2	97.2	86.0	82.2	67.4	94.0	72.3	38.0	52.7	60.8	83.1	70.5	51.4
Women (% age 15+)	80.0	97.0	87.7	79.4	70.2	93.8	72.5	33.6	47.1	56.9	83.0	67.3	47.4
Young adults (% ages15-24)	37.6	91.5	57.8	64.9	54.4	84.1	50.7	30.0	34.4	55.0	77.8	58.1	35.6
Used an account to receive wages*	43.4	46.1	43.2	45.4	37.9	44.3	35.9	10.8	18.6	24.2	31.5	18.1	22.5
Used an account to receive government transfers *	22.6	16.8	11.4	19.4	14.1	17.2	11.1	3.5	2.1	5.2	5.9	9.6	7.3
Used an account to pay utility bill*	41.2	48.4	9.8	53.8	12.2	61.1	31.9	2.6	3.0	6.9	6.2	12.3	12.5
Has debit card	70.5	91.3	71.1	64.0	44.3	79.7	59.9	21.8	34.4	45.8	57.8	45.9	36.9
Used a debit card to make payments	63.5	65.8	50.4	52.2	35.0	65.3	47.1	4.0	18.7	24.4	38	19.9	22.9
Used a credit card to make payments	13.6	29.9	32.8	20.0	16.6	46.7	8.9	4.0	6.2	9.8	12.0	14.4	14.9
Used the Internet to pay bills or make purchases	36.7	35.9	19.9	45.7	17.5	54.1	22.2	3.3	3.3	11.5	9.7	15.3	11.9
Sent remittances	9.9	NA	13.0	14.3	12.9	NA	9.4	19.5	8.0	11.1	13.2	15.4	12.9
via a fin. institution **	NA	NA	63.8	40.2	48.5	NA	NA	16.5	NA	32.3	24.2	37.2	31.5
via a mobile phone **	NA	NA	2.6	4.2	8.0	NA	NA	1.1	NA	0.0	8.5	8.8	2.5
via a money transfer operator**	NA	NA	4.7	3.0	28.0	NA	NA	10.9	NA	27.0	19.8	19.7	11.8
Received remittances	13.6	NA	15.8	15.9	12.0	NA	12.0	27.1	8.6	13.8	12.0	17.8	15.5
via a fin. institution **	22.5	NA	54.6	25.6	36.2	NA	17.1	13.9	NA	35.9	17.2	29.8	22.1
via a mobile phone **	0.0	NA	4.7	1.2	6.9	NA	0.0	1.4	NA	0.0	2.3	5.6	1.0
via a money transfer operator**	6.8	NA	2.8	1.9	19.1	NA	11.9	12.1	NA	42.2	21.2	17.9	15.6
Mobile account (% age 15+)	NA	NA	NA	NA	NA	NA	NA	NA	NA	0.5	NA	0.7	0.3

Note: (*) the use is referred to the previous year; (**) % of the total sent. SLA=Slovakia, SLE=Slovenia, HR=Croatia, CzRep=Czech Republic, RU=Russia, HU=Hungary, AL=Albania, BH=Bosnia and Herzegovina, RO=Romania, SRB=Serbia. NA= not available. The distribution of income used by the World Bank is as follows (refers to 2013): Low income countries: gross national income (GNI) per capita USD 1,045 or less in 2013; Middle-income countries: GNI more than USD 1,045 but less than USD 12,746; Lower-middle income and upper-middle income countries are separated by a GNI per capita of USD 4,125; High-income countries: GNI per capita of USD 12,746 or more. Source: World Bank 2015

The data referring to the use of a **mobile account** are not available for many countries[15]. Only in Romania there is a distribution, albeit modest (with 0.5% of the population older than 15 years of age), slightly below that referred to the Upper Middle Income category (0.7%).

With regards to **remittances** – sent to families and for savings reason – both sent and received, the use of bank accounts is significant, much more than in the *mobile phone* channel. Both the transmission and receipt of remittances, however, are still significantly carried out through money

[15] Data from the World Bank are not available for HI countries and the euro area. The distribution is very significant in Sub-Saharan Africa (11.5%) and in Low Income countries (10.0%). The other categories for which data are available are as follows: East Asia & Pacific (0.4%), Latin America & Caribbean (1.7%), Middle East (0.7%), South Asia (2.6%), Middle Income (1.5%), Lower middle income (2.5%), Low & Middle income (2.5%).

transfer operators. In some cases – notably Romania and Serbia among the countries examined and with reference to the receipt of remittances – they account for higher transaction volumes than bank accounts. The use of accounts for both inbound and outbound remittances is particularly significant in Russia, to a level that seems to be similar. The use of bank accounts is notable, and it is much larger than the mobile phone channel.

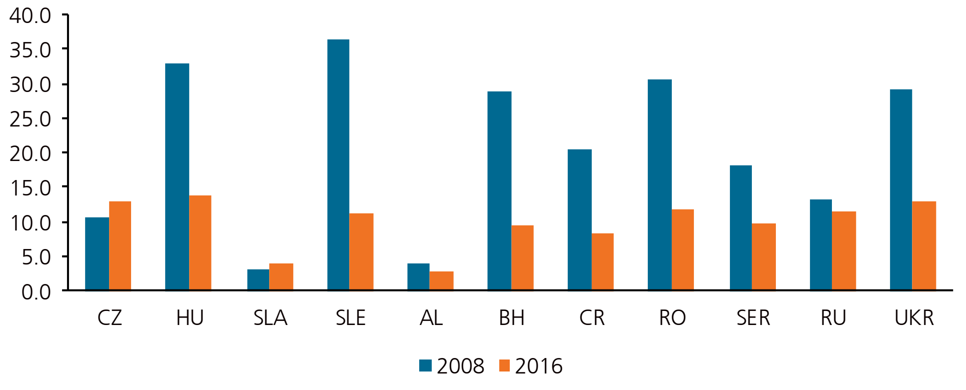
From external to internal funding

After the economic and financial international crisis, a relevant shift from external sources to national sources was realized in Emerging Europe [16].

In 2016 and in the first part of the current year, foreign liabilities continued to record negative percentage annual changes despite better financial conditions for western European banks. It furtherly proves the underlying trend of rebalancing the financing of EE subsidiaries towards local sources. Similarly, their impact on TA decreased further, although with less intensity in the last few years.

The foreign liabilities/TA ratios declined by around 20pp from 2008 to 2016 in Slovenia, where particularly in 2014 banks repaid most of their European Central Bank borrowing, but also in Bosnia, Hungary and Romania.

Foreign Liabilities/TA (countries with ISP subsidiaries, % share)



Note: in the Czech Republic and in Russia data as of December 2015. Source: ISP elaborations of central banks' data

Thanks to the recent macroeconomic recovery, a new rebound is expected but following a dynamic much less intensive than it was before the international crisis.

In Bosnia and in Hungary, foreign liabilities reported an increase as of May 2017, by +2.8% yoy and 5.4% yoy respectively, after negative monthly yoy changes since October 2009.

[16] Relevant changes occurred internationally also among global banks. One major trend has marked banks' adjustment to the post-crisis environment concerning funding mix. Banks have generally reduced their reliance on unsecured short-term wholesale funding and increased that on retail funding, such as customer deposits. This has formed part of a broader shift towards more retail-oriented business models, with relatively stable funding and income sources. See BIS, 87th Annual Report, June 2017.

Foreign capital inflows could have stronger effects for the corporate sector than for the household sector, because corporate saving in the CEE/SEE countries appears to be more dependent on the availability of foreign capital inflows than household saving does[17].

Furthermore, it is reasonable to believe that driven by increasing expected returns foreign investments into CEE/SEE assets may grow in the near future but stronger financial systems are necessary. Capital markets remain in their infancy in the area, although they are growing slowly. The development of capital markets is being supported by central authorities[18]. In fact, their clear policy message is that it is better to finance the real economy through several channels rather than relying on just one, banking[19]. Capital markets particularly can act as a useful 'spare tyre'[20].

Liquidity is not a source of concern

In the last few years, all countries with ISP subsidiaries showed a strong decrease in the LTD ratio from December 2008 to December 2016, with the only exception of Slovakia. In Slovenia and in Ukraine the decline was particularly intense, by 82pp and 59pp respectively. In Romania, the LTD decreased by over 50pp as well. It was due both to the fall or the deceleration of lending activity because of the strong economic crisis and to the positive dynamic of deposits, which increased quite strongly in all countries in the same period. Liquidity has been intensively supported in the last few years of course by central banks as well in order to support the economic recovery.

The comparison with Western European countries could be misleading. In fact, the European LTD average was around 150% and relatively stable in the last 5 years, but the dispersion is also high. In Italy, Belgium and Portugal the ratio was around 110% in 2016, while in Germany, Greece and Spain it was around 140%, but in Austria, Finland and the Netherland it was higher than 180%.

---

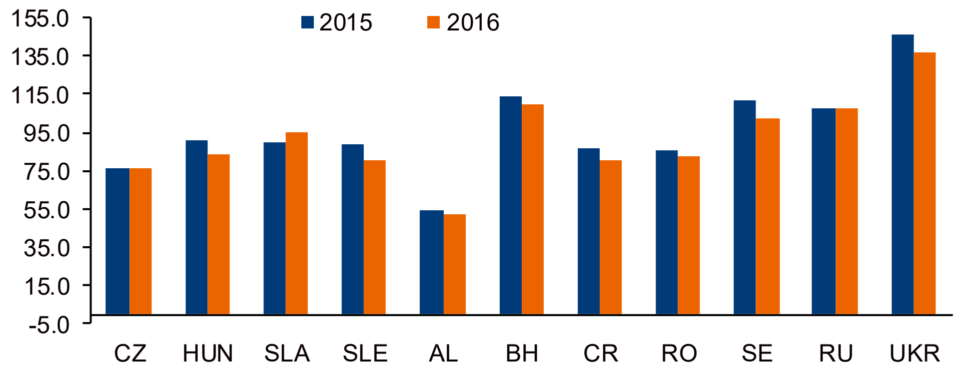
[17] See M.Kukk, K. Staehr, Macroeconomic Factors in Corporate and Household saving. Evidence from Central and Eastern Europe, Eesti Pank, WP 5/2015.

[18] Policy makers aim to have a smaller, safer and more consolidated banking system where higher risk is priced appropriately. See OECD, OECD Business and Finance Outlook 2016, OECD Publishing, Paris, 2016.

[19] The European banking sector has outgrown capital markets (see the widely cited report, ESRB Advisory Scientific Committee (ASC), *Is Europe Overbanked?*, No.4/June 2014). In the late 1990s, the ratio of total bank assets/equity and private bond market capitalisation in Europe was below two. By 2008, this ratio had risen to four. By contrast, the comparable ratio in the US remained below one over this period, and that of Japan remained below two. One of the most relevant effects of an excessive presence of banks in a country is procyclicality. Banks play a vital role in financing households and small and medium-sized enterprises, which are a key part of the European economy. This lending must continue to flow to productive projects if an economy is to prosper. But bank lending has a tendency to be procyclical: growing too quickly when an economy expands and shrinking sharply when it contracts. As a result, in the aftermath of a financial crisis, economic growth in countries with bank-based systems lags behind that of countries with more balanced financial systems. See Mario Draghi, President of the European Central Bank and Chair of the European Systemic Risk Board, *Welcome address at the first annual conference of the ESRB*, Frankfurt am Main, 22 September 2016.

[20] That is why the ESRB fully supports the capital markets union, which aims to remove barriers to the development of capital markets. Removing these barriers will foster changes in the structure of the financial system in Europe.

LTD ratio (countries with ISP subsidiaries, %)



Source: ISP elaboration of central banks' data

This high LTD level has to be interpreted taking into consideration the complex availability of many other funding products for banks in Western European countries, which can use bonds, covered bonds and also equity subordinated bonds with longer maturity.

Deposits count for most of total liabilities

In all countries with ISP subsidiaries, deposits count for most of liabilities. Their share (the deposits/TA ratio) is particularly high in Slovakia and in Albania, equal to 75% of total liabilities, while the lowest percentage refers to Hungary (48% as of December 2016), where foreign liabilities and liabilities from other financial institutions show relevant shares (more than 13% and 15%, respectively). Bonds and other funding products with longer maturity are missing in banking balance sheets.

Liabilities (composition, %, December 2016)

	Tot. Deposits	Foreign liabilities	Bond	Public funds	Banks	Equity	Other liab.	Total
Hungary	48.4	13.4	4.0	0.0	15.2	13.9	5.1	100
Slovakia	74.9	0.0	6.5	0.0	5.7	11.0	1.9	100
Slovenia	63.1	11.3	0.1	0.0	4.6	12.0	8.8	100
Albania	74.9	2.6	0.4	2.1	1.6	10.0	8.4	100
Bosnia	68.1	9.5	0.0	0.0	0.0	14.5	8.0	100
Croatia	64.4	8.3	0.6	4.2	2.4	20.8	-0.3	100
Romania	68.1	11.8	0.3	0.0	0.0	15.7	4.1	100
Serbia	58.0	9.7	0.0	2.0	0.0	24.9	5.4	100
Russia	62.5	0.0	1.4	3.4	11.7	10.8	10.2	100

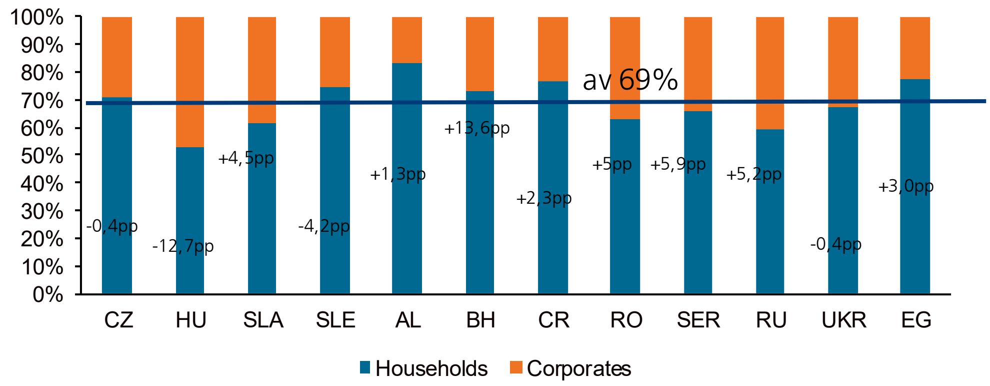
Source: ISP elaboration of central banks' data

In order to evaluate funding stability, household deposits have to be highlighted. Corporate deposits are held for transactions or prudential purposes, waiting for future investment, not for savings, therefore they are more volatile than household deposits.

The following chart shows that around 70% of total deposits were hold by households as of December 2016. Changes in the share were very modest from 2008 to 2016, most of them indicating an increase (by some pp only). In contrast, changes have been strong in Bosnia, where the share of household deposits increased by 13%, and in Hungary, where instead it decreased by the same percentage (13%), reflecting an average annual rise of household deposits by 8.4% in Bosnia and by a very low +1.7% in Hungary in the same period.

In contrast, corporate deposits increased by 2.7% (average of annual changes from 2008 to 2016) in Bosnia and by 6.3% in Hungary.

Deposits (from households and from corporates, December 2016, %)



Note: changes in pp are increases/decreases in HH deposits' shares vs 2008. Source: ISP elaboration of central banks' data

A further information in order to evaluate the funding stability is connected to deposits' composition. It is reasonable to believe that short-term deposits, with very low interest nowadays, could be more volatile. As highlighted in the following table, in almost all countries transaction/current account deposits account for most of total deposits. The available data don't allow to compare perfectly single categories among all the ISP countries, but the dominance of shorter maturities is clear.

Deposits (composition by maturity, %, December 2016)

	Transaction/ Current account	Demand Deposits	short-term	up to 1 y	up to 2 y	up to 5y and more	long term deposits	Total deposits
Hungary	61.4			25.3	1.2	12.1		100
Slovakia	60.6	6.0					33.4	100
Slovenia	51.9	2.0	14.1				31.9	100
Albania	28.7	5.4		46.7	7.9	11.3		100
Bosnia	24.2	24.7	5.2				45.9	100
Croatia	34.3		6.8				58.9	100
Romania	46.4			46.1			7.5	100
Serbia		52.0		29	7.0	12.0		100
Russia		19.3		32.4			48.3	100
Ukraine		45.9		34.3	18.7	1.1		100

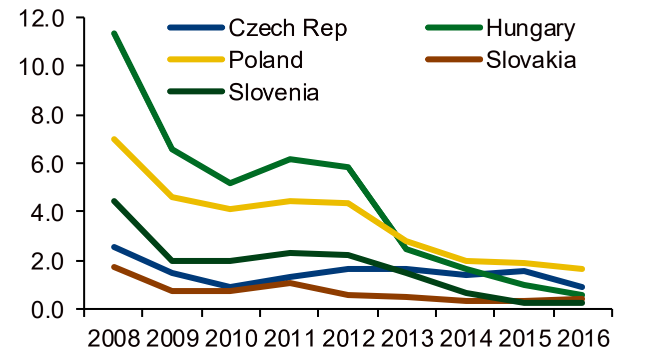
Source: ISP elaboration of central banks' data

Low interest rates

In the last few years, interest rates have been following a downturn trend. Extraordinary monetary policy action since the global financial crisis has brought interest rates down to historically low levels in Europe. In the countries with ISP subsidiaries, interest rates are following the same path. The direction remains clear, but the intensity of the fall varies among countries depending of course on specific economic, financial and liquidity conditions.

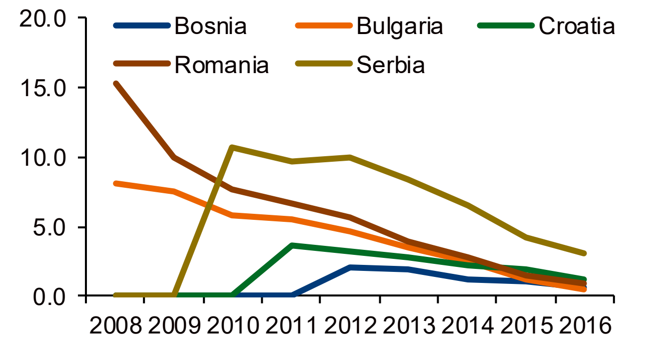
The fall of nominal interest rates on household deposits was particularly strong in Hungary (-7.6pp) from 2008 to 2016 among CEE countries and in Romania and Serbia (-10.4pp and -7.5pp respectively) among SEE countries.

Interest rates on household deposits (CEE countries, %)



Source: ISP elaboration of central banks' data

Interest rates on household deposits (SEE countries, %)

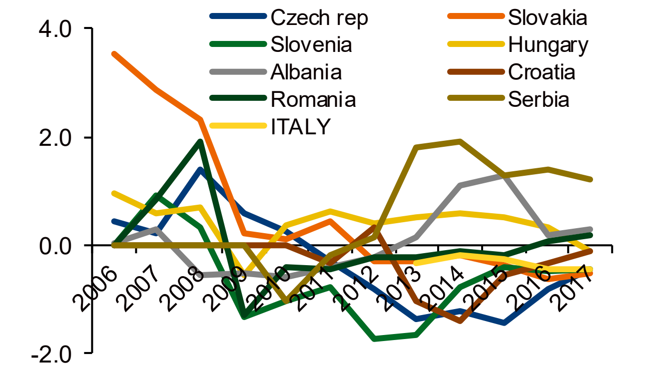


Source: ISP elaboration of central banks' data

The so-called "mark-down" – the difference among the money market (in general the interbank 3 months rate) and the household deposits interest rate, that indicates the "convenience" for banks to attract deposits instead of using interbank funds – shows that in the last few years it has been negative in most of the countries (with deposits interest rates higher than money market rates), particularly in the CEE countries. Deposits represent the most stable component of funding, while the utilization of interbank funds is usually limited to temporary funding needs. In "normal" market conditions, banks collect deposits from households (workers) and set deposit rates as mark-down of the interbank rate.

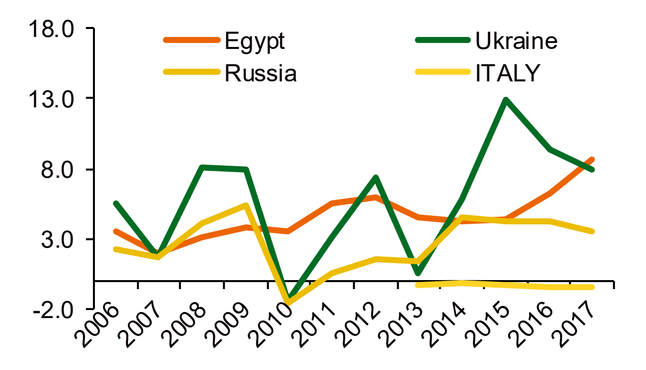
The pricing of deposits could also be influenced by competition. In CEE countries and Croatia, with very low deposits interest rates, the mark-down has been negative probably because of the need to support internal funding resources (especially deposits from households, the most stable funding source) while foreign liabilities were rapidly decreasing.

Mark-down (pp, CEE/SEE countries)



Source: ISP elaboration of central banks' data

Mark-down (pp, CIS countries)



Source: ISP elaboration of central banks' data

Nevertheless, negative mark down – connected to very high liquidity conditions in the market[21] – could indicate the possibility to lower further deposits interest rates, even though competition among banks could limit this strategic choice.

[21] The mark-down is not only a feature in the CEE/SEE countries. With regards to Italy, Mario Draghi wrote: "In two years net interest income has fallen from 2.0 to 0.9 per cent of total assets, owing to the slowdown in lending and the decrease in the mark-down on sight deposits caused by the low level of interest rates.", Mario Draghi: Economic growth outlook, regulatory measures and the situation of Italian Banks, Verona 26 February 2011.

Intesa Sanpaolo Research Department – Head of Department Gregorio De Felice		
Tel 02 8021 + (3) Tel 02 879 + (6)		
International Research Network - Head Gianluca Salsecci	35608	gianluca.salsecci@intesasanpaolo.com
Macro Economist – Latin America, CSI and MENA Giancarlo Frigoli	32287	giancarlo.frigoli@intesasanpaolo.com
Macro Economist – Emerging Asia Silvia Guizzo	62109	silvia.guizzo@intesasanpaolo.com
Macro Economist – EEC and EEA Antonio Pesce	62137	antonio.pesce@intesasanpaolo.com
Macro Economist – Trade and industry Wilma Vergi	62039	wilma.vergi@intesasanpaolo.com
Macro Economist – Banks and markets Davidia Zucchelli	32290	davidia.zucchelli@intesasanpaolo.com

Analyst certification and other important information

The financial analysts who prepared this document hereby state that the opinions, forecasts and estimates contained herein are the result of independent and subjective appraisal of the data, facts and information acquired and that no portion of their compensation has been or will be, either directly or indirectly, related to the investment strategy recommended or proposed in this document.

This publication was prepared by Intesa Sanpaolo SpA. The information and opinions contained herein were obtained from sources believed by Intesa Sanpaolo SpA to be reliable, but no guarantee is made as to their accuracy or completeness. This publication was prepared solely for information and illustrative purposes, and is not intended as a proposal for conclusion of a contract or solicitation of the purchase or sale of any financial products. The document may be reproduced wholly or in part only if Intesa Sanpaolo SpA is cited as the author.

This publication is not intended to replace the personal opinions of the parties to which it is addressed. Intesa Sanpaolo SpA and its subsidiaries, and/or any other party related to these, reserve the right to act on the basis of or to make use of any of the material described above and/or any information from which this material originates, before the same is published and made available to customers. Intesa Sanpaolo SpA and its subsidiaries, and/or any other party related to these, may occasionally assume long or short positions on the financial products mentioned above.