

## Euro area bank lending survey of March 2019: main results for Latvia

Latvijas Banka conducted a euro area bank lending survey in cooperation with the European Central Bank in March 2019, covering the lending developments during the first quarter of 2019 and expectations for the second quarter of 2019. Four Latvian banks whose total market share in lending to non-financial corporations and households is large enough to represent lending development in Latvia as a whole participated in the survey. Their replies have been incorporated in the euro area bank lending survey results.

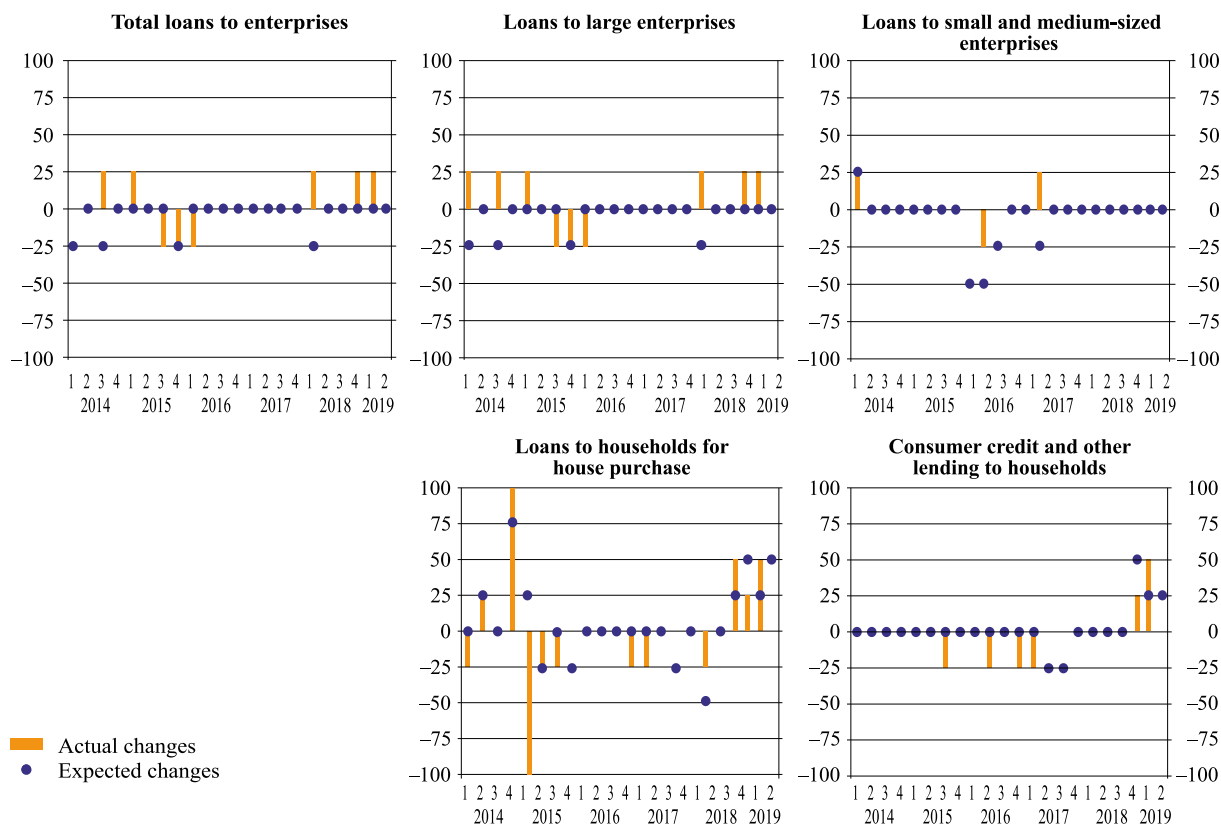
### Credit standards

In the first quarter of 2019, one of the four surveyed Latvian banks applied slightly tighter credit standards for loans to enterprises as a whole, but at the sectoral level – for long-term loans to large enterprises (see Chart 1). This bank explained that the decision on the application of tighter credit standards was taken due to the situation in and outlook of individual sectors or enterprises as well as owing to the deterioration in creditworthiness of individual borrowers. With credit standards tightening, the share of completely rejected applications for loans to enterprises expanded slightly in the above bank. The surveyed Latvian banks have no intention to change credit standards for loans to enterprises as a whole in the second quarter of 2019. However, they could apply somewhat tighter credit standards for individual groups of loans to enterprises (one of the four banks – for long-term loans to enterprises and the other one – for loans to large enterprises).

Chart 1

#### CHANGES IN CREDIT STANDARDS

(net percentage of banks reporting tightening credit standards; %)



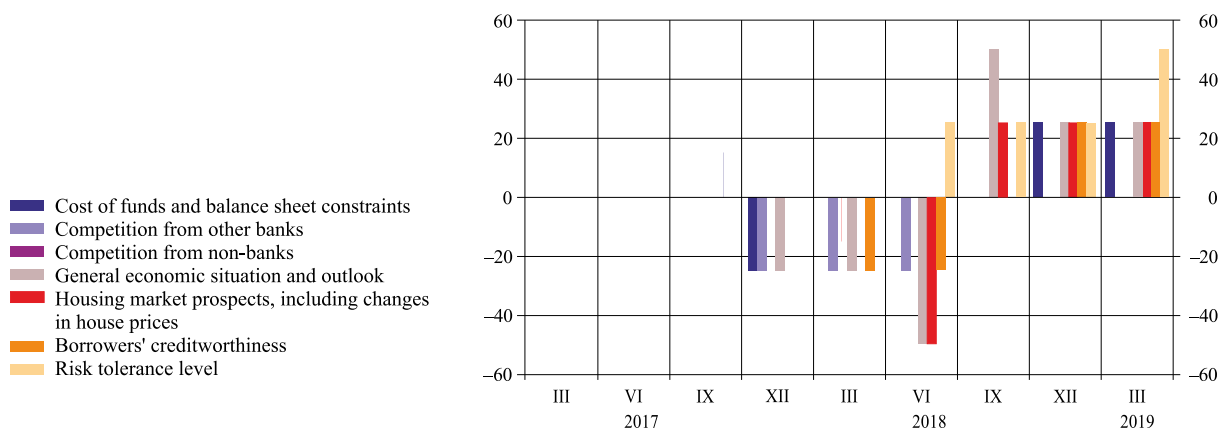
In the first quarter of 2019, the credit standards applied by several surveyed Latvian banks for loans to households were somewhat tighter than for loans to enterprises. Two of them pointed out that they had slightly tightened credit standards both for loans to households for house purchase and for consumer credit and other lending to households during the reporting period (see Chart 2).

The application of tighter credit standards for loans to households for house purchase in the two above Latvian banks was driven by the raising of the risk tolerance level, but in each of them individually – also by specific factors inherent in the particular bank (the cost of funds and balance sheet constraints, the general economic situation and outlook as well as the assessment of housing market prospects and the deterioration in borrowers' creditworthiness).

Chart 2

### FACTORS EXPLAINING THE APPLICATION OF TIGHTER CREDIT STANDARDS FOR LOANS TO HOUSEHOLDS FOR HOUSE PURCHASE

(net percentage of banks reporting positive factor contributions; %)



The factors behind the application of tighter credit standards for consumer credit and other lending to households were similar to those affecting credit standards for loans to households for house purchase. Two of the four surveyed Latvian banks somewhat tightened credit standards for consumer credit and other lending to households since their risk tolerance level was increased. A more critical assessment of the general economic situation and outlook and the deterioration in the consumers' creditworthiness were additional factors determining the application of tighter credit standards in the respective loan category by one bank.

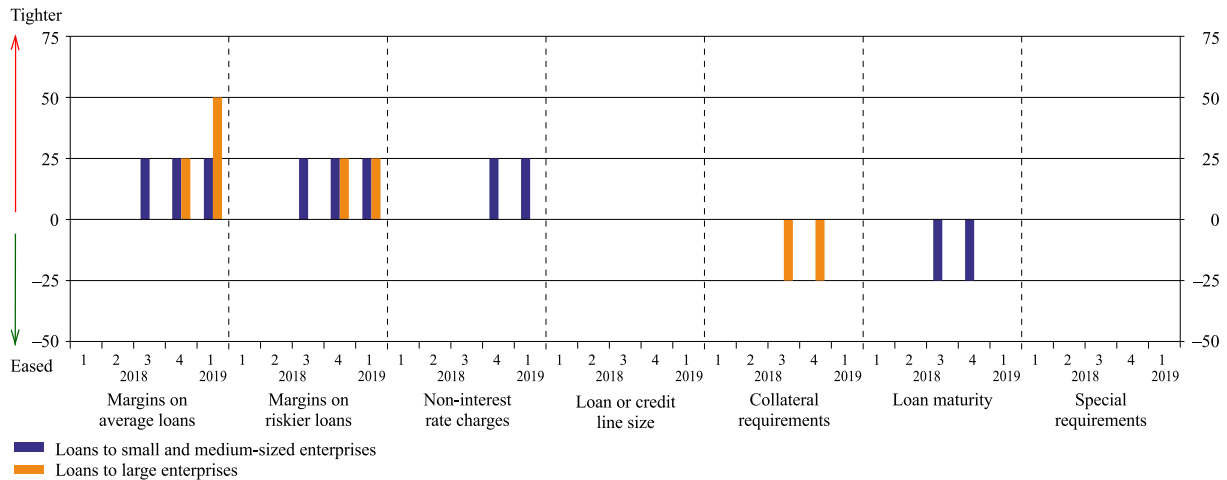
The surveyed Latvian banks intend to tighten credit standards for loans to households also in the next quarter. Two of the surveyed Latvian banks intend to tighten slightly credit standards for loans to households for house purchase and one – for consumer credit and other lending to households in the second quarter of 2019. During the reporting period, the share of completely rejected applications for consumer credit and other lending to households relative to the volume of all loan applications increased slightly in one surveyed bank, while the share of completely rejected applications for loans to households for house purchase remained unchanged in all banks.

#### Credit terms and conditions

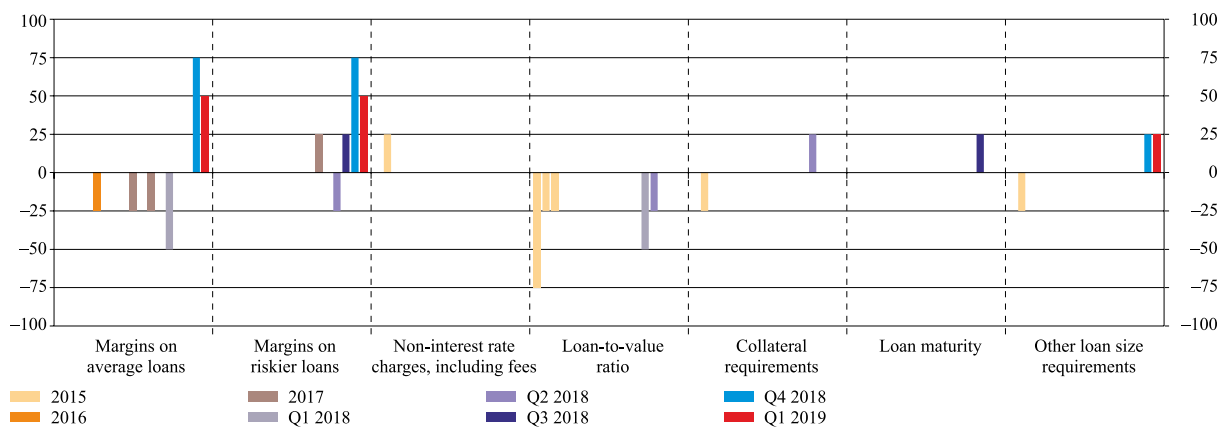
One surveyed Latvian bank tightened slightly its general credit terms and conditions for loans to enterprises. Two banks, without changing the general credit terms and conditions, tightened somewhat the aspects characterising these terms and conditions. As regards loans to enterprises as a whole, two surveyed Latvian banks slightly widened margins on average loans in the first quarter of 2019, but one bank – the margin on riskier loans. It also increased non-interest rate charges and reinforced the loan contract terms and conditions relating to the prevention of money laundering.

The bank, which tightened the credit standards for long-term loans to large enterprises, also tightened credit terms and conditions for large enterprises only. Meanwhile, other banks that had not changed the respective credit standards, applied equal tighter credit terms and conditions for both small and medium-sized enterprises and the large ones. Thus, Latvian banks were more favourable towards small and medium-sized enterprises in the first quarter of 2019, as was the case in the previous quarter (see Chart 3). One bank, in addition to the above changes in credit terms and conditions, which affected loans to enterprises as a whole, slightly decreased the loan or credit line size for loans to large enterprises. Meanwhile, one of the four surveyed Latvian banks narrowed margins on average loans to small and medium-sized enterprises.

Changes in margins on average loans to enterprises as well as in non-interest rate credit terms and conditions are related to cost of funds and balance sheet constraints in one of the surveyed Latvian bank and changes in risk assessment in two banks. Changes in margins on riskier loans to enterprises stem from constraints on funds and the balance sheet in one of the surveyed Latvian banks.

**Chart 3****CHANGES IN TERMS AND CONDITIONS FOR LOANS TO ENTERPRISES***(net percentage of banks reporting tightening of credit terms and conditions; %)*

Two surveyed Latvian banks applying slightly tighter credit standards for loans to households for house purchase somewhat tightened also the general terms and conditions for these loans (see Chart 4). During the reporting period, the two banks widened margins on both average and riskier loans to households for house purchase. Moreover, one of them notably widened margins on riskier loans. In addition, one bank adopted somewhat more stringent size limits on loans to households for house purchase.

**Chart 4****CHANGES IN CREDIT TERMS AND CONDITIONS FOR LOANS TO HOUSEHOLDS FOR HOUSE PURCHASE***(net percentage of banks reporting tightening of credit terms and conditions; %)*

The main reasons that led the surveyed Latvian banks to applying somewhat tighter credit terms and conditions for loans to households for house purchase in the first quarter of 2019 were the banks' cost of funds, balance sheet constraints, risk perceptions and the risk tolerance level (any of the four banks has mentioned each factor once).

In the first quarter of 2019, credit terms and conditions for consumer credit and other lending to households remained unchanged in all surveyed Latvian banks. However, two of them pointed out that the risk tolerance level contributed somewhat to the application of tighter terms and conditions for the respective category loans as a whole. Furthermore, this factor also affected margins on average and riskier loans in one bank. In addition, changes in risk perceptions in one bank contributed to tightening its general terms and conditions for consumer credit and other lending to households.

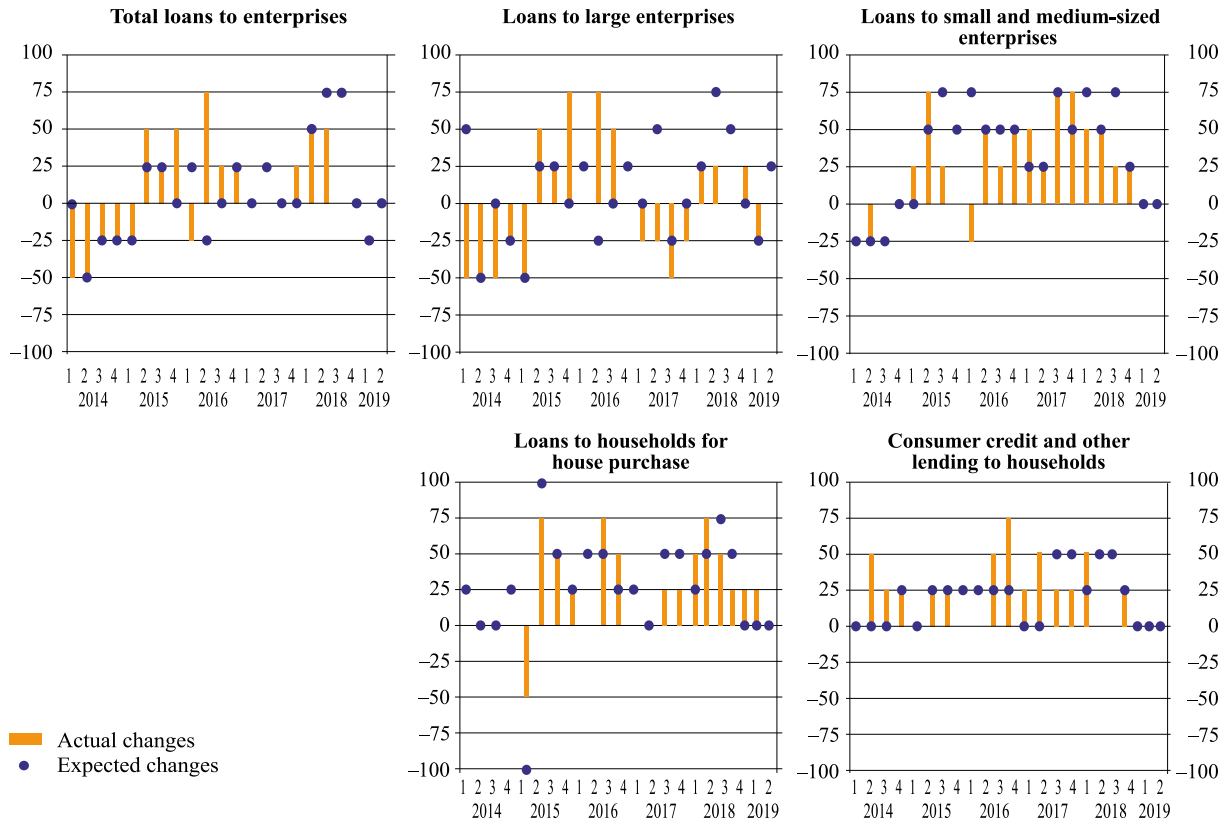
**Demand for loans**

In the first quarter of 2019, the demand for loans to large enterprises decreased marginally in one bank, but this decline had no effect on the demand for loans to enterprises as a whole (see Chart 5).

Chart 5

## CHANGES IN LOAN DEMAND

(net percentage of banks reporting increased demand for loans; %)



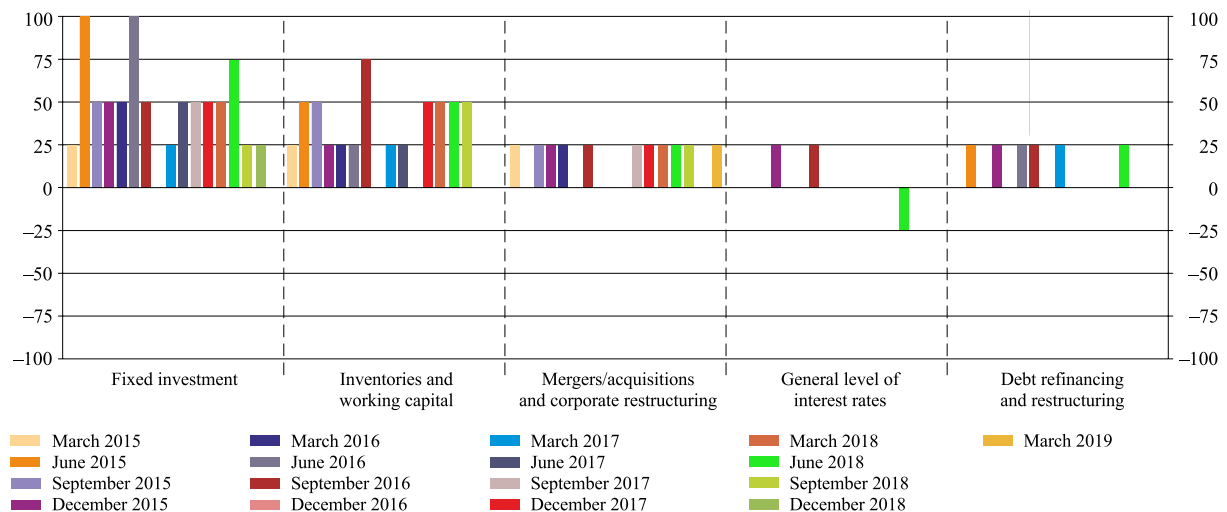
The weaker demand for loans to large enterprises in one bank was explained by a reduced need for fixed investment funding as well as by the availability of internal financing and loans from other banks (see Chart 6). Meanwhile, the banks, where the demand for loans to enterprises remained unchanged in the first quarter of 2019, believe that the need for fixed investment funding, mergers, acquisitions and corporate restructuring as well as less favourable loans from other banks still contribute to the demand for loans to enterprises. Since Latvian banks' assessment of the impact of various factors on firms' demand differ, their overall assessment reveals that during the reporting period mergers, acquisitions and corporate restructuring had a significant positive effect on the demand for loans to enterprises but a negative one – on the use of firms' internal financing.

Chart 6

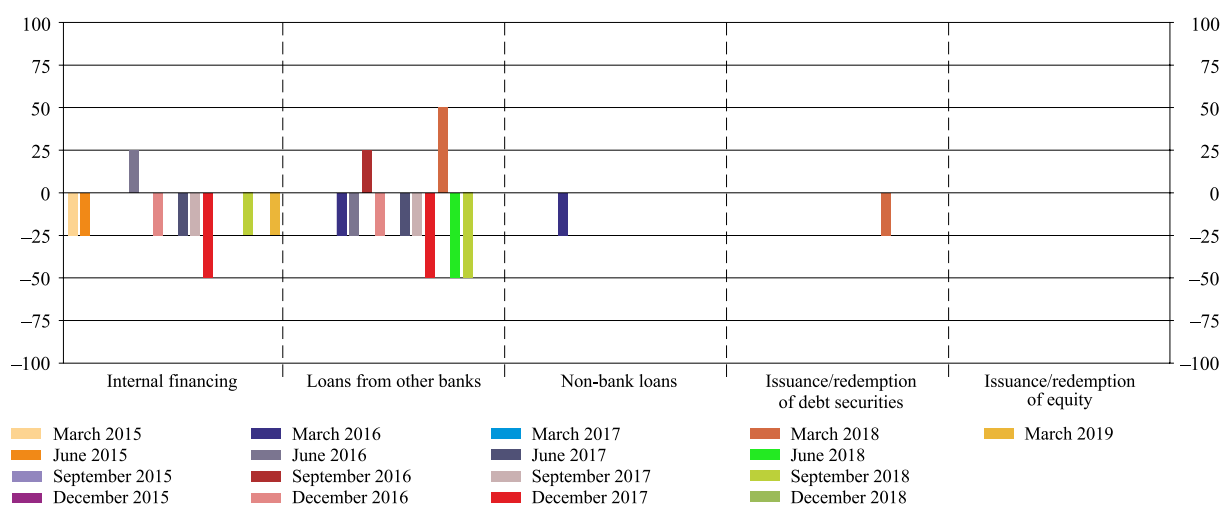
## IMPACT OF VARIOUS FACTORS ON DEMAND FOR LOANS TO ENTERPRISES

(net percentage of banks reporting positive factor contributions; %)

## a) Financing needs, contributing factors or objectives underlying the demand for loans



## b) Use of alternative sources of finance



When forecasting the demand for loans to enterprises in the second quarter of 2019, the surveyed Latvian banks were rather cautious, as was the case in the previous quarter. The above banks foresee that the demand for loans to enterprises will remain unchanged in the next quarter. One of the four surveyed banks pointed out that the demand for loans to large enterprises might move up slightly during the said period.

The demand for loans to households, unlike that for loans to enterprises picked up during the reporting period. One surveyed Latvian bank reported a considerably higher demand for loans to households for house purchase in the first quarter of 2019. Meanwhile, the demand for consumer credit and other lending to households remained unchanged.

The bank where the demand for loans to households for house purchase expanded during the reporting period attributed this increase to a higher consumer confidence. Meanwhile, another surveyed Latvian bank indicated that consumer confidence had edged down slightly in the first quarter of 2019.

The surveyed banks envisage that the demand for loans to households for house purchase as well as for consumer credit and other lending to households will remain unchanged in the second quarter of 2019. As regards loans to households for house purchase, banks do not share the same view on the direction of the potential changes in demand. One bank believes that the demand for the above loans will increase slightly in the second quarter of 2019, but another one – that it will decrease somewhat.

### Ad hoc questions

In the framework of the euro area bank lending survey of January 2019 on lending development trends, banks were asked several ad hoc questions concerning the level of credit standards and the effects of the negative deposit facility rate.

In response to an ad hoc question in relation to the level of credit standards, Latvian banks pointed out that the credit standards applied in the first quarter of 2019 compared to those applied from the first quarter of 2003 until the present day are tighter across all loan categories covered by the euro area bank lending survey (all loans to enterprises, loans to households for house purchase, consumer credit and other lending to households). The respective credit standards are still considerably tighter in two surveyed Latvian banks and slightly tighter in the other two.

Meanwhile, the credit standards prevailing in the first quarter of 2019 in comparison with those prevailing from the second quarter of 2010 to date have been eased in most of the surveyed Latvian banks (in three out of four banks). In one bank, where credit standards have been considerably tighter than the midpoint of the range from the first quarter of 2003 until now, they have been marginally tighter than the midpoint of the range from the second quarter of 2010 to date. In one bank, where credit standards have been considerably tighter than the midpoint of the range from the first quarter of 2003 until now, they have been basically in the midpoint of the range from the second quarter of 2010 to date. Meanwhile, in another bank, where credit standards were slightly tighter than the midpoint of the range in the former period, they were slightly eased relative to the midpoint range in the latter period.

When assessing the effects of the negative deposit facility rate, one of the four surveyed Latvian banks acknowledged that the above rate supported the shrinkage of net interest income over the past six months, and this situation will remain unchanged in the above bank during the next six months.