

Euro area bank lending survey of March 2022: main results for Latvia

- *Banks started tightening credit standards for loans to enterprises.*
- *Demand for short-term loans to small and medium-sized enterprises (SMEs) increased, but at the same time demand for long-term loans to large firms dropped.*
- *In the following quarter, the surveyed Latvian banks intend to tighten credit standards for loans to households and foresee a decline in demand.*

Latvijas Banka conducted a euro area bank lending survey in cooperation with the European Central Bank (ECB) in March 2022, covering the lending developments during the first quarter of 2022 and bank expectations for the second quarter of 2022. Four Latvian banks whose total market share in lending to non-financial corporations and households is high enough to represent the lending development in Latvia participated in the survey. Their replies have been incorporated in the euro area bank lending survey results.

Russia's war against Ukraine increased geopolitical risks in the region, and the first quarter of 2022 was a turning point when trends in the lending market began to change. In some banks and loan segments, for example, loans to households for house purchase, lending continued to grow owing to inertial effects. Meanwhile, uncertainty and the increasing risks had a negative impact on other banks and loan segments already in the first quarter of 2022. Next comes a more detailed presentation of the factors behind changes in credit standards, terms and conditions, as well as demand and how these changes affected lending in Latvia during the reporting period.

Loans to enterprises

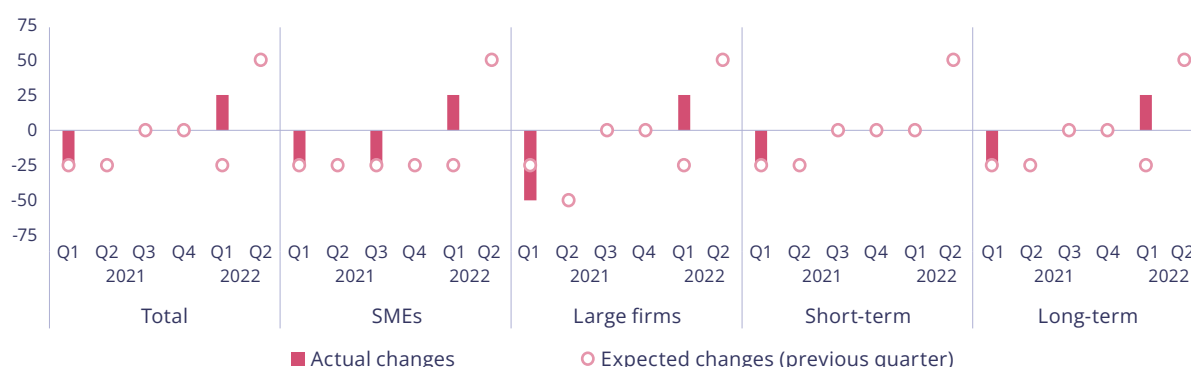
In the first quarter of 2022, one surveyed Latvian bank slightly tightened credit standards for loans to enterprises, except for short-term loans (see Chart 1). Credit standards for loans to both SMEs and to large firms were tightened since the general economic situation and prospects, as well as the situation of individual sectors and enterprises and their prospects and customers' creditworthiness weakened. However, two surveyed Latvian banks intended to somewhat tighten credit standards for loans to enterprises already in the second quarter of 2022.

During the preceding quarters, mutual competition was the most common reason why the surveyed Latvian banks eased certain terms and conditions for loans to enterprises. However, in the first quarter of 2022, all banks stopped easing terms and conditions for loans to enterprises, and they remained unchanged.

In the first quarter of 2022, the share of rejected applications for loans to enterprises also remained at the level of the previous quarter.

Chart 1¹

Changes in credit standards for loans to enterprises by loan segment
(net percentage of banks reporting tightening credit standards; %)

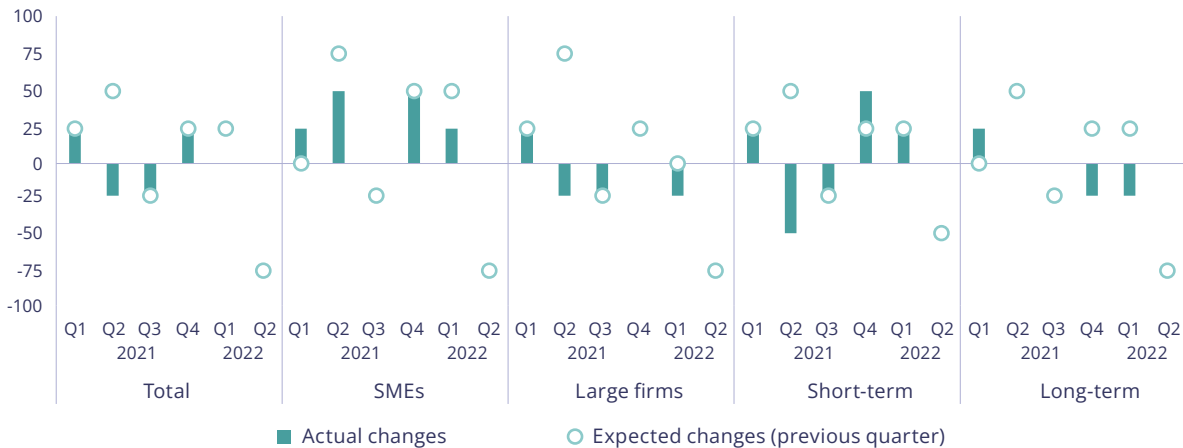


Demand for loans to enterprises posted an opposite development in different banks and loan segments in the first quarter of 2022 (see Chart 2): it grew for short-term loans to SMEs (net in one bank) but decreased for long-term loans to large firms (in one bank). It was expected that demand for loans to SMEs would rise, but the decline in demand for long-term loans to large firms was a surprise. Overall, demand for loans to enterprises remained unchanged in the first quarter of 2022.

Chart 2

Changes in demand for loans to enterprises by loan segment

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

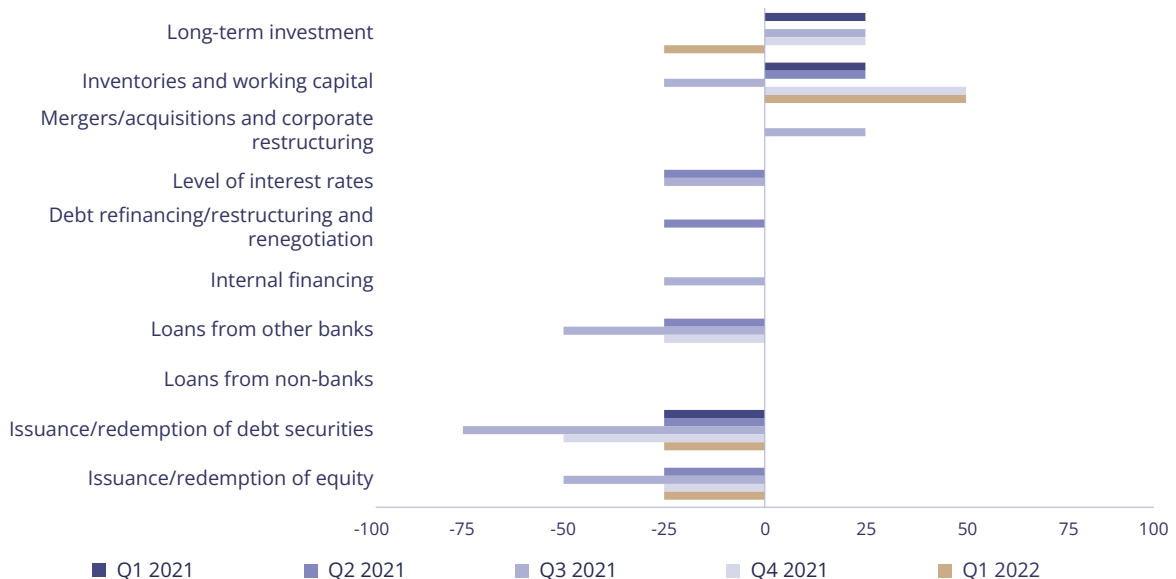


In the first quarter of 2022, the overall demand for loans to enterprises remained at the level of the previous quarter as it was affected by opposite factors (see Chart 3). On the one hand, demand for loans to enterprises (similar to the previous quarter) was supported by an increased need for inventories and working capital (in two cases). On the other hand, it was limited by a lower need for long-term investment (net in one case). The issuance of corporate debt securities and equity continued to have a negative effect on demand for loans to enterprises in the first quarter of 2022; however, the importance of these factors declined (a minor impact in one bank).

Chart 3

Contribution of various factors to demand for loans to enterprises

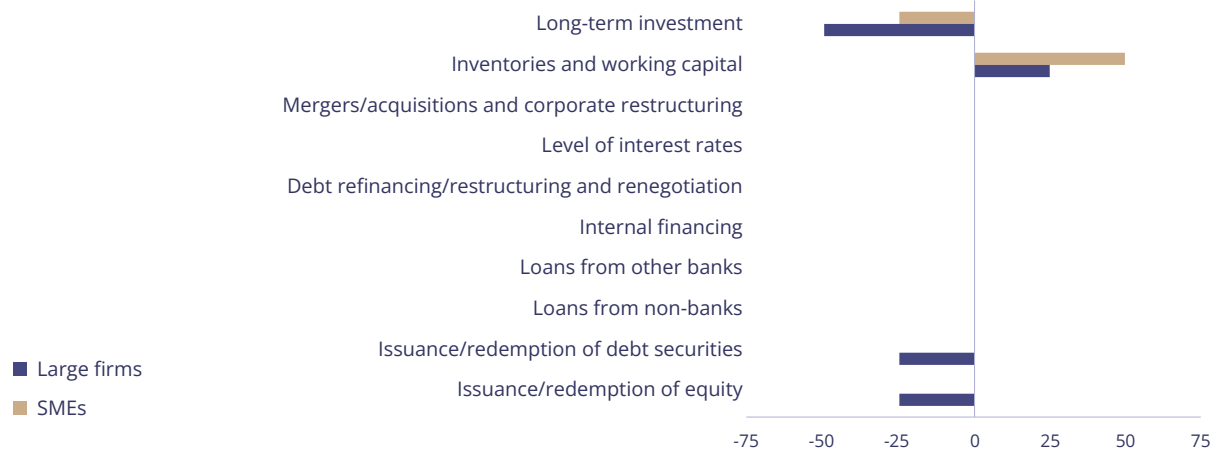
(net percentage of banks reporting positive factor contributions; %)



Similar factors affected demand for loans to SMEs and large firms, except the issuance of corporate debt securities and equity since this issuance concerned only loans to large firms (see Chart 4). Growth in demand for loans to SMEs was mainly driven by an increased need for inventories and working capital (net in two banks), but the need for long-term investment was less significant (net in one bank). Meanwhile, a reduced need for long-term investment (net in two banks) compared to an increased need for inventories and working capital (net in one bank) had a greater effect on the decline in demand for loans to large firms. >

Chart 4

Contribution of various factors to demand for loans to enterprises by enterprise size group
(net percentage of banks reporting positive factor contributions; %)



Three of the four surveyed Latvian banks expect that demand for loans will contract next quarter. A decline in demand for short-term loans to enterprises is foreseen less frequently (in two cases) than for long-term loans (in three cases).

Loans to households for house purchase

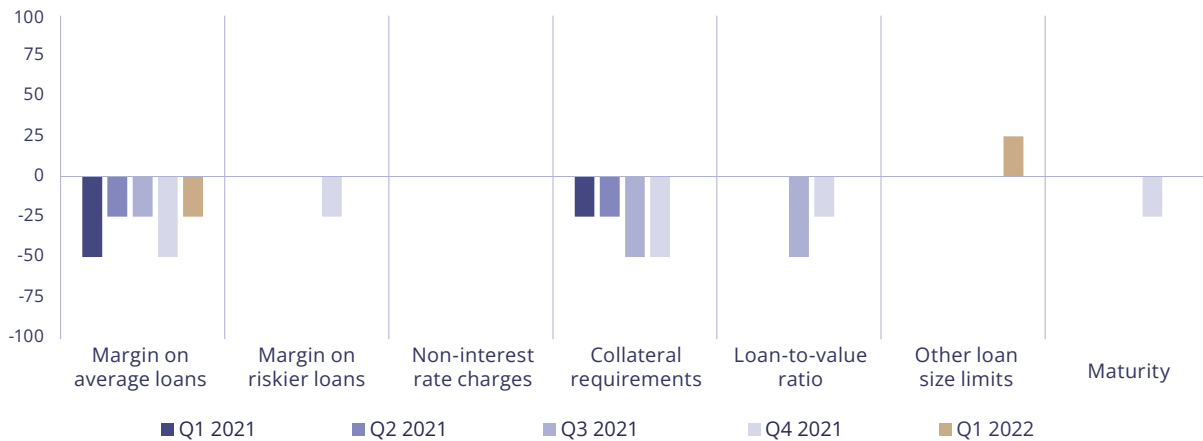
Credit standards for loans to households for house purchase remained unchanged in all surveyed Latvian banks in the first quarter of 2022 (see Chart 5); however, one bank intends to tighten them in the following quarter.

Chart 5

Changes in credit standards and demand for loans to households for house purchase
(net percentage of banks reporting a tightening of credit standards and higher demand; %)



Credit terms and conditions for loans to households for house purchase developed in the opposite direction in certain banks in the first quarter of 2022: one bank cut the margin on average loans due to mutual competition, but another one tightened the limits of loan size, the loan-to-income ratio, as well as the loan-to-value ratio. Such differences did not exist in the previous quarters when most of Latvian banks eased one or more terms or conditions on loans to households for house purchase owing to mutual competition. >

Chart 6
Changes in credit terms and conditions on loans to households for house purchase
 (net percentage of banks reporting tightening terms and conditions; %)


The share of rejected applications for loans to households for house purchase decreased slightly in one surveyed Latvian bank in the first quarter of 2022.

Although it was expected that demand for loans to households for house purchase would rise in the first quarter of 2022, Latvian banks were at opposite ends concerning the actual changes: one bank pointed to a considerable decrease in demand, but another one – to a slight increase. Therefore, demand for loans to households for house purchase has remained unchanged overall in the first quarter of 2022 (see Chart 5).

Both banks, which pointed to changes in demand for loans to households for house purchase, agreed that it was affected by housing market development prospects (including the expected price development), as well as consumer confidence. However, the assessment provided by banks regarding the direction of effect from these factors was opposite.

There is consensus among the surveyed Latvian banks concerning the development of demand in the second quarter of 2022. All surveyed Latvian banks expect a slight decline in demand for loans to households for house purchase in the next quarter.

Consumer credit and other lending to households

None of the surveyed Latvian banks changed credit standards for consumer credit and other lending to households in the first quarter of 2022. One surveyed Latvian bank intends to somewhat tighten credit standards in this segment in the following quarter (see Chart 7).

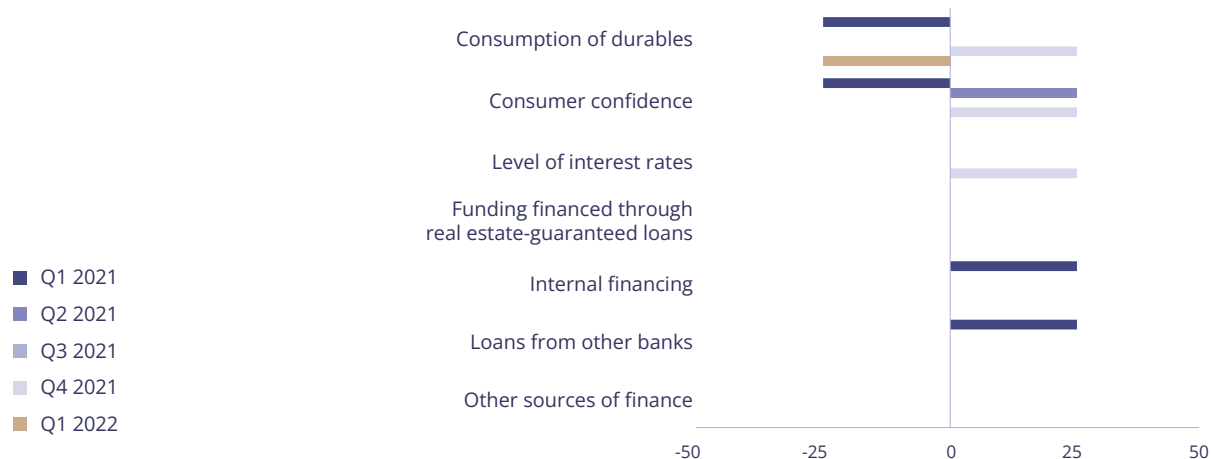
Chart 7
Changes in credit standards and demand for consumer credit and other lending to households
 (net percentage of banks reporting a tightening of credit standards and higher demand; %)


In the first quarter of 2022, terms and conditions for consumer credit and other lending to households, as well as the share of rejected applications for loans, also remained unchanged in the surveyed Latvian banks.

Overall, the first quarter of 2022 witnessed demand for consumer credit and other lending to households remain at the level of the previous quarter in Latvian banks. However, most of the surveyed Latvian banks (three out of four) expect a decrease in demand for consumer credit and other lending to households in the following quarter.

Chart 8

Contribution of various factors to demand for consumer credit and other lending to households
(net percentage of banks reporting the factors contributing to higher demand; %)



One bank pointed out that a lower need for durable consumer goods, for example, cars and furniture, has an adverse effect on demand for consumer credit and other lending to households (see Chart 8). Two banks were at opposite ends when providing their assessment of the impact of consumer confidence on demand for consumer credit and other lending to households in the first quarter of 2022.

Ad hoc questions

The euro area bank lending survey of March 2022 included several ad hoc questions to banks, including on the impact of various ECB non-standard monetary policy instruments on banks' financial situation and lending.

The negative ECB deposit facility rate affected or could potentially affect lending in three surveyed Latvian banks between the fourth quarter of 2021 and the first quarter of 2022. In one bank, the negative deposit facility rate might reduce profitability in the fourth quarter of 2021 and the first quarter of 2022, having a negative effect on net interest income. Within the same timeframe, the two-tier excess reserve system went in opposite directions in two surveyed Latvian banks, i.e. it increased their profitability by improving net interest income. In two surveyed banks, the negative deposit facility rate contributed to the reduction in the interest rate and a fall in volume of corporate deposits between the fourth quarter of 2021 and the first quarter of 2022. In one of them, according to the respective bank, the negative ECB deposit facility rate might facilitate a fall in interest rates on corporate deposits over the next six months.

Three out of four surveyed Latvian banks pointed out that the ECB's targeted longer-term refinancing operations affected them over the past six months and will affect them over the next six months. One bank revealed that it used the funds of the targeted longer-term refinancing operations for loans to non-financial corporations, purchases of government bonds and holding liquidity in the Eurosystem between the fourth quarter of 2021 and the first quarter of 2022. Over the next six months, two banks intended to use these funds for loans to non-financial corporations and purchases of government bonds, one bank – for holding liquidity in the Eurosystem and the remaining one – for replacing maturing debt securities and interbank loans.

Latvian banks indicated that owing to the ECB's targeted longer-term refinancing operations their profitability was on the rise, financing conditions improved and the liquidity position increased

(each factor was mentioned once) between the fourth quarter of 2021 and the first quarter of 2022. Meanwhile, one Latvian bank pointed out that the amount of loans to enterprises decreased over the six months before the survey under the impact of the ECB's targeted longer-term refinancing operations. Over the next six months, the ECB's targeted longer-term refinancing operations might contribute to easing terms and conditions for loans to enterprises in two surveyed banks and several other improvements in one bank: improvement of the bank's liquidity position, market financing and profitability, easing of credit standards and an uptrend in loans in all lending sectors, as well as easing of terms and conditions for loans to households.