Macroprudential Commentary

September 2022

NÁRODNÁ BANKA SLOVENSKA
EUROSYSTÉM

Summary

- Expansionary trends remain present in the domestic financial sector, though appear to be more moderate than in previous quarters. The potential build-up of risks associated with the financial cycle also remains higher.
- Lending to households remains robust and is not yet being checked by rising interest rates. Incentives for private sector borrowing are still strong, but factors dampening loan demand are gaining momentum.
- Growth in loans to firms has also been gathering pace, as rising prices stoke firms' financing needs for fixed investment and working capital.
- Housing prices have maintained high annual growth, but there are signs of moderation.
- Increasing interest margins and strong credit market growth are supporting an improvement in banking sector profitability. Banks remain sufficiently capitalised.

Also in this edition:

No change in the CCyB rate

Factors stimulating private sector borrowing remain present. Despite a deteriorating economic outlook, the labour market is still relatively stable. Elevated inflation is discouraging households from saving and, together with concerns about ongoing increases in interest rates and housing prices, is incentivising them to borrow. Loans remain affordable despite rising interest rates. Loans to non-financial corporations (NFCs) are now showing the sort of strong growth long seen in loans to households, as an environment of rising prices stokes firms' financing needs for working capital as well as for fixed investment. Looking ahead, however, factors dampening loan demand can be expected to gain momentum. At the same time, banks remain resilient in terms of their capitalisation and are able to bear the risks present. In this context, there is no need for now to further increase the countercyclical capital buffer (CCyB) rate.

The economy remains affected by risks related to the war in Ukraine, by energy supply disruptions, and by a continuing uptrend in prices, in particular energy prices. The solvency of households and firms may be adversely affected as the labour market situation deteriorates amid unfavourable economic developments and as costs surge because of rising prices. Národná banka Slovenska (NBS) is therefore closely monitoring these risks.

Expectations for the CCyB rate in the next quarter

Národná banka Slovenska (NBS) does not envisage having to adjust the countercyclical capital buffer rate in the next quarter.

The financial market's expansionary trends may be expected to persist, though they should moderate gradually given the economic situation and monetary policy tightening. Risks associated with the financial cycle will, however, continue to build up in banks' portfolios. Even so, banks' current capital levels should suffice to cover these risks.

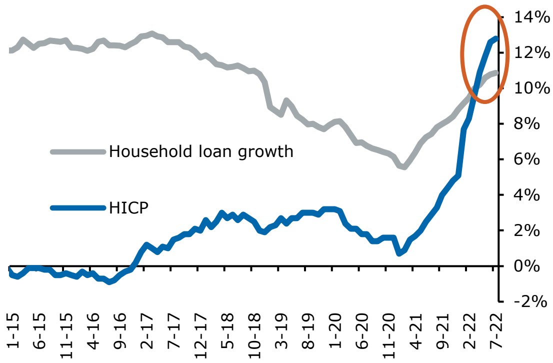
In the event of risks materialising and having an adverse impact on the financial sector, NBS stands ready to reduce the CCyB rate to an extent that provides banks with leeway to absorb excessive losses arising from these risks.

CCyB rate:
1.50%
as from 1 August 2023

Households are taking on more debt, but the incentives to borrow may be gradually fading

Loans to households maintained double-digit growth in the second quarter of 2022. The outstanding amount of these loans increased by 10.9% year-on-year. The upturn in retail interest rates resulting from rising market rates has not yet had any significant impact on lending growth, even though rates on new loans have risen to their highest level since the end of 2018.[1] People are disposed to borrow amid ongoing housing price growth, still accelerating inflation, expectations of an uptrend in interest rates, and a labour market situation that remains favourable. Household credit growth continues to be driven by housing loans,[2] while consumer credit is still recording a slight year-on-year decline.[3] As a result, in the second quarter, household loan growth in Slovakia was the third highest in the EU.[4] At same time, however, prices in the economy have in recent months already started outpacing loan growth.

Chart 1 Inflation is already outpacing loan growth
(annual percentage changes in HICP inflation and loans to households)



Zdroj: NBS

Banks expect loan demand to moderate in the period ahead.[5] Factors dampening loan demand can be expected to gain momentum in the coming period. These will include rising interest rates, declining incentive to refinance loans and cooling activity in the housing market, as well as households' mounting uncertainty, and therefore increasing caution, in response to the uptrend in prices, in particular energy prices.

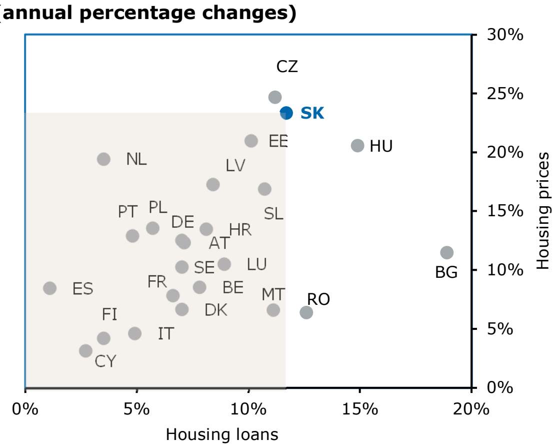
The share of loan prepayments has fallen sharply.[6] This implies that refinancing demand has eased since its upsurge in spring, with some borrowers having already refinanced in the previous period and others becoming less inclined to take this step at current interest rate levels. The average interest rate on new loans is now 80 basis points higher than the average rate on existing loans.[7] The refinancing of loans as a way of exploiting low interest rates has anyway been more prevalent among borrowers not facing serious financial difficulties and less prevalent among those with greater need of it.[8] At the same time, demand for the longest interest rate fixation periods is gradually fading, while, especially in the first quarter of this year, there has been an increase in demand for medium-term fixation periods.

The non-performing loan (NPL) ratio for loans to households has remained stable in recent months, with no significant change in the NPL ratio for overall household loans and only a slight decrease in the ratio for consumer credit.[9]

Housing prices maintain strong growth, though there are signs of moderation

Early summer brought no faltering in the housing market's exceptionally strong growth trend. Prices of houses and flats were on average one-quarter higher at the end of June 2022 that at the midpoint of the previous year.[10] In the first quarter, housing price growth in Slovakia was actually the second highest in the EU and twice as high as the euro area average. In the new-build market, too, price growth has remained above 20%, though it did not accelerate further in the second quarter. For flats in all regions and across all size categories, price growth was in double digits.

Chart 2 Growth rates for loans and housing prices have accelerated in several EU countries, but just in one more than in Slovakia
(annual percentage changes)



Sources: ECB, and NBS.

At the same time, however, the quarter-on-quarter growth in housing prices is starting to moderate gradually. Some changes are also being seen on the supply side, as the number of flats on the market increased in the second quarter of 2022 after falling for more than one year. This might indicate that sales velocity is not as strong as it was in the previous period. Housing is gradually becoming less affordable due to rising prices as well as to recent months' interest rate increases. Although wages have continued growing, it takes, on average, longer now than it did one year ago to earn the money to afford one square metre of residential property.

---

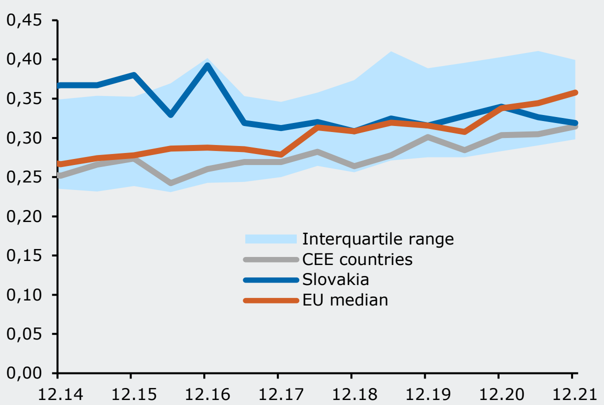
1 The average interest rate on new household loans increased by 90 basis points in the second quarter of 2022, to 2.5%, and then rose to 3.1% in July.
2 Annual growth in housing loans stood at 12.8% in July 2022.
3 The annual rate of change in total consumer credit remained slightly negative in July 2022, at -1.2%.
4 The only countries reporting a higher annual increase in household loans in the second quarter were Bulgaria and Lithuania; the growth rate in Hungary was the same as in Slovakia.
5 According to the bank lending survey for the second quarter of 2022.
6 Loans refinanced with another bank as a share of total loans climbed to 1.8% in May 2022 from a long-term average of 1.0%, before dropping back to 1.1% in July.
7 In July, the average interest rate on outstanding household loans was 2.2% while the average rate on new loans was 3.1%.
8 This topic is addressed in the following NBS Discussion Note (in Slovak only): "[(Ne)využitá príležitosť: Ako sa domácnosti chopili šance zafixovať si nízky úrok na dlhšie obdobie?]"(Opportunity taken or not: To what extent have households taken the chance to lock in a low interest rate for a longer term?).
9 For housing loans, the NPL ratio was 1.2%, while for consumer credit it fell by 20 basis points during the second quarter, to 7.5%.
10 While prices of flats were on average 28.2% higher, year-on-year, at the end of June 2022, prices of houses and villas were 19% higher.

Box 1: Electricity prices and household expenditure

The extraordinary surge in energy costs is now a pressing issue in all European countries. The main factor behind this increase is the reduction of natural gas supplies from Russia. The household electricity price in a given country is also dependent on the energy mix in that country as well as on local regulations, taxes and charges. The electricity price for 2023 continues to be a major unknown, with several countries presenting potential scenarios featuring substantial price increases.

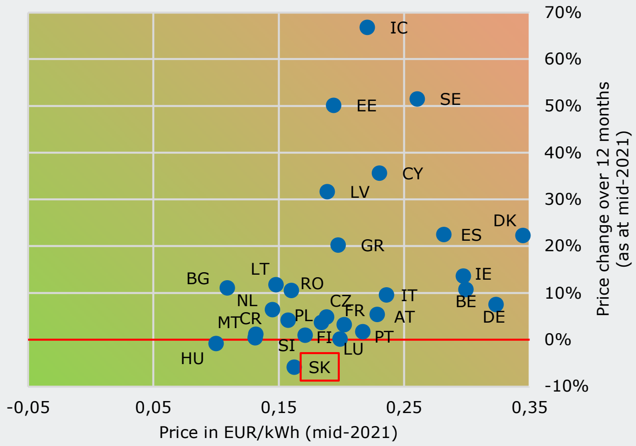
Household electricity prices in Slovakia are relatively moderate by EU standards. Expressed in purchasing power parity, the unit price of electricity for households in Slovakia, including all taxes and charges, has been at the EU median level in recent years (Chart 3). In 2021 Slovakia was the only EU country to report a material decrease in the average electricity price for households, while many other EU countries experienced a double-digit increase in this price (Chart 4).

Chart 3 Average household electricity prices in EU countries
(EUR/kWh; prices expressed in purchasing power parity)



Source: Eurostat

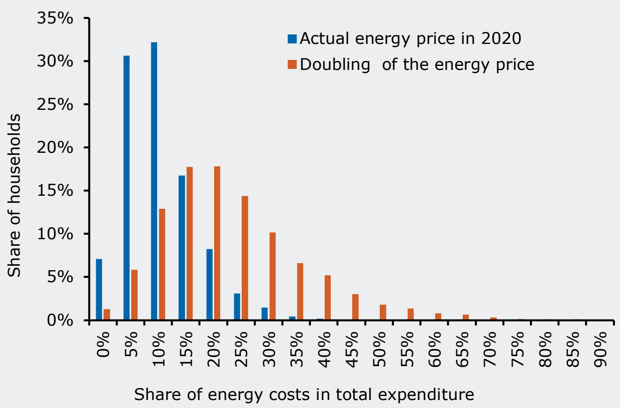
Chart 4 Current household electricity prices and its change vis-à-vis
(EUR/kWh; current prices)



Source: Eurostat

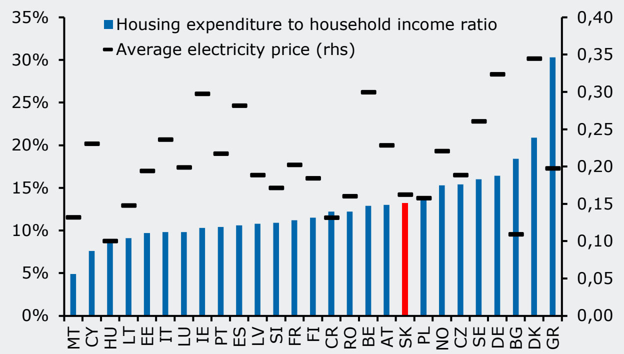
But although Slovak households currently have lower electricity prices, they are not necessarily at less risk in the event of price increases. Moreover, the situation among Slovak households is heterogeneous in terms of income and expenditure structure. An important indicator of households' sensitivity in this respect is the ratio of their energy[11] costs to their income or the share of energy costs in their total spending. In 2020, for example, the average share of energy costs in households' total costs was 13%, while 13% of households (the blue bars in Chart 5) had energy costs exceeding 20% of their total expenditure. A potential doubling of energy costs[12] would increase the average share to 26%, with 62% of households facing energy costs exceeding 20% of their total expenditure (the orange columns in Chart 5). While household electricity prices in Slovakia may be among the lowest in the EU, the share of housing expenditure in the total income of Slovak households is among the highest in the EU (Chart 6). Hence, a lower unit price of electricity for households does not necessarily mean a lower ratio of total housing costs to household income.

Chart 5 Share of energy costs in total Slovak household expenditure
(percentages)



Sources: SO SR, and own calculations.

Chart 6 Ratio of housing costs to household income vis-à-vis the average electricity price
(percentages; EUR/kWh)



Source: Eurostat.

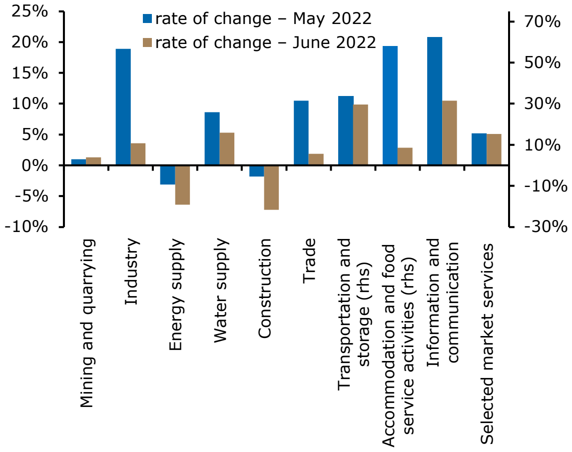
[11] Gas, electricity, solid and liquid for households, and thermal energy.
[12] Only the net effect of the increase in household energy prices is estimated; second-round effects on goods and services prices are not included.

Corporate lending has surged against a backdrop of unprecedented input price growth and a deteriorating economic outlook

Surging prices of inputs and increasing uncertainty are stoking firms' concerns about the way ahead. The corporate sector is currently faced with sharply rising input prices, in particular an unprecedented surge in energy prices. This situation is reflected in a widespread decline in economic sentiment indicators across EU countries, which point to a downturn in economic activity in the period ahead. The deteriorating situation is most evident in the slowdown of growth rates for foreign trade and revenues. Although their growth remains in double digits, input prices are rising far faster. Annual growth in firms' revenues was 8 percentage points lower in June 2022 than in previous period, at 20%. Revenue growth is less than half the rate of industrial producer growth.[13] The corporate revenue slowdown has been relatively broad-based, albeit heterogeneous in terms of intensity. The largest contribution to that slowdown has come from industry, where component supply shortages persist. In coming months, however, energy prices will have the largest negative impact on revenues.

Chart 7 The corporate revenue slowdown has been relatively broad-based

(month-on-month percentage change in revenues at constant prices)



Source: NBS.

The economic deterioration can also be seen in foreign demand developments. The annual growth rate in the value of goods exports has slowed sharply.[14] The largest deceleration has been in exports of automobiles and auto parts, and there has been slower growth in most other goods exports, in particular metals (iron and steel) and chemicals. A similar trend is observed on the import side,[15] with growth slowing across a swathe of goods imports. Although foreign trade growth remains in double digits, it is being driven almost entirely by the rising prices of traded goods.

Corporate loan growth has for several months now [16] been around the 10% mark. Its slight slowdown in July reflected mainly lower growth in loans with a maturity of more than five years[17] and to some extent in short-term loans. Annual growth in short term loans nevertheless remains in double digits.[18] Medium-term loans continued to make the largest positive contribution to corporate loan growth.[19]

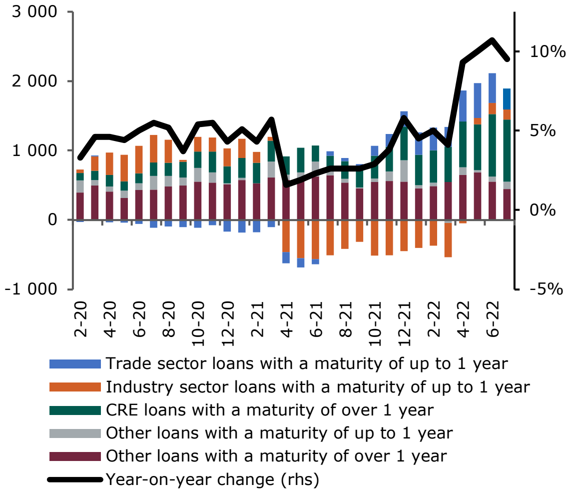
An important driver of loan growth has been the sharp rise in prices in the economy. High energy prices, with their pass-through to other sectors of the economy, have had the major impact in this regard.[20] As their inputs rise in price, firms have increasing need for working capital financing. The sector in which short-term financing has increased the most is trade, followed by industry.[21]

Growth in medium-term loans with a maturity of more than one year has been driven by lending to the commercial real estate (CRE) sector, which increased by 17.3% year-on-year. The growth in CRE lending may have been due largely to rising prices of construction work and materials. Most of the inflow of loans was for existing development projects, possibly implying an increase in financing necessitated by rising construction costs. There was, however, also an increase in loans for the financing of new projects.

Compared with the situation in other EU countries, current corporate loan growth in Slovakia is not exceptional. It is at the median for CEE countries and in the first quartile for EU countries.

Chart 8 Corporate loan growth is being driven mainly by CRE lending and short-term loans in trade and industry sectors

(contributions to year-on-year change in EUR billions; annual percentage changes)



Source: NBS.

13 Annual growth in industrial producer prices stood at 43% in June.

14 Annual growth in exports was almost 18 percentage points lower in July than June, at 13%.

15 Annual growth in imports was almost 14 percentage points lower in July than June, at 17%.

16 Annual growth in corporate loans was 0.4 percentage point lower in July than June, at 9.5%.

17 Annual growth in loans with a maturity of over 5 years was more than 1 percentage point lower in July than in June, at 7.7%.

18 Annual growth in short-term loans was 12.5% in July.

19 Annual growth in medium-term loans with a maturity of 1 to 5 years was 1.7 percentage points higher in July than in June, at 20.7%.

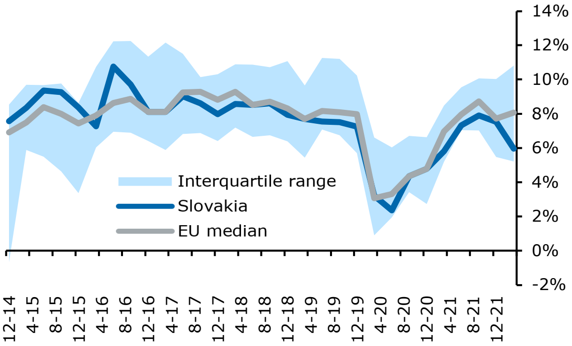
20 For example, annual growth in agricultural product prices was almost one-half higher in July than in June, with these prices experiencing a strong increase in July. The year-on-year increases in construction work prices and construction material prices 14% and 24% respectively.

21 Besides trade and industry, the other sectoral loan portfolios contributing to the growth in short-term loans are construction, energy supply, and professional activities.

Bank profits are doing well

Strong credit growth and gradually rising interest rates have been having a favourable impact on the performance of banks. Although the banking sector's profits are not growing as strongly as they did last year,[22] a number of banks have this year been performing better than in any recent years. The sector's net profit for the first seven months of 2022 was 1.2% higher than for the same period in 2021.[23] The profit growth included a significant contribution from net interest income.[24] After a decade at profit-squeezing low levels, banks' interest margins are gradually starting to stabilise owing to rising interest rates.[25] But despite the uptrend in interest rates, banks are managing to maintain strong credit growth. Thanks to an increase in new lending, sales of third-party insurance and investment products, and their fee policies, banks have also increased their net fee and commission income.[26] Another boon to profitability is that banks do not at present need to increase loan loss provisioning, given the current low level of NPL ratios and their conservative approach in previous years. Although there has been a 1.7-fold year-on-year increase in net provisioning,[27] this is due to a return to normal after two years of fluctuations caused by the pandemic crisis. Rising inflation and the necessity of IT upgrades is putting upward pressure on operating costs, which have risen by 3.3%[28] year-on-year. But although banks have improved their financial performance this year, their profitability has fallen further behind the average for EU countries.[29]

Chart 9 Although Slovak banks' have increased their profits in recent years, they are still less profitable compared with the average for EU banks
(return on equity)



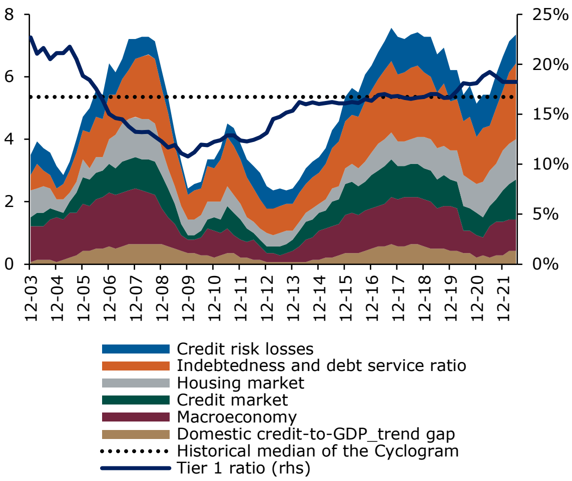
Source: ECB.

Banks are sufficiently capitalised. The banking sector's total capital ratio at the end of June was down by 1.6 percentage points year-on-year, at 19.2%, but nevertheless remains above its pre-pandemic level.[30] The situation differed, however, between significant and less significant banks. For significant banks, the second quarter of 2022 brought a reduction in their total capital ratio[31] due mainly to strong credit growth, while less significant banks saw their solvency increase in the same period owing to the retention of earnings.[32] The banking sector's capital structure remains stable, with highest-quality CET1 capital accounting for almost 90% of total capital.

The build-up of financial sector imbalances remains high

The financial sector's expansionary trends gained further momentum in the second quarter, mainly because of strong growth in the credit and property markets. The Cyclogram, NBS's composite indicator of the domestic financial cycle, is approaching its 2008 and 2018 highs. This means a build-up of imbalances related to financial cycle developments is highly likely. The main contributors to this situation are credit market and housing market trends. The financial cycle has not yet responded to the gradual rise in interest rates. Households remain strongly disposed to borrow in the current context of a favourable labour market situation, ongoing wage growth, and concerns about housing becoming less affordable because of rising property prices and an uptrend in interest rates. At the same time, corporate loan growth remains strong owing to firms' increasing financing needs for working capital and fixed investment. Nine of the fourteen indicators that make up the Cyclogram are now close to their historical highs. This situation confirms the rationale behind the current elevated level of the countercyclical capital buffer. Further developments indicate that the financial sector's expansionary trends should soften as a result of the slowdown in economic growth and intensification of factors dampening loan demand.

Chart 10 The financial cycle is now close to its historical highs
(composite index; percentages)



Source: NBS.
Note: Higher index values imply an intensive build-up of imbalances.

22 Last year, however, the banking sector was recovering from the pandemic crisis and benefited to a greater extent from the effects of the ECB's third series of targeted longer-term refinancing operations (TLTRO III).
23 The banking sector's net profit for the first seven months of 2022 was €452 million, €5 million higher than for the same period in 2021.
24 Banks' net interest income for the first seven months of 2022 increased by 1.9% year-on-year (by around €18 million).
25 The sector's net interest margin was 1.5% as at July 2022, 13 basis point lower year-on-year.
26 Net fee and commission income for the first seven months of 2022 increased by 14%, or almost €53 million, year-on-year.
27 Net provisioning for the first seven months of 2022 increased by 71%, or €41 million, year-on-year.
28 By €25 million.
29 The aggregate return on equity (ROE) of the Slovak banking sector for the first quarter of 2022 was 6%, while the median ROE for banking sectors across the EU was 8.1%.
30 From 2017 to 2019 the sector's total capital ratio was around 18.5%.
31 The total capital ratio of significant banks fell, quarter-on-quarter, by 0.7 percentage points.
32 The total capital ratio of less significant banks increased, quarter-on-quarter, by 0.7 percentage point.

What´s new in the world of macroprudential policy

Has the tightening of macroprudential regulation been reflected in default rates in Europe?

This question is addressed in a recent IMF paper.[33] Based on data from EU countries over the period 2008-2017, the authors conclude that the post-2008 tightening of macroprudential policy lowered default risk not only in the financial sector, but also in non-financial sectors. Default risk is reduced at both short and long horizons. At the same time, higher capital requirements improve the long-run resilience of the financial sector, but at the cost of raising long-term default risk in non-financial sectors. This is because banks typically respond to higher capital requirements by adjusting their balances and sometimes also credit supply, thereby affecting the financing of other sectors as well. Strengthening the resolution framework for failing banks has beneficial long-run effects on the default risks of the financial and non-financial sectors.

Can EU bonds serve as safe assets?

In seeking to answer this question, an ECB study[34] analysed data on bonds issued by the European Union for the financing of EU programmes. According to the authors, EU bonds have the potential to be a safe asset, defined as having high credit quality, retaining its value in bad times, and being traded in liquid markets. The authors show that EU bonds are widely considered to be of high credit quality. Moreover, they can hold their value in bad times, as evidenced by the fact that their yield spread over German Bunds remained contained during the COVID-19 pandemic. At the same time, recent bond issuances under the EU's SURE and NGEU initiatives helped improve EU bonds' market liquidity from previously low levels, also reducing liquidity risk premia. The main obstacle to EU bonds achieving a genuine euro-denominated safe asset status lies in the one-off, time-limited nature of the EU's pandemic-related policy responses.

What affects housing price developments more: supply or demand?

So ask the authors of a Federal Reserve Board paper.[35] Using a housing search model and data on individual home listings across the United State over the period 2002–2021, the authors decompose factors forming housing prices into supply or demand factors. According to the authors, housing demand drives short-run fluctuations in home sales and prices, while variation in supply plays only a limited role. Reduction of supply was a minor factor relative to increased demand in the tightening of housing markets during the COVID-19 pandemic. A 30% increase in the monthly number of homes coming on to the market would have been necessary to keep the rate of price growth at pre-pandemic levels given the pandemic-era surge in demand (implying that new construction would have had to increase by as much as 300%). The analysis further confirmed that housing demand is very sensitive to changes in mortgage rates, while supply is not as responsive to rate changes. This suggests that policies that affect housing demand through mortgage rates can influence housing market dynamics.

Does the publication of EU-wide bank stress test results affect bank stock prices?

According to an ECB study,[36] the publication of stress test results provides new information to markets. Banks performing poorly in stress tests experience, on average, a reduction in returns and an increase in volatility, while the reverse holds true for banks performing well. As for banks performing moderately, the price and volatility of their stocks do not change significantly. These results suggest that the publication of stress tests improves price discrimination between 'good' and 'bad' banks, which may be interpreted to mean that stress tests help the market to distinguish the soundness of individual banks.

The September 2022 Macroprudential Commentary was discussed by the NBS Bank Board on 27 September 2022. The publication has not been copyedited.

[33] Belkhir, M., Naceur, S.B., Candelon, B. and Wijnadts, J-C., "Macroprudential Regulation and Sector-Specific Default Risk", *IMF Working Papers*, No 2022/141, International Monetary Fund, Washington DC, July 2022.

[34] Bletzinger, T., Greif, W. and Schwaab, B., "Can EU bonds serve as euro-denominated safe assets?", *Working Paper Series*, No 2712, European Central Bank, Frankfurt am Main, August 2022.

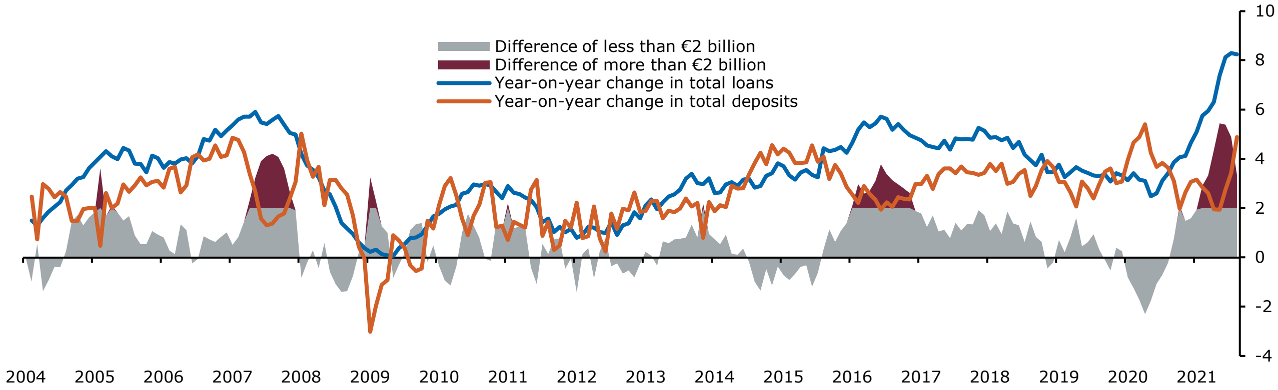
[35] Anenberg, E. and Ringo, D., "Volatility in Home Sales and Prices: Supply or Demand?", *Finance and Economics Discussion Series*, No 2022-041, Federal Reserve Board, Washington DC, June 2022.

[36] Durrani, A., Ongena, S. and Marques, A.P., "The certification role of the EU-wide stress testing exercises in the stock market. What can we learn from the stress tests (2014–2021)?" *Working Paper Series*, No 2711, European Central Bank, Frankfurt am Main, August 2022.

Special topic: Banks' changing liquidity management behaviour

The composition and cost of stable funding[37] is becoming an increasingly pressing issue for banks in Slovakia. In 2022 the year-on-year absolute increase in total loans far exceeded that of total customer deposits (Chart 11). Because of this conjunction of lending activity and current deposit market trends, the loan-to-deposit (LTD) ratio for the banking sector has settled firmly above 100%, after hovering at just above that mark from late 2016 to mid-2021 (Chart 12).

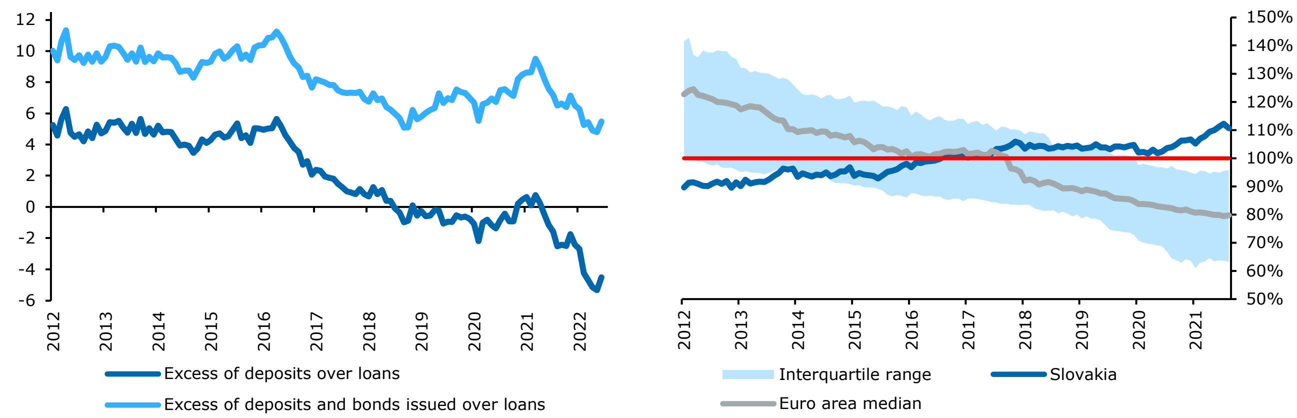
Chart 11 Large credit growth as the main cause of the decline in stable funding
(annual rate of change in total loans and total deposits in EUR billions, and the difference between them)



Source: ECB.

Although the amount of lending is now higher than the amount of deposits, the situation in the banking sector is unremarkable from a historical perspective. A look at the various levels of stable funding vis-à-vis long-term financial assets indicates that the domestic banking sector has ample sources of stable funding. However, it is worth noting developments over the past eighteen months, when the banking sector has in a short period of time consumed what was its highest ever surplus of stable funding.[38] The amount of that surplus was on a par with the amount of stable funding that the banking sector raised through bond issuances over the past three and a half years, which played a large part in increasing the sector's sources of stable funding from their historical lows of late 2018 and early 2019. Today, however, when market conditions are less favourable,[39] banks cannot rely on this source of funding despite its great potential.[40]

Chart 12 Rapid decline in sources of stable funding
(left-hand panel: net surpluses of different levels of stable funding; EUR billions)
(right-hand panel: loan-to-value ratio in international comparison; percentages)



Source: NBS.

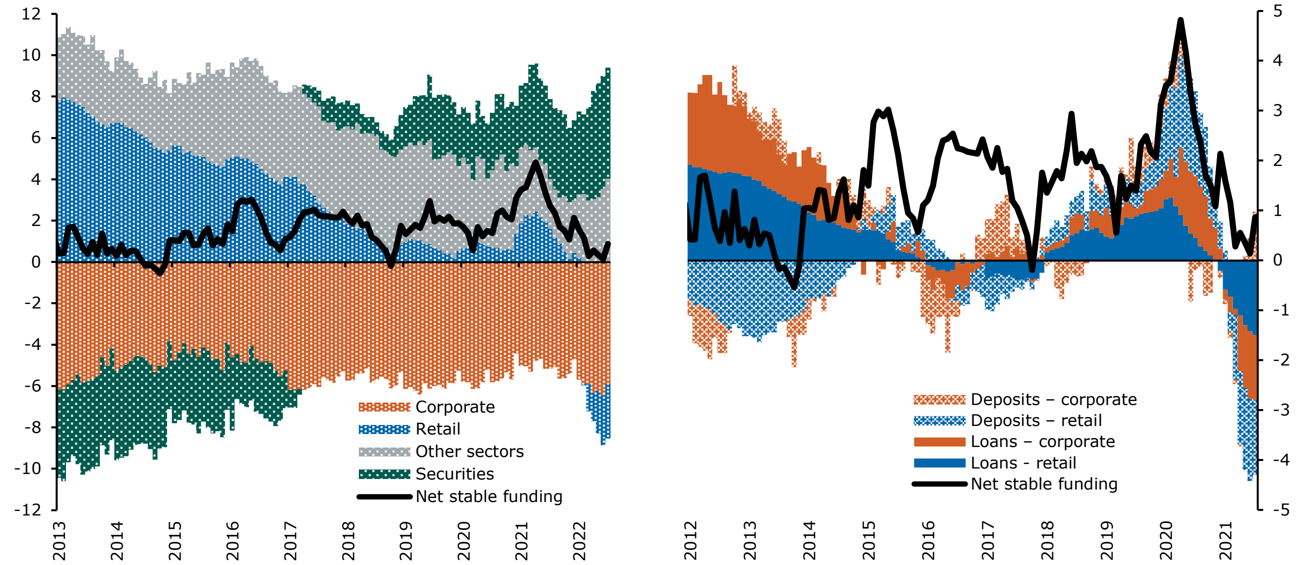
These shifts in the banking sector's balance sheet can largely be explained by the situation in the retail[41] segment. The acceleration of growth in loans, in particular housing loans, has far outpaced growth in households' current account deposits. These have actually fallen in some months, possibly because a change in household consumption behaviour in the context of the economy's post-pandemic reopening and inflation expectations. Thus, for the first time in the retail segment, we have a situation where the amount of loans has overtaken the amount of deposits.[42]

---

37 Stable funding is considered to comprise mainly customer deposits, long-term securities issued, and equity.
38 From April 2021 to June 2022 the excess of stable funding over long-term financial assets fell from €4.8 billion to €0.1 billion.
39 V July 2021 the yield to maturity on covered bonds issued by domestic banks with a residual maturity of five years averaged -0.15% p.a.; in 2021 the yield was into positive territory at around 0.3% p.a., while in July 2022 it was already over 1.5% p.a.
40 Assuming that the portfolio is continuously renewed in the amount of loans excluded from the potential cover pool on grounds of repayment, default, or other infringement of regulatory conditions, the potential amount of newly issued covered bonds is around €18 billion. This figure was calculated for banks domiciled in Slovakia which would be able to create a cover pool for a minimum issuance of €250 million.
41 For the purpose of this commentary, the retail sector comprises households, sole traders and non-profit institutions serving mostly households.
42 For the period from February 2022 to July 2022, the excess of retail loans over deposits was €2.7 billion.

As regards the aggregate liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) of the Slovak banking sector, the levels of these regulatory ratio are below the EU median and have been falling more quickly since June 2021. As at the end of the first quarter of 2022 the sector's LCR stood at 157%, more than 30 percentage points below the EU median and the third lowest reported figure in the EU.[43] The aggregate NSFR, which has been binding only since June 2021, was 126%, the fifth lowest in the EU.[44]

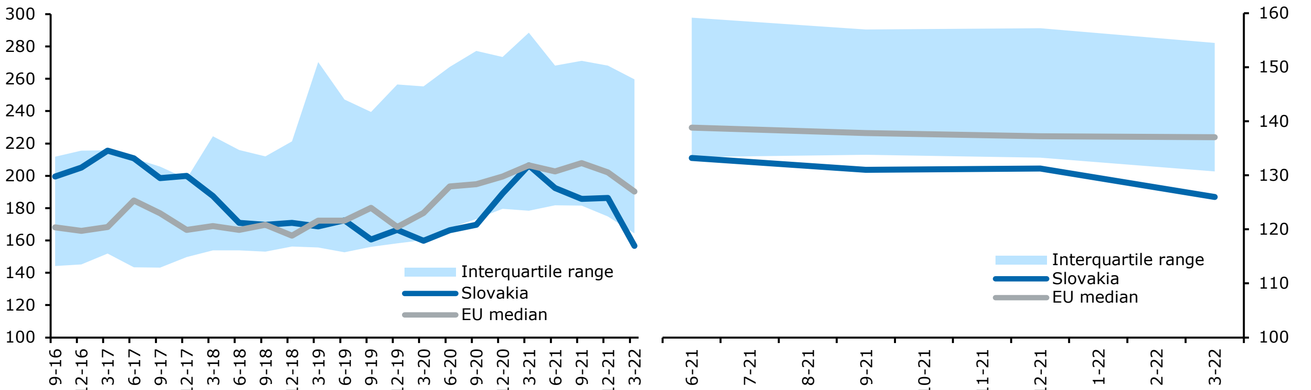
Chart 13 The retail segment as the main contributor to the decline in net stable funding
(left-hand panel: stable funding surpluses for individual segments; EUR billions)
(right-hand panel: contribution of the deviations of the annual growth in retail and corporate loans and deposits from their 2017–2019 average; EUR billions)



Source: ECB.

Note: Net stable funding is the difference between stable sources of funding (deposits, bonds issued, and equity) and long-term financial assets (loans and securities purchased).

Chart 14 Faster decline in liquidity buffer and stable funding surplus
(left-hand panel: liquidity coverage ratio in the EU; percentages)
(right-hand panel: net stable funding ratio in the EU; percentages)



Source: ECB.

Note: Net stable funding is the difference between stable sources of funding (deposits, bonds issued, and equity) and long-term financial assets (loans and securities purchased).

The trends observed in the banking sector since the first half of 2021 are therefore continuing to gain momentum. Their growing consequences are particularly evident in banks pursuing a more aggressive business strategy. With their liquidity buffers having been gradually depleted, largely through loan funding, banks are seeing their business model come under increasing pressure amid worsening market conditions. This trend could be further accelerated by banks' increased focus on short-term forms of financing. If used in a limited and temporary way, such forms of financing may not necessarily pose a major problem, but if employed widely in an environment of rising interest rates, they may adversely affect the sustainability of banks' business model via a more pronounced decline in net interest margins.

43 Ahead of France (154%) and Luxembourg (146%); the LCR values for Germany, the Czech Republic, Hungary and Greece have not been published.

44 The NSFR values for Lithuania and the Czech Republic have not been published. The countries reporting lower NSFR values were Greece (123%), France (120%), Sweden (120%) and Finland (117%).