

## 2012 ECRI Statistical Package: Debt crisis hits Europe's retail credit markets

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The European Credit Research Institute (ECRI) has just published its 2011 Statistical Package, a comprehensive collection of data on lending to households, covering all European countries and other major global economies for the period 1995-2010. Its purpose is to allow users to make reliable comparisons of the retail credit market across countries, including consumer credit, housing loans and other loans to households.

### Summary

After a slender recovery of retail credit in 2010, European households registered a downward adjustment of their stock of loans in 2011. The deleveraging remains uneven and is only loosely related to the overall indebtedness of households to GDP.

The Euro Area (EA) and the EU are roughly decoupling into two groups in this regard: the geographic core and the periphery. Peripheral countries generally shared a period of fast credit expansion during the pre-crisis period, followed by record levels of deleveraging. Core countries, on the other hand, which registered low levels of credit expansion before the crisis, now experience only moderate or no deleveraging during its aftermath.

This core-periphery dichotomy in household credit appears to be significant among Central and Eastern European new member states (CEE10) too, where the average household credit expansion was significantly higher than among the old member states (EU15). Central European new member states register more modest rates of deleveraging than their Eastern counterparts after a period of lower expansion.

For the first time since the crisis, the retail credit retrenchment extends to housing loans, illustrating a willingness on the part of households to reduce credit with higher maturities. Together with record-low interest rates in some countries, this finding most likely reflects lower consumer confidence and increased concerns about future unemployment.

Reduction of loans to non-financial corporations (NFCs) in Europe show an even stronger pattern of the geographic core-periphery dichotomy, most likely reflecting the flight of capital, an adjustment after the pre-crisis expansion, and the current above-average company indebtedness to GDP in the EU periphery.

Key findings of the 2012 ECRI Statistical Package:

### 1. Household deleveraging has started on the EU level

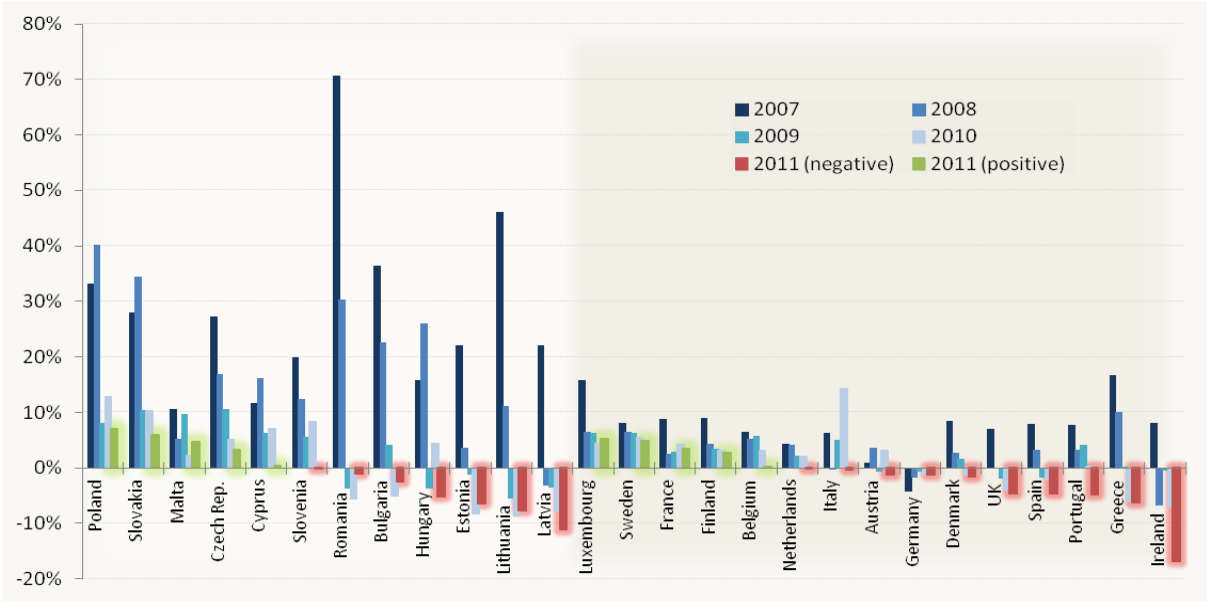
**In 2011, the stock of loans to EU households decreased by 1.1% in real terms for the first time since the 1990s, continuing the trend seen in retail credit markets since the beginning of the financial crisis. Seventeen states registered a reduction in the stock of loans in real terms, while only Malta and Luxembourg saw their retail credit markets growth rates expand.**

In 2011, the sovereign debt crisis and austerity measures had a knock-on effect on consumer confidence and levels of lending to households. The four countries under current troika programmes: Hungary, Bulgaria, Romania and the Baltic States recorded the deepest slump in lending to households in the EU15.

These countries (all implementing severe budgetary adjustments or being subject to IMF programmes) were the hardest hit among the new member states (new MS).

**Figure 1** illustrates the real growth of overall lending to households since the onset of the crisis.

**Figure 1 – Real growth rates of total household debt in new MS and in EU15 (2007-2011)**



Note: Italy’s credit expansion in 2010 is apparently explained by a break in the Bank of Italy’s [adjustment to ECB/2008/32](#).

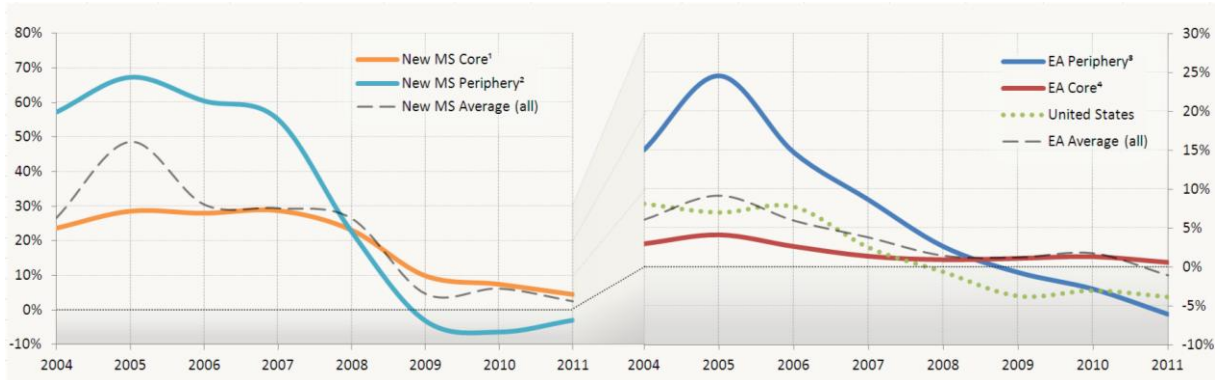
**2. Households in the European periphery are deleveraging in response to prior credit expansion**

Although deleveraging seems slow and unpronounced in Europe as a whole, an analysis of separate member states shows clearer patterns. In particular, the extent of deleveraging in different countries is significantly correlated with the country’s credit expansion prior to the financial crisis. This finding indicates that the level of post-crisis deleveraging depends on the rates of pre-crisis credit expansion.

The EU27 countries appear to be splitting into two groups, both in respect to pre- and post-crisis development. Countries having witnessed a large expansion of retail credit before the financial crisis are decreasing their stock of loans more steeply (in the EU’s geographic periphery). Conversely, countries having recorded modest rates of credit expansion relative to their overall household indebtedness before the crisis witness moderate rates of post-crisis deleveraging (France, Central and Northern Europe). Trends in remaining countries are less pronounced. Due to an adjustment by the Bank of Italy to the new Regulation EC/2009/32, an assessment of Italy’s position in this dichotomy is not possible. The geographic core-peripheral dichotomy could also be applied to the new MS, which sustained a faster but uneven catch-up process, and are also registering deleveraging in proportion to the credit expansion before the crisis.

**Figure 2** illustrates real growth rates of household debt in chosen core and peripheral countries, demonstrating the progress of deleveraging in peripheral countries and a stable development in others. Average EU and Euro Area (EA) trends do not properly represent the development of the household-debt cycle in any of these groups. However, the correlation between the credit expansion of 2004 and 2005 and the deleveraging of 2010 and 2011 among the whole of the EU27 is significant, suggesting that Europe is effectively adjusting its household debt relative to its recent expansion.

**Figure 2 – Weighted real growth rates of total household debt between 2004 and 2011**



Note: Apparent discrepancies may arise due to weighting and varying growth rates in countries outside the core-periphery dichotomy. Please note that the dichotomy does not imply any vocabulary-related judgement.

- 1) Czech Republic, Poland, Slovenia, Slovakia
- 2) Bulgaria, Estonia, Lithuania, Latvia, Romania
- 3) Greece, Ireland, Portugal, Spain
- 4) Austria, Finland, France, Germany, Luxembourg, Netherlands.

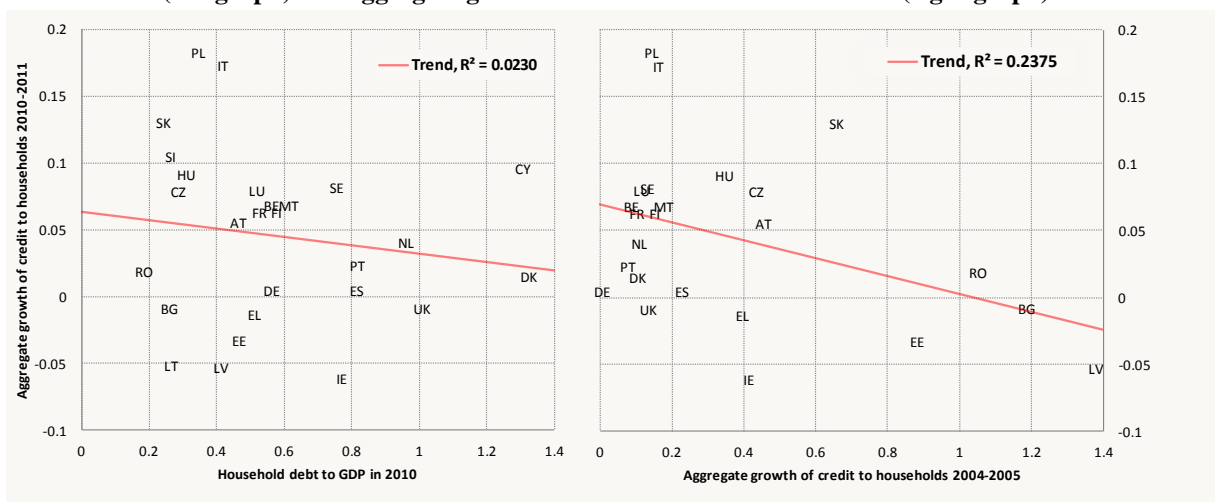
The total stock of household credit also decreased in relation to GDP but due to sustained recession in the most troubled countries and the relative rigidity of housing loans (e.g. due to Greece’s 2011 output loss of 7.5% the household debt-to-GDP ratio increased in Greece despite a real record drop of 6.3%), this measure appears to underestimate the extent of deleveraging. The household debt-to-GDP ratio remains a quality indicator of medium-term developments but fails to take account of the trend and the position of most crisis-hit countries in the deleveraging cycle.

### 3. Deleveraging related more to pre-crisis credit expansion than to household indebtedness

Countries with the most debt in the EU27 do not necessarily deleverage more: the correlation between the recent deleveraging and overall household indebtedness to GDP is very low. This indicates that the level of deleveraging is more closely linked to the degree of credit expansion prior to the crisis than to the current amounts of household debt to GDP.

**Figure 3** illustrates the rate of relative deleveraging of 2010 and 2011 if regressed with the overall household debt to GDP (left graph) and the pre-crisis credit expansion (2004-2005). The correlation of the degree of deleveraging with the household debt to GDP is as low as .152, while in respect to the pre-crisis credit expansion, the correlation stands at .491.

**Figure 3 – Aggregate growth rate of household credit 2010-2011 regressed by total household debt to GDP (left graph) and aggregate growth of household credit 2005-2006 (right graph)**



Note: The correlation between household credit growth in 2010-2011 and household debt to GDP is as low as -.152 and could be deemed insignificant due to the probability of the null hypothesis standing at .450. The correlation between household credit growth of the period 2004-2005 and 2010-11 is, on the other hand, as high as -.491 and the null hypothesis could be rejected at 99%. R<sup>2</sup> represents coefficients of determination.

#### 4. Convergence of European household debt-to-GDP levels continues despite the crisis

The convergence of household debt-to-GDP levels in the EU27 continues after a near divergence during the financial crisis. The catch-up process of new MS persists but is mostly due to increases in the western-most newcomers and to deleveraging in the EU15.

A continuing decrease in relative mean deviation among EU27 member states (population-weighted) indicates a persistent convergence in terms of household indebtedness to GDP since 2000. The rate of convergence tended to accelerate year after year until 2006, but was interrupted before the crisis by the indebtedness of the European periphery rising above the EU average and, subsequently, by the financial crisis and fast deleveraging of new MS. Overall, the fast growth of household debt in Europe's periphery until 2005 could be interpreted as a sign of a catch-up process, which probably disguised the true nature of the housing bubble. Although the rate of convergence is slower than before the crisis, especially in respect to new MS, European households continue to converge in terms of household debt to GDP.

The rate of convergence of CEE10 to EU15 has been significantly slowed down by the crisis. Despite low levels of overall household debt to GDP in all CEE10, seven out of ten countries in the region saw a decrease in real stocks of household debt in 2011. Although the westernmost new MS (Poland, Czech Republic, Slovakia, and Slovenia) continue to catch up, countries with the lowest household debt-to-GDP ratio among all EU27 countries (Romania, Lithuania, and Bulgaria) register a second or third year of credit decrease in real terms.

Figure 4 – Household debt to GDP (2011)

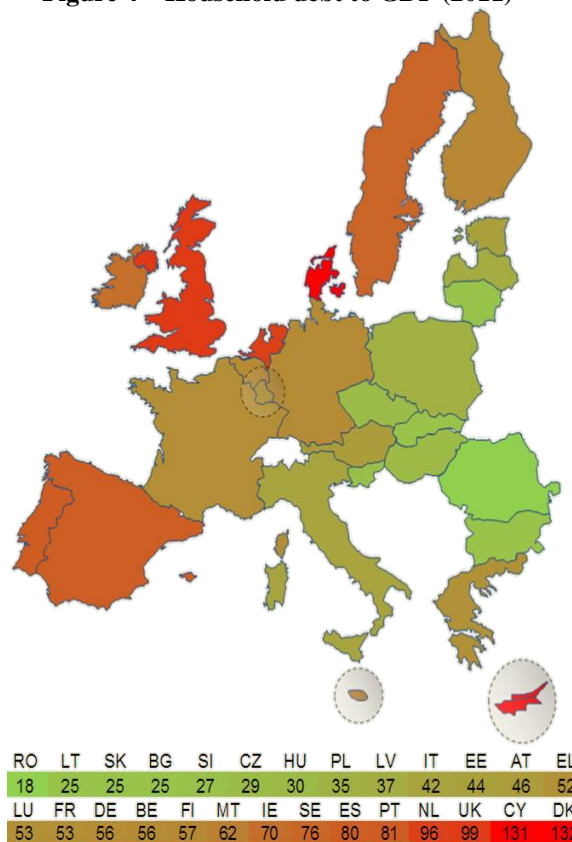
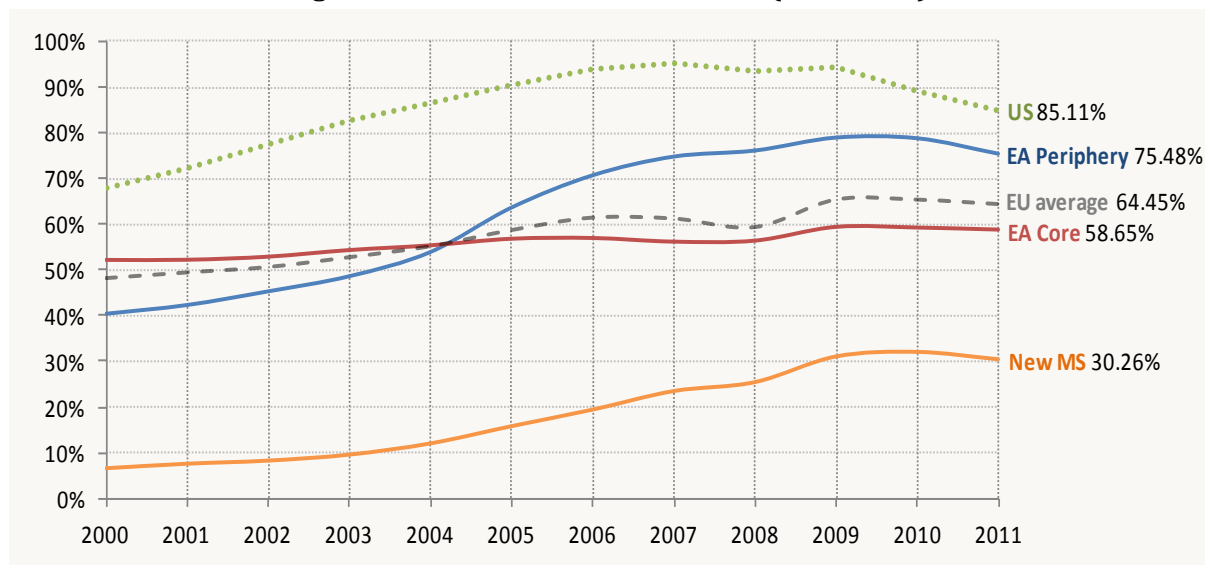


Figure 5 – Total household debt to GDP (2000-2011)

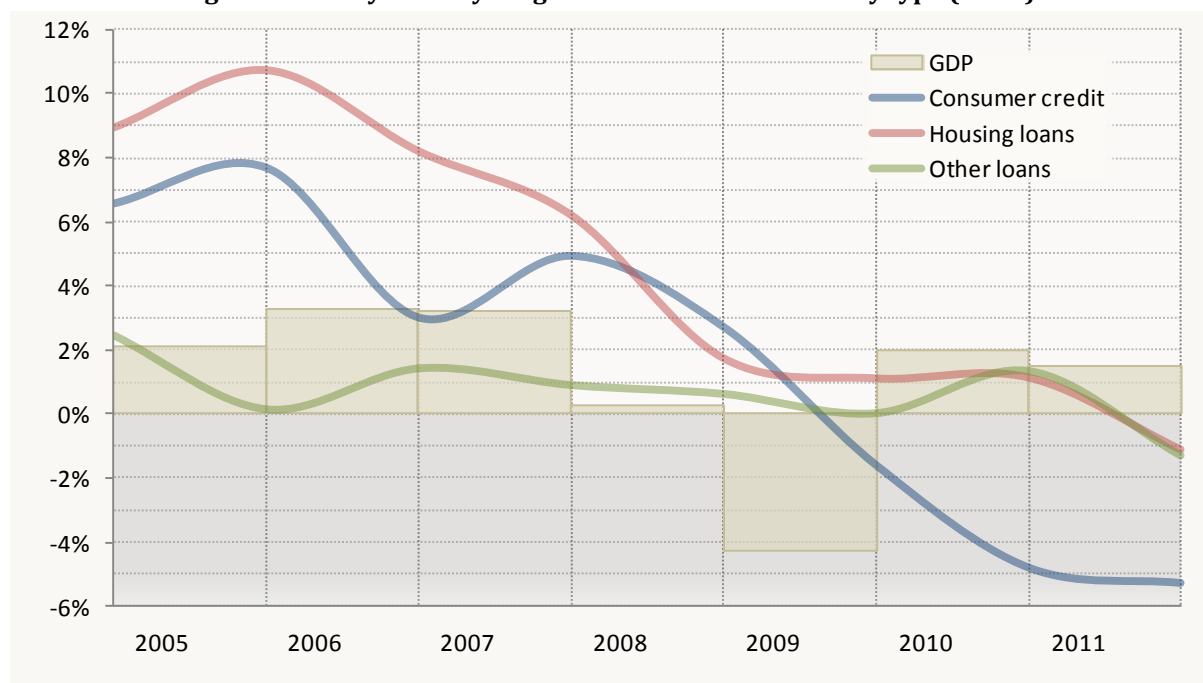


## 5. The pace of deleveraging by type of loan underlines lack of consumer confidence

Consumer credit in EU27 countries registered a third real negative year-on-year growth rate in a row, while housing loans and other loans to European households have declined in real terms for the first time since the crisis. Given the naturally higher rigidity of housing loans and their longer maturities, this pace of deleveraging demonstrates revised expectations regarding Europe's medium-term recovery.

Figure 6 shows the development of different loans to households in the EU. The negative development in loans with longer maturities, in addition to the previous development of more flexible consumer credit, is a clear sign of declining confidence regarding medium-term income and overall economic recovery in Europe. While in 2010 the expectations seemed to be adjusting and the growth rates were not set for a long-term decline in loans with longer maturities, 2011 shows a change in consumer behaviour in terms of housing loans. In 2011, consumers seem to have expanded the deleveraging, also to longer-term loans, probably anticipating modest increases or losses in disposable income in the medium-term future.

**Figure 6 – Real year-on-year growth in household debt by type (EU27)**

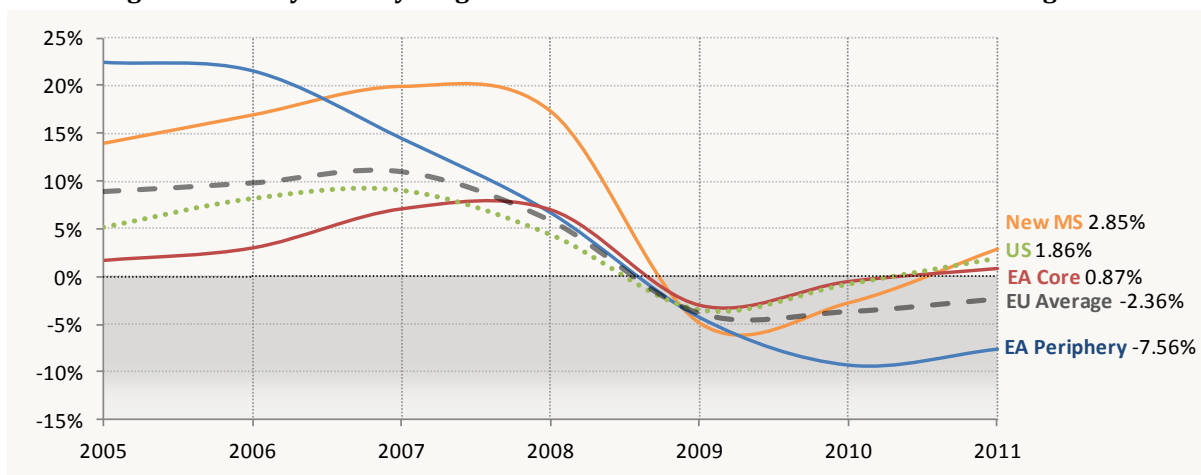


## 6. Deleveraging of NFCs reflecting low business confidence in Europe's periphery

In 2011, the loans to non-financial corporations increased in real terms for the first time since 2008 in the EA core and in new MS. Corporations in countries hit by the sovereign crisis and by austerity measures however continue to deleverage significantly, pulling the European average down and raising worries on investment levels and future growth in Europe's periphery.

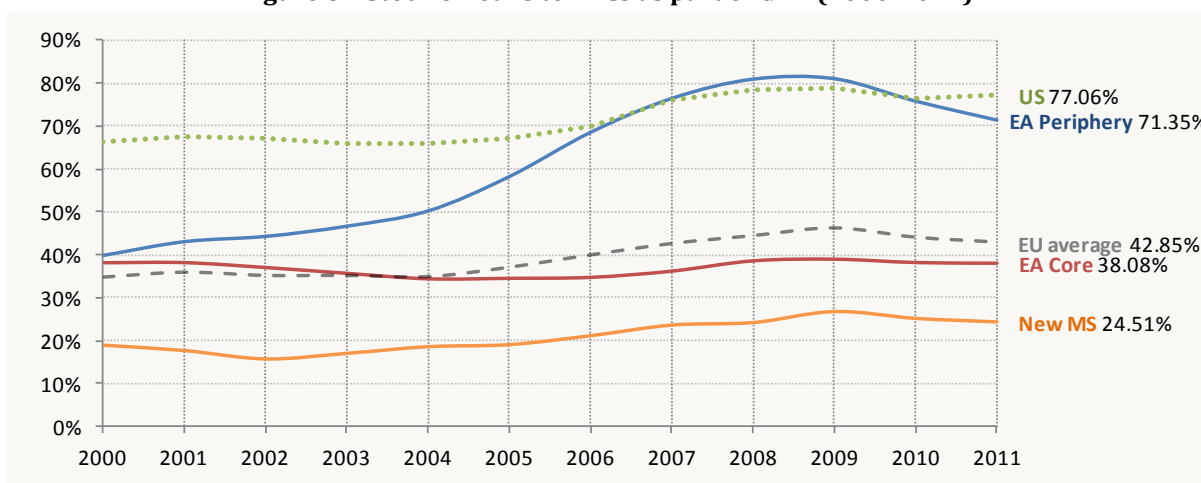
Contrary to household debt, the NFCs' debt cycle recorded a rising path both in the US and the EU. The EA core and new MS are recovering, but the slow growth in the European periphery is pulling the EU27 average down significantly. While the EA core countries show stable development, the dire development of loans to NFCs in 2011 in the crisis-hit countries is a worrying sign for the future of investment in the periphery and illustrates a generalised flight of capital.

**Figure 7 – Real year-on-year growth of the stock of loans to NFCs in chosen regions**



However, with a probable further convergence towards EA-core levels, more deleveraging could be expected in the medium term for the EU’s peripheral countries, as they witnessed a record-high increase of loans to NFCs, both to GDP and in real terms prior to the crisis. Figure 8 shows how starting at similar levels in 2000, the stock of loans to NFCs to GDP doubled in eight years in the EA? periphery, while remaining stable in the EA core and increasing moderately in new MS. Therefore, unlike household loans, the pre-crisis development of loans to NFCs could not be interpreted as a catch-up process of the EA periphery to its core. The large expansion of NFC debt to GDP therefore supports the bubble-like character of the pre-crisis period.

**Figure 8 – Stock of loans to NFCs as part of GDP (2000-2011)**



The ECRI Statistical Package is available in an Excel file in two versions:

Lending to Households in Europe (1995-2011)	€600 (excl. of VAT)
Consumer Credit in Europe (1995-2011)	€440 (excl. of VAT)

It may be purchased at <http://www.ceps.eu/books>