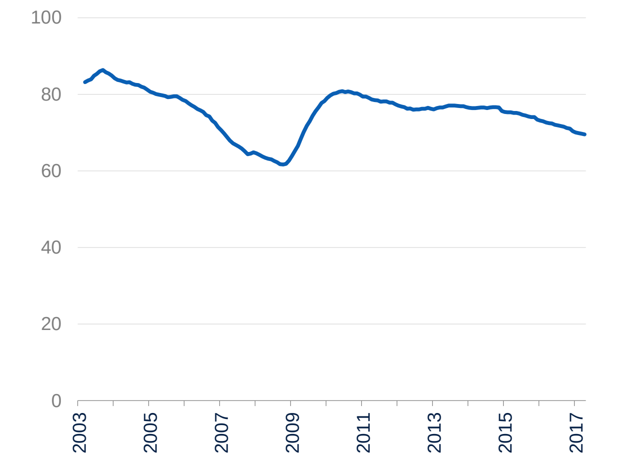
4 Net interest revenue and efficiency: the impact of the crisis on EU countries

The financial crisis triggered a restructuring of the banking systems across EU countries which has impacted banking business. Both revenues and expenses have been affected. Structural factors in each country such as the asset and liability mixes and how monetary policy is transmitted in terms of prices and volumes have been important determinants of the impact on interest margins and administrative costs of restructuring measures.

The expansionary monetary policy implemented on the wake of the crisis led to a reduction in both interest revenues and interest expenses. Given the downwards rigidities of deposits, the spread between lending and deposit rates (i.e. the price effect) has continuously and significantly contracted. This has contributed to the extensive debate about the low profitability of banks (and of financial institutions in general), which can lead to increases in the prices for some services or can, if protracted for too long, put into risk the viability of some institutions.

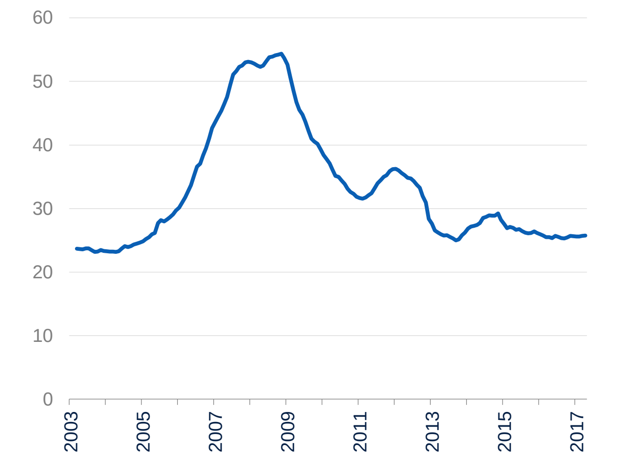
Despite the single monetary policy of the euro area, the transmission has been more complete in some countries than in others or achieved with certain lags. A series of idiosyncratic country factors limit the transmission of monetary policy and, therefore, influence the level of retail rates across countries and over time. Consequently, significant differences in the level of interest rates for loans and deposits, and the spread between both, are observed across euro area countries.

Figure 1 Interest margins, Germany, € billion, annual



Note: The interest margin refers to retail activities and is calculated as the loan volumes times the loan-deposit spread.
Source: ECB and BBVA Research

Figure 2 Interest margins, Spain, € billion, annual



Note: The interest margin refers to retail activities and is calculated as the loan volumes times the loan-deposit spread.
Source: ECB and BBVA Research

With the expansionary policy, monetary authorities seek at expanding the volume of credit. However, such an impact is not straight forward and the evolution of volumes may or may not compensate for the decline in rates as reflected in the evolution of interest margins across countries.

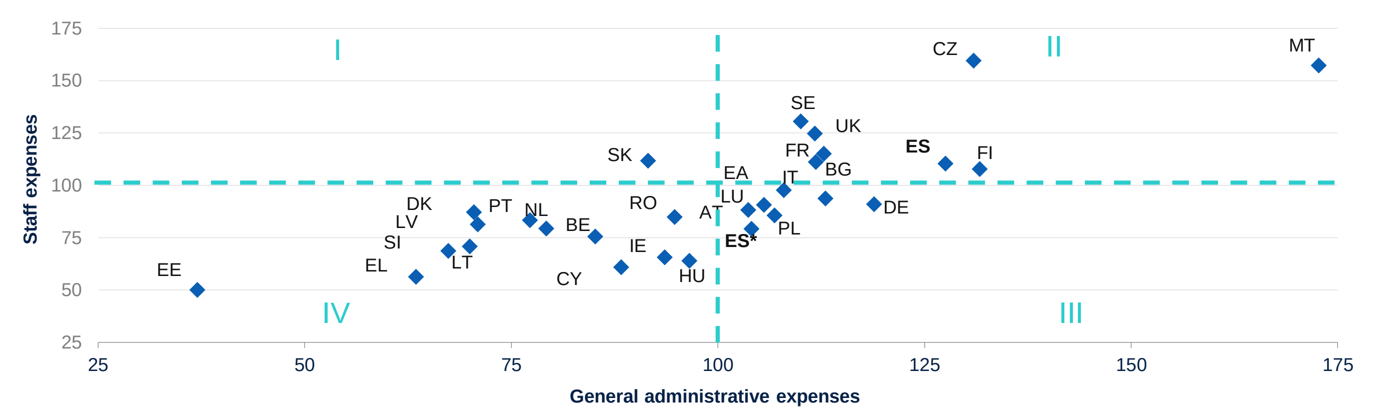
In a number of (mainly core) countries, interest margins have remained rather stable throughout the crisis, although they might have slightly decreased in the last couple of years. This was the case in Germany, where banks were obtaining an interest margin of about €80 billion a year (Figure 1), Belgium and Austria. In the Netherlands, the interest margin generated by banks even increased over the crisis.

In other (mainly peripheral) countries, interest margins plummeted. This was the case in Spain, where interest margins dropped from €50 billion a year to less than €30 billion a year (Figure 2), Italy, Ireland and Portugal. In general, these countries had significantly expanded their lending portfolio in the run up to the crisis.

In a majority of EU countries, staff expenses decreased over the crisis; however, in a few others, staff cost increased, sometimes significantly.

The evolution of general expenses is more mixed (Figure 3). In half of the countries, the outbreak of the crisis led to a rationalisation of general expenses with the largest reductions in costs observed in the countries more impacted by the crisis (e.g. Portugal, Latvia, Greece and Slovenia), as they were required to implement an adjustment program, which included a restructuring and rationalisation of their banking systems[4]. Banks in Lithuania and Estonia also show significant improvements in their general administrative expenses probably linked to the preparations and adoption of the euro.

Figure 3 Evolution of administrative expenses between 2008 and 2015, Index: 2008 =100



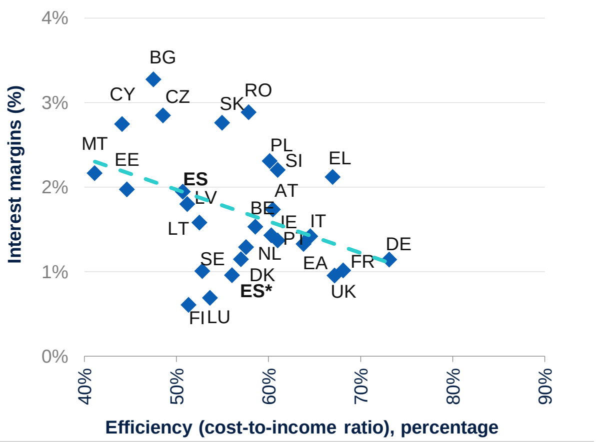
Note: Analysis based on consolidated banking data for domestic banks and subsidiaries and branches of foreign banks. Data include only FINREP (IFRS+GAAP) reporting banks. For Spain, the char includes both consolidated data (ES) and domestic business in Spain (ES*). Data for Lithuania and Czech Republic are for 2014.
Source: ECB and BBVA Research

In the other half of countries, we can observe an increase in general administrative expenses throughout the crisis (particularly in Malta, Finland, the Czech Republic, Spain -although much less for the domestic business- and Germany). It is important to highlight that general administrative costs may temporary increase because of transitional effects driven by the process of restructuring of the banking systems. For instance, closing a branch may entail a penalty if the lease is terminated earlier than what was initially foreseen in the contract.

4: Slovenia, although it did eventually not apply for external support, implemented a series of preventive measures.

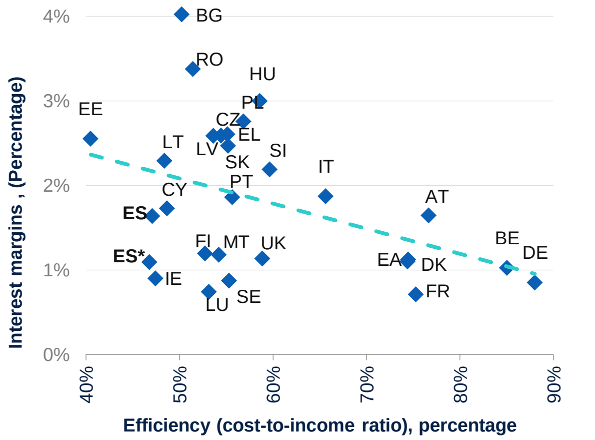
Given the evolution of income and expenses, we observe a compression in the distribution of countries in terms of their efficiency, as the ones with the lowest efficiency (e.g. Germany, Denmark, Austria France and Belgium) have significantly improved their cost-to-income ratios. The positive correlation between efficiency and better interest margins holds both in 2008 and in 2015 (Figures 4 and 5). Moreover, over the crisis, improvements in efficiency (lower CTI ratios) tended to lead to higher interest margins while reductions in efficiency (higher CTI ratios) tended to be accompanied with a deterioration in interest margins.

Figure 4 Efficiency and interest margins, 2008



based on consolidated data. Outliers are excluded from the analysis: the Netherlands, with a CTI of 186% in 2008; and Hungary, with a CTI of 83% and an interest margin of 3.4% in 2015. Data for Croatia are not available..
Source: ECB and BBVA Research

Figure 5 Efficiency and interest margins, 2015



Note: Interest margin: net interest income over total assets. Analysis based on consolidated data. Outliers are excluded from the analysis: the Netherlands, with a CTI of 186% in 2008; and Hungary, with a CTI of 83% and an interest margin of 3.4% in 2015. Data for Croatia are not available.
Source: ECB and BBVA Research

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Este informe ha sido elaborado por la unidad de Sistemas Financieros

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