Q1 2018 overview of banking sector

Yearly growth in the loan portfolio of banks operating in Estonia increased in the first quarter of 2018 from 2.1% to 2.6%. This is still low compared to the rates of growth in recent years because of the one-off reorganisation in the third quarter of last year of market participants within a consolidation group. If the effect of the reorganisation is removed, actual loan growth picked up to reach 7.3% in the first quarter, and would have been 6.8% in the previous quarter.

Key indicators	Q4 2017		Q1 2018
Yearly growth in the loan stock	2,1%	?	2,6%
Yearly growth in the stock of deposits	4,6%	?	2,7%
Loan-to-deposit ratio	107%	?	110%
Share of long-term overdue loans in the portfolio	0,8%	?	0,8%
Liquidity coverage ratio	165%	?	152%
Profit	78 mln €	?	81 mln €
Ratio of expenses to income	47%	?	45%
Return on equity	10,3%	?	10,1%
Return on assets	1,6%	?	1,5%
Core Equity Tier 1 ratio	30,1%	?	31,1%

As a result of intra-group transactions, the size of the corporate loan portfolio was 1.7% smaller than in the first quarter of the previous year, but without those transactions it would have increased by 7.5%. The yearly growth in the loan portfolio for private clients slowed though, to 6.4% in the first quarter, and the yearly growth in housing loans similarly slowed.

The yearly growth in deposits slowed to 2.7% in the first quarter from 4.6% in the previous quarter. As the growth in deposits was similar to the growth in loans, the loan-to-deposit ratio of the banking sector including branches remained at 110%, which is the same level as both in the previous quarter and a year earlier.

The share of loans overdue by more than 90 days continued to decline as there were fewer overdue loans and as the loan portfolio grew, and it stood at 0.8% at the end of the first quarter. The ratio for total overdue loans rose from 2.87% to 2.92%.

The liquidity position of the banks remains strong. All the banks met the Liquidity Coverage Ratio (LCR) with sufficient margin, and the average indicator for the sector was 152%. Alongside the funds dedicated for meeting the Liquidity Coverage Ratio, the banks also have other liquid assets, notably deposits in credit institutions, and these account for 20% of assets.

The total funding of the banks shrank in the first quarter by 1.3%. The type of funding that grew most was household deposits and local government deposits, while deposits of credit institutions and other non-financial companies decreased. Client deposits were down 1% over the quarter. Resident deposits were down 0.1% and non-resident deposits down 8%. In total the share of non-resident client deposits fell from 11.8% in the first quarter of last year to 10.9% in the first quarter of this year.

Banks and branches earned 81.3 million euros in profit in the first quarter, which is 4% more than in the fourth quarter of 2017. The operating income of the banking sector as a whole increased by 18% to 249 million euros. Among the main sources of income, interest income was down 2% over the quarter and service fee income was down 9%.

The return on equity of the banks fell in the quarter from 10.3% to 10.1%.

Indicators for prudential requirements improved in the first quarter. The Common Equity Tier 1 ratio rose from 30.1% to 31.3%. The rise in capitalisation came mainly from a reduction in risk exposures.

Main development trends and risks

- The share of loans overdue more than 90 days is declining and the overdue loans past due more than 90 days are fully covered by provisions.
- The profitability of the banks remains good. Return on equity of 10.1% in the first quarter indicates that banks are managing to maintain their profitability even with interest rates low.
- The share of non-resident deposits fell by the end of the first quarter to 10.9%. As non-resident deposits are by their nature more volatile, the banks are holding higher liquidity buffers to cover the liquidity risk from these deposits.
- The loan growth at several banks is fast and is above the average for the sector. Fast growth in loans comes with large risks.
- The risks related to the Swedish real estate sector remain and any realisation of these risks could impact the Estonian banking market. This makes it important for the banks to maintain sufficient capital buffers as a safeguard against the realisation of these risks. The presence of the high capital buffers reduces the impact of cross-border risks.

Quarterly reviews of the banking sector

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