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SME loans in southern Europe – are the lean times over?

Author: Dr Barbara Richter, phone +49 (0) 69 7431-8221, research@KfW.de

In 2013, lending to companies in the eurozone continued to contract (by 3 % year-on-year in December 2013, as defined in MFI interest rate statistics). The trend has continued in January 2014. It seems that weakness in lending was not due to the efforts of banks to keep their balance sheet totals low ahead of the ECB's Asset Quality Review (AQR) cut-off date of 31.12.2013.

Weak domestic demand slows loans to sole proprietors

In the southern European states, new business in loans to sole proprietors declined in 2013 compared to 2010 by between 33 % (in Portugal) and 40 % (in Spain). In Germany the figure was just 6 %. The risk premium relative to Germany (see figure) has risen steadily since 2010 and stood on average at approx. 500 base points (bp) for Portugal, approx. 400 bp for Spain and 300 bp for Italy in 2013.

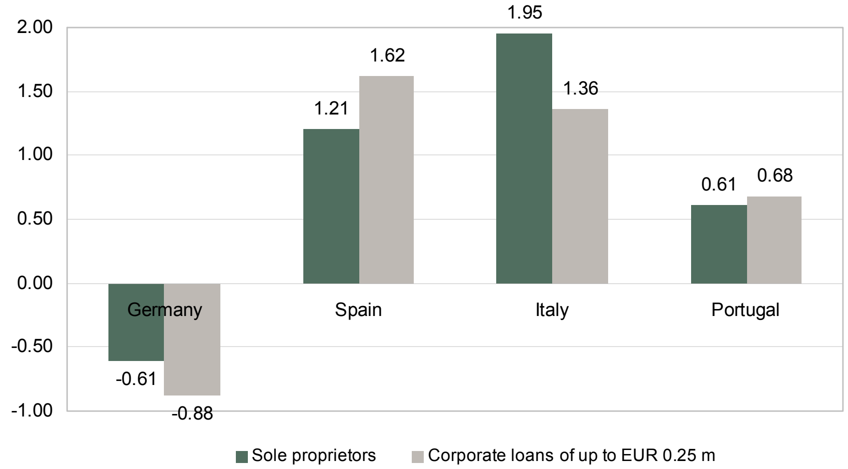
The low level of lending and the high risk premiums are attributed to weak domestic demand and the associated poor business outlook for sole proprietors. An upturn can only be expected once falling unemployment and a rise in salaries lead to an increase in domestic demand. More stable economic prospects for 2014 give some reason for optimism.

Decline bottoms out for companies in the south west

New business in corporate loans of up to EUR 1 million has also contracted compared to 2010, although the degree differs. The decline amounted to 36 % in Spain and 17 % in Portugal. In Germany and Italy the decline was less significant, at 7 % and 3 % respectively.

Smaller corporate loans of up to EUR 0.25 million provide a mixed picture. Compared to 2010, lending rose by 9 % in Germany and 6 % in Italy, while it fell by 22 % in Portugal and by 33 % in Spain. The average risk premium for corporate loans in 2013 was considerably lower in Italy and Spain (below 200 bp) than in Portugal (up to 350 bp).

Figure: Interest rate difference since the start of the euro crisis (2010 vs. 2013)
(in percentage points, yearly averages (from June 2010)



Source: MFI interest rate statistics, data as at December 2013

There is a glimmer of hope on the horizon for corporate loans in Spain and Portugal – compared to the previous year, new business for smaller loans rose slightly over the winter. Moreover, various surveys by the ECB indicate easier access to credit for Portuguese SMEs and an easing of loan terms in both countries. Growth prospects have improved notably there in recent times, mainly due to strong export growth.

By contrast, the positive figures in Italy are misleading: conditions for SME loans have been tightened further and demand is weak. The rise compared to 2010 is attributable to a base effect: 2010 marked the low point following the shock of the financial crisis, and the ensuing recovery remained poor.

The banks are preoccupied with themselves

Alongside weak demand, the banks' aversion to risk is contributing to lower lending volumes. Many of them are still busy adjusting their balance sheets following high loan losses. Furthermore, as part of the AQR, they are working on strengthening their equity capital and ensuring it is not burdened further by high-risk loans. Moreover, domestic government bonds can generate relatively high yields without encumbering equity (as their risk weight is zero), which means they are more favourable investments than SME loans.

Loan supply will not improve decisively before the banks' balance sheets are cleaned up. All the same, good annual results from some southern European banks indicate that the process of repairing balance sheets is progressing well. Furthermore, extending loans to SMEs could be made more attractive for the banks than buying government bonds (e. g. via bond purchasing by the ECB). ■