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EXECUTIVE SUMMARY

THE FINANCIAL CONDITION OF EU BANKS IMPROVED IN 2004 AND THE FIRST HALF OF 2005

EU banks' profitability continued to improve in 2004 and the first half of 2005, extending the positive trend started in 2003, although the interpretation of 2005 data is clouded by the start in the adoption of the International Financial Reporting Standards. Moreover, profitability also improved in those national banking sectors that had reported weaker results in 2002 and 2003. At the same time, net-interest margins continued to remain under pressure in nearly all national banking sectors.

The main drivers of increased profitability were lower provisioning, a sustained increase in lending, especially to households for housing purposes, and an incipient recovery in lending to non-financial corporates, including small and medium-sized enterprises. Cost-cutting, which had significantly contributed to increased profitability in 2003, abated in 2004 and the first half of 2005, indicating a levelling-off in this source of banks' profitability.

BANKS' RISK OUTLOOK

Although in the short-term the improved profitability is noticeable and has provided banks with the resources to increase their buffers, some downside risks remain over the medium or long-term.

With regard to the risks internal to the banking sectors, the fall in provisions to historically very low levels in most EU banking sectors could have left banks more exposed to a deterioration in credit quality. Banks are also faced with increased competition from their peers for the revenues currently received from lending to households. Competition has not only kept lending margins rather low, but may have also induced banks to loosen their credit standards, thus increasing their exposure to credit risk. Because of the likely difficulties experienced by banks in maintaining or increasing their interest income, in the more mature credit markets in particular, banks may have engaged in investments in alternative assets or geographical regions, thus increasing their risk-taking.

With regard to risks external to the banking sector, banks remain exposed to risks arising from their general economic operating environment. Credit risk remains the major source of risk for banks, following large lending volumes to households, especially for housing purposes. A risk of a rapid deterioration in credit quality may not be immediately incumbent on banks, given the still rather conservative loan-to-value ratios in most EU countries and the overall good condition of households' balance sheets, but it could materialise in the still rather unlikely event of a severe downturn in general macroeconomic conditions. This risk may be particularly acute in those countries where households' balance sheets are more stretched and housing prices have deviated from their long-term values.

Concerning lending to the non-financial corporate sector, the overall conditions for EU banks have changed rather significantly from those described in the 2004 EU Banking Sector Stability Report, as corporates, including the small and medium-sized enterprises, have returned to borrowing from banks. This development offers a welcome source of income differentiation for banks, and for as long as overall macroeconomic conditions remain positive, including developments in so far persistently high oil prices, does not necessarily increase banks' credit risk. Nonetheless, some signs of increased leverage in the corporate sector call for ongoing monitoring. In addition, new products in the credit market, to the extent that banks are involved in the launch/trading of the new instruments or have established credit or investment links with new entrants in the market, may have increased risks for banks. Examples of these recent developments are the emergence of the private equity business, the growing complexity of risk transfer instruments and the increasing leverage of loans.

With regard to market risks, banks' direct exposures (e.g. to hedge funds and emerging market economies, as well as to interest rate, equity and exchange rate risk) are in general contained. However, amid low or falling long-term interest rates, the risk of a flattening or even an inversion of yield curves has started to feature as a plausible risk scenario. As banks rely on maturity transformation for a large share of their interest income, a flattening of yield curves would put additional stress on this source of income for banks. Finally, concerning liquidity risk, ample global liquidity has sustained banks' profitability through lending growth and fees and commissions on trading activities, and has protected the quality of banks' loan portfolios. Should an abrupt correction in global liquidity occur, accompanied by an unexpected rise in long-term interest rates, banks could be exposed to losses. As discussed in the 2004 report, banks' direct exposures to a rise in long-term interest rates are in general limited, but indirect exposures, especially through a negative impact on credit risk, in the event of a downturn in general macroeconomic conditions, cannot be ruled out.

OVERALL ASSESSMENT

Over the near future, EU banks' good financial results in 2004-05 indicate an increase in the profitability of the EU banking sectors. Nonetheless, the present, positive conditions may not easily carry over into the medium or long-term, as they are dependent on currently very benign liquidity and credit conditions. In this light, the overall positive assessment based on the market indicators presented in this report, which are consistent with the other sources of information discussed throughout the report, may more adequately be considered as a baseline outlook. There are in fact some positive and negative factors that could affect this baseline scenario. On the negative side, the risks associated with the uncertainty surrounding the near-term macroeconomic outlook, not least because of very high oil prices, as well as the continuing global financial imbalances, increasing household indebtedness and low provisions by EU banks could materialise in a worsening in credit and liquidity conditions. Moreover, concerns over the sustainability of net-interest income growth have increased. On the positive side, EU banks have improved their risk management over the recent years, thus increasing their ability to cope with the growing complexity of products and counterparties links. However, while the use of complex risk transfer products may at least partly shelter banks from heavy losses, their full protection potential remains to be tested in stress situations.

Overall, although at present banks' financial condition is broadly satisfactory and no specific factors can be identified that could trigger the realisation of the more negative scenario, the underlying weakness of banks' provisions and their increased exposure to credit risk may render them sensitive to a potential, future deterioration in the currently benign credit and liquidity environment.

1 INTRODUCTION

The EU Banking Sector Stability Report contains the main findings of the regular annual macro-prudential analysis of EU banking sector stability by the Banking Supervision Committee (BSC) of the European System of Central Banks (ESCB). The BSC is composed of representatives of banking supervisory authorities and central banks of EU countries and the ECB. This is the fourth such report since February 2003.

The report reviews the performance of EU banks and their ability to withstand financial instability, and it identifies the potential threats to EU banks' stability. The risks thus identified are not necessarily the most probable outcomes; rather they are potential and plausible sources of downside risks for banks – with regard to the likeliest outcome.

The analysis in the report draws on a number of sources. A primary source of quantitative information is a large set of indicators provided by national supervisors, national central banks and the ECB. In addition, the report also draws on the information regularly exchanged in the context of the BSC. In relation to the quantitative information, the consolidated banking data, which are regularly collected by the BSC and every year refer to the preceding year's data, are the fundamental reference for the report. These data cover nearly all of the EU banking industry and are among the timeliest of comparable data collected by national authorities (see the box in the Statistical Annex). Publicly available data for large EU banking organisations have been used to complement this analysis for the first half of 2005, although the change in reporting standards for listed banks' public reports clouds the analysis of banks' results for 2005.

The report covers all twenty-five EU Members States, with additional information on two sub-samples, i.e. the twelve member countries of the euro area and the thirteen Member States not in the euro area (referred to in this report as EU-13). The collection of the banking data is run on a consolidated basis for all EU Member States, so that a split between the first fifteen EU Member States and the ten that joined in May 2004 made in the 2004 report is no longer presented.[1]

The report is structured as follows. Section 2 discusses the major developments in EU banks' financial condition in 2004 and the first half of 2005. It is based on the consolidated banking data for 2004, as well as for 2002 and 2003, to provide a comparison over time of the main indicators, and mainly on data from public sources for 2005. The discussion covers banks' profitability, income, costs, provisioning, asset quality, solvency and liquidity. Section 3 introduces and discusses the major risks faced by EU banks, covering credit and market risks, the latter in the form of interest rate, equity and foreign exchange risks, as well as exposures to hedge funds, private equity funds and emerging market economies. Section 4 combines information from market sources (i.e. various types of quantitative market indicators) with the information from the previous sections to formulate an assessment of EU banks' conditions. The report concludes with an overall assessment of the stability of the EU banking sector.

[1] In the 2004 EU Banking Sector Stability Report, the ten new EU Member States, who joined the EU in May 2004, delivered banking data on a solo basis, thus requiring a separate analysis of their banking sectors

II. EU BANKS' PERFORMANCE IN 2004 AND THE FIRST HALF OF 2005

BANKS' PROFITABILITY IMPROVED ACROSS THE BOARD

The profitability of EU-25[2] banks improved further in 2004 (see Chart 1), consolidating the recovery that began in the previous year. The main drivers of the strengthening of banks' profitability continued to be reductions in the flows of provisions and growth in lending to households, mostly for housing purposes. These trends continued in the first half of 2005, although the introduction of International Financial Reporting Standards (IFRS) clouds the comparison with data from the previous years (see Box 1).

In 2004, the average return on equity (ROE)[3] for EU-25 banks stood at 12.21% at end-2004 (see Statistical Annex, Tables 2, 6 and 10), more than two percentage points higher than the level in 2003. The increase was particularly marked in the euro area, albeit from a considerably lower level than in the EU-13. The developments in return on assets (ROA) were similar to those in the ROE.

In addition to the strengthening of average profitability, the distribution of ROE for EU-25 banks shifted to the right (see Chart 2). This improvement was common to the two subgroups of euro area and EU-13 banks.

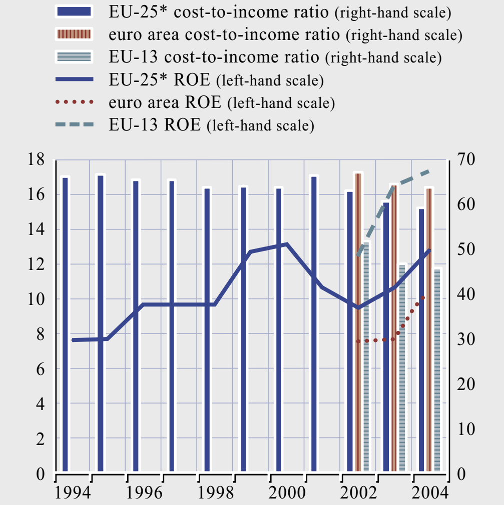
Looking at the average ROEs in the various size groups for domestic banks (see Statistical Annex, Tables 2, 6 and 10), in the EU-25 profitability remained higher and improved

[2] Three regional groups are discussed in this report: the twenty-five member countries of the EU, which are referred to as the EU (or, for clarification, as the EU-25, when compared with subgroups within the EU and in charts and tables), the euro area countries, and the non-euro area countries, or the EU-13. Given the larger size of the consolidated banking sector in the United Kingdom, Sweden and Denmark than in the other ten members of the EU-13, the banks in these three countries drive to a large extent developments in the EU-13 banking data. This is especially the case when the sub-set of large banks is considered, given the absence of large banks in the other ten EU-13 countries. For information on the definition of the size groups and the computation of the aggregate indicators for the EU-25, the euro area and the EU-13, see the box in the Statistical Annex.

[3] ROE figures are calculated on the basis of profits after tax and extraordinary items.

Chart 1 Profitability and cost-to-income ratios of EU-25 banks

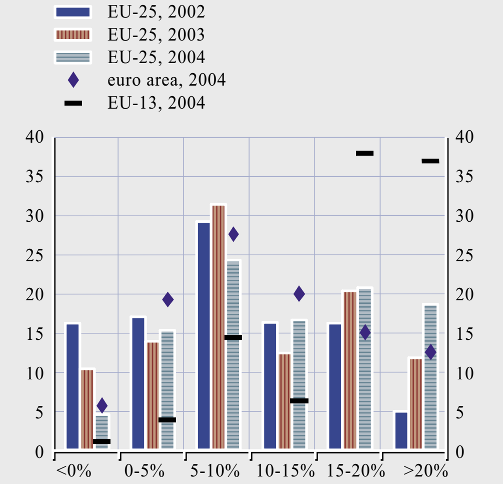
(1994-2004, all domestic banks, %)



Source: BSC.
Note: (*)Data for the EU-15 in the period 1994-2001.

Chart 2 Frequency distribution of ROE for EU-25 banks

(2002-2004, all domestic banks, after tax and extraordinary items, % of total assets)



Source: BSC.

markedly among the group of large domestic banks, with the group of large banks in the euro area experiencing the largest increase, in percentage points, among the group of domestic banks in all regions. For small banks, the ROE remained consistently lower than for medium-sized or large banks, a phenomenon that can, in general, be explained by the larger amount of equity held by small banks. In fact, the latter registered among the highest ROA levels among both domestic and foreign banks in each region. Concerning the group of foreign banks, which includes both EU and non-EU-owned foreign banks,[4] their profitability performances mirrored those of EU-25 banks. In the EU-25, their ROE stood at 11.70% at end-2004.

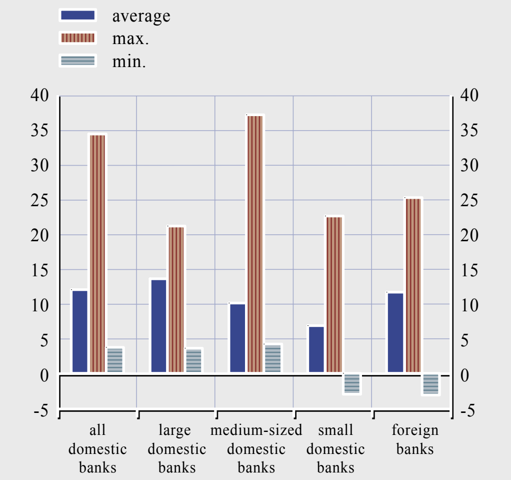
Some weakness, however, remained among small banks and foreign banks, as some of these banks, when information is viewed at the country rather than bank-specific level, endured losses (see Chart 3). Nevertheless, the banks concerned were rather small so the overall performance of their national banking sector was still satisfactory. Similarly, developments among foreign banks were usually significantly positive in those countries where foreign banks represent a large share of total national banking sector assets. As a result, the minimum negative levels recorded for foreign banks in the EU did not represent a large share of EU banking sector assets (see Statistical Annex, Tables 1, 14 and 15).

Additional insight can be gained from the change in the width of the distribution of ROE across different types of banks over time, although information is not available at the individual bank level but only at the country level. The dispersion in the levels of ROE among different groups of banks narrowed significantly in the period between 2002 and 2004 (see Chart 4). This narrowing was most pronounced among euro area domestic banks, largely due to developments in the group of large domestic banks, notwithstanding a small increase between 2003 and 2004. Together with the increase in the average level of ROE and the rightward shift of its distribution, the narrowing of the dispersion of ROEs across EU banks indicates that the improvement in performances in 2004

[4] See the box in the Statistical Annex for the definition of foreign banks.

Chart 3 EU-25 banks' ROE: average, maximum and minimum at the country level

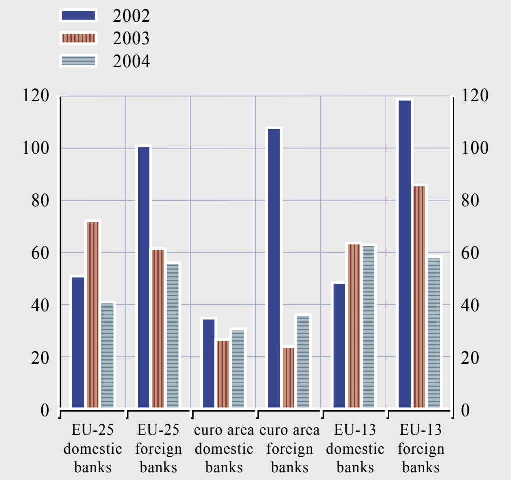
(after tax and extraordinary items, % of the average)



Source: BSC.

Chart 4 Interquantile range of ROE for EU-25, euro area and EU-13 banks, at the country level

(after tax and extraordinary items, % of the average)



Source: BSC.

was broad-based, both in the euro area and in the EU-13. In particular, conditions improved significantly in those national banking sectors that had lagged behind EU averages over the past couple of years.

Finally, dispersion of ROEs remains higher among the set of EU-13 banks, both for domestic and foreign banks, which can possibly be explained by the rather heterogeneous properties of the economies and of the banking sectors among these thirteen countries.

Regarding results for 2005, available data for the first half for a set of large EU banks indicate that the trend observed in the consolidated banking data for 2004 continued into the first half of 2005 (see Box 1 and Table 18 of the Statistical Annex). However, apart from a difference in the sample between the consolidated banking data and the data used in Box 1, a direct comparison between results for EU banks in 2004 and 2005 is hindered by the application of new reporting requirements in 2005, following the adoption of IFRS.

Box 1

FINANCIAL CONDITION OF LARGE EU BANKS[1]

Variation in the dates of implementation of IFRS by European banks has meant that of the set of 50 large EU banks used in previous EU Banking Sector Stability Reports, some banks have begun to compile their financial statements under IFRS, while others have continued reporting under local or US GAAP. Given that IFRS and non-IFRS accounts are not directly comparable, the analysis of recent financial results has become more complicated. Hence, in order to ensure a consistent analysis, the set of 50 banks was split into two sub-groups depending on whether the banks reported their 2005 accounts under IFRS or non-IFRS (see Statistical Annex, Table 18).

Non-IFRS reporting banks

Overall indications are that the financial positions of large EU banks not reporting under IFRS continued to improve in the first half of 2005, consolidating the performance of the previous two years. This was mainly driven by favourable economic conditions in some European countries; many banks also benefited from exposure to rapidly growing retail banking markets in Latin America and eastern Europe.

Overall profitability, as measured by the weighted average[2] ROE, continued to improve rising from 11% in 2004 to 16.4% in Q2 2005 (see Chart A). Furthermore, the weaker institutions also managed to improve their performances, with banks in the lowest 10% of the distribution raising profitability from 9.15% in 2004 to 13.64% in the first six months of 2005.

Banks' net interest income as a percentage of total assets continued to fall, dropping from a weighted average of 1.99% in 2004 to 1.56% in the first half of 2005, as the impact of increased volumes of lending in several countries was more than counterbalanced by margin erosion. This

[1] These large EU banks were selected on the basis of the size of their total assets and also because they are generally active in more than one EU Member State. Banks from the ten newest EU Member States were only included to the extent that they are consolidated within the accounts of parent entities. The sample of banks remains the same over the reference period. Figures are based on consolidated financial statements and are annualised for the first half of 2005. The sample consists of 50 banks in total; 35 of these report under IFRS and the remaining 15 do not.

[2] Averages are computed by weighting individual bank's indicators by the same bank's total assets.

Chart A Frequency distribution of return on equity for large EU-25 banks

(Non-IFRS)

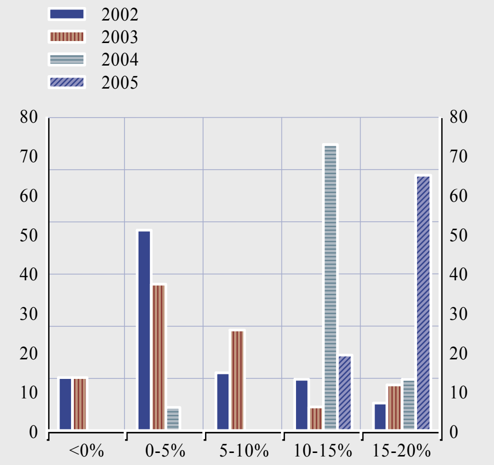
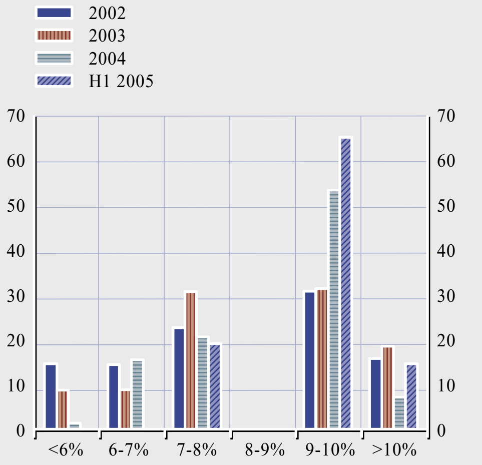


Chart B Frequency distribution of Tier I capital for large EU-25 banks

(Non-IFRS)



Source: ECB calculation based on published accounts of individual banks.
Note: Data for the first half (H1) of 2005 are annualised and unaudited and are not based on the full sample.

was due to flat yield curves, low absolute levels of interest rates, and the financing of lending growth by more expensive wholesale funding as opposed to cheaper retail deposit funding. Moreover, the effect of increased competition in certain retail segments also led to pressure on margins. Most institutions also reported increased non-interest income, especially fee and commission income. Nonetheless, the share of net interest income in total income increased from 41.74% in 2004 to 45.24% in the first half of 2005, although even the 2005 result is still far from the values registered in 2002 or 2003, when the share of net interest income was around 50%.

On the whole, improved credit risk conditions led to a continued decline in provisions from a weighted average 0.28% of total assets in 2004 to 0.07% at the end of the second quarter of 2005. This level of provisioning was very low compared with historical norms. While some individual institutions have indicated that provisions may increase slightly during the second half of the year, it cannot be ruled out that the adequacy of some banks' provisioning could be tested if credit conditions were to deteriorate.

Cost-cutting measures continued to be implemented by banks in the first half of 2005 in order to sustain profitability. The weighted average cost-to-income ratio decreased marginally from 65.1% in 2004 to 64.9% in the first half of 2005. This contrasts with the larger decreases in the ratio that had taken place during 2002 and 2003. Over this period, the weighted average ratio decreased from about 73.2% to 68.6%. The gradual slowing of cost cutting may indicate that, for some institutions, costs may now be firmly under control. The weighted average Tier 1 ratio increased from 8.62% in 2004 to 9.31% in Q2 2005, with the weakest performing institutions also managing to increase their Tier 1 ratios (see Chart B)

IFRS reporting banks

As only one-quarter of historical data exists for comparison, any inferences on performances must be treated with a high degree of caution. This is because the restated accounts for 2004 or mid-2005 are not audited and because institutions have varied considerably in the degree to which they have implemented the accounting standards IAS 32, IAS 39 and IFRS 4. Furthermore, given that 2005 is viewed by banks and rating agencies as a transitional year for accounting purposes, there are uncertainties about the extent to which the development of banks financial results reflects either underlying circumstances or accounting changes. This will probably only become evident in 2006. In the short term, there may be important country-specific effects related to IFRS implementation that may affect the interpretation of the results.

The evaluation of profitability for IFRS reporting banks is difficult to assess and some caveats should be borne in mind, as it is not yet fully clear the degree to which the change in accounting standards affected ROE results.[3] As far as the information in public reports by banks is concerned, profitability, as measured by the weighted average ROE of the largest EU banks reporting under IFRS, increased from 10.95% in 2004 to 20.57% in the first six months of 2005 (see Chart C). Should the 2004 value of ROE be calculated prior to the change in accounting standards, it would be higher, at 13.3%, thus raising the question of whether the restatement of 2004 financial results under IFRS may have produced a more impressive ROE growth between 2004 and 2005. Given the information available at present, this question cannot be answered, although on the face of it, ROE for IFRS banks suggest that the underlying performances of most large EU banks have remained solid. In fact, all institutions in the sample reporting results for the period up to the end of June 2005 posted positive ROEs. Concerning net interest income as a share of total income, it rose from 53.36% in 2004 to 54.98% in the first half of 2005, but coverage on this indicator is significantly limited, thus further hindering a substantial analysis of its developments among IFRS reporting banks.

For banks reporting under IFRS, net interest income fell from 1.18% of total assets in 2004 to 1.03% in Q2 2005. As with those banks that did not report financial results under IFRS, this reflected ongoing margin erosion. By contrast, the non-interest income, especially fee and commission income, of most institutions rose in the first half of 2005. Provisions declined from 0.20% of total assets at the end of 2004 to 0.14% of total assets at the end of the second quarter of 2005. Costs declined, with the weighted average cost-to-income ratio falling from 58.03% in 2004 to 56.49% in Q2 2005. The cost-to-income ratio decreased only marginally in the best performing group of institutions (the bottom 10% for the cost-to-income indicator), perhaps signifying that cost control has been firmly established and that there is limited room for profit generation through one-off cost-saving measures as opposed to sustainable revenue growth.

Regarding the solvency indicators, the same caveats mentioned in relation to the analysis of ROE apply. On the face of it, increased profitability has also led to the continued strengthening of capital ratios: the Tier 1 ratio increased from 6.56% in 2004 to 7.67% in 2005 (see Chart D).

[3] For instance, a rise in ROEs could be due to changes in goodwill valuation techniques, reallocation of assets in different banking portfolios, the inclusion in results of previously unrealised gains in some portfolios, or the reclassification of items from equity or liabilities. A special feature in the December 2005 issue of the ECB Financial Stability Review will describe these points in more detail.

Chart C Frequency distribution of return on equity for large EU-25 banks

(IFRS)

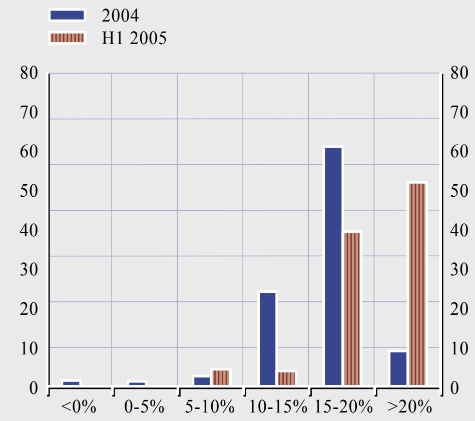
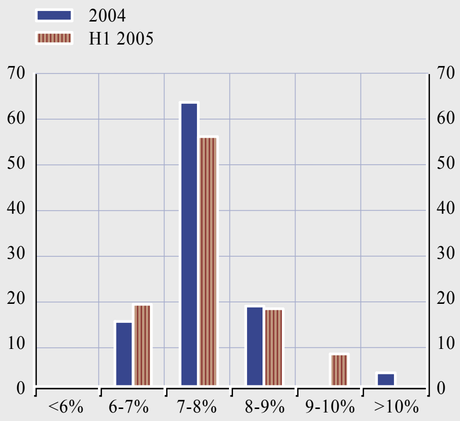


Chart D Frequency distribution of Tier I capital for large EU-25 banks

(IFRS)



Source: ECB calculation based on published accounts of individual banks.
Note: Data for the first half (H1) of 2005 are annualised and unaudited and are not based on the full sample.

While the IFRS and non-IFRS data are not comparable, it is noteworthy that most indicators of financial conditions for both sets of banks have improved regardless of the accounting method used. If this process continues, the resilience of EU banks to adverse shocks should improve further. However, for some institutions without strong underlying performances in their most important markets, it remains to be seen how durable the current return to profitability will be given the reliance of these institutions on certain types of non-interest income sources and cost-cutting to boost overall profitability.

OPERATING INCOME FELL MARGINALLY

Total income as a percentage of total assets fell marginally between 2003 and 2004 in the EU-25, the euro area and the EU-13 across nearly all size and ownership groups. Moreover, the share of net interest income in total income fell between 2003 and 2004 both for the euro area and especially for the EU-13, across nearly all size and ownership groups, continuing the negative trend discussed in the 2004 report (see Statistical Annex, Tables 2, 6 and 10). In fact, banks' operating environment created increased difficulties for banks in increasing or maintaining their interest income, especially in mature markets where the more traditional lines of interest-income generating business have already been exhausted (for instance, loans fell marginally, as a share of total assets; see Statistical Annex, Tables 3, 7 and 11). Moreover, even in those banking sectors where growth in lending volumes has been robust, banks have generally been unable to sustain or increase their interest income proportionally due to margin erosion.

Regarding lending volumes, their increase continued to be mostly associated with lending to households for housing purposes. For instance, looking at the euro area,[5] the low interest rate

[5] These data are based on lending by monetary financial institutions (MFIs) to households in the euro area for housing purposes, considering all maturities. MFI data differ from the 2002-04 consolidated banking data used for the EU banking sector because MFI data are on a solo basis, and because MFIs comprise the Eurosystem central banks, credit institutions, money market funds, and other institutions whose business it is to receive deposits and/or close substitutes for deposits from entities other than MFIs and, for their own account, grant credit and/or make investments in securities. The MFI data used in this report exclude the Eurosystem central banks.

environment supported a rise in lending to households for housing purposes to an annual rate of 7.9% in December 2004, a rate similar to what was experienced in 2003. This growth rate further accelerated to 10.2% on an annual basis, according to preliminary data for the first six months of 2005. Growth in lending for housing purposes recorded even higher rates in some EU-13 countries, where general macroeconomic conditions have generally been more favourable than in the euro area.

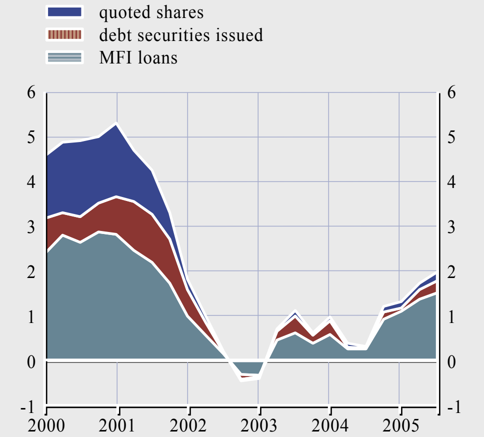
In addition, there is some evidence of an incipient recovery in lending by EU banks to non-financial corporates, especially the smaller ones. Notably, borrowing by SMEs had reportedly been sluggish in 2002 and 2003, but started to recover in 2004 and early 2005. Looking once again at developments in the euro area (see Chart 5), loans by MFIs became an increasingly important source of funds for non-financial corporates in 2004, a development that contacts with banks confirm for the first half of 2005 in at least some EU countries. So far, the rate of corporates' borrowing growth and the share of MFIs lending in it is still far from the heights of the 1999-2000. Nonetheless, if prolonged, the increase in corporates' borrowing in 2004-05 could provide banks with a desirable differentiation of sources of income. In fact, in the persistently low interest rate environment of the last few years, banks have likely faced constraints in supporting their operating income in mature markets, which may have led them to increase their exposures to potentially more risky assets or geographical regions. In this light, a recovery in borrowing by the corporate sector would be beneficial to banks. For instance, this development could reduce banks' dependence on lending to households for housing purposes, especially for banks in those areas where house prices have increased substantially over the last few years.

Developments in non-financial corporates' borrowing in the EU-13 have been characterised by a similar recovery in borrowing volumes.

Despite the signs of a potential recovery in borrowing by corporates, evidence of a sustained improvement in this source of banks' income is still elusive. For instance, looking at

Chart 5 Breakdown of the real annual rate of growth of external financing to non-financial corporations in the euro area

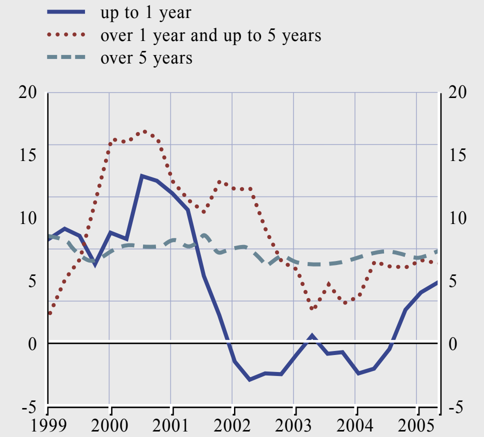
(Q1 2000-Q2 2005, % per annum)



Source: ECB
Note: The annual rate of growth is defined as the difference between the actual annual rate and the growth rate of nominal GDP.

Chart 6 Annual growth of loans to non-financial corporations in the euro area for selected maturities

(Q1 1999-Q2 2005, % per annum)



Source: ECB
Note: Data are based on MFI loan transactions.

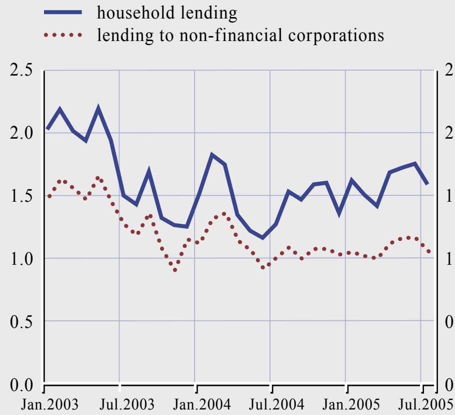
euro area corporates, the latter appear to still be reluctant to increase their borrowing for long periods of time. The largest part of the increase in borrowing volumes is for maturities of no more than five years, irrespective of the potential benefits of locking in generally low interest rates at present (see Chart 6).

Considering information on loans to customers from banks' balance sheets in the consolidated banking data, the aggregate figure for domestic banks in the EU-25 indicates a very small fall in lending as a share of total assets, a development which is broadly similar between the euro area and the EU-13 at the aggregate level and across size groups (see Statistical Annex, Tables 3, 7 and 11). This fall can partly be ascribed to the more rapid increase in EU banks' assets (see Statistical Annex, Table 1), but it is remarkable that most of the drop in loans as a share of total assets took place in the group of large banks. For the EU-13, the aggregated information may conceal the different lending patterns between the ten newest and the three older EU members, where lending in the former group is reportedly buoyant. However, the absence of large banks in these ten newest EU members, on a consolidated basis, conceals this information at the EU-13 level. For the euro area, the developments in lending by large banks may more closely represent a broad-based containment in lending by banks, in relation to their accumulation of total assets.

Turning to developments in banks' margins, as already announced, they remained narrow, thus counterbalancing the effect of lending growth on net interest income. As it can be gauged from the various sources of information presented in this section, the broad margin erosion in the EU, and especially in the euro area, derived from a flatting of yield curves, low absolute levels of interest rates and increased competition among banks. Unconsolidated MFI data show how lending margins in the euro area fluctuated rather sharply in the first half of 2004, stabilised around the middle of the range in the second half of the year, but fell again in the first part of 2005 (see Chart 7). In fact, banks have reportedly experienced strong competition in their lending activities, especially to households,

Chart 7 Lending margin of euro area MFIs

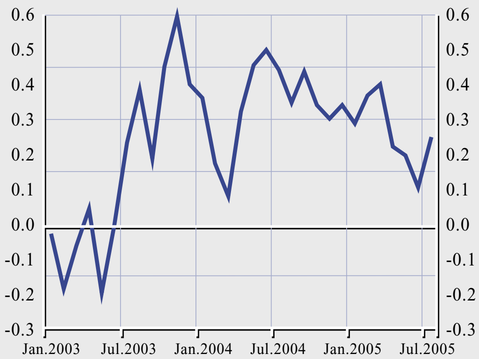
(Jan. 2003-Jul. 2005, percentage points)



Source: ECB
Note: The weighted lending margins are the difference between the interest rate on new lending and the interest swap rate, where the two rates have corresponding maturities.

Chart 8 Deposit margin of euro area MFIs

(Jan. 2003-Jul. 2005, percentage points)



Source: ECB
Note: The weighted deposit margins are the difference between the interest rate swap rate and the deposit rate, where the two rates have corresponding maturities.

thus facing significant constraints in increasing their lending margins.

Developments in deposit margins have also been rather unfavourable for EU banks. As banks have increased their lending, they have competed for depositors' funds, but with the household sector increasingly burdened by housing debt, deposits have not been amply available for banks. Some evidence of the scarcity of funding from deposits for the euro area MFIs can be found in the declining margins for most of 2004 and a further narrowing in the first half of 2005 (see Chart 8). The information from banks' balance sheets confirms the scarcity of customer deposits in the EU: as a share of total assets, deposits by customers fell in the EU-25 and especially in the EU-13, while remaining broadly unchanged in the euro area (see Statistical Annex, Tables 3, 7 and 11).

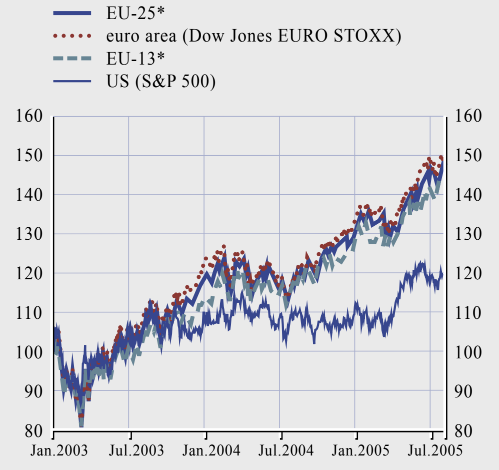
Looking forward, banks' ability to sustain or improve their net interest income may be impaired by the incipient flattening of yield curves, as long-term interest rates have remained low or have fallen. This type of yield curves would reduce revenues from the traditional maturity transformation by banks. Moreover, the ongoing increase in lending by banks, as also indicated by the sustained demand for consumer and housing loans found in the latest euro area bank lending survey (July 2005), coupled with strong competition among banks, could negatively affect the quality of banks' loan portfolios. Such a deterioration in banks' asset quality could increase banks' exposure to credit risk.

Turning to net non-interest income, its increase as a share of total income is the mirror image of the change in net interest income (see Statistical Annex, Tables 2, 6 and 10). Among the components of non-interest income, fees and commissions increased in 2004 in terms of total assets in the euro area and the EU-25 and in terms of total income in all three regions, and made a positive contribution to net non-interest income of EU banks. However, profits from trading operations in securities and in foreign exchange (referred to as "trading and forex results" from now on) fell as a share of total assets in both the euro area and the EU-13 for domestic banks, but marginally increased as a share of total income in the EU-13. While fees and commissions may also be earned by banks on their more traditional lending activities, trading and forex results are more directly correlated with securities market conditions. Global developments in these markets in 2004 and the first half of 2005 were positive overall (see Chart 9), thus offering an opportunity for positive results in banks' net non-interest income, although generally low volatility may have reduced the scope for trading activity.

Globally low long-term yields have preserved the value of banks' fixed-income portfolios, while improving or stabilising GDP growth expectations have contributed to increasing stock markets values in the EU. Consensus forecasts for the euro area, arguably one of the weakest regions in the EU in terms of macroeconomic developments, stabilised in 2004 and a number of indicators have improved more recently, although they remain at a still relatively low

Chart 9 Stock prices in the EU and the US

(Jan. 2003-Sep. 2005, index; Jan. 2003=100)



Source: BSC.
Note: (*) Market capitalisation weighted averages.

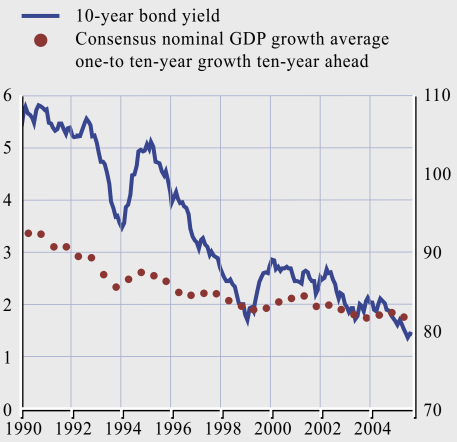
level (Chart 10). Looking forward, however, should an improvement in macroeconomic fundamentals produce an unexpected upturn in long-term interest rates, banks could suffer losses on their fixed income portfolios.

COST EFFICIENCY MARGINALLY UP

Cost containment, which contributed positively to banks' profitability in 2002 and 2003, abated in 2004 (see Chart 1). Total costs as a share of total assets fell in the EU both for the euro area and the EU-13, although the positive result may be partly attributable to the rapid increase in assets (see Statistical Annex, Tables 2, 6 and 10). Nonetheless, the cost-to-income ratios slightly fell in all regions, while remaining considerably lower in the EU-13 than in the euro area. In the euro area, cost-to-income ratios fell for all size and ownership groups, except for small banks where they remained broadly unchanged. Cost containment among large banks produced a reduction in the asset share of banks with cost-to-income ratios higher than 80% in both the euro area and the EU-13 for most domestic bank groups.[6] However, foreign banks in both regions and medium-sized banks in the EU-13 experienced an increase in this indicator. Given the consolidation of EU-owned foreign banks in the domestic banking sector of their parent company, the deterioration in the indicator for foreign banks may have been largely driven by developments in non-EU foreign banks. For medium-sized banks, the development could be at least partly attributable to changes in the largest countries in the group.

Chart 10 Euro area ten-year bond yield and consensus ten-year nominal GDP growth expectations

(Jan. 1990-Aug. 2005, %)



Sources: ECB and Consensus Economics.

When considering the different components of total costs, the share of staff costs increased in the EU-25 and the euro area, while for the EU-13 it fell for large domestic banks. This left banks relying on administrative costs (in the euro area) and other costs to reduce their total costs, hinting that the scope for future increases in cost efficiency may be limited. As banks have relied on cost-cutting to support their profitability over the last few years, the exhaustion of this profitability lever may put pressure on banks' results in the future.

PROVISIONS FELL, BUT THE COVERAGE RATIO INCREASED

In 2004, general economic conditions in the EU were supportive of banks' activities: insolvencies in the household and corporate sectors were low, deterioration in banks' asset quality was marginal, loan losses declined, and significant write-offs or write-downs of credit overdue in the previous years in at least a few EU countries reduced the impact of credit risk on the resulting banks' balance sheets.

On account of such a benign credit environment, the flow and to some extent also the stock of provisions have fallen in the EU-25, the euro area and the EU-13 at an aggregate level between 2003 and 2004 (see Chart 11, and in the Statistical Annex, Tables 2, 6, and 10 for the flow of provisions, and Tables 3, 7 and 11 for the stock). In addition, in at least one large

[6] The threshold of 80% is a rule of thumb to set apart relatively cost-efficient banks from those whose capacity to match cost with income generation is rather weak.

euro area country, the level of provisions fell, normalising after the high provisioning activity in 2002, when insolvency figures had risen sharply. There, the decline in provisioning was especially pronounced for large banks financing internationally active large companies, which benefited from buoyant external demand in 2004.

In 2005, an additional factor expected to affect the flow of provisions is the move of stock market listed banks, and, in some countries, all banks, to IFRS. Although it is still premature to make a precise assessment of the impact on the level of provisions, and this impact is likely to be different across the EU depending on the accounting regime adopted until 2004, two broad observations can already be made: (1) provisioning requirements under IFRS are likely to be more restrictive, as there must be objective evidence of impairment that is supported by cash flows before an impairment provision can be created; and (2) the "funds for general banking risks" no longer exist.[7] The impact of these accounting changes on provisions calls for careful monitoring in 2005, as it remains important that capital buffers remain at a prudent level, especially at this potentially delicate juncture in the credit cycle.

Indeed, looking forward, the overall low level of provisions in the EU, although currently justified by the benign credit risk environment, may be problematic: should credit quality deteriorate, possibly on account of a rise in long-term interest rates or an increase in unemployment, the adequacy of provisions could be called into question. As in at least a few EU countries there is a perception that credit quality, mostly in the household sector, could weaken in the near future, the ability of the present stock of provisions to provide a sufficient buffer may be tested.[8]

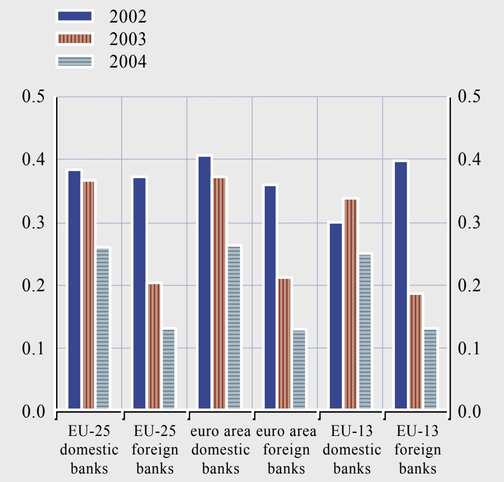
Looking in more detail at the consolidated banking data for 2003-04, the flow of provisions

[7] A special feature in the forthcoming ECB Financial Stability Review (December 2005) will discuss in more detail the impact of IFRS on the main indicators of the condition of banks.

[8] In most EU countries, banks are in general not allowed to provision in anticipation of the credit cycle, and provisioning levels are mostly based on historical asset impairment. Nonetheless, the present low levels of provisions have reduced banks' buffers in the event of a downturn in the credit cycle.

Chart 11 EU-25, euro area and EU-13 banks' provisions (flows)

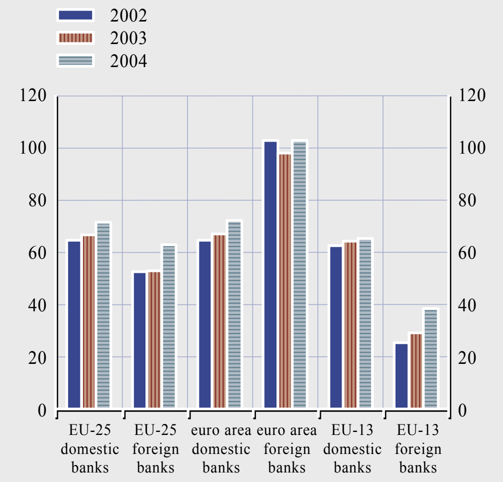
(% of total assets)



Source: BSC.

Chart 12 EU-25, euro area and EU-13 banks' coverage ratio

(total provisions as a share of non-performing and doubtful assets, %)



Source: BSC.

for large banks fell more rapidly than in other size groups, although the fall in the provisioning flow for small banks was a close second (see Statistical Annex, Tables 2, 6 and 10). Foreign banks reduced their flow of provisions quite markedly, although by less than large domestic banks. As for the stock of provisions as a share of total assets, it increased for small and medium-sized banks in the euro area (see Statistical Annex, Tables 3, 7 and 11), but it decreased or remained broadly unchanged for all other bank.

In contrast to the changes in the flow of provisions, however, the changes in asset quality and the coverage ratio, i.e. the ratio of provisioning stocks to total non-performing and doubtful assets, paint a more positive picture (see Chart 12).

For the group of domestic banks, in both the euro area and the EU-13 the share of non-performing and doubtful assets in both total loans and advances and own funds decreased between 2003 and 2004 (see Statistical Annex, Tables 4, 8 and 12). In addition, the coverage ratio increased in both regions. For small banks, the coverage ratio did not change in the euro area but fell rather sharply in the EU-13.

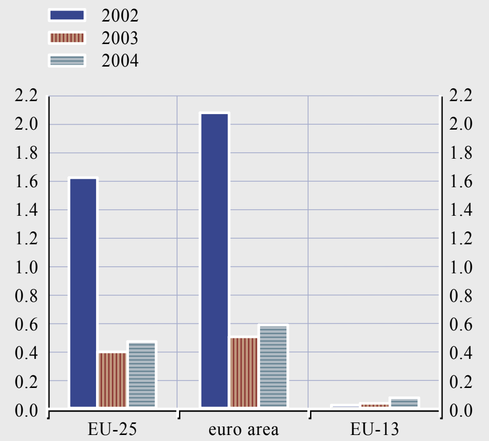
Looking forward, the positive developments in coverage ratios in most groups of banks, although certainly positive in the short-term, should be viewed with caution over the longer-term, as the quality of banks asset portfolios is in general highly sensitive to changes in the phase of the credit cycle. Should there be a sudden deterioration of credit quality, coverage ratios would fall, in which case the absolute amount of the flow and the stock of provisions would return to being a more meaningful indicator.

SOLVENCY BROADLY UNCHANGED

EU banks' capital adequacy remained broadly unchanged in 2004. The overall solvency ratio slightly fell for both foreign banks and the aggregate group of domestic banks in both the euro area and the EU-13. Nonetheless, for the same group of banks, the Tier 1 ratio remained broadly constant, both in the euro area and

Chart 13 Asset share of EU-25, euro area and EU-13 banks with overall solvency ratios below 9%

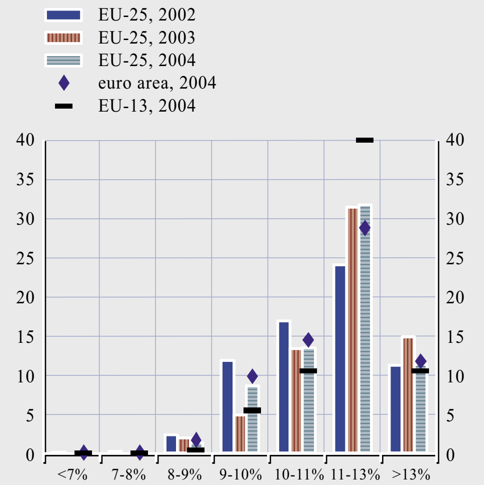
(% of total assets)



Source: BSC.

Chart 14 Frequency distribution of overall solvency ratios for EU-25 banks, at the country level

(all domestic banks, % of risk-weighted assets)



Source: BSC.

the EU-13 (see Statistical Annex, Tables 5, 9 and 13). This is consistent with the indicators for large banks based on published accounting data for the first half of 2005 (see Box 1). In the consolidated banking data, the solvency indicators slightly deteriorated only for domestic large banks in both regions, foreign banks in the euro area and small banks in the EU-13.

Because of the impact of large banks on the aggregate indicators, the share of the total banking sector with an overall solvency ratio less than 9% slightly increased in both the euro area and the EU-13 (see Chart 13).

At the same time, over the period 2002-2004, the distribution of banks' overall solvency ratios, collected at the country level and not at the bank-specific level, shifted towards the higher brackets, although the increase was very modest (see Chart 14). The shape of the distribution of overall solvency ratios across the different brackets represented in Chart 14 was tighter for EU-13 banks than for euro area banks, and slightly more concentrated in the upper brackets for the EU-13.

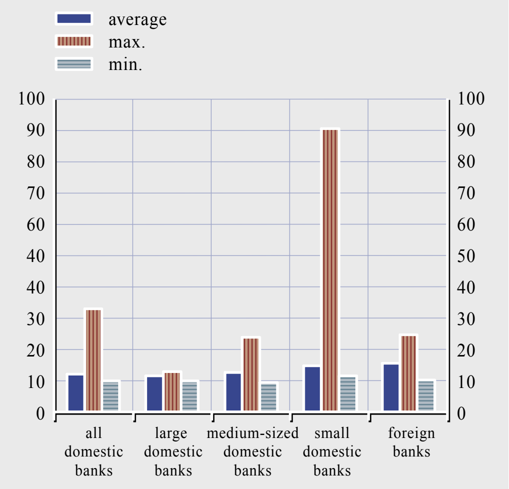
In the EU-25, differences across size and ownership groups at the country level rather than at the individual bank level indicate that the group of small banks has the largest range of variation in this indicator, although regulatory requirements make the variation in the minimum levels of this indicator very contained (see Chart 15).

Furthermore, using available data collected at the country rather than bank level, the dispersion of the overall solvency ratios in the EU-25, EU-13 and euro area increased in 2004, indicating that some pockets of fragility may be developing (see Chart 16).

Finally, developments in risk-weighted assets point to an improvement in banks' condition: for the group of domestic banks, risk-weighted assets as a share of total risk-adjusted assets fell in the EU-25, the euro area and the EU-13 (see Statistical Annex, Tables 5, 9 and 13). This was due to a decline in the risk-adjusted trading book assets. However, the risk-adjusted off-balance-sheet assets increased, possibly on account of a change in holdings of credit

Chart 15 EU-25 banks' overall solvency ratios: average, maximum and minimum, at the country level

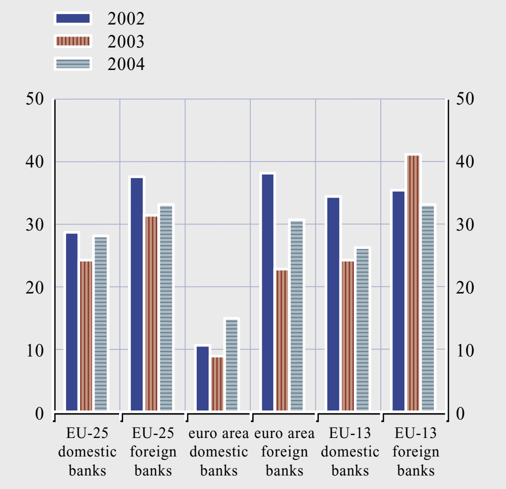
(2004, %)



Source:BSC.

Chart 16 Interquantile ranges of overall solvency ratios for EU-25, euro area and EU-13 banks, at the country level

(% of the averages)



Source: BSC.

derivatives, at least in the EU-13 (see Statistical Annex, Table 7).

DEVELOPMENTS IN LIQUIDITY WERE MIXED

There were mixed developments in EU banks' liquidity in 2004. On the assets side of banks' balance sheets, liquidity increased on the basis of the indicator covering the most liquid assets (with a minimal decline in the EU-13), but it declined in relation to the indicator for the least liquid assets (see Statistical Annex, Tables 3, 7 and 11, and Charts 17 and 18).[9]

This pattern was common among size and ownership groups in the three regions.

Given the present environment of very low interest rates by historical standards, the expectation of an upward shift in long-term interest rates may have caused banks to keep most of their funds only in the most liquid assets, such as cash and short-term government debt.

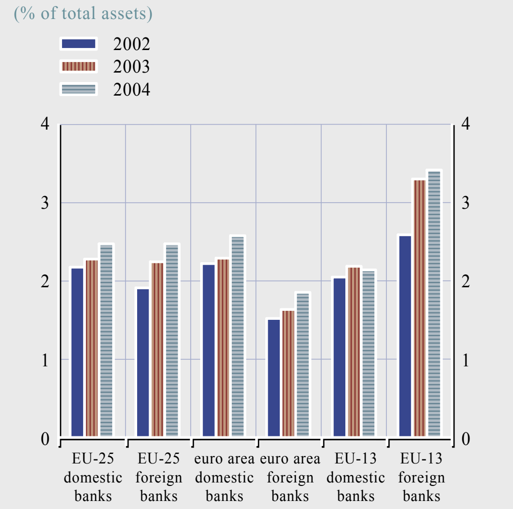
Turning to banks' liabilities side, banks reduced their reliance on the interbank market, as the amounts owed to credit institutions as a share of total assets fell for domestic banks in the EU-25 and in the euro area, although they increased in the EU-13 (see Statistical Annex, Tables 3, 7 and 11).

The divergence between the euro area and the EU-13 is partly reflected in how banks changed their holdings of customer deposits, which fell in the EU-13 and remained flat in the euro area.

Banks also increased their funding by stepping up their use of market instruments, such as debt certificates and to a lesser extent subordinated liabilities, both in the euro area and the EU-13. The use of market funding and the drop in deposits in some EU countries point to a tightening in bank liquidity conditions in those countries. Moreover, as market funding is more expensive for banks, it may negatively impact their profitability in the near future.

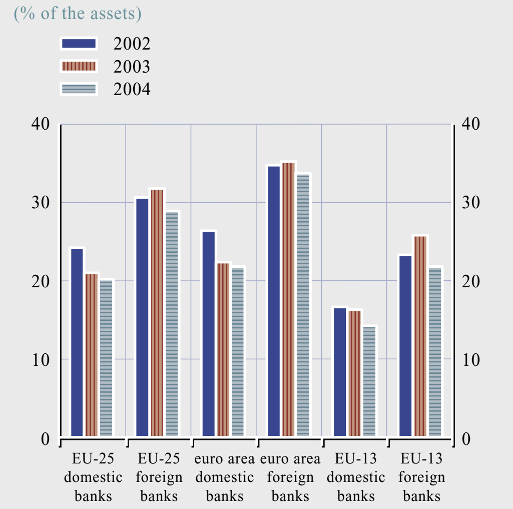
[9] The indicator for the most liquid set of assets, called "Liquid asset ratio 1" in the tables in the Statistical Annex, covers only cash and short-term government debt, as a share of total assets; the intermediate indicator "Liquid asset ratio 2" includes also loans to credit institutions, and the broader liquidity indicator "Liquid asset ratio 3" includes in addition longer-term debt securities issued by public bodies.

Chart 17 EU-25, euro area and EU-13 banks' liquid asset ratio 1



Source: BSC.
Note: Liquid asset ratio 1 includes cash and short-term government debt.

Chart 18 EU-25, euro area and EU-13 banks' liquid asset ratio 3



Source: BSC.
Note: Liquid asset ratio 3 includes cash and short-term government debt, loans to credits institutions and debt securities issued by public bodies.

III EU BANKS' RISK OUTLOOK

This section considers the risks facing the EU banking sectors in the period ahead. It should be emphasised that these risks are not highlighted with an aim of identifying the most probable outcome. The section instead aims to identify potential and plausible sources of downside risks, with regard to the likeliest outcome.

Against the background of a further and broad-based improvement in the financial performance of the EU banking sectors during 2004 and in the first half of 2005, which included many of the weakest-performing banks, the baseline assessment of the outlook for banks is broadly positive. Hence, over the near future, banks' condition looks in fact fairly robust in most EU countries. Nevertheless, over the medium or longer-term, banks' current resilience may be tested by currently latent vulnerabilities, some of which originate inside and others outside of the banking sector.

Regarding sources of risk and vulnerabilities internal to the banking sector, the improvement in EU banking sector profitability presented in Section 2 was associated with a substantial reduction in the number of corporate sector defaults and non-performing loans between 2002 and the first half of 2005 and the corresponding reduction by banks in almost all countries of their provisioning for loan losses. In an increasing number of cases, banks have reported that provisions reached all-time low levels. Going forward, the adequacy of low levels of provisioning will therefore rely on the viability of expectations that the credit quality of bank loan portfolios will continue to develop favourably, which in some countries could be questioned in the current phase of the credit cycle.

Banks' profitability in 2004 was only partly supported by further cost-cutting in the EU banking sectors, as the contribution of this factor abated. Nonetheless, banks' efforts to cut costs, as a share of total assets, reflect intensified competition among banks and, in some countries, difficulties in generating income from the core maturity transformation business in the low interest rate environment. Since provisioning and costs both have lower limits, in order to sustain profitability banks might face pressures to increasingly resort to raising non-interest income and possibly taking on greater risk.

A further complicating, albeit transitory, factor affecting the assessment of risks facing banks is the uncertainty surrounding the likely impact of the adoption of the IFRS accounting methodology on reported provisions. Preliminary information suggests that the effects have varied significantly across countries.

Regarding the sources of external risks and vulnerabilities in the operating environment of banks, ever-higher oil prices and persistently large global imbalances have remained of high importance. Banks are unlikely to be directly exposed to the oil market, but should the strength of oil prices persist, it could adversely affect the ability of the non-financial sectors to honour their liabilities to banks, thereby increasing banks' credit risk.

An unruly unwinding of global imbalances, if it were to materialise, could affect banks through several channels. Concerning banks' sources of income, a reversal in the currently ample global liquidity would reduce banks' profits deriving from large lending volumes and from fees and commissions associated with trading activity in financial markets. At the same time, banks' credit risk would likely increase, as the currently benign credit environment would deteriorate. Moreover, ample global liquidity has contributed – via the global quest for yield – to a compression of spreads across the credit spectrum to exceptionally low levels, possibly inducing mis-pricing of credit risk by banks. In addition, banks would also be affected through their exposure to market risk. An abrupt unwinding of global imbalances would likely be associated with heightened exchange rate and bond market volatility. While the direct exposures of EU banks to foreign exchange risks are likely to be limited, the risks posed by exchange rates could prove to be correlated with the credit risks of non-financial sectors – especially firms in the export sector and their suppliers such as SMEs. Finally, the tightness of credit spreads could represent a greater than normal market risk for banks.

To assess the possible impacts of these risks, this section provides an overall assessment of EU banks' household and corporate sector credit risk, interest rate, exchange rate and other market related risks, as well as banks' exposures to emerging markets, hedge funds and private equity funds.

OUTLOOK FOR CREDIT RISKS IS CURRENTLY BENIGN, BUT COULD BECOME LESS SO OVER TIME

BANKS' EXPOSURE TO THE HOUSEHOLD SECTOR CONTINUED TO INCREASE

As discussed in Section 2, a significant share of the lending portfolios of EU banks is accounted for by loans extended to households (unconsolidated data for the euro area suggest that lending to households represents roughly 36% of the total stock of lending by banks as of June 2005). Given that lending to the household sector has, for several years, been the most rapidly growing line of business for these banks, continued growth in exposures to the household sector counts as a potentially growing source of credit risk despite the generally higher quality of credit granted to households relative to the corporate sector.

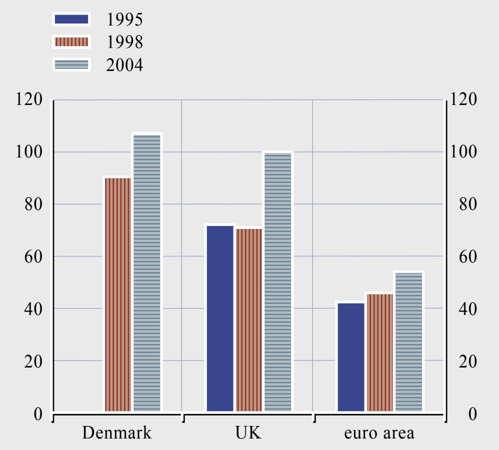
Reflecting favourable financing conditions, households continued to accumulate more debt in 2004 and in early 2005. In the euro area the household debt-to-GDP ratio recorded a further rise, to around 55.5 % in the first quarter of 2005 (see Chart 19). Given the buoyant growth of household borrowing in many of the non-euro area EU countries, the average level of household indebtedness in the EU is also likely to have increased in 2004 and the first half of 2005.

As household debt ratios rise, the vulnerability of households to any negative income or interest rate shocks should also rise. All else being equal, this means that adverse disturbances could have a greater impact on the non-performing loan rates of banks than in the past.

However, there are certain structural factors that could help to explain the increasing leverage of households over recent years. Low and stable inflation rates have contributed to lower interest rates, implying less uncertainty about income streams and lower debt-servicing burdens. Under these circumstances, and if they are expected to continue over time, households can take on more debt without necessarily incurring more risk. In addition, demographic factors and previously low owner-occupancy ratios could help to explain the strong demand for housing in some EU countries. Indeed, most of the rise in household indebtedness reflects strong mortgage financing growth.

Chart 19 Household debt ratios

(% of GDP)



Sources: ECB, Bank of England and Danmarks Nationalbank.

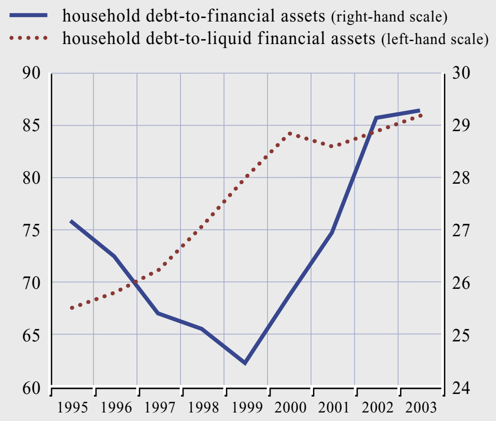
Together with the rapid growth in mortgage lending, house prices have risen substantially in many EU countries. In some countries there are concerns that valuations may have become stretched. Estimations for the euro area show that residential property prices could have increased by slightly more than 7% in 2004, but there were tentative signs of house price inflation slowing down somewhat during the first part of 2005. Due to the importance of mortgage lending as a revenue source for banks, developments in residential property prices have become an important factor in the assessment of risks to banking sector stability, warranting further close monitoring of the housing market.

While house prices could be vulnerable to correction in some countries, the impact of a potential fall in house prices on the credit quality of banks' asset portfolios would depend on the particular shock that triggered the downturn and the applied loan-to-value (LTV) ratios. Everything else being equal, falling house prices would erode the value of collateral (i.e. the residential property), but this would not necessarily have a substantial impact on the risk of default among borrowers. Since the average LTV ratios of the mortgage lending stock in the EU are still rather conservative, house prices would have to fall by a fairly large magnitude before credit quality was more seriously eroded.

In the unlikely materialisation of a macroeconomic shock causing both a rise in unemployment and falling house prices, the risk of default would rise in tandem with the erosion of the collateral value, thereby reducing credit quality more directly. However, the impact of a shock to income depends on the distribution of debt across categories of households facing different financial conditions. Available evidence at the EU level suggests that the bulk of household sector debt tends to be held by households belonging to the highest income categories. As these households have relatively large wealth buffers, they are likely to be in a better position to weather a deterioration of their financial situation. In those countries where household indebtedness is spread out to include also lower income households, however, the impact of falling house prices on households' loan servicing capacity could be more severe.

Chart 20 Ratio of household debt to financial assets and to liquid financial assets in the euro area

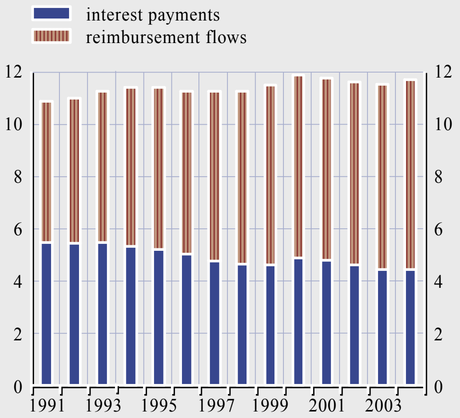
(1995-2003, %)



Source: ECB.

Chart 21 Total debt-servicing burden of the euro area household sector

(1991-2004, % of disposable income)



Source: ECB calculations.
Note: Data for 2004 are estimates.

Information available for the euro area suggests that the current household sector financial buffers should help households to absorb reasonably large adverse macroeconomic shocks. The ratio of debt to financial assets stabilised in 2003 at around 30% (see Chart 20). Moreover, the estimated total debt service burden of the household sector (repayment of principal and interest payment) has remained broadly stable since 2000, at around 10% of disposable income (see Chart 21).

Despite the currently benign credit conditions, the credit quality of households could suffer in the event of an abrupt upturn in long-term interest rates. However, the impact of a change in long-term interest rates on the sustainability of households' debt will depend notably on country-specific features of mortgage contracts, in particular the interest rate variability regime of the outstanding loans. Clearly, the impact on households could be more substantial in countries where variable rates are more common. In particular, across the EU, new borrowers would be more sensitive as a greater proportion of them are indebted at variable rates and as they have not yet amortised a large amount of their principal. Moreover, the maturity of mortgage loans is already generally high by historical standards, thus making it harder for household to adjust to a potential increase in the cost of their mortgage by extending their repayment period.

Over the past years, the mortgage lending market has been characterised by increased competition, to some degree spurred by the favourable risk-weighting of mortgage loans within the Basel II framework. In most EU countries, there has been a general tendency over the last few years towards granting higher LTV ratios. In an increasing number of countries, first-time buyers can borrow up to 100% of the value of the house, and sometimes even more, to finance additional costs (such as stamp duties, notary fees, etc.). This has gone together with an extension of the loan maturity, up to 30-35 years in some countries, so that the typical monthly instalment has remained broadly unchanged (usually granted up to 30% of household monthly income). While the monthly debt-service burden has not increased dramatically, the likelihood for the borrower of experiencing a payment difficulty over a longer repayment period with a slower loan amortisation has become higher.

In many countries competition among banks for mortgage borrowers has offset incentives to tighten credit standards. At the same time, banks have improved their risk management techniques to cope better with the increasingly complex risk transfer instruments they have used to shed part of their credit risks in the secondary market. The July 2005 Eurosystem bank lending survey suggests that some banks in the euro area could have started to tighten their credit standards as a response to a growing perception of risk, particularly in terms of worsening housing market prospects. Such tightening is typically achieved by more stringent collateral requirements, lower LTV ratios and larger margins on riskier loans. Against this background, there are some tentative signs that banks are beginning to consider the future prospects of the housing markets more negatively than households, although their prudent reaction through a tightening of credit standards may not be generalized across the euro area or the European Union.

Turning to the developments in unsecured consumer credit, outstanding amounts continued to rise at a brisk pace in some countries while the overall developments were more moderate. For example, data on the euro area show that the growth rate of consumer credit continued on a modest upward trend in the first quarter of 2005, with the stock of consumer loans and other credit as a proportion of total household loans standing at 13.5%. Intense competition among banks has contributed to a slight net easing of banks' credit standards for consumer credit, although this has been recently mitigated by an increased perception of risk related to required collateral and consumer creditworthiness.

Since households in financial distress tend to default on consumer credit before defaulting on mortgages, payment arrears are more likely to show first in the former category of loans. However, there are currently no indications of a systemic increase in payment disturbances and worsening consumer credit quality.

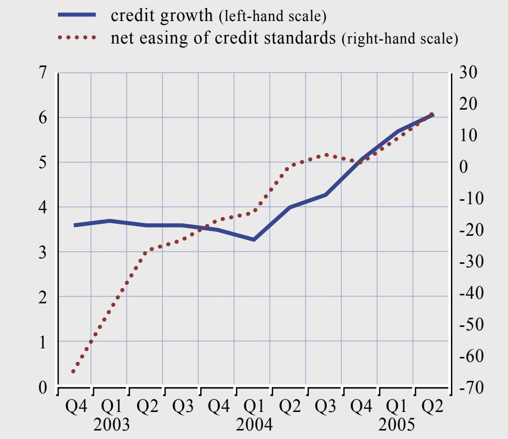
CORPORATE SECTOR CREDIT RISKS HAVE DECLINED

The quality of EU banks' corporate loan portfolios showed signs of improvement in 2004 and in early 2005. The main factors underlying this were the strength of corporate profitability and favourable financing conditions. Looking forward, downside risks to corporate credit quality may arise from a slower than expected economic recovery in some Member States due to weak domestic demand and persistently high oil prices, or from a possible turnaround in the credit cycle.

Concerns that sluggish corporate credit demand could hurt banks' profitability seem to have eased since mid-2004. This seemed to be particularly the case in the euro area countries. Bank lending to non-financial corporations picked up in several countries in the year up to mid-2005. As discussed in Section 2, data available for the euro area show that the annual growth of short-term MFI loans to non-financial corporations have increased, although from a low base (see Charts 5 and 22). Available evidence suggests that increasing financing needs for inventories, working capital, merger and acquisition activity, as well as leveraged buy-out activity, may have contributed to accelerating credit growth in the first half of 2005. However, weak fixed investment activity and the ongoing availability of internal funding sources due to improved corporate profitability continued to have a dampening effect on corporate credit demand. In many of the countries that joined the EU in May 2004, the growth of lending to non-financial corporations remained higher than in the euro area due to stronger economic growth.

Chart 22 Annual growth of euro area MFI loans to non-financial corporations and changes in credit standards

(Q4 2002-Q2 2005, % per annum and net percentages)



Source: ECB and Eurosystem bank lending survey.
Note: The net percentages in credit standards refer to the difference between the sum of percentages for 'eased somewhat' and 'eased considerably' and the sum of percentages for 'tightened somewhat' and 'tightened considerably'.

Banks continued to ease their credit standards for loans to enterprises in the first half of 2005, suggesting that supply-side factors might have also played a role in stronger loan growth. Banks may in fact be sufficiently reassured by the improvement in corporate credit quality to be willing to increase their lending to them. More bank-lending to corporates would allow banks to differentiate their sources of income away from households and would be beneficial for risk diversification purposes.

The July 2005 Eurosystem bank lending survey indicates that for the banks in the euro area, the relaxation of credit standards has been mainly the result of intensified competition. In the event of slower than expected economic growth, it cannot be excluded that the loosening of credit standards, combined with the low level of provisioning in several EU banking sectors, could leave some banks with a rather thin cushion against deteriorating credit quality. Moreover, some preliminary evidence of leverage in loans granted to the corporate sector could indicate a risk of faster deterioration in corporate credit quality in the event of a downturn in the credit cycle.

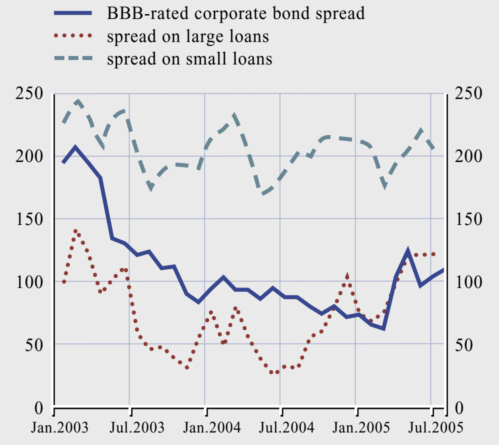
Compared with the situation at the time of the 2004 EU Banking Sector Stability Report, there are some tentative indications that risk perceptions of banks concerning SMEs might have started to improve in several countries. Country-level experiences suggest that the number of corporate insolvencies, which were mainly driven by developments in the SME sector for the EU as a whole, may have not risen further or may have even slightly decreased in some EU countries in the first half of 2005. This positive development, however, should be treated with caution as in some countries the decline took place from historically high levels. Banks in the euro area have reported that the recent easing of credit standards was extended also to SMEs, suggesting an increased willingness of banks to lend to smaller companies. However, developments in the pricing of small loans by banks, which can be used as a rough approximation of lending to SMEs, have been mixed in the first half of 2005. Whilst lending margins narrowed in the first months of the year, they have widened in the second quarter of 2005 and they have flattened out afterwards (see Chart 23).

Notwithstanding accelerating growth in credit to non-financial corporations since mid-2004, EU banks' aggregate exposures at risk are likely to have declined across most industries due to a continued decline of the median expected default frequencies (see Chart 24). Lending to those sectors which are vulnerable to further increases in oil prices is, however, still perceived relatively risky and could result in higher credit losses for banks with sizeable exposures to these sectors. Moreover, banks could be more generally affected by the high oil prices if they persisted and started to have a negative impact on general macroeconomic conditions.

As regards banks' exposures to the commercial real estate sector, significant differences continue to exist across EU banking sectors. In many countries, loans related to the commercial real estate sector do not account for a significant part of banks' loan portfolios. Experiences of those countries where banks have sizeable exposures to this sector have been diverse over

Chart 23 Euro area corporate bond and bank loan spreads

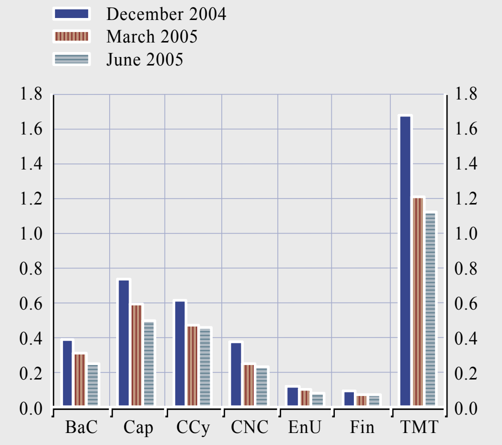
(Jan. 2003-Aug. 2005, basis points)



Source: ECB and Thomson Financial Datastream.
Note: Spread between the rate on loans to non-financial corporations with one up to five years initial rate fixation, below (small) and above (large) 1 EUR million, and the three-year government bond yield.

Chart 24 Expected default frequency for different sectors in the EU-25

(medians)



Source: Moody's KMV.
Note: The sectors are basic materials and construction (BaC), capital goods (Cap), consumer cyclicals (CCy), consumer non-cyclicals (CNC), energy and utilities (EnU), financial (Fin), and technology and telecommunications (TMT).

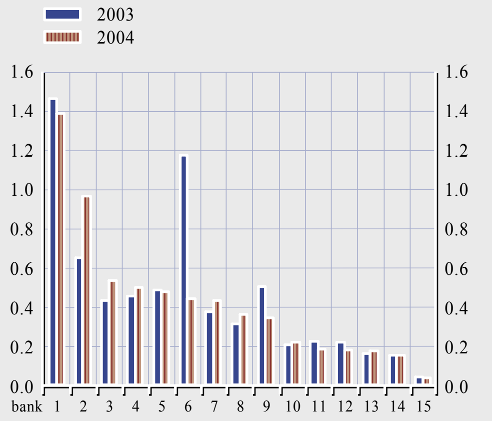
the past year. In at least one large country, risks continued to be relatively high due to falling rents and commercial real estate prices. In some countries, however, the risk perception with regards to this sector may have improved somewhat since mid-2004 due to a recovery of rental growth or relatively high pre-sale rates for offices.

A structural development in the area of commercial real estate financing is the rapidly expanding activity by specialised distressed loan investors in those markets where the number of non-performing assets has been high and economic growth subdued. The increasing activity in the market for distressed loans is to be welcomed from a market efficiency point of view since it will allow banks to offload high risk-weighted assets to investors who are specialised in pricing and restructuring such loans.

Finally, looking at the market indicators of corporate credit risk, developments have been mixed over the past year. After a continuous tightening in late 2004 and in early 2005, spreads on bonds issued by euro area non-financial corporations rose sharply in April and May, triggered by the credit event affecting the US automobile manufacturers. Corporate bond spreads have moderated somewhat since then, but remained slightly higher than in early 2005. Expected default frequencies of large euro area firms continued to decline in the first three months of the year, although the improvement appears to have stopped in the second quarter. Overall, there are no indications yet that the recent fluctuation in corporate bond spreads would reflect a permanent worsening of perceptions of corporate credit risk by market participants.

Chart 25 Interest rate Value at Risk (VaR) for selected large EU-25 banks

(% of Tier 1 capital)



Source: Financial disclosures of banks.

INTEREST RATE RISKS HAVE NOT MATERIALLY CHANGED

Banks may be exposed to interest rate risk either directly, via interest rate-sensitive positions in their trading and banking books, or indirectly through credit risk. Possible interest rate risk scenarios may include, on the one hand, a sudden upturn in long-term interest rates or, on the other hand, a protracted low interest rate environment associated with a flattening of yield curves.

Estimates of direct exposures to interest rate risk may be gauged by the relative size of capital requirements for traded debt instruments. Information available on interest rate Values at Risk (VaRs) for a sample of 15 large EU banks indicates that some large banks increased their exposure to interest rate risk in 2004, although others reduced their exposure to a significant extent (see Chart 25). Based on country-level information and financial disclosures of large banks, some banks might have further increased their risk-taking in the first half of 2005. It is important to stress, however, that the VaR values remain low relative to banks' capital or income.

Potential direct losses stemming from adverse changes in interest rates could also arise from interest-sensitive positions in the banking book. Given the lack of consistent information, it is difficult to gauge the relative importance of this type of risk exposure across EU banking sectors. Banks may be vulnerable to interest rate increases, however, in countries where fixed income portfolios account for a significant part of the banking book.

Available evidence suggests that indirect effects of potential interest rate increases materialising via credit risk may be more important for banks than the risk of direct losses.[10] Moreover, the risk of an increased correlation between interest rate and credit risk may also be considered as an important source of risk for banks. A possible sudden widening of credit spreads triggered by an increase in risk aversion or a significant negative credit event could affect banks through a rise in credit risk related to certain asset classes (such as corporate and emerging market-related loans), as well as an increase in trading book losses. Likewise, a tightening of global liquidity conditions associated with an increase in long-term interest rates would likely put pressure on banks' loan portfolios, as well as on their income depending on lending growth and trading activity. These losses would need however to be balanced against the benefit of increased income from the maturity transformation on new loan business.

While the gradual increase of long-term interest rates remains the main scenario, a more protracted period of low long-term yields and a flattening of yield curves cannot be excluded. Such an environment has a negative impact on banks' net interest income and could encourage banks to seek revenues from riskier activities, such as lending to emerging markets, or further ease their credit standards. Moreover, the low interest rate environment could lead to a persisting build-up of financial imbalances, for example through a rise in private sector indebtedness, which may have an impact on banks' credit risk with a significant time-lag.

DIRECT EXCHANGE RATE EXPOSURES REMAINED SMALL

Since the publication of the 2004 EU Banking Sector Stability Report, no significant change in the direct exposure of banks to exchange rate risk has been reported. Banks' open foreign exchange positions have in general remained low, both in absolute terms and as a share of regulatory own funds. The share of the banks' trading book own funds requirements for foreign exchange risk remained broadly unchanged in 2004 (see Statistical Annex, Tables 5, 9 and 13). These exposures are substantially smaller than the requirements for debt or equity instruments. Moreover, there is little evidence of currency mismatches between the assets and liabilities sides of banks' balance sheets.

Nevertheless, internationally active banks – in particular those from EU countries where loan growth has stabilised or declined and those with branches or subsidiaries in EU countries outside their domestic currency area, in the United States or in emerging markets – might not only be exposed to currency risk via unhedged currency mismatches, but also via the translation on the balance sheets of their branches or subsidiaries in currencies other than their domestic currency.

Banks can also be exposed to foreign exchange risk indirectly through changes in the competitiveness of non-financial firms or defaults on loans denominated in foreign currencies. So far, there has been little sign that the fluctuations of the EU countries' currencies have translated into balance sheet problems for firms. The latter types of indirect effects could materialise via repayment difficulties triggered by adverse currency movements in those countries where substantial lending in foreign currencies both to households and corporates has been encouraged by favourable interest rate differentials. Moreover, it cannot be ruled out

[10] See Box 12 in the June 2005 ECB Financial Stability Review.

that large exchange rate movements, possibly connected with a correction in the global imbalances and the associated adjustments in consumption in deficit countries, could become problematic for EU banks more generally.

EQUITY MARKET EXPOSURES INCREASED

Equity markets in almost all EU countries recorded strong gains in 2004 (see Chart 9). Subsequently, banks generally reported increased income both in fees and commissions and on trading activity, as already shown in Section 2. In some cases these revenue sources were able to more than offset lower income from the core maturity transformation business. The expanding trading activity contributed to an increase in banks' exposures to equity market risk as illustrated by the increase in the share of the banks' trading book own funds requirements for equity in both the euro area and the EU-13, raising by more than two percentage points, to 23.9% in 2004, in the EU-25 (see Statistical Annex, Table 5).

EXPOSURES TO HEDGE FUNDS AND PRIVATE EQUITY FUNDS REMAINED SMALL, BUT MAY STILL WARRANT MONITORING

Since early 2003, inflows into hedge funds have grown at a rapid pace and this continued in 2004 and in early 2005, although with some moderation in the second quarter of 2005 due to weaker hedge fund performance. The CSFB/Tremont Hedge Fund Index recorded an increase of only 1.34% in the first six months of 2005, even though this was still better than returns in the US and world equity markets over the same period (-0.81% on the S&P 500; -0.4% on the MSCI $ World Index). In particular, certain credit strategies suffered in May 2005 after the downgrades of General Motors and Ford to sub-investment-grade category. As fixed income strategies are usually associated with higher levels of leverage, largely provided by banks, some banks could have faced higher risks on their trading and lending exposures to hedge funds during this period.

Given the increased presence of hedge funds in the markets for complex relative value instruments, it cannot be excluded that the risks of further volatility in the credit market could expose banks to future losses from their activities with hedge funds.

For banks, the biggest challenge remains the interaction of market, credit and liquidity risks when larger price movements or unexpected changes in correlations force hedge funds to liquidate their leveraged positions. In such cases, leveraged market risk faced by hedge funds leads to credit risk for banks, which could be further exacerbated by the drying-up of liquidity in affected markets. Moreover, the so-called "crowding" of hedge fund trades could further magnify the risks for banks, especially if proprietary trading desks of banks use similar hedge fund-like strategies.

A BSC survey on EU-25 banks' exposures to hedge funds found that the exposures to hedge funds varied significantly across countries.[11] In most countries exposures seemed negligible and/or were mainly in the form of direct equity investments. Moreover, the existing direct exposures are generally not large in relation to banks' balance sheets or in comparison to similar exposures undertaken by US peers. This reflects the fact that the global prime brokerage market is largely dominated by US financial institutions. Regarding recent developments, in most countries banks did not see any systematic increase in risk-taking by their hedge fund counterparts. Nevertheless, the opacity of the hedge funds industry affects banks' ability to aggregate their exposures to hedge funds, so that in those few cases where EU banks have exposures to hedge funds, monitoring may nonetheless be called for.

A more recent development concerning new entrants in financial markets is represented

[11] "Large EU banks' exposures to hedge funds", ECB, 2005, *forthcoming*.

by the increase in size and activity of private equity funds. These funds are usually involved in venture capital operations, and they have recently taken advantage of the improved corporate sector conditions and the availability of funding at favourable rates by banks. As banks have on the other hand met difficulties in sustaining their more traditional business activities, they may have increased their lending to private equity funds, although detailed information is not available. Given the opacity of the private equity industry, and the usual high leverage on the loans secured by these funds, increasing banks' exposures to them, although reportedly still low and not common to most EU banks, represent a new source of risk that requires further monitoring.

EMERGING MARKET EXPOSURES INCREASED FURTHER

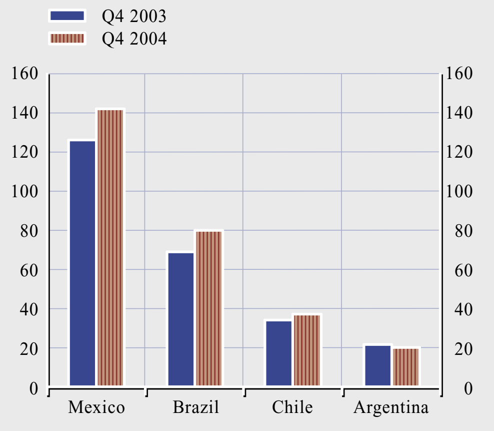
Increasing commodity prices and the low interest rate environment contributed positively to the economic performance of many emerging markets in 2004. Consequently, data available for the EU countries show that banks further increased their exposures to these countries (see Charts 26 and 27).

Regarding the individual regions of the world, banks have further increased their already relatively large exposures to Latin America where most large economies, with the exception of Argentina, have seen further inflows. The exposures have risen particularly strongly in Mexico and Brazil due to their rather benign economic performance, which may have eased earlier concerns of risks arising from investments in the local bond markets. At the same time, completed negotiations on the restructuring of the defaulted debt in Argentina mitigated one major source of uncertainty in the market. Nonetheless, international investors, including some euro area banks, were forced to accept a significant discount on their claims on debt issued by the Republic of Argentina.

Exposures of euro area banks to selected markets in Asia have also increased further since the 2004 EU Banking Sector Stability Report, with the exception of a moderate reduction in exposures to Thailand.

Chart 26 International exposures of EU-25 banks to Latin American economies

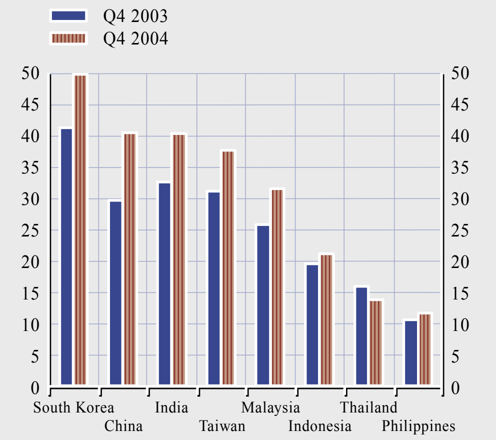
(USD billions)



Source: Bank for International Settlements (BIS).
Note: Data only for BIS reporting banks.

Chart 27 International exposures of EU-25 banks to Asian economies

(USD billions)



Source: BIS
Note: Data only for BIS reporting banks.

IV. EU BANKS' OUTLOOK ON THE BASIS OF MARKET INDICATORS

MARKET INDICATORS CONTINUE TO SUGGEST A POSITIVE SHORT-TERM OUTLOOK

Throughout much of 2004 and the first half of 2005, financial market indicators suggested that market participants remained optimistic and confident about the robustness of EU banks and the banking industry's future earnings prospects. Therefore, for the time being, the markets seem convinced that the EU banks' shock absorption capacity remains adequate, despite the continued decline in loan loss provisioning reported in 2004.

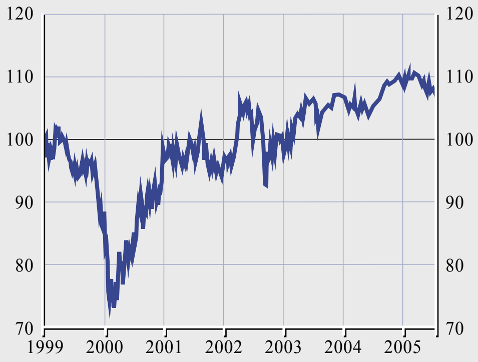
In the euro area, the ratio of banks' share prices to the general stock market index rose overall between late 2003 and mid-2005, reaching new heights (see Chart 28). This suggests that market participants may have become more optimistic about the future earnings prospects of banks and/or that they perceived the risks facing the banking industry to have declined. On the performance side, EU banks' profitability improved significantly in 2004 and in the first half of 2005, (see Section 2), possibly creating expectations of further growth. On the vulnerabilities side, EU banks' outlook for risks in the near future has also improved (see Section 3). In particular, the substantial reduction in the number of corporate sector defaults and more in general the fall in non-performing assets is legitimising market participants' perception of the risks lying ahead.

Supporting the hypothesis of positive future earnings prospects, in the second quarter of 2005 the earnings-per-share forecasts for large banks in the euro area showed a continued very positive outlook. This assessment should be qualified, however, as the forecasts made a year earlier turned out to be slightly over-optimistic (see Chart 29).

The fact that the euro area banks' earnings grew faster than their stock prices in 2004 and in the first half of 2005 – despite a further increase in the equity index in the same period – is reflected by the moderate decline in the price/earnings ratio (see Chart 30). Growth in banks' earnings

Chart 28 Ratio of bank stock market index to the overall market index for the euro area

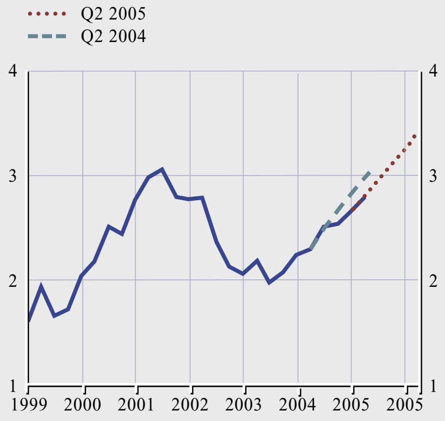
(Jan. 1999-Sep. 2005, index: Jan. 1999 = 100)



Source: Thomson Financial Datastream.

Chart 29 Large euro area banks' earnings per share (EPS) and 12-month-ahead forecasts

(Q1 1999-Q2 2006, weighted average, %)



Sources: Thomson Financial Datastream, I/B/E/S and ECB calculations.

in this period was still mainly driven by cost-efficiency improvements, lower provisions for loan losses and a further increase in lending to households, as highlighted in Section 2.

Turning to market-based assessments of the resilience of the EU banking sector, the median distance-to-default (DD) for the set of large EU banks improved more or less continuously from early 2004 onwards (see Chart 31).[12] For banks belonging to the lowest percentile, notwithstanding some deterioration in early 2004, there was a notable improvement in the DD, which rose to levels not reached since early 1999. The behaviour of this indicator is in line with the improvement in EU banks' performance and the overall balance of risks facing the banking sector discussed in the other parts of this report. The rise in the DDs, which started in early 2004, is possibly being driven by an increase in the market value of banks' assets, which was not matched by an increase in the asset price volatility, a measure that is derived using option-pricing theory. According to this information, the EU banking sector is in a comfortable position to honour its debt obligations, and continues to move away from the possibility of future financial distress.

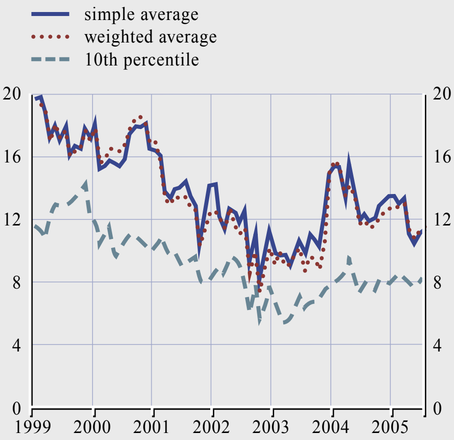
Credit default swap spreads on the debt of EU financial institutions declined nearly continuously in 2004. However, these spreads widened in the second quarter of 2005 (see Chart 32) and the deterioration appeared to have been driven by the downgrading of General Motors and Ford to sub-investment grade status. Investors' concerns about possible exposures of large EU banks to the troubled automobile makers proved to be limited, although by no means negligible, as witnessed by the widening of EU banks' subordinated debt spreads to over 50 basis points. These spreads subsequently reverted back towards the low levels seen at the beginning of 2005.

Spreads between the offers to buy and sell protection on European non-financial

[12] The distance to default measures the distance between the market value of a firm's (a bank's) assets and the point at which it is insolvent. For more details, see Box 14 entitled "Distance to default as a measure of banking sector fragility" in the June 2005 ECB Financial Stability Review.

Chart 30 Price/earnings ratios for large euro area banks

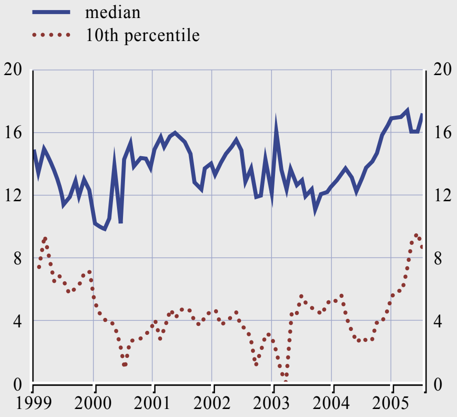
(Jan. 1999-Jul. 2005, %)



Sources: Thomson Financial Datastream and ECB calculations.

Chart 31 Distance to default for large EU-25 banks

(Jan. 1999-Jun. 2005)



Sources: Moody's KMV and ECB calculations.
Note: An increase in the distance to default reflects an improving assessment.

institutions' debt suffered a similar widening in the second quarter of 2005, apparently triggered by the above-mentioned downgrades. Although the widening of spreads was rather short-lived, spreads moved back to levels slightly higher than those seen in the first quarter of 2005. Spreads on both senior and subordinated debt issued by financial institutions remained lower than spreads on non-financial institutions' debt throughout 2004, which reflects confidence among investors regarding the resilience and robustness of the European financial sector.

A comparison between the message that emerges from the forward-looking financial market indicators, on the one hand, and the view that is provided by the discussion of risks in Section 3 of this report, on the other hand, shows an agreement in the positive assessment of banks' condition at present. Looking forward, the market view points towards a baseline scenario of continuing EU banking sector stability in the near future.

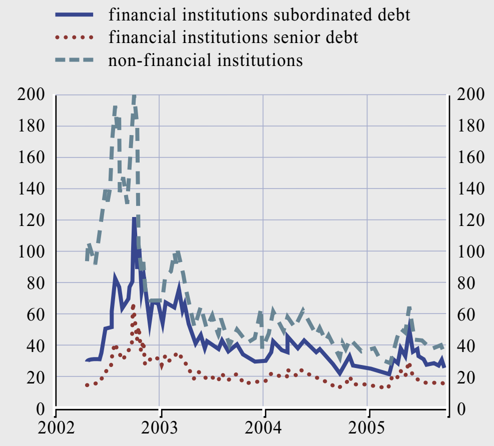
However, while the market indicators analysed in this section necessarily focus on the most likely outcome, a full risk assessment must extend to the analysis of the distribution of risks around this baseline scenario. On the negative side, given the uncertainty regarding the near-term macroeconomic outlook, particularly due to the very high oil prices, the continuing imbalances in the global financial system, as well as the increasing indebtedness of the household sectors in most EU countries, the vulnerabilities arising from the low level of provisioning by EU banks could materialise in a scenario where worsened credit conditions would affect banks more markedly. On the positive side, higher profitability has increased banks' resilience in the short-term, and EU banks have improved their risk management techniques, thus raising their ability to cope with complex risk transfer instruments that could shelter them from credit losses.

THE IMPROVEMENT IN CREDIT RATINGS DECELERATED IN LATE 2004 AND EARLY 2005

According to the three major rating agencies, the average credit quality of EU banks improved

Chart 32 European financial and non-financial institutions' credit default swaps

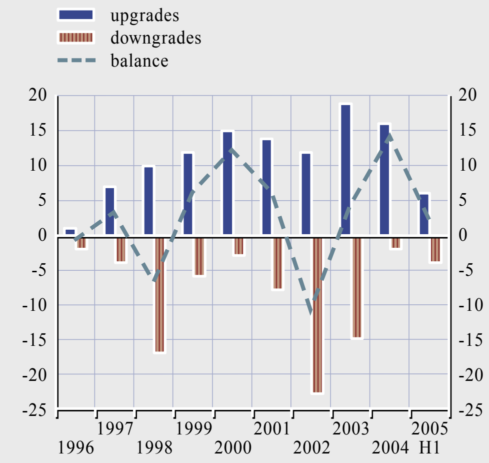
(May 2002-Sep. 2005, basis points, five-year maturity)



Source: JP Morgan Chase & Co.
Note: European financial institutions and non-financial institutions are defined according to JP Morgan Chase & Co. definitions.

Chart 33 Western European banking sector's rating downgrades, upgrades and balance

(1996-H1 2005, number)



Source: Moody's.
Note: Western European corresponds to the Moody's definition.

further in 2004 and in the first half of 2005, albeit at a decelerating rate. For the set of western European banks monitored by Moody's, the latter reports a significant decrease in the upgrade-to-downgrade ratio from 4 in 2004 to 0.5 in the first semester of 2005, indicating that until June, the number of downgrades was twice as much as the one of upgrades (see Chart 33, which illustrates annual figures). Moderate economic growth and increasing competition were seen as the main factors behind the slowdown in the upward migration rate from mid-2004. The still positive assessment of the credit quality of banks was, on the other hand, supported by the strength of banks' earnings growth in 2004 and the first half of 2005, as well as some signs of an accelerating pace of cross-border consolidation in the EU banking sector.

The largest EU banks' ratings remained stable during the second quarter of 2005. There remains little upside potential for the long-term ratings of these banks, however, as the majority are now rated in the "AA" range. Most upgrades affected banks rated within the range of "A" to "B+", while among banks with a rating of "A" or higher there were no upgrades.

V. OVERALL ASSESSMENT

EU banks' financial condition improved in 2004 and the first half of 2005, continuing the positive developments recorded in 2003. Profitability increased for the full spectrum of banks, as well as in those national banking sectors that had substantially underperformed EU averages in 2002 and 2003. However, interest income, both as a share of total income and of total assets, continued to fall in 2004, as it did in 2003. Notwithstanding sustained growth in lending to households, mostly for housing purposes, and an incipient recovery in lending to the corporate sector, including SMEs, banks suffered from margin erosion. In fact, banks experienced increased competition from their peers in granting loans, especially to households, which contributed to persistently narrow lending margins.

While EU banks at least partially continued to exploit the benefits to profitability that can be reaped from cost-cutting, banks' profitability increased mostly on account of reduced provisions, in terms of flows of new provisions throughout the EU and in terms of stocks in a more differentiated pattern across different types of EU banks. Given the contemporaneous improvement in asset quality, however, the coverage ratio has increased.

Overall, with regard to the outlook for EU banks over the near future, broadly positive short-term indicators of banks' condition suggest that, notwithstanding some country-differences, the EU banking sectors have benefited from generally benign credit and liquidity conditions. At the same time, taking a longer-term view to banks' resilience, some risks remain, some of which are internal to the banking sectors, while others are external. Concerning the first set of risks, banks have found it increasingly difficult to increase or maintain their interest income and their interest margins in mature markets given the low interest rate environment and the strong competition from their peers to secure sustained lending growth. As a result, banks may have loosened their credit standards, possibly increasing their future exposure to credit risk, or could have searched for alternative, possibly riskier sources of income. Moreover, should the present flattening or inverting of yield curves continue, banks' ability to sustain their income through the regular transformation of liquidity would be dented. A second risk internal to the banking sectors is the currently very low levels of provisions in historical terms. Although the coverage ratio has increased among EU banks, current provisioning levels may leave banks exposed to material losses in the event of a significant deterioration in credit quality.

With regard to the vulnerabilities external to the banking sector, while at present very benign credit and liquidity conditions persist, high and rising oil prices and the persistently large global imbalances figure among the most prominent sources of risk. Although banks are unlikely to be directly exposed to the oil market, the strength of oil prices, if protracted, could contribute to a deterioration in the credit cycle and impair the repayment capability of banks' non-financial borrowers. The deterioration in corporate credit quality could also dampen the tentative recovery currently under way in corporates' borrowing volumes, which has allowed for a welcome differentiation in banks' sources of income in 2004 and the first half of 2005. Moreover, should high oil prices affect the general macroeconomic conditions, households' credit quality could also deteriorate. As EU households' indebteness has increased over the last few years thanks to generally favourable credit conditions, a downturn in households' credit quality could have relevant effects for banks. Nonetheless, the likelihood of the materialisation of a worsening in general macroeconomic conditions and a fall in house prices sufficient to significantly affect households' credit quality is still considered rather remote.

Concerning large global imbalances, should an unruly unwinding materialise, the ensuing contraction in ample, global liquidity could affect banks in several ways. First, it could reduce banks' profits deriving from large lending volumes and from fees and commissions associated with trading activity in financial markets. Banks' credit risk would also likely increase, as the currently benign credit environment would deteriorate. Second, ample global liquidity has contributed – via the global quest for yield – to a compression of spreads across the credit spectrum to exceptionally low levels, which may have made banks' pricing of credit risk less accurate. Third, banks would also be affected through their exposure to market risk. An abrupt unwinding of global imbalances would likely be associated with heightened exchange rate and bond market volatility. While the direct exposures of EU banks to foreign exchange risks are likely to be limited, the risks posed by exchange rates could prove to be correlated with the credit risks of non-financial sectors – especially firms in the export sector and their suppliers such as SMEs. Finally, the tightness of credit spreads could represent a greater than normal market risk for banks.

Looking forward, market indicators motivate a broadly positive assessment of the current risk and profitability outlook for EU banks, which is in line with the other data presented in this report. Such conditions are likely to extend into the near future, but looking further ahead some risks may still materialise. In this light, while the market indicators analysed here focus on the most likely outcome, an overall risk assessment should emphasise the most disruptive, although plausible, outcome in terms of the distribution of risks around this baseline scenario. Overall, on the negative side, the risks associated with the uncertainty regarding the near-term macroeconomic outlook, not least because of very high oil prices, as well as the continuing global financial imbalances, increasing household indebtedness and low provisions by EU banks, could materialise in a deterioration in credit conditions. On the positive side, over the last few years banks have improved their risk management techniques, thus raising their ability to cope with increasingly complex risk transfer instruments. These instruments may shelter banks from at least part of the losses deriving from a deterioration in credit quality.

To sum up, the current financial condition of EU banks is broadly satisfactory and no specific factors can be identified that would trigger the materialisation of the more negative scenario. Despite the overall positive assessment over the near future, in the medium or long-term, the combination of increased loan growth and lower provisioning levels may leave banks more exposed to credit risk and a sudden deterioration in the currently benign credit and liquidity environment.

STATISTICAL ANNEX

Box 1

DATA ON EU BANKS

The macro-prudential analysis conducted by the Banking Supervision Committee (BSC) is based on the pooling of relevant aggregated information. The key set of data for this analysis is the consolidated banking data provided by the member organisations of the BSC. These data include detailed information on bank profitability, balance sheets and solvency and cover nearly 100% of the EU banking sector. The data contain information on EU banks divided into three size groups (small, medium and large). In addition, they provide information on foreign-controlled institutions active in EU countries.

This box summarises the key definitions used in tables 1-17 in the Statistical Annex and describes some of the most important changes in the data collection in 2005 from the one conducted in 2004.[1]

Key definitions for domestic banks

Consolidation

In order to provide a fully consolidated view of risks, the EU authorities report cross-border and cross-sector consolidated data on domestically controlled banks. In the cross-border consolidation, data on branches and subsidiaries located outside the domestic market (from the reporting country's point of view) are included in the data reported by the parent. In the cross-sector consolidation, branches and subsidiaries of banks that can be classified as other financial institutions are included. The definition of other financial institutions excludes insurance companies.

Size groups

Large domestic banks are defined as banks with total assets greater than 0.5% of the total consolidated assets of EU banks; medium-sized banks have total assets between 0.5% and 0.005%; and banks with total assets of less than 0.005% are considered small. The thresholds in terms of absolute amounts are defined using the total assets of the banking sector available from the data collection run in the preceding year. In the 2005 collection, the thresholds were computed using the total assets from the 2004 data collection of EUR23,801,306 million. This figure comprises total assets of domestic banks and non-EU foreign branches and subsidiaries in the first fifteen EU Member States (EU-15) at end-2003. The figure is comparable to the one used in the 2004 EU Banking Sector Stability Report in relation to the sample population (domestic and foreign banks), but it is smaller because it is not affected by double-counting.[2] Finally, only assets of EU-15 banks at end-2003 have been used for the computation of the thresholds, as data collected in 2004 from the ten countries that joined the EU in 2004 were on a solo basis; given the high rate of foreign ownership of banks in these new member countries, especially by banks in the EU-15, their banks' assets are already largely consolidated in the data of the parent banks in the EU-15.

[1] See the EU Banking Sector Stability Report, ECB, November 2004.

[2] The reference data used for the 2004 report comprised assets of domestic banks and all foreign branches and subsidiaries, although branches and subsidiaries from any EU-15 country were already consolidated in the domestic banking sector of the other EU-15 countries where the parent bank was headquartered.

Key definitions for foreign banks

Foreign banks are defined as subsidiaries and branches that are controlled by either an EU or a non-EU parent that is "foreign" from the reporting country's point of view. The data for these institutions are excluded from the definition of the domestic banking sector and are aggregated under the heading "foreign banks" in the following tables. A separate analysis for foreign banks is justified by their large share of the domestic banking sector in some EU countries.

Key definitions for all banks

For some items in the tables presenting the consolidated banking data, a separation between domestic and foreign banks is not available. For these items, which mostly refer to solvency indicators, the category "all banks" which includes all domestic and foreign banks is reported.

Differences in the data between the 2004 and 2005 Banking Sector Stability Reports

Differences in EU membership
In the sub-groups of foreign banks, due to the entry of ten new members to the EU in 2004, some banks that had been reported as foreign and owned by a non-EU bank in the 2004 data collection became foreign and owned by an EU bank afterwards. Nonetheless, given the aggregation of all foreign banks in one class in the following tables, the change does not affect the aggregate data there.

Changes in size groups
Owing to the change in the level of the thresholds for the definition of large, medium and small banks, some banks that were reported as belonging to one size group in the 2004 data collection have shifted to the next one due to the faster/slower growth of their assets relative to total EU assets. Such shifts have, however, had a limited impact on the aggregate EU data.

Differences in coverage
Some member countries reported data on different sets of banks in the 2004 and 2005 issues of the EU Banking Sector Stability Report. In Greece, data on non-performing assets and provisions for foreign branches were not included in the 2004 report, whereas they are in the 2005 report. For Cyprus, in both reports data exclude the operations of international banking units and cooperative credit institutions, but they will be included in the 2006 report. For Germany, data for domestic banks in the 2004 report include both domestic and foreign owned banks, while for the 2005 report the set of domestic banks does not include foreign banks. For the Netherlands, in both the 2004 and 2005 reports data on asset quality cover only large banks.

Differences in definitions of specific data items
No major differences were introduced in the definition of the consolidated banking data collected by the BSC for the 2005 data collection. Some minor differences with the 2004 EU Banking Stability Report were introduced due to the refinement in the definition of selected items for the computation of the solvency indicators. In the banking book, "general provisions"

is now composed of general and statistical provisions; innovative capital instruments and hybrid capital are now included among the items that compose banking book own funds. In the trading book's own funds used under the Capital Adequacy Directive (CAD) to cover market risk, the definition contained in CAD Annex V paragraph 2 has been adopted. This change affects the definition of Tier 3, although the quantitative impact has been modest. As regards asset quality indicators, the caveats mentioned in the 2004 report remain valid for the 2005 report: these data should be interpreted with caution owing to large differences between national definitions of both impaired assets (non-performing and doubtful assets) and provisions.

Country-level tables and aggregation

Although the EU Banking Sector Stability Reports aim to analyse banking sector developments at the aggregate EU level or in relevant subsets of countries, additional information at the country level is provided in the Statistical Annex for reference. When analysing the data presented in these tables, and especially when attempting a comparison across countries, it should be borne in mind that the country-level indicators reflect differences in coverage and in definitions; in addition, differences in the banking sector structures across the EU should be taken into consideration.[3] Finally, country-level information presented in tables 14-17 may differ from the one published in individual country's reports due to differences in reporting populations.[4] Using the consolidated banking data presented in tables 1-13, two sets of country-level tables are produced: the first one (tables 14 and 15), including only domestic banks, and the second one (tables 16 and 17), including both domestic and foreign banks operating in each EU-25 country. Tables 14 and 15[5] present a disaggregated view of the data used in the computation of the averages for the EU-25, the euro area and the EU-13 reported in tables 1-13. Such averages are calculated by computing the indicators in two ways, depending on whether the indicator represents a number of institutions in the reporting population or a ratio. In the first case, the country-level indicators are simply summed up to obtain the EU-25/euro area/EU-13 total. In the second case, for each ratio, the numerator of the aggregate indicator is obtained by summing up the numerators of the corresponding country-level indicator, and the denominator likewise. This procedure ensures that country-level information is properly weighted in the computation of aggregate indicators.

The country-level data in tables 16 and 17 are presented for the group "all banks", i.e. both domestic and foreign banks in each country. For this reason, they are affected by double-counting if a cross-country aggregation is attempted, and are also not directly comparable with the data presented in tables 1-13. Nonetheless, given the extensive foreign ownership of the banks operating in some EU Member States, tables 16-17 offer a more realistic picture of country-level banking developments for these countries.

[3] See, for instance, the 'Report on EU banking structures' (ECB, 2005).

[4] For instance, for Portugal tables 14-17 include institutions with head-offices located in Madeira, or whose activities are exclusively based on Madeira's off-shore status and/or carrying over their activity mostly with non-residents and non-deposit taking credit institutions. These institutions are not included in the Banco de Portogal's publications on the banking sector.

[5] Data for Luxembourg are not provided in tables 14 and 15 for confidentiality reasons, as they would mostly reflect developments in one large bank.

Table 1 EU banking sector structure (2004)

	EU-25	*Change from 2003*	euro area	*Change from 2003*	EU-13	*Change from 2003*
Number of credit institutions						
Stand-alone credit institutions	5,562	*-230*	4,102	*-219*	1,460	*-11*
Banking groups	552	*-18*	458	*-35*	94	*17*
Credit institutions	6,105	*-270*	4,551	*-259*	1,554	*-11*
Domestic credit institutions	4,934	*-243*	3,681	*-234*	1,253	*-9*
Foreign-controlled subsidiaries and branches	1,171	*-27*	870	*-25*	301	*-2*
Total assets of credit institutions in the sample (end-2004, EUR billions)						
Domestic credit institutions	24,604	*7.3*	18,963	*5.9*	5,641	*12.1*
of which (%):						
Large	*71.9*	*2.3*	69.4	*2.5*	80.6	*1.0*
Medium-sized	*24.5*	*-1.8*	26.5	*-2.0*	17.8	*-0.9*
Small	*3.6*	*-0.5*	4.2	*-0.6*	1.7	*-0.1*
Foreign-controlled subsidiaries and branches	4,382	*13.3*	2,936	*8.7*	1,446	*24.1*

Source: BSC.
Note: Changes from 2003: for the number of institutions, they are in absolute numbers; for total assets, in percentages; for the size distribution breakdown of total assets, in percentage points.

Table 2 EU-25 banks' profitability and efficiency (2004)

	All domestic banks	Change from 2003	Large domestic banks	Change from 2003	Medium domestic banks	Change from 2003	Small domestic banks	Change from 2003	Foreign banks	Change from 2003
Income (% of total assets)										
Net interest income	1.31	-0.08	1.12	-0.10	1.69	0.01	2.55	-0.01	1.07	-0.08
Interest receivable	3.69	-0.29	3.44	-0.30	4.28	-0.17	4.57	-0.23	3.96	-0.25
Interest payable	2.37	-0.20	2.32	-0.21	2.59	-0.18	2.02	-0.21	2.89	-0.16
Net non-interest income	1.01	-0.01	1.04	-0.02	0.87	0.03	1.31	0.00	0.91	-0.02
Fees and commissions (net)	0.65	0.01	0.65	0.00	0.63	0.04	0.94	0.08	0.65	0.02
Trading and forex results	0.19	-0.01	0.23	-0.02	0.06	0.00	0.08	-0.02	0.21	0.01
Other operating income (net)	0.17	0.00	0.16	0.00	0.18	0.00	0.29	-0.06	0.04	-0.05
Total income	2.32	-0.09	2.16	-0.12	2.56	0.04	3.86	-0.01	1.98	-0.10
Expenditure structure (% of total assets)										
Staff costs	0.85	-0.04	0.81	-0.06	0.87	0.01	1.51	0.02	0.64	-0.05
Administrative costs	0.43	-0.02	0.40	-0.02	0.47	-0.01	0.92	-0.01	0.40	-0.04
Other	0.10	-0.01	0.08	-0.01	0.13	-0.01	0.26	-0.02	0.14	-0.01
Total expenses	1.38	-0.08	1.28	-0.09	1.47	-0.01	2.69	-0.01	1.18	-0.10
Profitability (% of total assets)										
Operating profits	0.94	-0.01	0.88	-0.03	1.09	0.05	1.17	0.00	0.80	0.00
Specific provisions	0.26	-0.10	0.20	-0.12	0.41	-0.04	0.37	-0.10	0.14	-0.06
Funds for general banking risk	0.00	0.00	0.00	-0.01	0.02	0.01	0.02	0.00	-0.01	-0.02
Extraordinary items (net)	0.00	0.00	-0.02	0.00	0.06	0.01	0.02	-0.05	0.02	-0.01
Tax charges	0.20	0.01	0.19	0.02	0.21	0.01	0.25	-0.01	0.14	0.00
Profits (before tax and extraord. items)	0.70	0.11	0.70	0.11	0.68	0.10	0.78	0.11	0.67	0.08
Profits (after tax and extraord. items) (ROA)	0.50	0.09	0.49	0.09	0.53	0.09	0.55	0.07	0.56	0.07
Return on equity										
Profits (after tax and extraord. items) (% Tier 1) (ROE)	12.21	2.25	13.75	2.77	10.24	1.48	7.01	0.90	11.70	1.57
Income structure (% of total income)										
Net interest income	56.58	-1.36	51.92	-1.47	66.09	-0.84	66.04	-0.14	54.14	-1.31
Net non-interest income	43.42	1.36	48.08	1.47	33.91	0.84	33.96	0.14	45.86	1.31
Fees and commissions (net)	28.10	1.42	29.89	1.38	24.47	1.11	24.28	2.11	32.90	2.62
Trading and forex results	8.02	-0.17	10.75	-0.35	2.54	-0.02	2.15	-0.41	10.69	0.94
Other operating income (net)	7.30	0.12	7.44	0.44	6.90	-0.24	7.53	-1.55	2.27	-2.24
Expenditure structure (% of total costs)										
Staff costs	61.54	0.42	62.92	0.06	59.46	0.95	56.12	0.94	54.36	-0.05
Administrative costs	31.40	0.02	30.93	0.34	31.81	-0.61	34.32	-0.13	33.82	-0.16
Other	7.06	-0.45	6.15	-0.39	8.72	-0.34	9.56	-0.81	11.85	0.23
Efficiency										
Cost-to-income ratio (% of total income)	59.42	-1.02	59.28	-0.91	57.48	-1.32	69.80	-0.02	59.52	-1.98
Asset share of banks with cost-to-income ratio over 80%	4.63	-3.01	4.39	-3.85	4.24	-0.91	12.06	-1.32	23.09	4.95

Source: BSC.
Note: Changes from 2003 are in percentage points.

Table 3 EU-25 banks' balance sheet and off-balance sheet items (2004)

	All domestic banks	*Change from 2003*	Large domestic banks	*Change from 2003*	Medium domestic banks	*Change from 2003*	Small domestic banks	*Change from 2003*	Foreign banks	*Change from 2003*
Assets (% of total assets)										
Cash and balances	1.19	*-0.07*	1.10	*-0.01*	1.36	*-0.20*	1.98	*-0.05*	1.00	*0.05*
Short-term government debt	1.67	*0.36*	1.40	*0.28*	2.12	*0.67*	3.16	*0.17*	1.85	*0.15*
Loans to credit institutions	14.98	*-0.51*	15.50	*-0.64*	13.77	*-0.38*	12.97	*-0.23*	23.47	*-2.87*
Debt securities	17.98	*-0.27*	19.76	*-0.05*	13.42	*-1.44*	13.23	*-0.13*	15.39	*1.03*
Debt securities (public bodies)	5.95	*1.15*	6.70	*1.50*	4.58	*0.14*	2.26	*1.09*	4.43	*-0.01*
Debt securities (other borrowers)	7.10	*-6.43*	8.06	*-6.13*	5.24	*-6.79*	3.44	*-10.64*	7.76	*0.58*
Loans to costumers	50.74	*-0.01*	47.34	*-0.08*	59.73	*1.15*	57.58	*0.55*	44.88	*-0.07*
Shares and participating interest	3.43	*0.01*	3.24	*0.03*	3.78	*-0.05*	4.91	*0.37*	3.30	*0.00*
Tangible and intangible asssets	1.62	*-0.05*	1.65	*-0.09*	1.47	*0.03*	2.12	*0.02*	1.22	*-0.05*
Other assets	8.64	*0.69*	10.36	*0.63*	4.50	*0.39*	2.47	*-0.01*	9.23	*2.12*
Liquidity										
Liquid asset ratio 1 (cash and short-term government debt)	2.50	*0.20*	2.15	*0.20*	3.16	*0.34*	4.92	*0.08*	2.49	*0.23*
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	17.48	*-0.31*	17.65	*-0.43*	16.93	*-0.05*	17.90	*-0.15*	25.96	*-2.77*
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	20.39	*-0.95*	20.73	*-0.99*	19.63	*-1.05*	18.72	*-0.27*	29.32	*-2.79*
Liabilities (% of total assets)										
Amounts owed to credit institutions	19.60	*-0.48*	21.13	*-0.41*	16.15	*-1.04*	12.70	*-1.42*	36.05	*-2.23*
Amounts owed to customers	41.72	-0.50	38.68	*-0.07*	47.00	*-0.83*	66.54	*1.58*	31.82	*0.02*
Debt certificates	21.19	*0.47*	21.45	*0.20*	22.67	*0.96*	5.91	*0.44*	12.70	*0.77*
Accruals and other liabilities	9.30	*0.54*	11.11	*0.57*	4.79	*0.02*	3.79	*-0.34*	11.81	*1.87*
Funds for general banking risk	0.14	*-0.01*	0.12	*-0.03*	0.18	*0.04*	0.19	*0.01*	0.14	*-0.04*
Provisions for liabilities and charges	1.16	*-0.02*	1.04	*-0.09*	1.55	*0.19*	1.00	*0.01*	0.60	*-0.04*
Subordinated liabilities	1.85	*0.02*	1.88	*-0.08*	1.96	*0.30*	0.63	*-0.09*	1.34	*-0.07*
Equity	4.14	*-0.08*	3.71	*-0.17*	4.86	*0.25*	7.87	*0.15*	5.04	*-0.18*
Other liabilities	0.48	*0.02*	0.51	*0.00*	0.46	*0.09*	0.10	*0.02*	0.12	*-0.03*
Profit or loss for the financial year	0.42	*0.05*	0.34	*0.07*	0.52	*0.08*	1.50	*-0.37*	0.48	*0.01*
Selected off-balance-sheet items (% of total assets)										
Credit lines	15.28	*1.03*	17.86	*0.99*	9.30	*0.62*	4.51	*-0.99*	14.94	*-0.82*
Guarantees and other commitments	5.58	*-1.00*	5.04	*-1.60*	7.15	*0.53*	5.57	*0.30*	11.07	*5.44*
Derivatives	6.72	*-0.51*	6.77	*-3.08*	7.15	*4.74*	1.12	*0.89*	34.57	*10.51*

Source: BSC.

Note: Changes from 2003 are in percentage points. Concerning the item "debt securities", some countries provided information only on the total amount and not on the split between the two sub-items, i.e. "issued by public bodies" and "issued by other borrowers". Consequently, the sum of these two sub-items is smaller than the total amount.

Table 4 EU-25 banks' non-performing assets and provisioning (2004)

	All domestic banks	*Change from 2003*	Large domestic banks	*Change from 2003*	Medium domestic banks	*Change from 2003*	Small domestic banks	*Change from 2003*	Foreign banks	*Change from 2003*
Asset quality (% of loans and advances)										
Non-performing and doubtful asssets (gross)	2.73	*-0.40*	2.28	*-0.35*	3.35	*-0.45*	6.63	*0.09*	1.83	*-0.64*
Asset quality (% of own funds)										
Non-performing and doubtful assets (gross)	43.52	*-6.27*	40.05	*-5.82*	47.17	*-8.55*	59.43	*-0.53*	25.46	*-6.93*
Non-performing and doubtful assets (net)	12.25	*-4.03*	8.40	*-3.15*	16.88	*-6.52*	27.49	*-1.50*	9.56	*-5.96*
Provisioning (stock) (% of loans and advances)										
Total provisions	1.95	*-0.14*	1.80	*-0.16*	2.07	*-0.07*	3.55	*0.03*	1.15	*-0.18*
Provisioning (stock) (% of non-performing and doubtful assets)										
Total provisions	71.84	*4.54*	79.03	*4.19*	64.21	*5.90*	53.75	*-0.28*	63.52	*9.69*

Source: BSC.
Note: Changes from 2003 are in percentage points. Definitions of non-performing and doubtful assets differ between countries. Consequently, these data should be interpreted with caution.

Table 5 EU-25 banks' regulatory capital ratios and risk-adjusted items (2004)

	All domestic banks	*Change from 2003*	Large domestic banks	*Change from 2003*	Medium domestic banks	*Change from 2003*	Small domestic banks	*Change from 2003*	Foreign banks	*Change from 2003*
Overall solvency ratio	11.87	*-0.18*	11.42	*-0.37*	12.45	*0.20*	14.68	*0.34*	15.57	*-0.34*
Tier 1 ratio	8.46	*0.06*	7.94	*0.01*	8.96	*0.17*	12.77	*0.31*	12.40	*-0.84*
Risk-adjusted items (% of total risk-adjusted assets)										
Risk-weighted assets	82.32	*-0.33*	79.51	*-0.18*	87.27	*-0.54*	92.12	*-0.61*	76.91	*1.24*
Risk-weighted off-balance-sheet items	11.59	*0.48*	12.78	*0.39*	9.64	*0.59*	6.53	*0.71*	10.32	*-1.41*
Risk-adjusted trading book	6.09	*-0.15*	7.72	*-0.21*	3.09	*-0.05*	1.37	*-0.09*	13.13	*0.21*

	All banks	*Change from 2003*
Overall solvency ratio	12.25	*-0.16*
Tier 1 ratio	8.86	*0.01*
Distribution of overall solvency ratio		
Overall solvency ratio <7%	0.02	*-0.01*
Overall solvency ratio 7%-8%	0.02	*0.01*
Overall solvency ratio 8%-9%	1.96	*-0.96*
Overall solvency ratio 9%-10%	13.02	*5.72*
Overall solvency ratio 10%-11%	20.18	*0.10*
Overall solvency ratio 11%-13%	47.67	*0.36*
Overall solvency ratio >13%	17.13	*-5.22*
Overall solvency ratio below 9%		
Number of banks	102	*-31*
Asset share (% of total banking sector assets)	0.66	*0.28*

	All banks	*Change from 2003*
Risk-adjusted items (% of total risk-adjusted assets)		
Risk-weighted assets	81.77	*-0.23*
Risk-weighted off-balance-sheet items	11.46	*0.30*
Risk-adjusted trading book	6.81	*-0.06*
Composition of trading book own funds requirement (% of total trading book own funds requirement under CAD)		
Own funds requirement for traded debt instruments	39.64	*-1.11*
Own funds requirement for equities	23.91	*2.62*
Own funds requirement for foreign exchange risk	6.28	*-0.20*
Own funds requirement for other trading book items	30.22	*-1.33*

Source: BSC.
Note: Changes from 2003 are in percentage points.

Table 6 Euro area banks' profitability and efficiency (2004)

	All domestic banks	*Change from 2003*	Large domestic banks	*Change from 2003*	Medium domestic banks	*Change from 2003*	Small domestic banks	*Change from 2003*	Foreign banks	*Change from 2003*
Income (% of total assets)										
Net interest income	1.21	*-0.05*	0.95	*-0.06*	1.70	*0.02*	2.42	*0.00*	0.88	*-0.15*
Interest receivable	3.71	*-0.24*	3.47	*-0.21*	4.22	*-0.22*	4.41	*-0.24*	3.95	*-0.62*
Interest payable	2.50	*-0.18*	2.52	*-0.15*	2.53	*-0.25*	1.99	*-0.23*	3.06	*-0.46*
Net non-interest income	1.08	*-0.03*	1.16	*-0.06*	0.86	*0.03*	1.26	*-0.01*	0.97	*-0.02*
Fees and commissions (net)	0.61	*0.02*	0.61	*0.01*	0.57	*0.03*	0.88	*0.08*	0.58	*0.00*
Trading and forex results	0.19	*-0.01*	0.25	*-0.02*	0.05	*0.00*	0.04	*-0.01*	0.16	*-0.01*
Other operating income (net)	0.29	*-0.03*	0.30	*-0.05*	0.23	*0.01*	0.33	*-0.07*	0.23	*-0.01*
Total income	2.29	*-0.08*	2.11	*-0.12*	2.55	*0.05*	3.68	*-0.01*	1.85	*-0.17*
Expenditure structure (% of total assets)										
Staff costs	0.85	*-0.03*	0.80	*-0.05*	0.88	*0.01*	1.47	*0.02*	0.59	*-0.09*
Administrative costs	0.50	*-0.03*	0.48	*-0.03*	0.48	*-0.01*	0.90	*-0.01*	0.44	*-0.05*
Other	0.11	*-0.01*	0.10	*-0.01*	0.13	*0.00*	0.21	*-0.02*	0.10	*0.00*
Total expenses	1.46	*-0.07*	1.38	*-0.09*	1.49	*-0.01*	2.58	*-0.01*	1.13	*-0.14*
Profitability (% of total assets)										
Operating profits	0.83	*-0.01*	0.73	*-0.03*	1.06	*0.06*	1.09	*-0.01*	0.72	*-0.03*
Specific provisions	0.26	*-0.11*	0.18	*-0.13*	0.45	*-0.03*	0.37	*-0.10*	0.15	*-0.05*
Funds for general banking risk	0.00	*0.00*	0.00	*-0.01*	0.02	*0.01*	0.02	*0.00*	-0.01	*-0.03*
Extraordinary items (net)	0.00	*0.00*	-0.02	*0.01*	0.07	*0.01*	0.03	*-0.05*	0.04	*-0.01*
Tax charges	0.17	*0.01*	0.15	*0.02*	0.21	*0.01*	0.24	*-0.02*	0.13	*0.01*
Profits (before tax and extraord. items)	0.59	*0.12*	0.57	*0.13*	0.62	*0.09*	0.71	*0.10*	0.58	*0.04*
Profits (after tax and extraord. items) (ROA)	0.42	*0.11*	0.39	*0.12*	0.49	*0.09*	0.49	*0.06*	0.49	*0.02*
Return on equity										
Profits (after tax and extraord. items) (% Tier 1) (ROE)	10.54	*2.78*	11.68	*3.79*	9.50	*1.45*	6.52	*0.90*	10.46	*0.14*
Income structure (% of total income)										
Net interest income	52.77	*-0.47*	45.07	*-0.13*	66.50	*-0.54*	65.76	*0.15*	47.92	*-3.22*
Net non-interest income	47.23	*0.47*	54.93	*0.13*	33.50	*0.54*	34.24	*-0.15*	52.08	*3.22*
Fees and commissions (net)	26.50	*1.71*	28.73	*2.07*	22.21	*0.65*	24.03	*2.14*	31.32	*2.83*
Trading and forex results	8.25	*-0.22*	11.83	*-0.41*	2.12	*-0.20*	1.13	*-0.36*	8.40	*-0.05*
Other operating income (net)	12.49	*-1.02*	14.37	*-1.53*	9.17	*0.09*	9.09	*-1.93*	12.35	*0.45*
Expenditure structure (% of total costs)										
Staff costs	57.98	*0.69*	57.76	*0.55*	58.77	*0.97*	56.96	*0.86*	52.58	*-1.48*
Administrative costs	34.26	*-0.20*	34.99	*0.00*	32.32	*-0.73*	34.83	*-0.27*	38.97	*0.64*
Other	7.77	*-0.48*	7.25	*-0.55*	8.91	*-0.24*	8.21	*-0.58*	8.45	*0.84*
Efficiency										
Cost-to-income ratio (% of total income)	63.67	*-0.88*	65.34	*-0.70*	58.52	*-1.52*	70.31	*0.13*	61.08	*-1.76*
Asset share of banks with cost-to-income ratio over 80%	5.18	*-3.29*	5.91	*-3.51*	2.26	*-3.25*	11.51	*-1.26*	9.04	*2.27*

Source: BSC.
Note: Changes from 2003 are in percentage points.

Table 7 Euro area banks' balance sheet and off-balance sheet items (2004)

	All domestic banks	Change from 2003	Large domestic banks	Change from 2003	Medium domestic banks	Change from 2003	Small domestic banks	Change from 2003	Foreign banks	Change from 2003
Assets (% of total assets)										
Cash and balances	1.31	-0.08	1.24	0.00	1.41	-0.23	1.90	-0.11	0.88	-0.12
Short-term government debt	1.78	0.53	1.48	0.44	2.17	0.83	3.13	0.17	1.39	0.48
Loans to credit institutions	16.52	-0.69	17.70	-0.74	14.03	-1.05	12.64	-0.13	28.17	-1.95
Debt securities	20.50	-0.06	23.56	0.16	13.58	-1.47	13.54	-0.01	21.31	2.68
Debt securities (public bodies)	7.37	2.85	9.43	3.82	4.57	1.36	2.09	1.49	5.79	0.41
Debt securities (other borrowers)	7.62	-8.57	9.94	-7.95	4.30	-9.02	3.34	-11.57	12.29	1.74
Loans to costumers	48.39	-0.01	43.92	-0.16	58.68	1.56	57.25	0.35	37.90	-1.69
Shares and participating interest	3.41	-0.02	3.04	0.04	4.09	-0.11	5.38	0.46	2.78	-0.11
Tangible and intangible asssets	1.34	-0.03	1.24	-0.06	1.51	0.07	1.84	-0.02	0.88	-0.06
Other assets	7.11	0.59	8.30	0.47	4.70	0.61	2.50	0.00	7.02	1.26
Liquidity										
Liquid asset ratio 1 (cash and short-term government debt)	2.60	0.28	2.24	0.29	3.20	0.41	4.85	0.06	1.87	0.21
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	19.12	-0.41	19.94	-0.45	17.22	-0.63	17.48	-0.06	30.05	-1.74
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	22.13	-0.53	23.24	-0.67	19.84	-0.64	18.20	0.17	34.08	-1.40
Liabilities (% of total assets)										
Amounts owed to credit institutions	22.18	-0.79	24.50	-0.72	17.53	-1.52	13.09	-1.57	38.52	0.13
Amounts owed to customers	40.59	-0.06	36.92	0.03	46.22	0.66	65.75	1.71	30.15	-1.42
Debt certificates	21.36	0.42	21.99	0.57	22.04	-0.27	6.49	0.55	15.54	0.92
Accruals and other liabilities	7.91	0.31	9.39	0.31	4.67	-0.03	3.87	-0.37	8.53	1.26
Funds for general banking risk	0.17	-0.01	0.16	-0.03	0.21	0.04	0.19	0.02	0.19	-0.03
Provisions for liabilities and charges	1.34	0.02	1.19	-0.09	1.77	0.33	1.08	0.01	0.70	-0.09
Subordinated liabilities	1.91	0.06	1.95	-0.07	2.01	0.35	0.63	-0.11	1.51	-0.19
Equity	3.68	0.00	3.07	-0.07	4.68	0.32	7.44	0.15	4.30	-0.49
Other liabilities	0.44	0.03	0.44	0.00	0.49	0.09	0.11	0.02	0.18	-0.01
Profit or loss for the financial year	0.41	0.03	0.31	0.06	0.51	0.08	1.56	-0.41	0.46	-0.04
Selected off-balance-sheet items (% of total assets)										
Credit lines	12.67	0.83	14.72	0.91	8.66	0.34	4.06	-1.22	12.14	-0.38
Guarantees and other commitments	5.91	-0.11	5.26	-0.38	7.73	0.62	5.02	0.32	7.14	0.28
Derivatives	2.47	-6.43	3.33	-12.33	1.75	-0.15	0.32	0.09	8.45	-5.48

Source: BSC.

Note: Changes from 2003 are in percentage points. Concerning the item "debt securities", some countries provided information only on the total amount and not on the split between the two sub-items, i.e. "issued by public bodies" and "issued by other borrowers". Consequently, the sum of these two sub-items is smaller than the total amount.

Table 8 Euro area banks' non-performing assets and provisioning (2004)

	All domestic banks	*Change from 2003*	Large domestic banks	*Change from 2003*	Medium domestic banks	*Change from 2003*	Small domestic banks	*Change from 2003*	Foreign banks	*Change from 2003*
Asset quality (% of loans and advances)										
Non-performing and doubtful asssets (gross)	3.05	*-0.36*	2.56	*-0.29*	3.55	*-0.47*	7.00	*0.12*	1.24	*-0.19*
Asset quality (% of own funds)										
Non-performing and doubtful assets (gross)	49.23	*-6.49*	46.86	*-5.00*	49.65	*-10.56*	65.41	*-1.22*	16.41	*1.12*
Non-performing and doubtful assets (net)	13.34	*-4.60*	8.65	*-3.03*	17.54	*-8.19*	31.22	*-2.53*	-0.37	*1.07*
Provisioning (stock) (% of loans and advances)										
Total provisions	2.19	*-0.09*	2.09	*-0.12*	2.20	*-0.03*	3.64	*0.07*	1.25	*-0.17*
Provisioning (stock) (% of non-performing and doubtful assets)										
Total provisions	72.90	*5.09*	81.55	*4.05*	64.68	*7.01*	52.28	*0.23*	103.49	*4.47*

Source: BSC.
Note: Changes from 2003 are in percentage points. Definitions of non-performing and doubtful assets differ between countries. Consequently, these data should be interpreted with caution.

Table 9 Euro area banks' regulatory capital ratios and risk-adjusted items (2004)

	All domestic banks	*Change from 2003*	Large domestic banks	*Change from 2003*	Medium domestic banks	*Change from 2003*	Small domestic banks	*Change from 2003*	Foreign banks	*Change from 2003*
Overall solvency ratio	11.50	*-0.11*	10.92	*-0.30*	12.13	*0.20*	14.35	*0.29*	14.81	*-0.66*
Tier 1 ratio	8.42	*0.06*	7.92	*-0.01*	8.75	*0.18*	12.21	*0.17*	12.50	*-0.50*
Risk-adjusted items (% of total risk-adjusted assets)										
Risk-weighted assets	81.77	*-0.21*	78.15	*-0.25*	86.85	*-0.29*	92.69	*0.20*	79.50	*-0.43*
Risk-weighted off-balance-sheet items	12.23	*0.41*	13.86	*0.50*	10.15	*0.36*	5.94	*-0.16*	12.31	*-1.37*
Risk-adjusted trading book	6.01	*-0.20*	7.99	*-0.25*	3.00	*-0.07*	1.36	*-0.04*	8.20	*1.80*

	All banks	*Change from 2003*
Overall solvency ratio	11.78	*-0.14*
Tier 1 ratio	8.76	*0.02*
Distribution of overall solvency ratio		
Overall solvency ratio <7%	0.03	*0.01*
Overall solvency ratio 7%-8%	0.03	*0.02*
Overall solvency ratio 8%-9%	2.49	*-1.35*
Overall solvency ratio 9%-10%	14.80	*7.10*
Overall solvency ratio 10%-11%	21.74	*-0.90*
Overall solvency ratio 11%-13%	43.31	*-2.24*
Overall solvency ratio >13%	17.60	*-2.65*
Overall solvency ratio below 9%		
Number of banks	67	*-27*
Asset share (% of total banking sector assets)	0.76	*0.30*

	All banks	*Change from 2003*
Risk-adjusted items (% of total risk-adjusted assets)		
Risk-weighted assets	81.58	*-0.24*
Risk-weighted off-balance-sheet items	12.23	*0.27*
Risk-adjusted trading book	6.19	*-0.03*
Composition of trading book own funds requirement (% of total trading book own funds requirement under CAD)		
Own funds requirement for traded debt instruments	49.07	*0.49*
Own funds requirement for equities	9.96	*0.27*
Own funds requirement for foreign exchange risk	7.78	*-0.02*
Own funds requirement for other trading book items	33.19	*-0.74*

Source: BSC.
Note: Changes from 2003 are in percentage points.

Table 10 EU-13 banks' profitability and efficiency (2004)

	All	*Change*	Large	*Change*	Medium	*Change*	Small	*Change*	Foreign	*Change*
	domestic	*from*	domestic	*from*	domestic	*from*	domestic	*from*	banks	*from*
	banks	*2003*	banks	*2003*	banks	*2003*	banks	*2003*		*2003*
Assets (% of total assets)										
Net interest income	1.66	*-0.21*	1.62	*-0.23*	1.65	*-0.08*	3.65	*-0.22*	1.35	*0.00*
Interest receivable	3.61	*-0.47*	3.36	*-0.58*	4.55	*0.09*	5.95	*-0.28*	3.99	*0.39*
Interest payable	1.95	*-0.26*	1.74	*-0.35*	2.91	*0.17*	2.30	*-0.06*	2.63	*0.39*
Net non-interest income	0.75	*0.09*	0.70	*0.10*	0.93	*0.05*	1.75	*0.07*	0.82	*0.00*
Fees and commissions (net)	0.80	*-0.04*	0.76	*-0.06*	0.92	*0.07*	1.39	*0.06*	0.76	*0.04*
Trading and forex results	0.18	*-0.01*	0.18	*-0.01*	0.12	*0.02*	0.43	*-0.08*	0.30	*0.04*
Other operating income (net)	-0.22	*0.13*	-0.25	*0.17*	-0.11	*-0.04*	-0.07	*0.09*	-0.24	*-0.08*
Total income	2.42	*-0.12*	2.32	*-0.13*	2.57	*-0.03*	5.40	*-0.16*	2.17	*0.00*
Expenditure structure (% of total assets)										
Staff costs	0.86	*-0.08*	0.84	*-0.09*	0.85	*0.00*	1.85	*-0.01*	0.72	*0.00*
Administrative costs	0.21	*0.00*	0.15	*0.01*	0.39	*0.00*	1.13	*-0.01*	0.34	*-0.01*
Other	0.04	*0.00*	0.02	*0.00*	0.10	*-0.01*	0.64	*-0.13*	0.21	*-0.03*
Total expenses	1.11	*-0.08*	1.00	*-0.08*	1.34	*-0.02*	3.61	*-0.14*	1.25	*-0.04*
Profitability (% of total assets)										
Operating profits	1.31	*-0.04*	1.31	*-0.05*	1.23	*-0.02*	1.79	*-0.01*	0.92	*0.04*
Specific provisions	0.25	*-0.09*	0.25	*-0.08*	0.23	*-0.10*	0.36	*-0.16*	0.13	*-0.07*
Funds for general banking risk	0.00	*0.00*	0.00	*0.00*	0.01	*0.00*	0.02	*0.01*	0.00	*0.01*
Extraordinary items (net)	0.00	*-0.03*	0.01	*-0.03*	-0.02	*-0.01*	0.00	*-0.05*	-0.01	*0.01*
Tax charges	0.29	*0.01*	0.30	*0.01*	0.25	*0.02*	0.34	*0.02*	0.15	*-0.02*
Profits (before tax and extraord. items)	1.07	*0.05*	1.07	*0.03*	1.01	*0.10*	1.43	*0.15*	0.81	*0.12*
Profits (after tax and extraord. items) (ROA)	0.77	*0.01*	0.78	*-0.01*	0.74	*0.08*	1.09	*0.08*	0.65	*0.15*
Return on equity										
Profits (after tax and extraord. items) (% Tier 1) (ROE)	17.22	*0.68*	18.57	*0.15*	13.85	*1.95*	9.85	*0.99*	13.52	*3.68*
Income structure (% of total income)										
Net interest income	68.75	*-4.88*	69.96	*-5.68*	64.02	*-2.32*	67.64	*-2.09*	62.33	*-0.09*
Net non-interest income	31.25	*4.88*	30.04	*5.68*	35.98	*2.32*	32.36	*2.09*	37.67	*0.09*
Fees and commissions (net)	33.20	*0.21*	32.95	*-0.59*	35.75	*2.99*	25.69	*1.80*	34.98	*1.81*
Trading and forex results	7.29	*0.03*	7.90	*-0.10*	4.62	*0.77*	7.97	*-1.16*	13.69	*1.87*
Other operating income (net)	-9.24	*4.64*	-10.81	*6.37*	-4.39	*-1.43*	-1.30	*1.51*	-11.00	*-3.57*
Expenditure structure (% of total costs)										
Staff costs	77.32	*-1.40*	83.42	*-2.31*	63.31	*0.51*	51.14	*1.79*	56.87	*1.84*
Administrative costs	18.75	*1.55*	14.78	*2.00*	28.99	*0.33*	31.23	*1.02*	26.55	*0.09*
Other	3.94	*-0.15*	1.80	*0.31*	7.70	*-0.84*	17.64	*-2.82*	16.62	*-1.88*
Effiency										
Costs-to-income ratio (% of total income)	45.87	*-0.88*	43.29	*-1.00*	52.29	*-0.03*	66.89	*-0.72*	57.46	*-1.87*
Asset share of banks with cost-to-income ratio over 80%	2.80	*-1.90*	0.00	*-4.71*	14.19	*10.97*	16.65	*-2.43*	44.45	*5.52*

Source: BSC.
Note: Changes from 2003 are in percentage points.

Table 11 EU-13 banks' balance sheet and off-balance sheet items (2004)

	All domestic banks	*Change from 2003*	Large domestic banks	*Change from 2003*	Medium domestic banks	*Change from 2003*	Small domestic banks	*Change from 2003*	Foreign banks	*Change from 2003*
Assets (% of total assets)										
Cash and balances	0.79	-0.01	0.68	-0.01	1.11	0.00	2.58	0.38	1.17	0.34
Short-term government debt	1.38	-0.05	1.24	-0.03	1.87	-0.08	3.36	0.10	2.36	-0.31
Loans to credit institutions	9.83	0.44	9.12	-0.14	12.49	3.35	15.80	-1.53	16.33	-3.48
Debt securities	9.50	-0.53	8.78	-0.31	17.03	-1.22	10.72	-0.99	6.38	-0.58
Debt securities (public bodies)	3.35	-2.19	3.11	-1.25	4.60	-5.70	3.16	-3.95	2.73	-0.43
Debt securities (other borrowers)	6.14	1.19	5.59	0.46	9.12	4.72	3.95	1.86	2.10	-0.34
Loans to customers	58.65	-0.47	57.22	-0.18	64.97	-1.56	60.26	2.11	55.48	1.26
Shares and participating interest	3.50	0.09	3.83	0.00	2.22	0.38	0.97	0.00	4.08	0.10
Tangible and intangible assets	2.57	-0.19	2.83	-0.21	1.23	-0.17	4.46	0.06	1.74	-0.10
Other assets	13.79	0.71	16.31	0.89	3.49	-0.70	2.22	-0.02	12.58	3.02
Liquidity										
Liquid asset ratio 1 (cash and short-term government debt)	2.16	-0.06	1.91	-0.04	2.95	-0.08	5.56	0.19	3.43	0.10
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	11.99	0.39	11.04	-0.18	15.44	3.27	21.36	-1.34	19.76	-3.59
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	14.52	-2.11	13.44	-1.73	18.61	-3.20	23.06	-4.82	22.07	-1.10
Liabilities (% of total assets)										
Amounts owed to credit institutions	10.94	1.10	11.36	0.85	9.20	2.16	9.46	0.27	32.29	-5.80
Amounts owed to customers	45.53	-2.26	43.77	-0.54	50.92	-9.25	73.12	-0.32	34.37	2.16
Debt certificates	20.61	0.67	19.87	-0.85	25.84	7.40	0.99	-0.09	8.36	1.09
Accruals and other liabilities	13.98	1.08	16.10	1.17	5.36	0.21	3.15	0.03	16.81	2.24
Funds for general banking risk	0.01	0.00	0.00	0.00	0.05	0.01	0.11	-0.10	0.07	-0.05
Provisions for liabilities and charges	0.59	-0.15	0.62	-0.08	0.44	-0.48	0.39	0.10	0.45	0.05
Subordinated liabilities	1.67	-0.09	1.69	-0.12	1.69	0.05	0.64	0.07	1.08	0.16
Equity	5.70	-0.47	5.56	-0.53	5.77	-0.20	11.50	-0.26	6.16	0.19
Other liabilities	0.64	-0.03	0.73	-0.06	0.27	0.06	0.01	0.00	0.04	-0.03
Profit or loss for the financial year	0.46	0.11	0.44	0.11	0.53	0.11	0.83	0.21	0.50	0.09
Selected off-balance-sheet items (% of total assets)										
Credit lines	24.05	1.25	26.92	0.93	12.51	1.85	8.28	0.73	19.35	-2.05
Guarantees and other commitments	4.47	-4.12	4.40	-5.22	4.25	0.27	10.14	-0.37	17.03	13.55
Derivatives	9.61	4.17	8.16	2.28	17.84	14.11	3.37	3.14	43.38	5.95

Source: BSC.

Note: Changes from 2003 are in percentage points. Concerning the item "debt securities", some countries provided information only on the total amount and not on the split between the two sub-items, i.e. "issued by public bodies" and "issued by other borrowers". Consequently, the sum of these two sub-items is smaller than the total amount.

Table 12 EU-13 banks' non-performing assets and provisioning (2004)

	All domestic banks	*Change from 2003*	Large domestic banks	*Change from 2003*	Medium domestic banks	*Change from 2003*	Small domestic banks	*Change from 2003*	Foreign banks	*Change from 2003*
Asset quality (% of loans and advances)										
Non-performing and doubtful asssets (gross)	1.75	*-0.43*	1.52	*-0.48*	2.45	*-0.26*	3.78	*0.19*	2.59	*-1.43*
Asset quality (% of own funds)										
Non-performing and doubtful assets (gross)	26.67	*-5.67*	24.17	*-7.27*	35.74	*-1.29*	25.90	*2.10*	37.89	*-19.58*
Non-performing and doubtful assets (net)	9.04	*-2.39*	7.82	*-3.41*	13.86	*0.16*	6.59	*3.34*	23.20	*-17.19*
Provisioning (stock) (% of loans and advances)										
Total provisions	1.16	*-0.25*	1.03	*-0.26*	1.50	*-0.21*	2.82	*-0.28*	1.00	*-0.19*
Provisioning (stock) (% of non-performing and doubtful assets)										
Total provisions	66.11	*1.44*	67.63	*3.38*	61.22	*-1.79*	74.58	*-11.81*	39.00	*9.28*

Source: BSC.
Note: Changes from 2003 are in percentage points. Definitions of non-performing and doubtful assets differ between countries. Consequently, these data should be interpreted with caution.

Table 13 EU-13 banks' regulatory capital ratios and risk-adjusted items (2004)

	All domestic banks	*Change from 2003*	Large domestic banks	*Change from 2003*	Medium domestic banks	*Change from 2003*	Small domestic banks	*Change from 2003*	Foreign banks	*Change from 2003*
Overall solvency ratio	12.99	*-0.52*	12.60	*-0.71*	14.24	*0.27*	17.33	*-0.49*	16.68	*-0.01*
Tier 1 ratio	8.57	*0.07*	8.00	*0.05*	10.15	*0.16*	17.28	*-0.48*	12.27	*-1.40*
Risk-adjusted items (% of total risk-adjusted assets)										
Risk-weighted assets	84.03	*-0.87*	82.71	*-0.38*	89.59	*-1.82*	87.51	*-8.16*	73.15	*4.92*
Risk-weighted off-balance-sheet items	9.64	*0.88*	10.22	*0.42*	6.83	*1.78*	11.40	*9.26*	7.15	*-0.87*
Risk-adjusted trading book	6.33	*-0.01*	7.07	*-0.05*	3.58	*0.04*	1.43	*-0.82*	20.32	*-4.04*

	All banks	*Change from 2003*
Overall solvency ratio	13.57	*-0.38*
Tier 1 ratio	9.15	*-0.07*
Distribution of overall solvency ratio		
Overall solvency ratio <7%	0.01	*-0.06*
Overall solvency ratio 7%-8%	0.00	*-0.04*
Overall solvency ratio 8%-9%	0.45	*0.32*
Overall solvency ratio 9%-10%	7.98	*1.92*
Overall solvency ratio 10%-11%	15.77	*3.52*
Overall solvency ratio 11%-13%	60.00	*7.31*
Overall solvency ratio >13%	15.80	*-12.97*
Overall solvency ratio below 9%		
Number of banks	35	*-4*
Asset share (% of total banking sector assets)	0.39	*0.22*

	All banks	*Change from 2003*
Risk-adjusted items (% of total risk-adjusted assets)		
Risk-weighted assets	82.31	*-0.25*
Risk-weighted off-balance-sheet items	9.28	*0.62*
Risk-adjusted trading book	8.54	*-0.33*
Composition of trading book own funds requirement (% of total trading book own funds requirement under CAD)		
Own funds requirement for traded debt instruments	21.46	*-3.25*
Own funds requirement for equities	50.78	*5.75*
Own funds requirement for foreign exchange risk	3.41	*-0.38*
Own funds requirement for other trading book items	24.55	*-2.19*

Source: BSC.
Note: Changes from 2003 are in percentage points.

Table 14 Key country-level indicators: all domestic banks (2004)

	AT	BE	DE	ES	FI	FR	GR	IE	IT	LU	NL	PT
Banking sector ownership												
Total assets of domestically owned banks (% of total national banking sector assets)	78.35	80.71	94.48	90.22	38.66	88.84	87.86	69.66	90.50		90.08	76.51
Profitability (% of total assets, if not otherwise indicated)												
Net interest income	1.72	1.11	0.95	1.79	1.83	0.70	2.87	1.09	2.09		1.38	1.97
Net non-interest income	0.76	0.73	0.75	1.07	0.91	1.87	1.21	0.75	1.33		0.99	1.36
Total expenses	1.56	1.18	1.17	1.55	1.57	1.69	2.47	0.96	1.98		1.61	2.03
Profits (after tax and extraord. items) (ROA)	0.64	0.48	0.12	0.82	0.86	0.55	0.67	0.72	0.62		0.50	0.76
Profits (after tax and extraord. items) (% of Tier 1) (ROE)	14.93	14.13	3.87	15.54	11.21	12.63	10.49	20.87	10.59		13.24	12.11
Net interest income (% of total income)	69.29	60.26	55.86	62.54	66.70	27.13	70.28	59.31	61.17		58.22	59.10
Cost-to-income ratio (% of total income)	62.91	64.37	68.89	54.17	57.11	65.79	60.44	52.56	57.87		67.84	60.98
Solvency												
Overall solvency ratio	11.84	13.06	11.82	11.51	14.89	10.25	12.94	9.96	11.64		11.82	10.44
Tier 1 ratio	8.02	9.45	7.51	7.83	12.61	9.30	10.14	7.90	8.63		9.52	8.67
Liquidity												
Liquid asset ratio 1 (cash and short-term government debt)	8.28	1.10	1.75	1.79	9.60	1.58	6.21	0.83	5.82		3.48	3.40
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	28.48	17.79	22.32	9.96	12.69	22.03	15.92	9.69	16.10		13.87	12.46
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	28.49	33.24	22.32	18.97	13.43	22.03	25.64	9.69	18.73		23.25	15.77
Balance sheet structure (% of total assets)												
Debt securities	3.66	26.54	22.84	14.23	4.19	27.05	12.21	26.22	7.09		22.49	8.25
Loans to customers	50.34	42.59	42.91	64.70	77.99	39.48	63.44	53.09	59.41		55.66	68.53
Shares and participating interest	10.98	2.52	4.43	3.70	0.99	1.49	2.63	0.37	2.72		2.71	4.25
Amounts owed to credit institutions	22.39	23.64	27.63	13.91	4.23	23.89	8.66	21.69	12.37		18.56	11.27
Amounts owed to customers	42.91	49.56	35.17	56.54	59.14	32.87	70.01	31.58	44.56		47.46	54.80
Debt certificates	22.03	10.86	22.86	12.43	22.62	27.14	6.52	30.01	19.87		19.76	19.79
Subordinated liabilities	2.75	2.22	1.52	2.51	1.65	1.86	2.39	2.08	2.66		1.49	3.34

Source: BSC.
Note: See the Statistical Annex's box for an explanation on the differences between tables 14-15 and 16-17.

Table 14 - Key country-level indicators: all domestic banks (2004) (cont'd)

	CY	CZ	DK	EE	HU	LT	LV	MT	PL	SE	SI	SK	UK
Banking sector ownership													
Total assets of domestically owned banks (% of total national banking sector assets)	90.29	3.81	80.49	1.46	37.49	7.69	51.94	28.20	32.67	94.13	80.68	7.15	80.84
Profitability (% of total assets, if not otherwise indicated)													
Net interest income	2.38	1.31	1.07	2.43	5.71	2.05	2.37	2.06	3.86	1.29	2.70	3.61	1.75
Net non-interest income	0.98	1.53	0.52	2.15	1.36	1.46	2.56	0.95	2.12	0.77	1.94	0.77	0.75
Total expenses	2.07	1.97	0.88	3.38	3.58	2.69	3.09	1.54	4.07	1.20	2.87	2.51	1.05
Profits (after tax and extraord. items) (ROA)	0.22	0.61	0.55	0.83	2.65	0.57	1.43	0.77	1.33	0.64	0.72	1.02	0.82
Profits (after tax and extraord. items) (% of Tier 1) (ROE)	3.84	8.70	12.37	5.44	34.73	7.14	22.83	12.58	19.16	16.05	13.42	6.47	18.04
Net interest income (% of total income)	70.76	46.02	67.09	53.04	80.74	58.48	48.10	68.30	64.56	62.63	58.17	82.37	70.00
Cost-to-income ratio (% of total income)	61.67	69.51	55.16	73.69	50.60	76.58	62.63	51.23	68.11	58.05	61.69	57.22	41.94
Solvency													
Overall solvency ratio	13.58	26.06	13.03	32.86	13.18	12.34	11.47	15.77	15.74	10.60	11.29	25.08	13.39
Tier 1 ratio	10.14	24.17	10.51	29.69	13.65	11.14	10.79	13.06	15.64	8.39	7.70	26.13	8.29
Liquidity													
Liquid asset ratio 1 (cash and short-term government debt)	14.99	8.32	0.45	6.27	23.29	12.26	4.98	9.66	19.39	4.55	2.78	8.94	1.42
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	27.64	42.86	9.58	50.15	36.97	42.08	39.63	16.16	37.17	13.52	9.97	14.70	11.36
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	32.21	43.93	21.73	50.15	37.03	43.57	45.45	30.42	44.18	13.52	27.48	14.70	14.60
Balance sheet structure (% of total assets)													
Debt securities	10.45	6.17	23.35	3.02	1.19	2.13	15.04	38.29	7.61	7.87	28.14	26.63	9.42
Loans to customers	57.27	47.56	59.41	37.43	54.36	41.02	41.03	39.08	49.48	62.27	53.50	54.31	58.01
Shares and participating interest	1.19	0.07	1.56	0.94	1.06	1.57	0.61	0.78	1.04	0.90	3.36	0.40	3.14
Amounts owed to credit institutions	3.30	35.02	12.56	1.36	8.37	8.46	9.52	14.70	6.80	14.48	16.61	11.41	10.06
Amounts owed to customers	83.60	28.42	22.14	74.72	66.81	80.38	76.49	73.89	74.73	28.93	64.68	64.59	51.07
Debt certificates	1.01	20.75	50.08	0.98	11.24	0.03	1.04	0.50	0.24	32.69	4.46	0.00	14.90
Subordinated liabilities	3.69	0.61	1.43	2.11	0.57	0.31	0.79	1.44	0.26	1.92	2.56	0.00	1.65

Source: BSC.
Note: See the Statistical Annex's box for an explanation on the differences between tables 14-15 and 16-17.

Table 15 Key country-level indicators: all domestic banks (2004, percentage point change from 2003)

	AT	BE	DE	ES	FI	FR	GR	IE	IT	LU	NL	PT
Banking sector ownership												
Total assets of domestically owned banks (% of total national banking sector assets)	0.72	1.12	-0.06	0.62	-0.93	-0.30	-0.97	-1.84	-1.32		-0.47	-1.13
Profitability (% of total assets, if not otherwise indicated)												
Net interest income	0.08	-0.05	-0.06	-0.39	-0.21	0.03	0.03	-0.07	-0.09		-0.11	-0.03
Net non-interest income	0.06	0.05	-0.06	-0.12	0.00	-0.01	0.04	0.01	-0.08		0.03	0.10
Total expenses	0.12	-0.06	-0.10	-0.33	-0.17	0.02	-0.05	-0.05	-0.11		-0.05	0.04
Profits (after tax and extraord. items) (ROA)	0.19	0.08	0.12	-0.08	-0.01	0.07	-0.05	0.12	0.21		0.07	-0.02
Profits (after tax and extraord. items) (% Tier1) (ROE)	0.00	1.98	3.85	-0.27	-0.32	1.28	-1.14	2.59	3.34		1.70	-1.75
Net interest income (% of total income)	-0.54	-2.73	0.33	-2.09	-2.36	1.13	-0.44	-2.06	0.32		-2.52	-2.10
Cost-to-income ratio (% of total income)	1.36	-3.10	-1.10	-1.72	-1.47	0.07	-2.35	-0.86	-0.54		0.35	-0.16
Solvency												
Overall solvency ratio		0.55	0.13	-0.79	0.18	-0.51	0.78	-1.44	0.30		-0.19	0.50
Tier 1 ratio		0.99	-0.06	-0.59	-0.02	-0.13	0.08	-0.24	0.42		0.39	0.75
Liquidity												
Liquid asset ratio 1 (cash and short-term government debt)	5.01	-0.21	0.41	-0.39	-0.37	0.26	2.10	-0.02	-0.69		0.44	-2.25
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	4.96	-0.86	1.04	-1.45	-0.98	-2.37	0.90	-0.61	-0.97		0.44	-2.88
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	1.35	-2.90	1.04	-4.74	-0.84	-2.37	-4.52	-0.61	1.66		-0.59	-2.79
Balance sheet structure (% of total assets)												
Debt securities	-0.71	-1.80	0.45	-2.24	0.24	0.01	-6.18	-0.53	1.07		1.06	0.24
Loans to customers	-0.01	0.96	-2.58	3.85	1.35	2.11	5.82	1.42	0.00		-2.57	2.37
Shares and participating interest	-3.19	0.41	0.18	-0.11	0.06	-0.19	-0.44	-0.04	0.01		0.57	0.31
Amounts owed to credit institutions	0.64	1.04	-0.01	-1.69	-0.70	-1.92	-3.42	-1.97	-0.38		0.88	-3.70
Amounts owed to customers	-1.04	0.10	-0.99	0.24	-2.24	0.40	-1.21	-0.85	-0.33		-1.10	0.78
Debt certificates	0.62	-1.77	-0.07	1.55	3.07	2.24	3.53	2.73	0.87		-0.46	2.24
Subordinated liabilities	1.40	-0.21	0.04	0.23	0.14	-0.06	0.87	0.24	-0.15		-0.19	0.10

Source: BSC.
Note: See the Statistical Annex's box for an explanation on the differences between tables 14-15 and 16-17.

Table 15 Key country-level indicators: all domestic banks (2004, percentage point change from 2003) (cont'd)

	CY	CZ	DK	EE	HU	LT	LV	MT	PL	SE	SI	SK	UK
Banking sector ownership													
Total assets of domestically owned banks (% of total national banking sector assets)	*-0.13*	*-0.21*	*1.44*	*-0.25*	*1.50*	*0.35*	*-1.67*	*-3.19*	*0.32*	*-0.26*	*-1.07*	*2.49*	*-2.25*
Profitability (% of total assets, if not otherwise indicated)													
Net interest income	*0.22*	*0.43*	*-0.16*	*-0.93*	*0.53*	*-0.16*	*0.10*	*0.20*	*-0.04*	*-0.20*	*-0.31*	*0.48*	*-0.23*
Net non-interest income	*-0.09*	*-0.42*	*-0.10*	*0.03*	*-0.07*	*-0.15*	*-0.39*	*0.03*	*-0.04*	*0.07*	*0.07*	*0.00*	*0.11*
Total expenses	*-0.02*	*0.40*	*-0.02*	*-1.06*	*-0.09*	*-0.59*	*-0.22*	*0.00*	*-0.24*	*-0.19*	*-0.21*	*-0.40*	*-0.07*
Profits (after tax and extraord. items) (ROA)	*0.46*	*-0.61*	*-0.12*	*-0.16*	*0.43*	*-0.03*	*0.21*	*0.37*	*0.34*	*0.07*	*-0.06*	*0.44*	*0.00*
Profits (after tax and extraord. items) (% Tier1) (ROE)	*7.62*	*-9.29*	*-2.05*	*-2.88*	*6.27*	*1.34*	*3.56*	*5.78*	*4.03*	*2.03*	*0.08*	*1.65*	*0.60*
Net interest income (% of total income)	*4.04*	*15.04*	*0.95*	*-8.28*	*2.44*	*0.50*	*4.63*	*1.60*	*0.22*	*-5.44*	*-3.39*	*2.26*	*-5.65*
Cost-to-income ratio (% of total income)	*-3.04*	*13.89*	*6.85*	*-7.25*	*-4.81*	*-9.36*	*-0.76*	*-4.00*	*-3.04*	*-5.24*	*-1.37*	*-17.07*	*-0.91*
Solvency													
Overall solvency ratio	*-0.69*	*-3.96*	*0.05*	*4.00*	*-0.81*	*-1.94*	*1.28*	*0.34*	*1.64*	*0.02*	*-0.93*	*4.02*	*-0.62*
Tier 1 ratio	*-0.58*	*-3.83*	*-0.22*	*5.15*	*-0.55*	*-1.97*	*0.52*	*0.75*	*1.59*	*0.27*	*-1.55*	*5.12*	*-0.16*
Liquidity													
Liquid asset ratio 1 (cash and short-term government debt)	*3.99*	*-0.34*	*-0.14*	*-0.14*	*-1.71*	*-4.09*	*-3.30*	*-2.13*	*-4.56*	*0.43*	*-0.20*	*-7.89*	*-0.20*
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	*4.01*	*-0.62*	*0.23*	*-1.61*	*-0.29*	*3.86*	*-1.08*	*-2.72*	*-0.72*	*-0.83*	*1.55*	*-14.00*	*0.55*
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	*-0.26*	*-1.35*	*-0.62*	*-1.61*	*-0.25*	*5.35*	*-0.06*	*-2.30*	*-1.08*	*-9.90*	*-10.30*	*-20.15*	*-0.92*
Balance sheet structure (% of total assets)													
Debt securities	*-3.34*	*-1.72*	*1.34*	*-0.77*	*0.10*	*2.05*	*-5.70*	*0.81*	*-0.39*	*-1.20*	*-4.47*	*6.00*	*-0.27*
Loans to customers	*0.15*	*1.94*	*-0.82*	*2.62*	*-0.33*	*0.29*	*3.61*	*1.71*	*0.42*	*0.94*	*3.81*	*12.34*	*-0.71*
Shares and participating interest	*-0.23*	*0.06*	*0.01*	*0.03*	*0.11*	*-0.73*	*-0.32*	*0.10*	*0.04*	*0.16*	*-0.27*	*-0.72*	*-0.13*
Amounts owed to credit institutions	*-7.33*	*3.08*	*0.43*	*1.34*	*3.75*	*2.00*	*-0.14*	*0.25*	*0.28*	*1.73*	*1.95*	*-3.79*	*1.08*
Amounts owed to customers	*8.07*	*-1.07*	*-1.14*	*2.51*	*-8.20*	*1.34*	*-0.44*	*-0.10*	*-1.91*	*-3.37*	*-1.77*	*7.83*	*-2.05*
Debt certificates	*-0.12*	*-3.32*	*0.62*	*0.98*	*3.49*	*-0.19*	*0.27*	*-0.05*	*-0.06*	*1.26*	*-0.21*	*-1.07*	*0.40*
Subordinated liabilities	*-0.16*	*0.15*	*0.10*	*-0.38*	*-0.07*	*0.31*	*0.36*	*-0.08*	*-0.01*	*-0.10*	*0.60*	*0.00*	*-0.11*

Source: BSC.
Note: See the Statistical Annex's box for an explanation on the differences between tables 14-15 and 16-17.

Table 16 Key country-level indicators: all banks (2004)

	AT	BE	DE	ES	FI	FR	GR	IE	IT	LU	NL	PT
Profitability (% of total assets, if not otherwise indicated)												
Net interest income	1.70	1.14	0.95	1.72	1.29	0.66	2.75	1.01	2.07	0.58	1.36	1.88
Net non-interest income	0.84	0.70	0.75	1.04	0.63	1.87	1.22	0.71	1.32	0.82	0.96	1.26
Total expenses	1.61	1.20	1.17	1.53	1.09	1.67	2.48	0.85	1.97	0.76	1.57	1.85
Profits (after tax and extraord. items) (ROA)	0.60	0.47	0.12	0.76	0.71	0.55	0.61	0.71	0.61	0.48	0.50	0.75
Profits (after tax and extraord. items) (% Tier1) (ROE)	14.46	14.06	3.87	15.12	8.03	12.62	10.11	15.38	10.58	11.30	13.08	11.75
Net interest income (% of total income)	66.95	61.73	55.86	62.41	67.12	26.01	69.31	58.50	61.08	41.35	58.63	59.93
Cost-to-income ratio (% of total income)	63.31	65.33	68.89	55.32	56.81	66.02	62.37	49.40	58.08	53.94	67.26	58.89
Solvency												
Overall solvency ratio	11.87	12.94	11.82	11.59	19.36	10.42	12.91	12.30	11.65	16.88	11.87	11.57
Tier 1 ratio	7.93	9.38	7.51	7.91	16.73	9.57	10.18	10.18	8.67	13.92	9.57	9.64
Liquidity												
Liquid asset ratio 1 (cash and short-term government debt)	8.08	0.98	1.75	1.69	6.81	1.45	5.77	1.16	5.71	3.49	3.28	2.88
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	27.96	19.00	22.32	11.57	27.93	21.34	17.78	14.94	16.11	49.78	14.81	16.06
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	28.13	34.62	22.32	20.01	28.22	21.34	27.24	14.94	18.75	56.80	23.74	19.05
Balance sheet structure (% of total assets)												
Debt securities	3.62	26.39	22.84	15.44	2.24	27.19	12.30	27.28	7.44	24.53	21.29	9.49
Loans to customers	50.55	42.55	42.91	62.27	53.16	39.59	62.03	47.50	59.17	20.57	55.65	64.36
Shares and participating interest	11.85	2.18	4.43	3.72	0.66	1.47	2.33	0.58	2.66	1.12	3.03	3.95
Amounts owed to credit institutions	23.63	24.66	27.63	19.26	13.10	24.26	11.52	29.14	12.92	42.50	20.84	16.33
Amounts owed to customers	42.33	50.02	35.17	53.18	40.15	30.98	68.96	28.69	43.84	37.44	46.11	50.41
Debt certificates	19.94	10.11	22.86	11.29	19.86	27.98	5.78	25.72	20.22	10.94	18.52	19.29
Subordinated liabilities	2.95	2.10	1.52	2.32	1.53	1.84	2.10	1.88	2.59	1.27	1.45	3.38

Source: BSC.
Note: See the Statistical Annex's box for an explanation on the differences between tables 14-15 and 16-17.

Table 16 Key country-level indicators: all banks (2004) (cont'd)

	CY	CZ	DK	EE	HU	LT	LV	MT	PL	SE	SI	SK	UK
Profitability (% of total assets, if not otherwise indicated)													
Net interest income	2.42	2.27	1.07	2.85	4.58	2.23	2.52	1.43	3.09	1.42	2.64	2.71	1.59
Net non-interest income	0.99	2.50	0.53	1.74	1.55	1.25	2.14	0.79	2.38	0.76	1.81	1.04	0.70
Total expenses	2.09	2.99	0.89	2.26	3.43	2.33	2.68	0.82	3.56	1.31	2.83	2.33	0.98
Profits (after tax and extraord. items) (ROA)	0.21	1.29	0.55	2.02	1.89	0.94	1.51	1.07	1.32	0.64	0.62	1.03	0.75
Profits (after tax and extraord. items) (% Tier1) (ROE)	3.51	24.71	13.07	24.34	24.92	15.95	22.81	10.15	16.54	15.81	11.47	14.24	16.75
Net interest income (% of total income)	71.04	47.61	66.98	62.02	74.69	64.14	54.08	64.53	56.49	65.24	59.36	72.31	69.26
Cost-to-income ratio (% of total income)	61.27	62.59	55.92	49.17	55.98	66.89	57.40	37.05	65.04	60.10	63.46	62.30	42.93
Solvency													
Overall solvency ratio	13.30	11.90	12.97	11.47	12.21	11.42	11.10	21.27	15.59	10.82	11.11	17.78	14.07
Tier 1 ratio	10.22	11.57	10.33	11.07	11.17	8.64	10.26	22.58	15.34	8.63	7.75	17.93	8.80
Liquidity													
Liquid asset ratio 1 (cash and short-term government debt)	14.46	12.50	0.61	7.12	17.97	14.18	4.59	4.05	19.27	4.55	2.69	21.90	1.21
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	27.93	43.45	12.37	16.42	30.61	26.00	28.95	13.11	37.16	14.43	10.48	27.31	12.00
Liquid asset ratio 3 (ratio 2 + debt sec.by public bodies)	32.06	46.42	25.41	16.42	30.64	27.56	33.64	31.91	41.96	14.43	27.98	27.31	15.08
Balance sheet structure (% of total assets)													
Debt securities	9.45	8.37	22.85	5.59	1.21	3.47	11.45	35.16	5.76	7.66	26.49	32.39	8.41
Loans to customers	58.15	40.10	57.79	73.25	61.32	65.43	55.58	39.62	47.92	61.26	55.45	35.92	58.14
Shares and participating interest	1.16	0.72	1.56	0.66	0.70	0.48	0.38	6.35	1.37	0.86	2.81	0.36	3.52
Amounts owed to credit institutions	5.08	14.46	16.92	15.49	19.58	22.23	21.26	22.84	10.67	16.21	21.62	16.36	14.98
Amounts owed to customers	82.14	64.74	23.29	57.21	59.74	63.83	64.77	42.40	68.14	28.77	60.99	66.67	46.57
Debt certificates	0.91	7.38	44.90	13.27	6.03	2.07	1.14	0.24	1.22	31.30	3.75	3.52	13.55
Subordinated liabilities	3.36	0.30	1.40	0.30	1.18	0.68	0.87	3.85	0.58	1.91	2.36	0.05	1.55

Source: BSC.
Note: See the Statistical Annex's box for an explanation on the differences between tables 14-15 and 16-17.

Table 17 Key country-level indicators: all banks (2004, percentage change from 2003)

	AT	BE	DE	ES	FI	FR	GR	IE	IT	LU	NL	PT
Profitability (% of total assets, if not otherwise indicated)												
Net interest income	0.08	-0.06	-0.06	-0.36	-0.90	0.00	0.01	-0.08	-0.09	-0.02	-0.12	-0.03
Net non-interest income	0.22	-0.02	-0.06	-0.12	-0.26	-0.01	0.02	0.01	-0.07	0.04	0.01	-0.01
Total expenses	0.11	-0.10	-0.10	-0.32	-0.75	-0.01	-0.08	-0.04	-0.11	0.01	-0.07	0.01
Profits (after tax and extraord. items) (ROA)	0.31	0.06	0.12	-0.07	-0.56	0.07	-0.02	0.07	0.20	0.07	0.05	0.00
Profits (after tax and extraord. items) (% Tier1) (ROE)	0.00	1.95	3.85	-0.08	-5.93	1.59	-0.66	1.38	3.25	1.07	1.44	-1.28
Net interest income (% of total income)	-5.49	-0.56	0.33	-1.91	-3.91	0.11	-0.26	-2.20	0.25	-2.04	-2.15	-0.21
Cost-to-income ratio (% of total income)	-3.55	-2.71	-1.10	-1.54	-3.16	0.05	-2.45	-0.22	-0.48	-0.07	0.17	1.06
Solvency												
Overall solvency ratio	-0.24	0.06	0.13	-0.79	0.28	-0.59	0.71	-1.21	0.28	0.19	-0.19	0.43
Tier 1 ratio	0.39	0.60	-0.06	-0.60	0.30	-0.24	0.08	-0.24	0.40	0.51	0.38	0.87
Liquidity												
Liquid asset ratio 1 (cash and short-term government debt)	5.15	-0.27	0.41	-0.34	0.26	0.20	1.47	0.13	-0.66	-0.80	0.36	-1.69
Liquid asset ratio 2 (ratio 1 + loans t o cred. inst.)	4.84	-1.53	1.04	-1.76	-0.29	-2.10	1.42	-0.85	-0.95	-1.44	0.24	-2.50
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	2.21	-2.65	1.04	-4.72	-0.92	-2.10	-3.44	-0.85	1.70	-0.36	-0.86	-2.49
Balance sheet structure (% of total assets)												
Debt securities	0.22	-0.86	0.45	-1.18	-0.98	0.38	-5.50	0.49	1.18	2.97	0.74	1.33
Loans to customers	0.00	0.54	-2.58	2.99	-1.27	1.28	4.64	0.73	-0.11	-1.33	-2.34	0.79
Shares and participating interest	-4.04	0.32	0.18	0.01	0.03	-0.19	-0.43	0.11	0.02	-0.15	0.85	0.27
Amounts owed to credit institutions	0.07	-0.30	-0.01	-1.12	1.43	-1.68	-3.04	-2.26	-0.41	1.13	1.14	-2.52
Amounts owed to customers	-0.39	0.67	-0.99	-0.21	-3.58	0.19	-0.85	-0.86	-.041	0.00	-1.62	0.76
Debt certificates	0.67	-1.13	-0.07	1.46	0.74	2.02	3.07	3.98	1.03	-0.78	-0.40	1.17
Subordinated liabilities	1.07	-0.24	0.04	0.20	-0.12	-0.07	0.72	0.11	-0.15	-0.15	-0.20	0.01

Source: BSC.
Note: See the Statistical Annex's box for an explanation on the differences between tables 14-15 and 16-17.

Table 17 Key country-level indicators: all banks (2004, percentage change from 2003) (cont'd)

	CY	CZ	DK	EE	HU	LT	LV	MT	PL	SE	SI	SK	UK
Profitability (% of total assets, if not otherwise indicated)													
Net interest income	0.24	0.13	-0.15	-0.44	0.41	-0.14	0.21	-0.32	0.00	-0.22	-0.33	-0.32	-0.20
Net non-interest income	-0.08	0.23	-0.08	-0.15	0.29	-0.35	-0.31	0.47	-0.06	0.07	0.05	0.13	0.08
Total expenses	-0.01	-0.07	-0.02	-0.45	-0.03	-0.80	-0.24	-0.09	-0.21	-0.20	-0.22	-0.38	-0.06
Profits (after tax and extraord. items) (ROA)	0.42	0.08	-0.08	0.10	0.53	-0.06	0.25	0.29	0.85	0.08	-0.04	-0.24	0.01
Profits (after tax and extraord. items) (% of total income)	3.87	-0.91	0.37	-1.44	-2.11	4.44	5.62	-20.07	0.65	-5.31	-3.40	-4.73	-4.92
Cost-to-income ratio (% of total income)	-3.60	-6.52	6.04	-3.12	-7.75	-11.85	-3.91	-7.23	-3.07	-4.77	-0.86	-6.73	-0.45
Solvency													
Overall solvency ratio	-0.65	-1.93	0.14	-1.06	-0.30	-1.07	0.78	0.66	1.79	0.01	-0.79	-3.82	-0.39
Tier 1 ratio	-0.55	-1.38	-0.11	-0.42	-0.12	-0.94	0.23	-0.87	1.44	0.26	-1.38	-3.94	-0.24
Liquidity													
Liquid asset ratio 1 (cash and short-term government debt)	3.61	-1.42	-0.38	-0.55	-0.43	-5.62	-3.46	-1.58	-0.37	0.34	-0.25	0.57	-0.17
Liquid asset ratio 2 (ratio 1 + loans to cred. inst.)	3.78	0.29	-0.97	0.25	-0.76	-1.59	-2.49	0.26	3.97	-0.40	1.33	-2.87	-0.34
Liquid asset ratio 3 (ratio 2 + debt sec. by public bodies)	-0.09	0.45	-2.10	0.25	-0.75	-0.42	-0.83	3.44	2.99	-9.32	-9.87	-5.78	-1.64
Balance sheet structure (% of total assets)													
Debt securities	-3.03	-0.56	1.04	-1.43	-0.11	0.50	-4.03	4.43	-1.26	-1.26	-4.95	6.08	-0.35
Loans to customers	0.03	1.47	-0.18	2.79	0.61	3.25	3.45	-2.74	-2.92	0.39	4.50	-2.61	-0.29
Shares and participating interest	-0.20	0.19	-0.27	0.20	-0.07	-0.08	-0.61	-0.27	-0.17	0.16	-0.21	0.30	-0.08
Amounts owed to credit institutions	-6.54	2.21	-1.01	1.94	0.80	1.02	1.17	-1.56	0.01	1.50	3.02	7.24	0.05
Amounts owed to customers	7.29	0.19	-0.04	-4.15	-3.43	-0.79	-1.16	-2.79	-1.35	-3.36	-2.71	-8.53	-1.65
Debt certificates	-0.11	0.04	0.88	3.62	1.86	1.19	0.22	-0.07	0.14	1.50	-0.34	1.39	0.47
Subordinated liabilities	-0.15	0.00	0.12	-0.55	-0.12	-0.11	0.20	1.94	-0.08	-0.01	0.56	0.04	-0.08

Source: BSC.
Note: See the Statistical Annex's box for an explanation on the differences between tables 14-15 and 16-17.

Table 18 Selected indicators of 50 major EU-25 banks' asset quality profitability and solvency (%)

Banks reporting under IFRS	weighted average (range of variation between highest and lowest 10%)											
	2002			2003			2004			mid-2005		
Asset quality												
Loan loss provisions/total assets	n.a.	*n.a.*	*n.a.*	n.a.	*n.a.*	*n.a.*	0.20	*0.04*	*0.75*	0.14	*0.13*	*0.44*
Profitability												
Net interest income/total operating income	n.a.	*n.a.*	*n.a.*	n.a.	*n.a.*	*n.a.*	53.36	*43.97*	*65.85*	54.98	*43.77*	*66.45*
Net interest income/total assets	n.a.	*n.a.*	*n.a.*	n.a.	*n.a.*	*n.a.*	1.18	*0.81*	*3.66*	1.03	*0.70*	*2.28*
Cost-to-income ratio	n.a.	*n.a.*	*n.a.*	n.a.	*n.a.*	*n.a.*	58.03	*44.18*	*75.74*	56.49	*43.16*	*64.94*
Return on equity (after tax and extraordinary items	n.a.	*n.a.*	*n.a.*	n.a.	*n.a.*	*n.a.*	10.95	*4.78*	*20.96*	20.57	*15.59*	*25.70*
Solvency												
Tier 1 ratio	n.a.	*n.a.*	*n.a.*	n.a.	*n.a.*	*n.a.*	6.56	*7.00*	*8.20*	7.67	*6.50*	*8.45*
Total capital ratio	n.a.	*n.a.*	*n.a.*	n.a.	*n.a.*	*n.a.*	8.60	*9.96*	*12.67*	11.65	*9.87*	*12.80*

Banks reporting under local or US GAAP	weighted average (range of variation between highest and lowest 10%)											
	2002			2003			2004			mid-2005		
Asset quality												
Loan loss provisions total assets	0.31	*0.12*	*0.68*	0.25	*0.09*	*0.45*	0.28	*0.19*	*1.56*	0.07	*0.01*	*0.11*
Profitability												
Net interest income/total operating income	53.20	*36.66*	*72.77*	48.59	*27.22*	*71.45*	41.74	*35.46*	*69.90*	45.24	*36.79*	*76.05*
Net interest income/total assets	0.97	*0.32*	*2.57*	1.00	*0.28*	*2.43*	1.99	*0.45*	*6.07*	1.56	*0.29*	*4.72*
Cost-to-income ratio	73.15	*54.77*	*83.78*	68.59	*54.66*	*76.69*	65.10	*58.36*	*78.41*	64.96	*32.98*	*72.34*
Return on equity (after tax and extraordinary items)	2.19	*-10.41*	*12.32*	3.45	*-18.91*	*16.55*	11.00	*9.15*	*20.56*	16.43	*13.64*	*23.16*
Solvency												
Tier 1 ratio	5.70	*5.64*	*10.02*	7.65	*5.86*	*10.52*	8.62	*6.11*	*10.07*	9.31	*8.06*	*11.58*
Total capital ratio	11.15	*9.10*	*12.32*	11.84	*9.90*	*13.78*	11.00	*10.03*	*12.80*	13.64	*12.08*	*15.76*

Source: ECB calculations based on published accounts.

Note: Data for the first half of 2005 are annualised, unaudited and not based on the full sample. IFRS and non-IFRS banking data are not comparable

Table 19 EU-25 banks' exposes at risk to seven aggregate sectors (2005)

		BaC	EnU	Cap	CCy	CNC	Fin	TMT
9 euro area countries								
Total exposure	EUR billion	608.9	223.9	223.9	1,682.5	805.3	6,360.5	218.2
Sectoral EDF	March 2005	0.25	0.08	0.50	0.46	0.23	0.07	1.13
Exposure at risk, March 2005	EUR billion	152.2	17.9	112.0	773.9	185.2	445.2	246.5
% change, March 2005 - June 2004*		-66.91	-87.59	-50.29	-14.52	32.06	46.25	-14.46
8 non-euro area EU-25 countries								
Total exposure	EUR billion	56.4	10.4	62.5	141.4	20.5	56.2	1,244.2
Sectoral EDF	March 2005	0.25	0.08	0.50	0.46	0.23	0.07	1.13
Exposure at risk, March 2005	EUR billion	14.1	0.80	31.2	65.1	4.70	3.90	1,405.9
% change, March 2005 - June 2004**		-54.7	-92.8	20.1	-26.6	-80.7	-53.6	-64.5
17 EU-25 countries								
Total exposure	EUR billion	665.3	234.3	286.4	1,823.9	825.8	6,416.7	1,462.4
Sectoral EDF	March 2005	0.25	0.08	0.50	0.46	0.23	0.07	1.13
Exposure at risk, March 2005	EUR billion	166.3	18.7	143.2	839.0	189.9	449.2	1,652.5
% change, March 2005 - June 2004***		-66.1	-87.9	-42.9	-15.6	19.9	19.4	-28.9
% change in EDF, March 2005 - June 2004		-60.32	-91.75	-44.44	-20.00	2.22	46.15	-53.21

* Changes are based on 7 euro area countries
** Changes based on 3 non-euro area EU countries
*** Changes based on 10 EU countries

Source: BSC.
Note: The sectors are basic materials and construction (BaC), capital goods (Cap), consumer cyclicals (CCy), consumer non-cyclicals (CNC), energy and utilities (EnU), financial (Fin), and technology and telecommunications (TMT).