



**LIETUVOS BANKAS**  
EUROSISTEMA

# Countercyclical Capital Buffer

Background material for decision

December

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Unless otherwise indicated, the cut-off date for data used in the publication is 8 November 2019.

Periods indicated in charts include data for the respective year, quarter, etc.

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## DECISION BASIS FOR SETTING THE COUNTERCYCLICAL CAPITAL BUFFER RATE

On 20 December 2019, the Board of the Bank of Lithuania took a decision<sup>1</sup> to leave the countercyclical capital buffer (CCyB) rate unchanged at 1%, as set in June 2018. Such a decision was taken in view of the recent financial and economic trends, as well as core and additional indicators for setting the CCyB rate.

The latest credit and real estate (RE) market trends point to no significant imbalances in the financial system. The credit-to-GDP ratio remains stable, the current account balance is positive, the loan-to-deposit ratio continues to decline, fluctuating at around 94%, while RE prices are close to their reference value. Nonetheless, household lending remains strong, especially due to rapid growth in housing loans. Although business lending continues to contract, corporate liabilities have been overall growing significantly. In periods of moderate systemic risk, when credit and RE market activity is relatively high, the domestic economy is expanding and corporate financial health is strong, the Bank of Lithuania seeks to ensure that banks accumulate a 1% CCyB.

## CREDIT AND REAL ESTATE MARKET DEVELOPMENTS

**Crediting in Lithuania remains active, although on a quarter-on-quarter basis its annual growth rate somewhat scaled down.** According to the latest financial accounts, the annual growth rate of Lithuania's total financial liabilities stood at 7.7% in Q2 2019 (8.3% in Q1 2019). The annual growth rate of the portfolio of MFI loans to the private non-financial sector stood at 3.6% in September 2019, a quarter-on-quarter increase of 1.4 percentage points. These developments mainly reflected the slowdown in the deceleration of growth of the corporate loan portfolio. The portfolio of MFI loans to households, conversely, continued to grow rapidly.

**The MFI corporate loan portfolio continued to shrink, yet total liabilities have been increasing.**

According to the data of September 2019, the MFI corporate loan portfolio decreased by an annual 1% (3.6% at the end of Q2 2019). These trends might have been still led by the stricter lending conditions of some banks<sup>2</sup> and greater concentration in the banking sector. On a quarterly basis, the portfolio somewhat expanded (0.5%). Interest rates on new bank loans to enterprises continued to rise – their annual average increased by 0.45 percentage point year on year, growing by 0.03 percentage point over the quarter. The portfolios of loans to RE, trade and manufacturing companies shrunk by, respectively, €8 million (0.3%), €142 million (7%) and €64 million (5%) year on year. During the respective period, lending to enterprises engaged in professional, scientific and technical activities<sup>3</sup>, transportation and storage services as well as accommodation and catering services increased (€234 million, or 41%, €63 million, or 9 %, and €11 million, or 5%, respectively). The flows of new loans followed similar trends to those observed in Q2 2019. On a year-on-year basis, the annual flow of loans up to €1 million (including renegotiations) was almost one-third lower at the end of Q3 2019, while that of loans exceeding €1 million decreased by around 5%. Although bank lending to corporates reduced, total corporate liabilities increased by 7% over the year, hence their financial leverage continued improving.

**Growth in the portfolio of MFI loans to households continued at a rapid pace, mostly driven by active lending for house purchase.** The household loan portfolio increased by an annual 8% in September 2019. The portfolio of loans for house purchase grew by 8.9%, maintaining the same pace as the previous quarter. At the end of Q3 2019, the growth rate of the consumer loan portfolio decreased by 0.4 percentage point, reaching 4%. The net flow of new housing loans amounted to €1.3 billion, a year-on-year increase of 5.2% (a quarter-on-quarter increase of 0.4%). Overall, household lending remained largely underpinned by the relatively low unemployment rate and rising wages, whose annual growth rate reached 13.3%<sup>4</sup>. The improving financial situation of households led to stronger household sentiment: the consumer confidence

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<sup>1</sup> Resolution No 03-236 of the Board of the Bank of Lithuania of 20 December 2019 on the application of the countercyclical capital buffer.

<sup>2</sup> As evidenced by surveys of banks and non-financial corporations carried out by the Bank of Lithuania.

<sup>3</sup> Including holding companies.

<sup>4</sup> Based on the data of Q2 2019 of Statistics Lithuania, domestic growth in net wages, excluding sole proprietorships.

indicator in Q3 2019 remained high, although showing signs of moderation in September–October. Interest rates on new housing loans stabilised, amounting to 2.42% in September 2019. Their annual average increased by 0.03 percentage point on a quarterly basis (a year-on-year increase of 0.19 percentage point). However, interest rates on consumer loans have continued on a downward path – at the end of Q3 2019, their annual average decreased by 0.82 percentage point year on year (0.13 percentage point quarter on quarter).

**Growth in house prices in Lithuania decelerated in Q2 2019, while annual price changes in Vilnius and the rest of the country converged.** According to Statistics Lithuania, the annual growth rate of house prices in Lithuania stood at 6.6% in Q2 2019, a quarter-on-quarter decrease of 1.3 percentage points. This was largely driven by the significant slowdown in new-build house prices outside the capital city: having amounted to 16.2% in Q1 2019, their growth rate declined to 7.2% in Q2 2019. In terms of price changes for old and new-build housing, house prices in Vilnius increased by 6.2%, in the rest of the country – 6.8% (5.2% and 10.0% respectively in the previous quarter). House prices in Lithuania have been growing significantly above the EU average (4.2% in Q2 2019) for quite some time. The latest data provided by RE market participants<sup>5</sup> revealed that apartment prices in the country's biggest cities rose by an annual 6.3% in Q3 2019, a quarter-on-quarter increase of 1.1 percentage points. Expectations regarding house price dynamics remained moderate: the majority of RE market participants and banks surveyed by the Bank of Lithuania believe that in the next 12 months new-build apartment prices in Lithuania will rise by up to 5%, hence it continues to be likely that house prices in Lithuania will increase at a somewhat slower pace, close to the medium-term average (6.4%). Bank of Lithuania estimates reveal that house prices are still close to their reference value.

**Activity in Lithuania's RE market increased considerably in Q3 2019, yet on a year-on-year basis the share of housing acquired with a loan remained largely unchanged.** According to the Centre of Registers, the number of housing sold in Lithuania in Q3 2019 rose by 10.9% year on year. In terms of total population, activity in the domestic RE market remained at historical highs. The share of mortgaged housing is still stable at 38.5% (39.4% in Q3 2018). According to the data of UAB Eika, the share of purchase-sale transactions in Vilnius primary new-build apartment market (both registered and non-registered) increased by 26.9% in Q3 2019 year on year. The number of unsold new-build apartments in Vilnius remains high, although decreasing slightly (1.6%) in Q3 2019 (a year-on-year decrease of 5.4%). The main bulk of unsold new-build apartments in Vilnius (74.3%) consisted of apartments in houses that are still under construction.

**The gap between the credit-to-GDP ratio and its long-term trend somewhat narrowed, yet remained negative.** The ratio between credit (including non-banks) to the private non-financial sector and GDP amounted to 66.2% in Q2 2019, a quarter-on-quarter increase of 1.1 percentage points, reflecting the difference in quarterly credit and GDP gains (3.5% and 1.4% respectively). The gap between the credit-to-GDP ratio and its long-term trend turned less negative, fluctuating at -9.4 and -2.9 percentage points in Q2 2019 (depending on the method of assessment) (see Chart B and C in Annex 2). In Q3 2019 the gap between the ratio of MFI loans to the private non-financial sector to GDP and its long-term trend also narrowed, amounting to -4.8%. Other indicators remained largely unchanged: the loan-to-deposit ratio decreased further and stood at 93.9%, the current account balance increased to 1.8% of GDP in Q2 2019, while the house price-to-income ratio decreased.

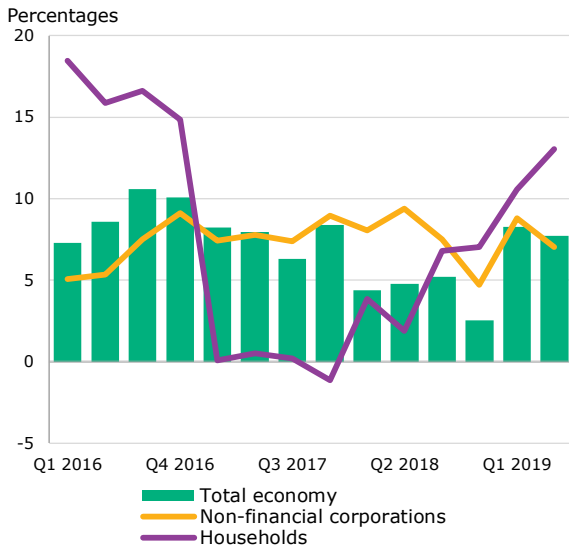
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<sup>5</sup> According to UAB Ober-Haus nekilnojamas turtas.

## ANNEX 1. CREDIT AND HOUSING MARKET TRENDS

Chart 1. Annual growth rate of Lithuania's financial liabilities

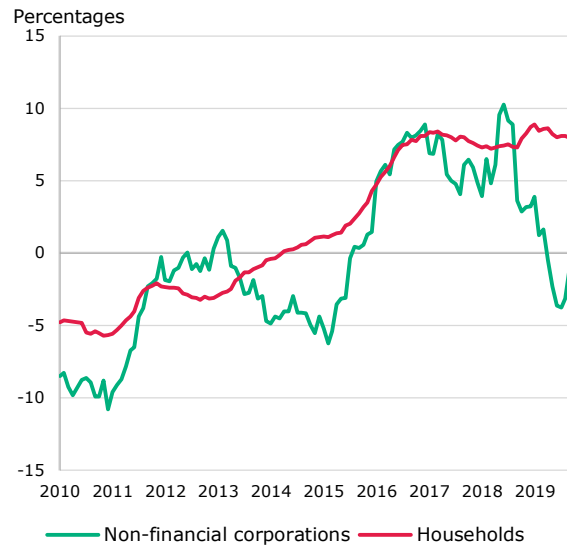
(Q1 2016–Q2 2019)



Source: Bank of Lithuania.

Chart 2. Annual growth of the portfolio of MFI loans to non-financial corporations and households

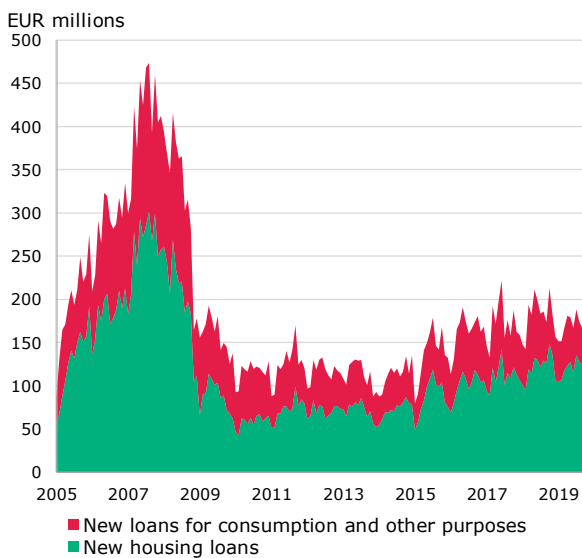
(January 2010–September 2019)



Source: Bank of Lithuania.

Chart 3. Flow of new MFI loans to households

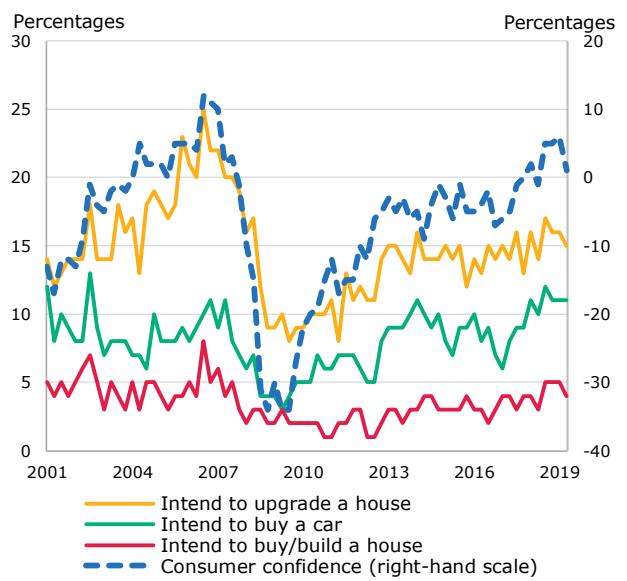
(January 2005–September 2019)



Source: Bank of Lithuania.

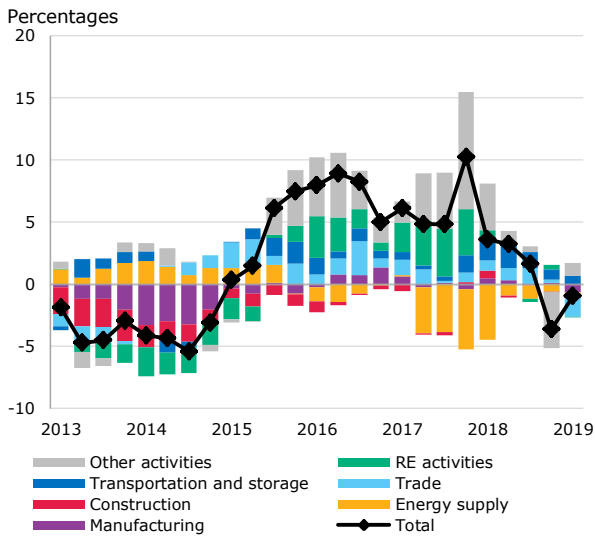
Chart 4. Consumer survey results

(July 2001–October 2019)



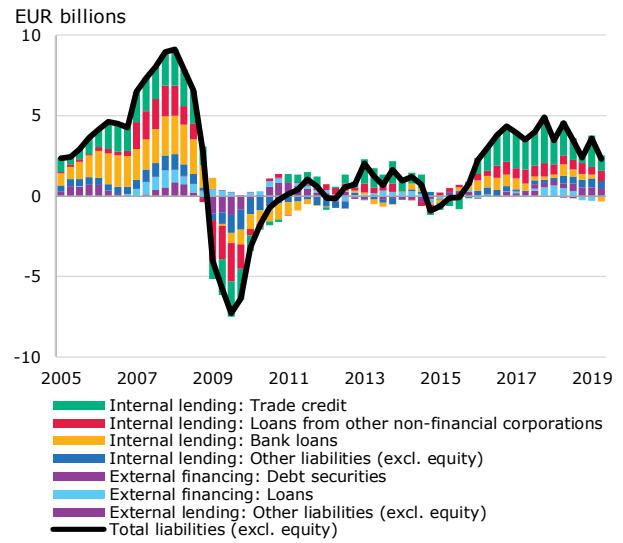
Sources: Statistics Lithuania and Bank of Lithuania calculations.

Chart 5. Annual change in the portfolio of MFI loans to non-financial corporations by economic activity (Q3 2013–Q3 2019)



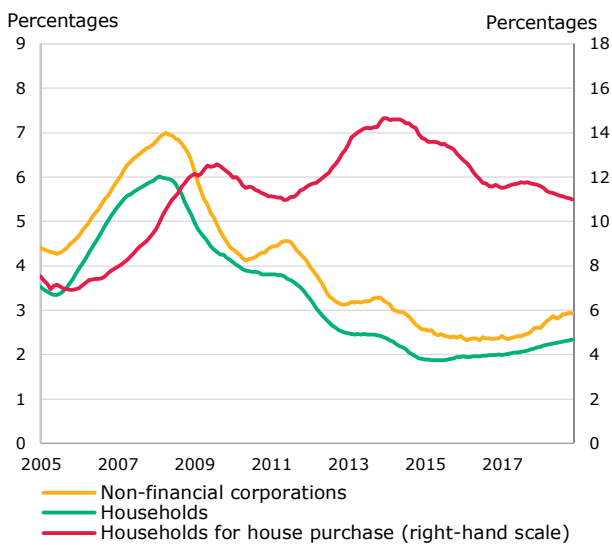
Source: Bank of Lithuania.

Chart 6. Annual change in credit granted to non-financial corporations (Q1 2005–Q2 2019)



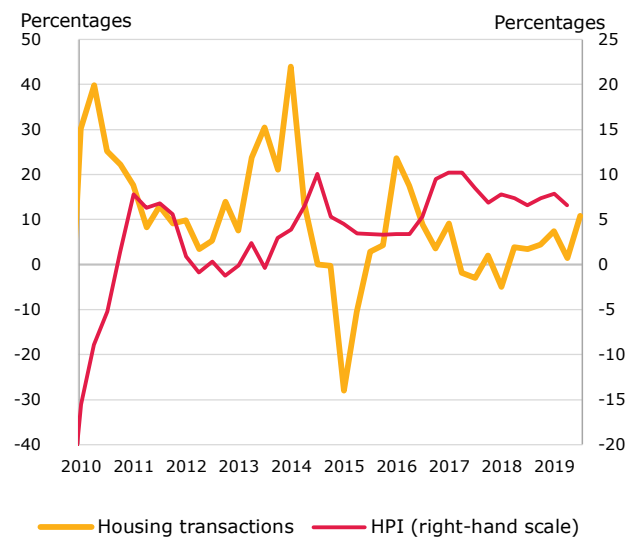
Source: Bank of Lithuania.

Chart 7. Average weighted interest rates on new loans to non-financial corporations and households (12-month moving average) (October 2005–August 2019)



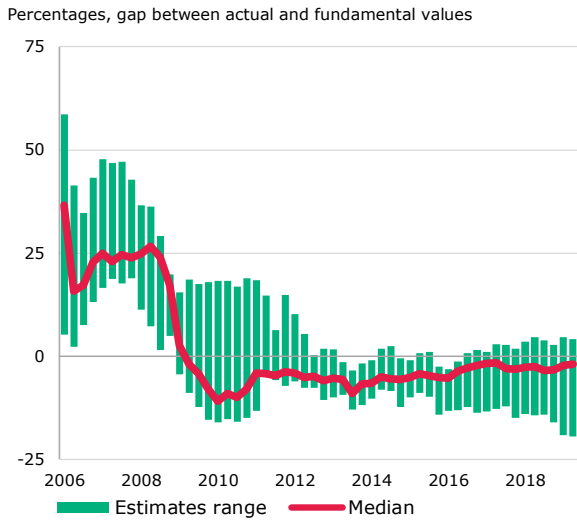
Source: Bank of Lithuania.

Chart 8. Annual change in the number of housing transactions and the house price index (HPI) (Q1 2010–Q3 2019)



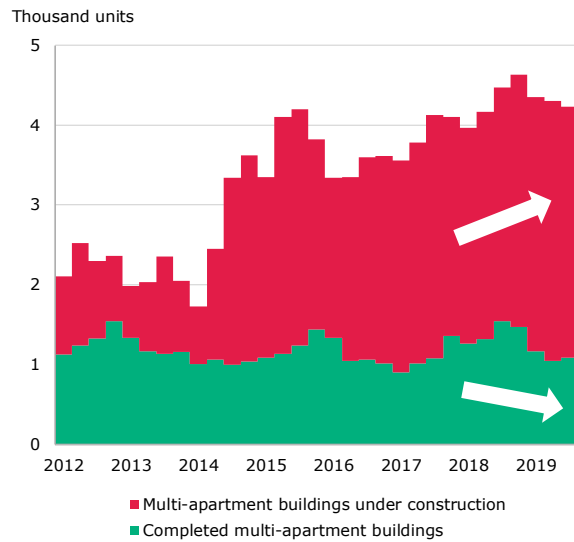
Sources: Centre of Registers and Statistics Lithuania.

Chart 9. Gap between actual house prices and their fundamental values  
(Q1 2006–Q2 2019)



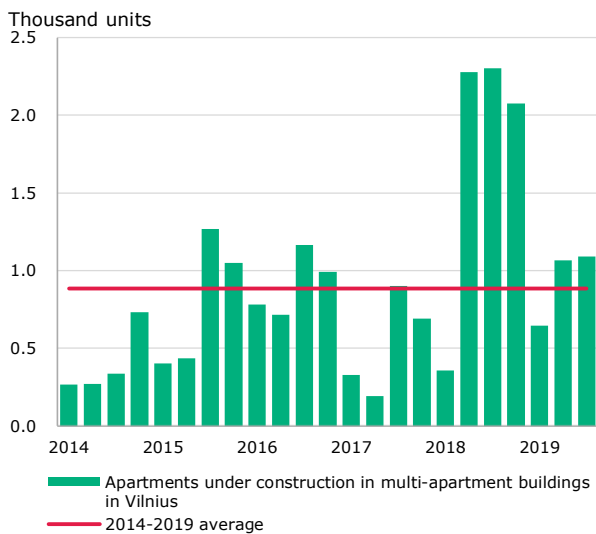
Source: Bank of Lithuania.  
Note: Calculated based on the house price-to-rent ratio, house price-to-income ratio, an econometric model and the HP filter.

Chart 10. Number of unsold apartments in under-construction and completed multi-apartment buildings in Vilnius  
(Q1 2012–Q3 2019)



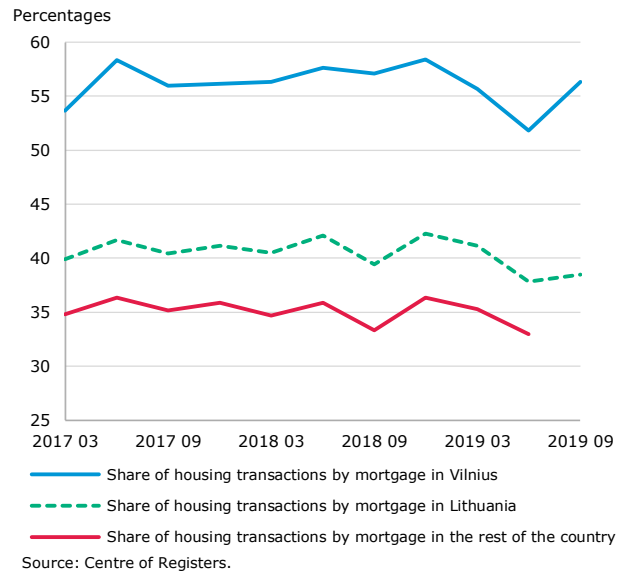
Sources: UAB Ober-Haus and UAB Eika.

Chart 11. Under-construction apartments in multi-apartment buildings in Vilnius  
(Q1 2014–Q3 2019)



Source: Statistics Lithuania.

Chart 12. Share of housing transactions by mortgage  
(Q1 2017–Q3 2019)

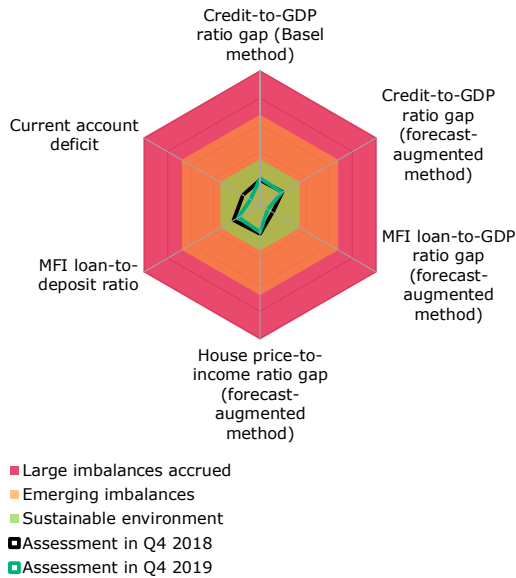


Source: Centre of Registers.

## ANNEX 2. CREDIT AND HOUSING MARKET IMBALANCES

Chart A. Evaluation of credit market imbalances based on core and additional indicators

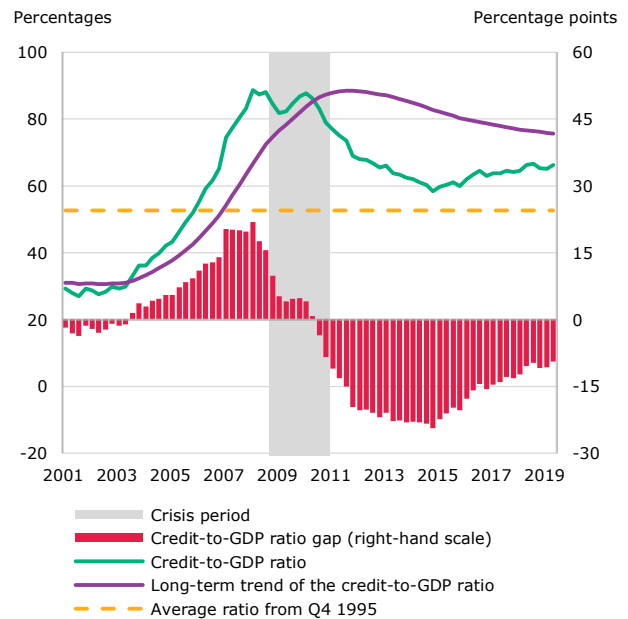
(Q4 2019)



Sources: Statistics Lithuania and Bank of Lithuania calculations.  
Note: Axes are scaled according to the range of a particular indicator: from its minimal value up to the maximal value.

Chart B. Core indicator I: Credit to the private non-financial sector-to-GDP ratio gap (calculated using the standardised Basel method)

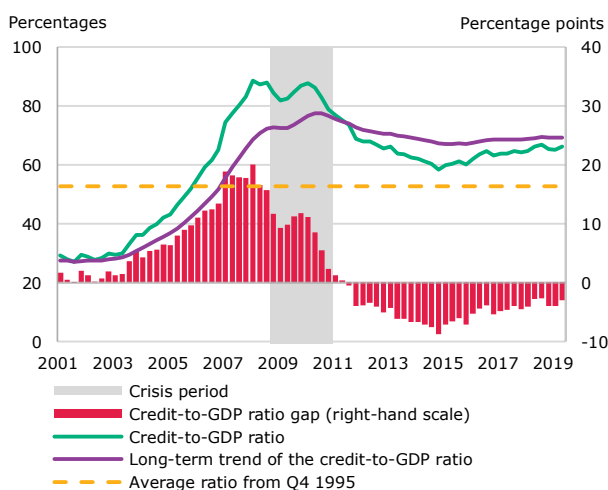
(Q1 2001–Q2 2019)



Sources: Statistics Lithuania and Bank of Lithuania calculations.  
Note: The long-term trend is computed using a one-sided HP filter with a smoothing parameter of 400,000.

Chart C. Core indicator II: Credit to the private non-financial sector-to-GDP ratio gap (based on the forecast-augmented method)

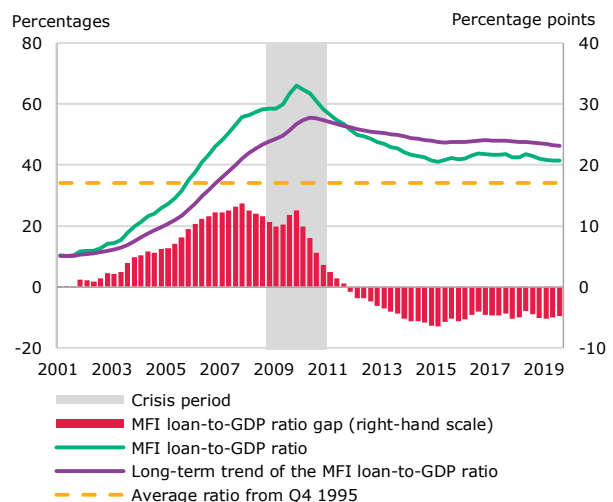
(Q1 2001–Q2 2019)



Sources: Statistics Lithuania and Bank of Lithuania calculations.  
Note: The long-term trend is computed by applying a one-sided HP filter with a smoothing parameter of 400,000; before applying the filter, the ratio is modelled for the next 5-year window using a 4-quarter weighted average.

Chart D. Additional indicator I: MFI loan to the private non-financial sector-to-GDP ratio gap (calculated using the forecast-augmented method)

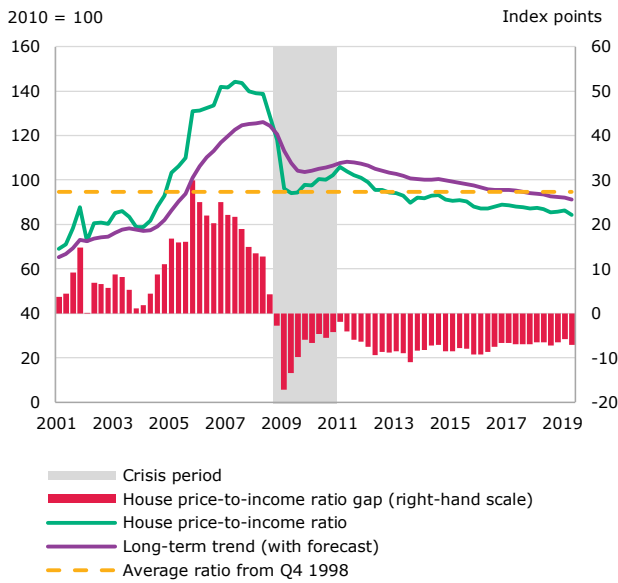
(Q1 2001–Q3 2019)



Sources: Statistics Lithuania and Bank of Lithuania calculations.  
Note: The long-term trend is computed by applying a one-sided HP filter with a smoothing parameter of 400,000; before applying the filter, the ratio is modelled for the next 5-year window using a 4-quarter weighted average.

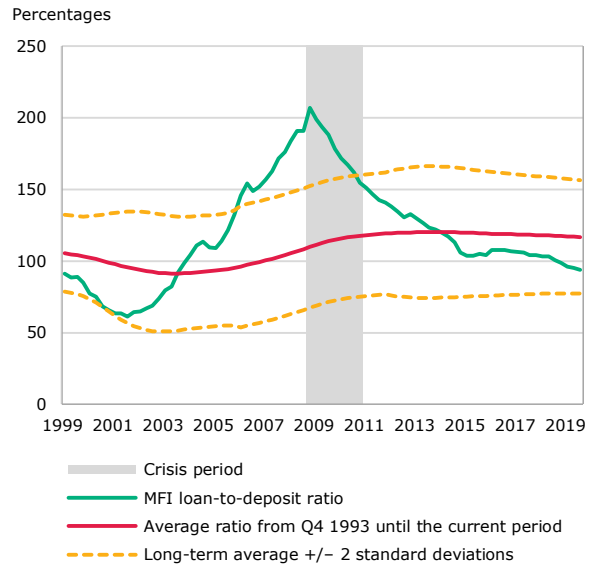


Chart E. Additional indicator II: House price-to-income ratio gap (calculated using the forecast-augmented method) (Q1 2001–Q2 2019)



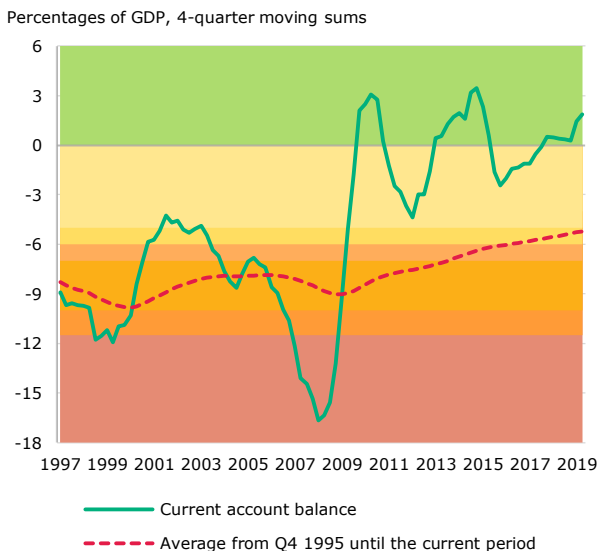
Sources: Statistics Lithuania and Bank of Lithuania calculations.  
Notes: 1) Income – household wages and salaries; 2) The long-term trend is estimated by applying a one-sided HP filter with a smoothing parameter of 400,000; before applying the filter, the ratio is modelled for the next 5-year window using a 4-quarter weighted average.

Chart F. Additional indicator III: Ratio between MFI loans to the private sector and private sector deposits (adjusted for seasonal effects) (Q1 1999–Q3 2019)



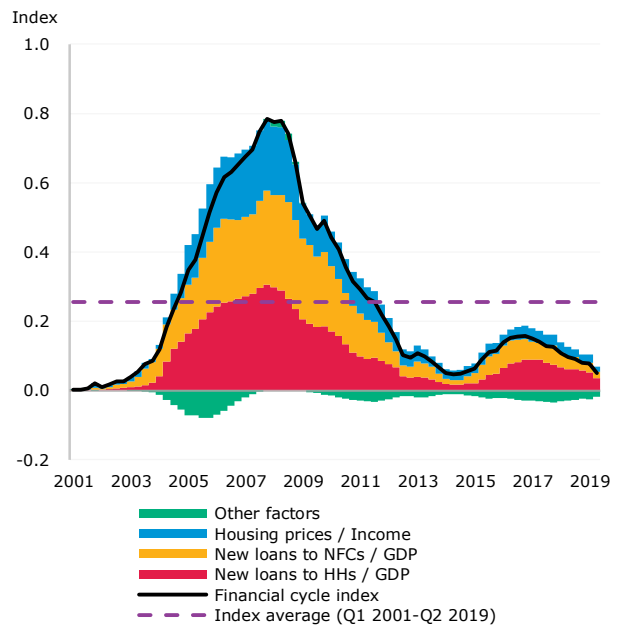
Source: Bank of Lithuania calculations.  
Notes: The ratio develops in a balanced way if it does not deviate from its long-term average by more than two standard deviations. Standard deviation is computed on the basis of data covering the period of moderate changes in the ratio, excluding data for Q2 2006–Q4 2011.

Chart G. Additional indicator IV: Ratio between the current account balance (4-quarter moving sums) and GDP (Q1 1997–Q2 2019)



Sources: Statistics Lithuania and Bank of Lithuania calculations.  
Note: Different colours indicate different levels of risk which have been set based on Reinhart S. M. and V. R. Reinhart (2008): "Capital flow bonanzas: An encompassing of the past and present", NBER working paper, 14321.

Chart H. Contributions to Lithuania's financial cycle index (Q1 2001–Q2 2019)



Sources: Statistics Lithuania and Bank of Lithuania calculations.