



CONSUMER LENDING IN THE EU BANKING SECTOR

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Executive summary

Consumer lending in the EU banking sector has recorded substantial growth rates across most countries in recent years. In September 2019, EU banks' exposure to consumer loans stood at EUR 1.14 trillion, up by 14% compared with September 2015 (EUR 1 trillion). This has outpaced overall credit growth (+10%) over the same period.

The high growth in consumer lending may be attributed to strong demand due to benign macroeconomic conditions, with declining unemployment as well as increasing disposable income and private consumption supported by consumer confidence. On the supply side, in a low to negative interest rate environment banks are keen to supply unsecured credit, seeking yield and better returns.

Despite the increased growth, consumer loans still represent only a small part of the aggregate loan portfolio of EU banks. In September 2019, consumer loans were 5.6% of total loans at amortised cost. However, banks in central and eastern Europe report increases in consumer loans as a proportion of total loans that ranged from 10% to 20%.

Consumer loans also tend to show higher than average impairment rates compared with other segments. In September 2019, 5.5% of the consumer loans granted by EU banks were non-performing, whereas the average EU non-performing loan rate stood at 2.9%.

In an environment of persistently low/negative interest rates, deteriorating macroeconomic forecasts and lagging profitability, banks may be inclined to increase exposures to riskier products with increased margins and to lower credit standards. Supervisors are encouraged to monitor closely developments in consumer lending to identify in a timely manner potential pockets of risk associated with this segment.

The EBA is also looking at improving banks' lending standards and loan origination practices, including assessments of borrowers' creditworthiness, in Guidelines on loan origination and monitoring, which deal with, among other topics, specific requirements for creditworthiness assessments in relation to consumer loans.

1. Introduction

1. Consumer lending is defined as loans extended to individuals for personal use in the consumption of goods and services (e.g. vehicles and electronics), typically through credit cards. This would exclude, for example, loans granted for purposes of education or debt consolidation.¹ Consumer credit generally takes the form of revolving credit² or instalment loans.
2. Consumer loans represent a small part of the aggregate loan portfolio of EU banks. In September 2019, consumer loan volumes stood at EUR 1.14 trillion, which is 5.6% of total loans at amortised cost and 14.7% of loans to households.³ The total amount of household lending in the EU stood at EUR 7.78 trillion, of which EUR 5.29 trillion was mortgage lending. However, some countries have particularly high consumer lending as a proportion of total loans, in particular, Hungary (20%), Bulgaria (17%), Romania (16%), Slovenia (15%) and Poland (13%).
3. EU banks' exposure to consumer loans has increased significantly (+14%) over the past 4 years, (EUR 1 trillion in September 2015), outpacing overall credit growth (+10%) over the same period. During this period, the growth in consumer lending has been widely dispersed across countries. On average, consumer lending increased by 3% per year, and during the first three quarters of 2019 it increased by 5.3% (total loans increased by 3.4% in the same period). This growth may be attributed to:
 - a. strong borrower demand due to better macroeconomic conditions observed over recent years in a few countries. Decreasing unemployment has increased disposable income and private consumption has been boosted by growing consumer confidence;
 - b. banks searching for higher returns in a low interest environment.
4. Owing to the intrinsically riskier nature of consumer loans, as they are typically unsecured, they tend show higher impairment rates than mortgage loans but higher coverage ratios too (in

¹ As defined in the Implementing technical standards on supervisory reporting, Annex V, Part 2.88(a), credit for consumption includes loans granted mainly for the personal consumption of goods and services (European Central Bank (ECB) Balance Sheet Item (BSI) Regulation). The ECB BSI Regulation, Part 3 (<https://www.ecb.europa.eu/ecb/legal/pdf/02001r2423-20080104-en.pdf>), defines three main categories as loans granted to households: 'loans granted to households in the form of consumer credit (loans granted for the purpose of personal use in the consumption of goods and services), lending for house purchases (credit extended for the purpose of investing in housing, including building and home improvements) and other (loans granted for purposes such as business, debt consolidation, education, etc.). Lending for house purchases comprises loans secured on residential property that are used for the purpose of house purchase and, where identifiable, other loans for house purchases made on a personal basis or secured against other forms of assets'.

² Revolving credit is a type of credit facility that allows drawdown of credit, up to a fixed credit limit, and repayments on a flexible basis subject to a minimum amount paid in each period. Repayments refresh the available credit. If the minimum repayment amount is low, relative to the amount outstanding, and the consumer chooses not to repay more, it can take a long time to repay the principal, and total interest charges may be high.

³ EBA supervisory data have been used for EU figures from FINREP data. These data cover 147 banks in European Economic Area countries, which is roughly 80% of the total EU banking sector. The sample of banks included in each year may differ.

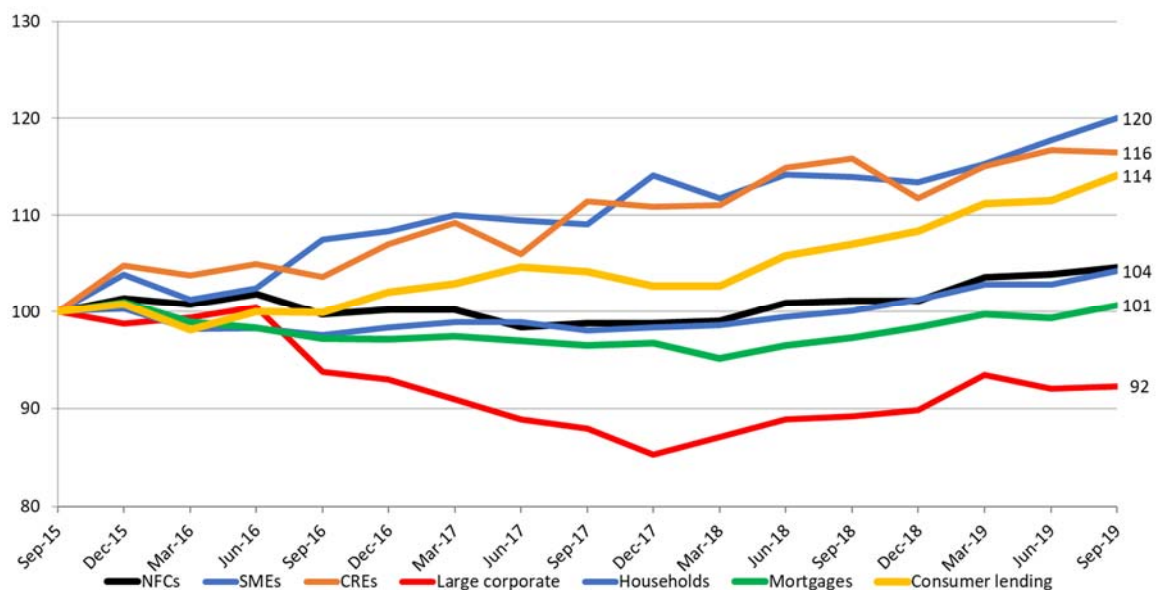
September 2019, consumer loans had a coverage ratio of more than 60%, considerably higher than any other lending segment). In September 2019, 5.5% of EU banks' stock of consumer loans were non-performing, whereas the average EU non-performing loan (NPL) rate stood at 2.9%. The higher delinquency rate of consumer loans is compensated for by higher interest rates than those paid on other personal credit, such as mortgage loans.

5. In an environment of persistently low/negative interest rates, deteriorating macroeconomic forecasts and lagging profitability, banks may be inclined to increase exposures to riskier products with increased margins and to lower credit standards.
6. The purpose of this note is to assess in detail supervisory data available for this portfolio to assess risks associated with EU banks' consumer lending, identifying potential vulnerabilities for the banks and financial system, if any, that may arise from these exposures.

2. Consumer lending in the EU

8. Consumer lending at EU level has been increasing in volume since September 2015.⁴ The growth rates reported are significantly higher than those for mortgage and household lending. Between September 2015 and September 2019, consumer lending grew by 14.1%. Volumes reached EUR 1.14 trillion at the end of the September 2019. In contrast, lower growth rates were reported for mortgage and total household loans, at 0.7% and 4.3% respectively. During the same period, only the small and medium-sized enterprise (SME) and commercial real estate (CRE) segments reported slightly higher growth than consumer lending (20% and 16% respectively). However, during the past year consumer lending has shown the highest growth, with an increase of 6.6% (Figure 1).

Figure 1: Growth of non-financial corporate (NFC) and household sub-segments at amortised cost (September 2015 = 100), September 2015 to September 2019

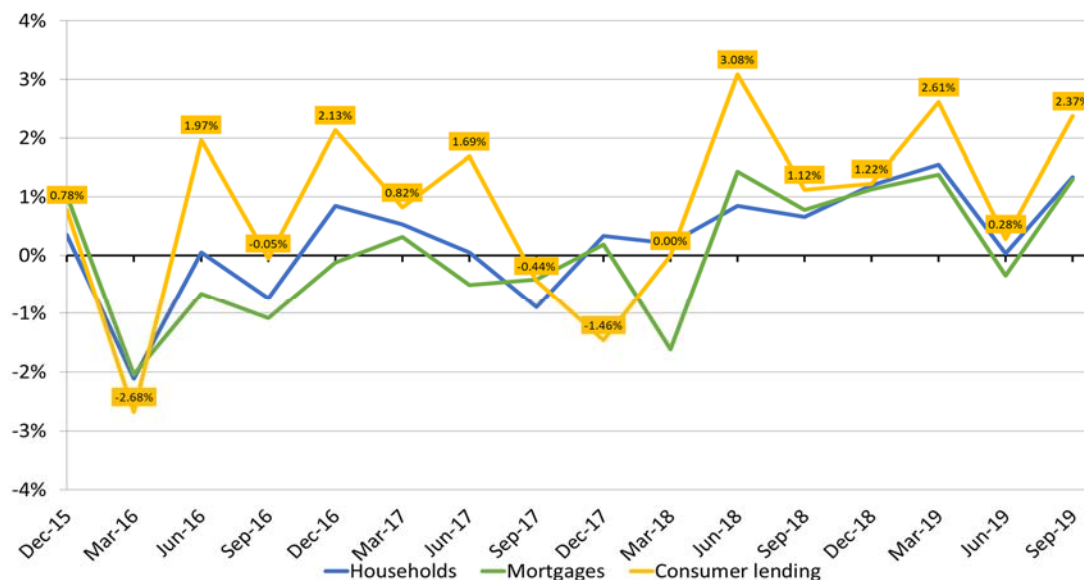


Source: EBA supervisory data.

9. The quarterly growth rates of consumer loans have been consistently higher than those of other household loans (e.g. mortgage loans). In addition, consumer lending is reported to have grown by around 11% since March 2018, outpacing by a significant margin all other lending segments (Figure 1 and Figure 2).

⁴ Based on available EBA supervisory data.

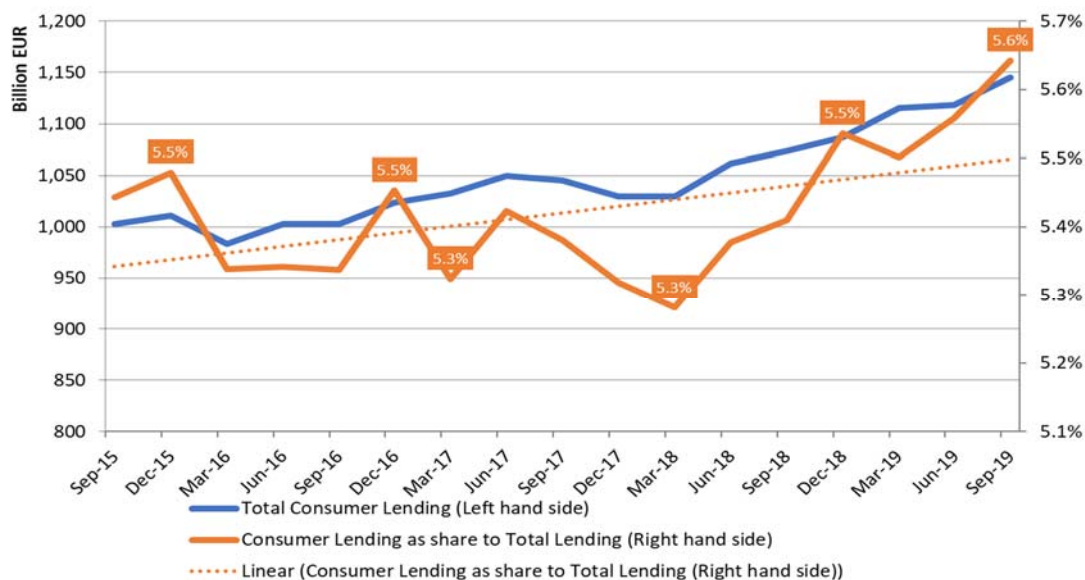
Figure 2: Quarterly growth rates of consumer, mortgage and total household lending, EU aggregate, September 2015 to September 2019



Source: EBA supervisory data.

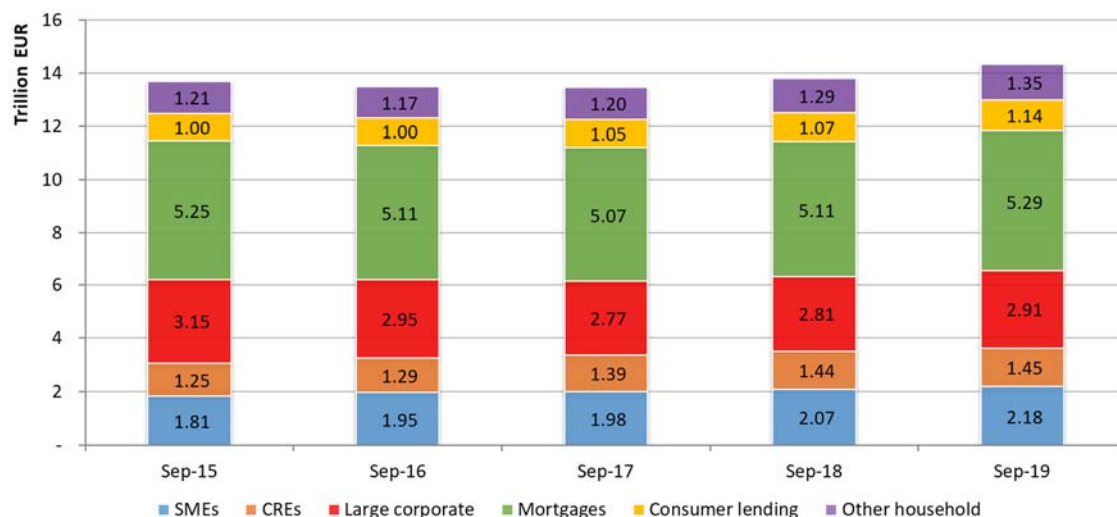
10. Despite the strong growth in recent years, consumer lending as a proportion of total loans has not significantly changed. The amount of consumer lending as a proportion of total loans and advances at amortised cost increased by just 20 bp between September 2015 and September 2019 (from 5.4% to 5.6%). During the same period, consumer lending gained in size as a proportion of total household lending, expanding from 13.4% in September 2015 to 14.7% by September 2019 (Figure 3 and Figure 4).

Figure 3: Evolution of consumer lending in comparison with total loans and advances, EU aggregate, September 2015 to September 2019



Source: EBA supervisory data.

Figure 4: Evolution of consumer lending in comparison with other segments (household and NFC), September 2015 to September 2019



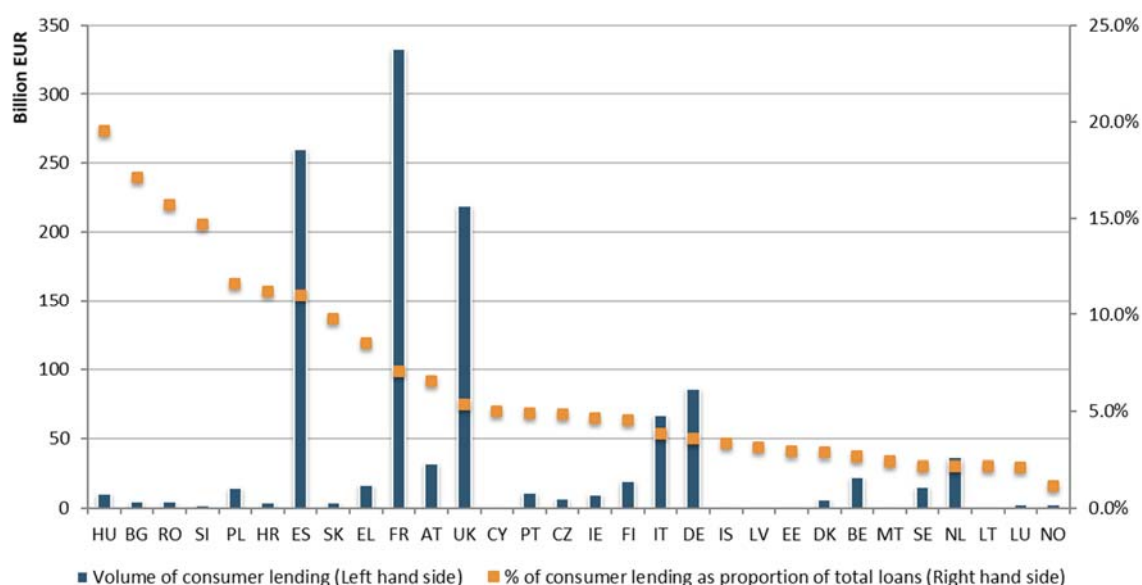
Source: EBA supervisory data.

11. In September 2019, banks in France (EUR 333 billion, 7% of total lending), Spain (EUR 260 billion, 11% of total lending) and the UK (EUR 219 billion, 5% of total lending) reported 75% of the total

consumer lending stock in the EU. They were followed by Germany (EUR 86 billion, 4% of total lending) and Italy (EUR 65 billion, 4% of total lending) (Figure 5).⁵

12. Central eastern European (CEE) countries had the highest figures for consumer lending as a proportion of total lending. In particular, of Hungarian banks’ total lending, 20% was towards consumer credit; Hungary was followed by Bulgaria (17%), Romania (16%), Slovenia (15%) and Poland (12%) (Figure 5).⁶

Figure 5: Volumes of consumer lending (billion EUR) and consumer lending as a proportion of total lending (%) by country, September 2019



Source: EBA supervisory data.

13. The growth of consumer lending across the EU in the past 4 years⁷ has been driven mainly by France and Spain, which have the largest volumes of consumer lending and also reported strong growth rates during this period. Spanish banks increased their exposures by more than 25%, while French banks increased theirs by around 20%. CEE countries, which report increases in consumer lending as a proportion of total lending, increased their reported volumes of consumer lending by 50% on average, significantly higher than the EU average. In fact, more than half of EU countries reported at least a double-digit percentage increase in consumer lending in recent years. However, volumes of consumer lending in Greece were affected by the general deleveraging of the Greek banking sector and decreased significantly (−50%), while

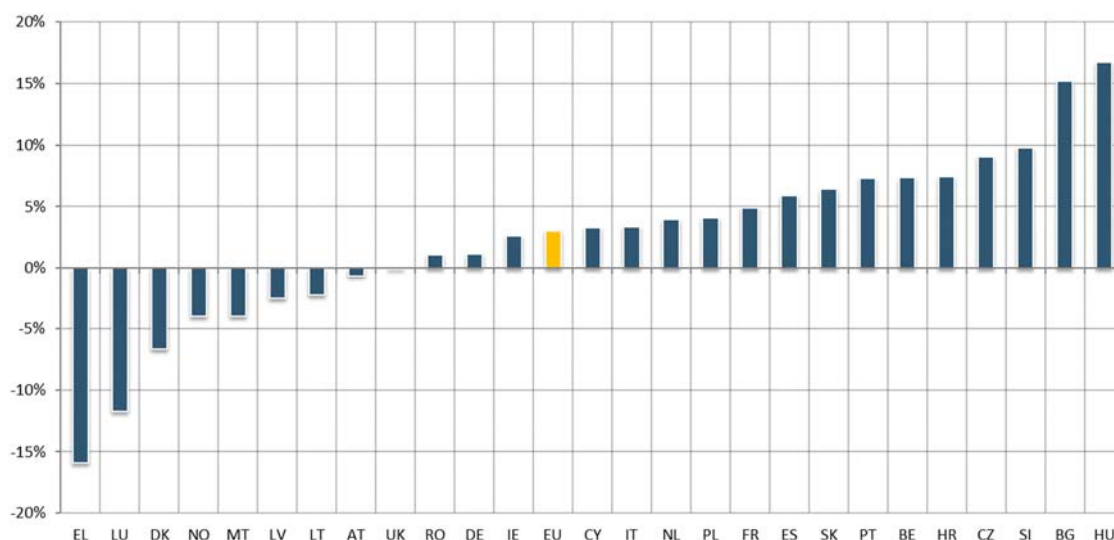
⁵ Percentages shown in brackets are total consumer lending as a proportion of total lending in the Member State in question. Figures are for the highest level of consolidation.

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⁷ Growth rates were calculated using a homogeneous sample of banks for each country.

annualised growth rates were reported around -15%. A few other countries have also reported negative growth rates during the same period (Figure 6).

Figure 6: Annualised growth rates of consumer lending by country, September 2015 to September 2019^a



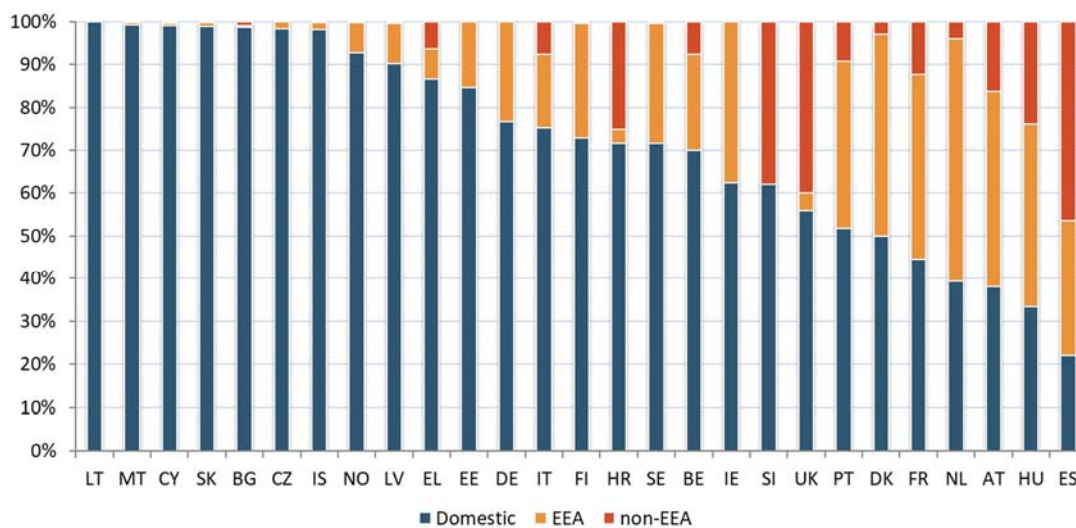
^aFinland and Sweden have been excluded due to significant change in sample. In addition Norwegian consumer lending market is dominated by several niche banks which have considerably grown the last years, and which are not represented in the EBA sample.

Source: EBA supervisory data.

14. The data show that, in September 2019, several countries also had increased consumer credit exposures to non-EU countries. In particular, in eight countries at least 10% of total consumer credit loans were extended to non-EU counterparties. Spain, the UK and Slovenia reported higher proportions of consumer lending to non-EU consumers (Figure 7).⁸

⁸ This is mostly done through branches or subsidiaries.

Figure 7: Distribution of consumer lending loans by domicile of counterparty, September 2019^a



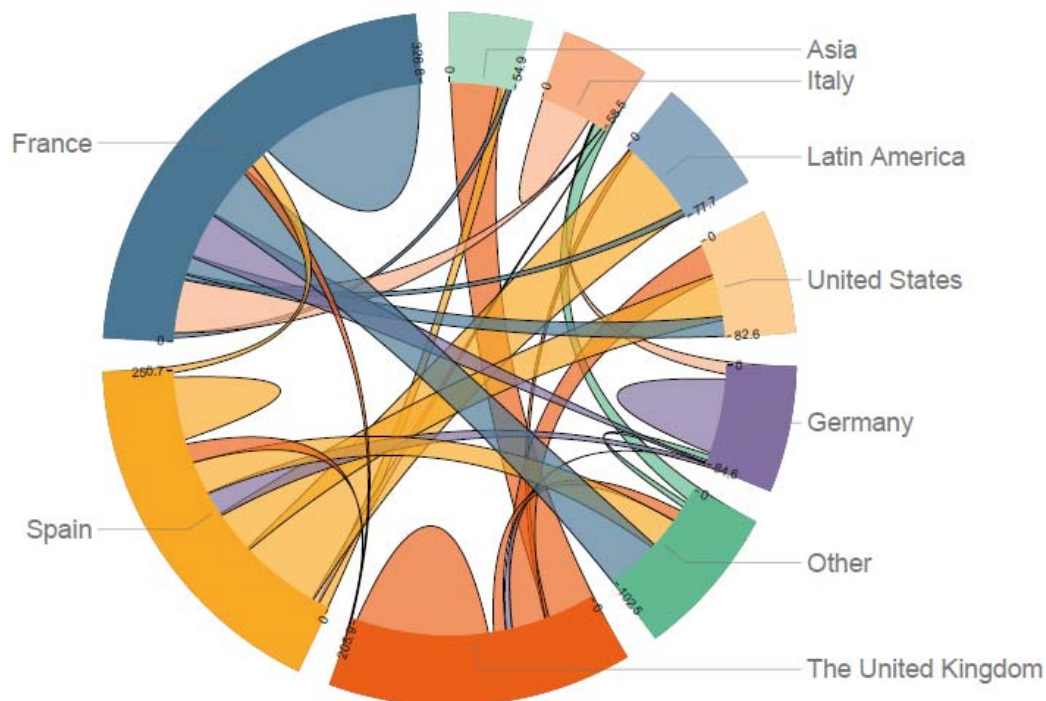
^aBased on financial reporting (FinRep) template 20.04. Some entities are not required to report the data if they do not exceed certain thresholds. Luxembourg is excluded from the graphical representation.

Source: EBA supervisory data.

15. Figure 8⁹ shows the exposures of the five EU countries with the largest volumes of consumer lending granted by domestic banks by domicile of counterparty. France has about 45% domestic exposure and around 33% exposure to counterparties domiciled in Italy, Germany, Spain and the UK. Spain⁹, however, has only 20% domestic exposures and significant exposures to Latin America. France, the UK and Spain have considerable exposures to US counterparties.

⁹ For Spanish banks, this is mostly done through branches or subsidiaries that are funded by local funds.

Figure 8: Heatmap distribution of the exposures of the five EU countries with the largest volumes of consumer lending by domicile of counterparty, September 2019^a



^aBased on FinRep template 20.04. Some entities are not required to report the data if they do not exceed certain thresholds.

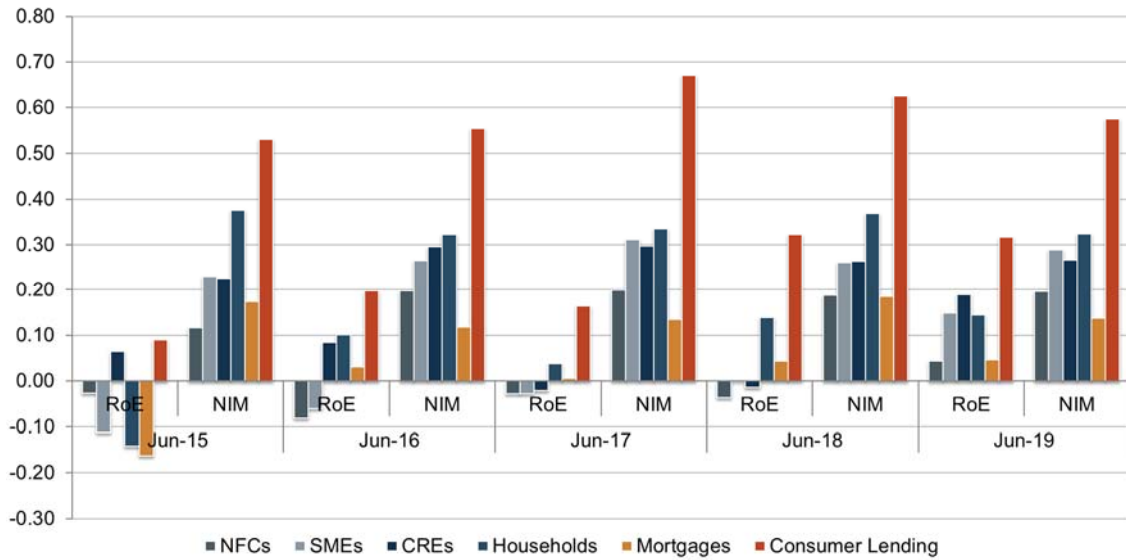
Source: EBA supervisory data.

3. Risks of consumer lending

3.1 Profitability of the consumer lending segment

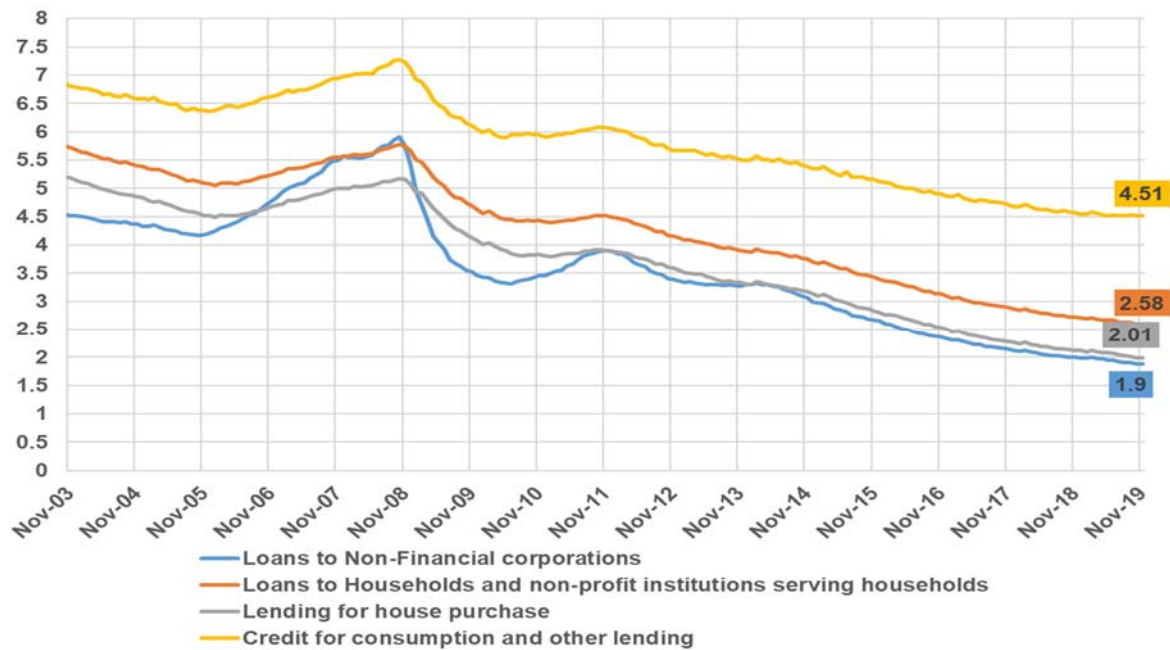
16. A bank that allocates a relatively high proportion of its portfolio to consumer lending usually has a relatively high net interest margin. In other words, the consumer lending as a proportion of total loans has a stronger link with net interest margin than other lending segments. A similar conclusion can be drawn with regard to return on equity, as this is also positively affected by an increased consumer lending allocation. This may be partly driven by a causality effect, as CEE countries, which have higher policy rates than other jurisdictions, have also increased asset allocation to consumer lending. Nevertheless, margins for consumer lending have historically been attractive to banks, as they have been significantly higher than those for any other lending segment (Figure 9 **Error! Reference source not found.** and Figure 10 **Error! Reference source not found.**).

Figure 9: Correlation of asset allocation with net interest margin (NIM) and return on equity (RoE), June 2015 to June 2019



Source: EBA supervisory data.

Figure 10: MFI interest rate statistics for outstanding loans by segment, November 2003 to November 2019^a



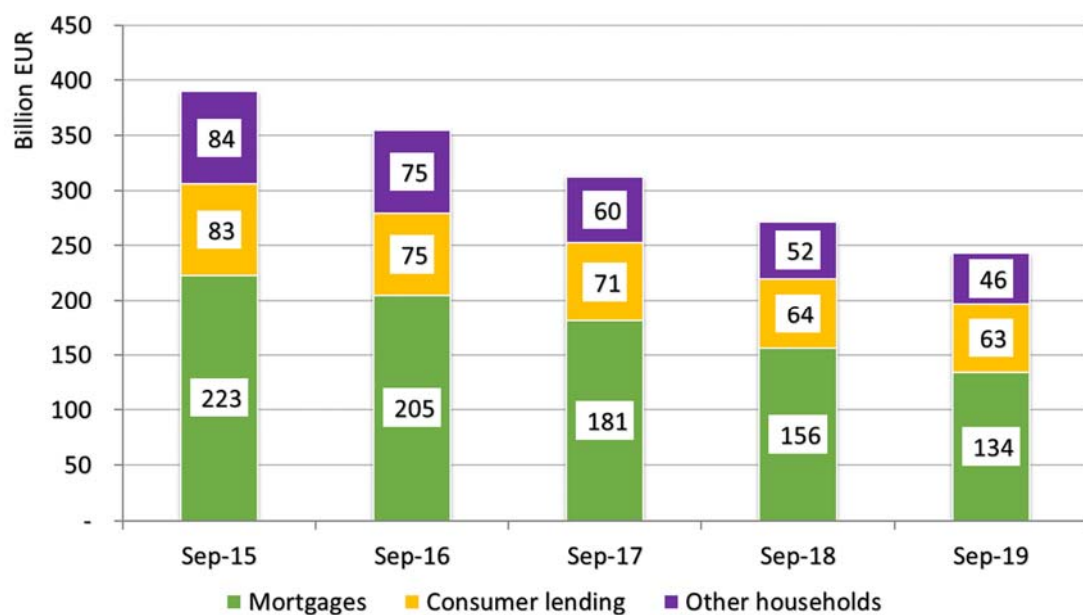
^aFor a definition of MFI interest rates, see https://www.ecb.europa.eu/stats/financial_markets_and_interest_rates/bank_interest_rates/mfi_interest_rates/html/index.en.html.

Source: European Central Bank Statistical Data Warehouse.

3.2 Non-performing consumer loans

17. In September 2019, the volume of consumer lending NPLs stood at EUR 63.2 billion, having decreased from EUR 83 billion in September 2015. The decrease in consumer lending NPLs (24%) was significantly smaller than the overall decrease in total NPL volume (around 45%). An explanation for this may be that consumer loans are generally small amounts per loan and unsecured, and therefore harder to cure. In many cases, banks may lack the critical mass needed to sell these portfolios in the secondary market. In addition, as a result of a loosening of credit standards, inflows of NPLs could be relatively high in this segment. In September 2019, consumer lending NPLs represented more than 25% of household NPLs and roughly 10% of total NPLs (Figure 11).

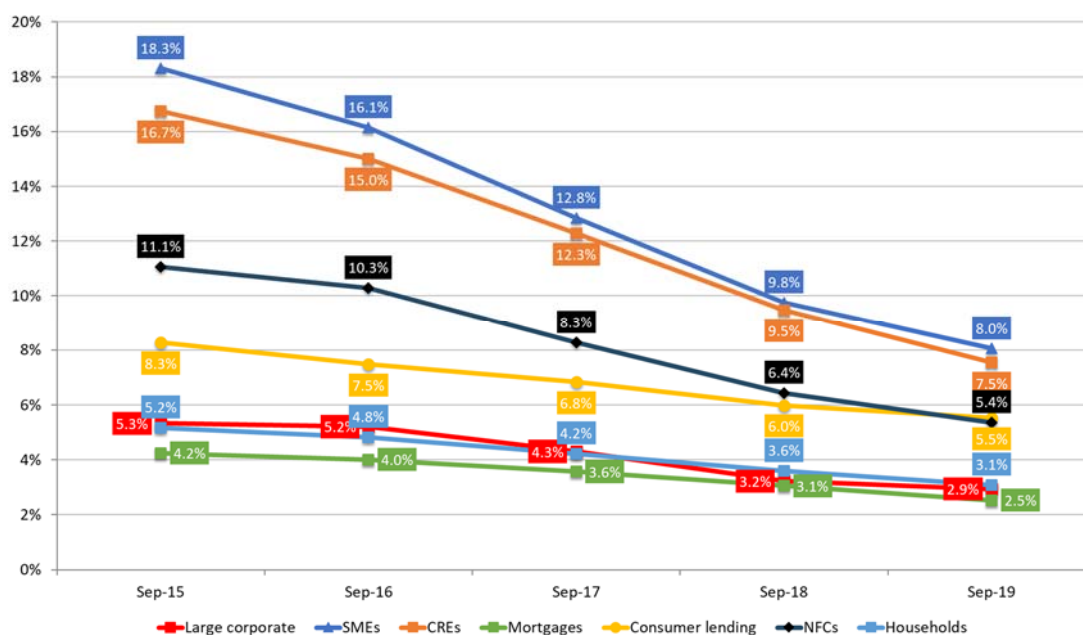
Figure 11: Consumer NPLs compared with other household NPLs and mortgage NPLs (billion EUR), September 2015 to September 2019



Source: EBA supervisory data.

18. In September 2019, the NPL ratio for consumer lending stood at 5.5%, having decreased from 8.3% in September 2015 (a 2.8 percentage point (p.p.) change). However, it remains significantly higher than the overall NPL ratio (2.9% in September 2019). By way of comparison, the mortgage NPL ratio decreased by 1.7 p.p. (from 4.2% in September 2015 to 2.5% in September 2019). The NPL ratio for consumer lending was lower only than the NPL ratios for SME and CRE lending; significantly higher NPL ratios were reported for these segments (Figure 12).

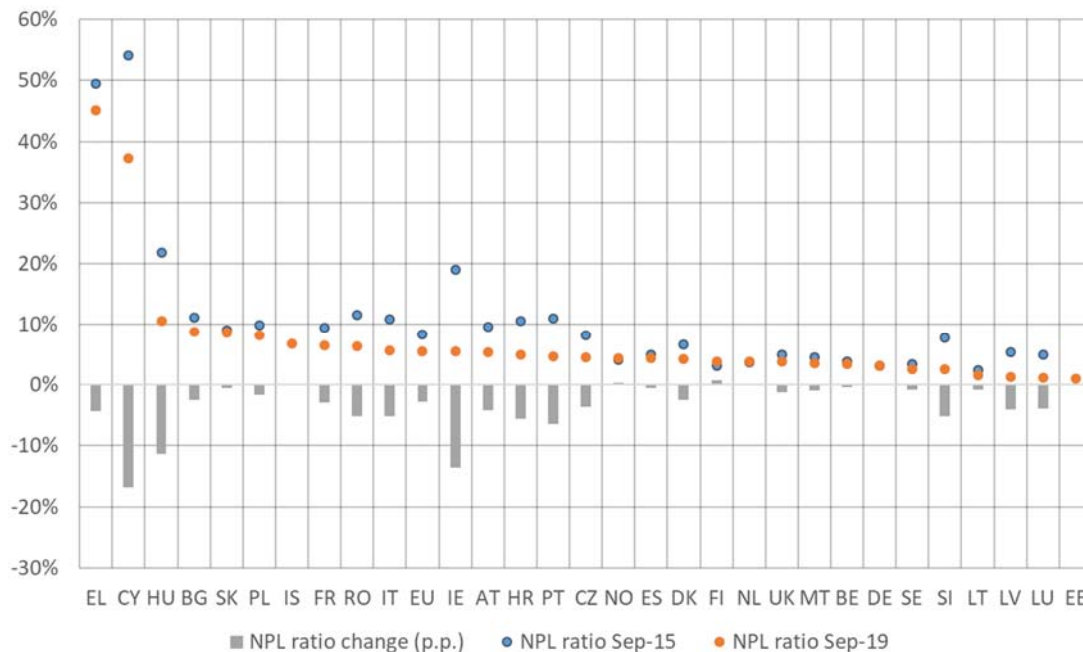
Figure 12: Trends in the NPL ratio by segment, September 2015 to September 2019



Source: EBA supervisory data.

19. With the exception of Greece, Cyprus and Hungary, in September 2019 all EEA countries reported a single-digit NPL ratio for consumer credit exposures. Greece and Cyprus reported double-digit NPL ratios for all lending segments. NPL ratios have in fact considerably decreased since 2015 for all countries except Greece (again, driven by the significant deleveraging of the banking sector, i.e. there has been an approximately 50% decrease in both the numerator and the denominator). Consumer lending NPL ratios are, however, still high compared with NPL ratios for total loans and advances. It is therefore important that these exposures are closely monitored, especially given the high sensitivity of these exposures to economic cycles (Figure 13).

Figure 13: Consumer NPL ratios (%) in September 2015 and September 2019 and changes in the ratios between September 2015 and September 2019, by country

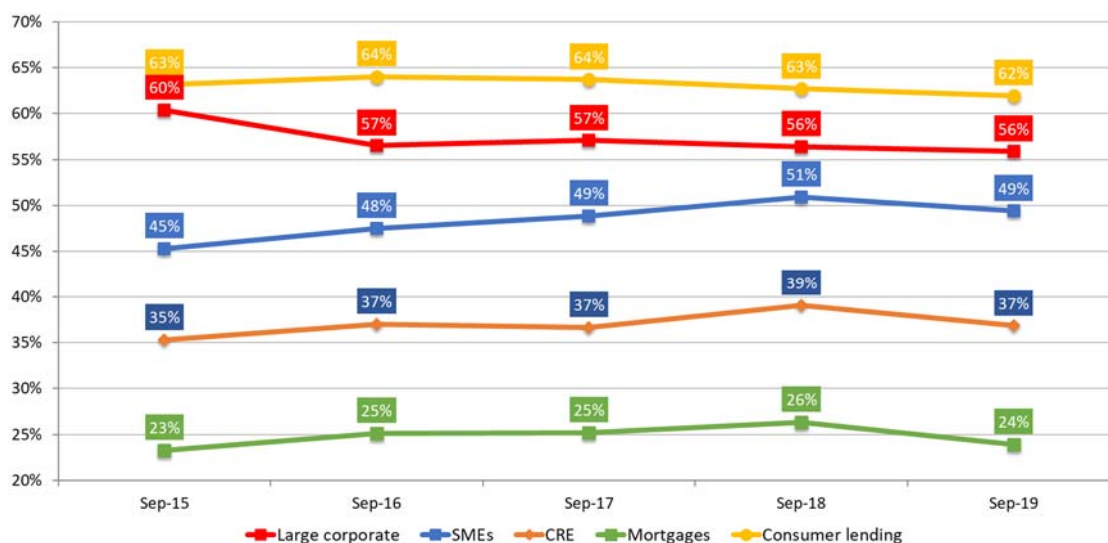


Source: EBA supervisory data.

3.3 Coverage of consumer loans

20. The coverage ratio for consumer lending NPLs is considerably higher than for all other lending segments (including NFCs). In September 2019, more than 60% of consumer lending NPLs were provisioned against potential losses. A comparison shows that mortgage NPLs had the lowest coverage ratio, at around 25%. However, this is largely driven by the fact that mortgage loans are highly collateralized, whereas consumer lending consists mostly of unsecured loans. NPLs to SMEs and large corporates were slightly less well provisioned than consumer lending. The coverage ratios for all segments have been fairly steady since September 2015 (Figure 14).

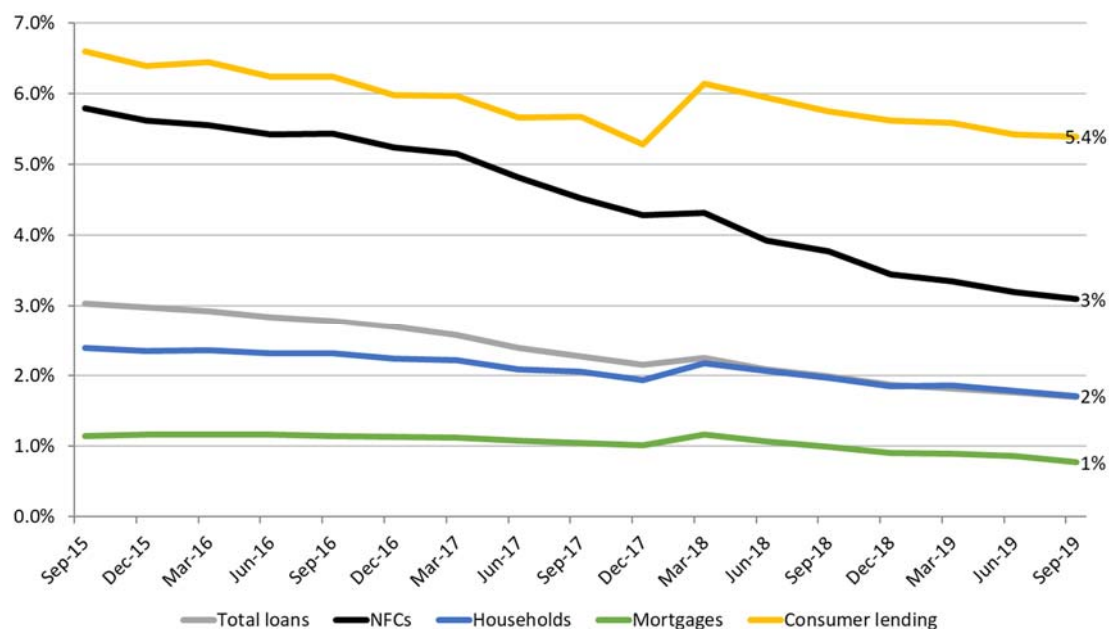
Figure 14: Evolution of coverage ratios for NPLs by segment, September 2015 to September 2019



Source: EBA supervisory data.

21. Provisions for performing loans decreased between 2015 and 2019 (to 1.7% from 3%). As for NPLs, performing consumer lending had a higher coverage ratio than other segments. However, the coverage ratio for performing consumer loans decreased slightly from 6.6% in 2015 to 5.4% in 2019. A comparison shows that consumer loans are the riskiest subgroup, as the coverage ratio for performing loans has a higher value than those for other segments. In general, downwards trends in coverage ratios for performing loans suggest that banks' estimations of credit risk have reduced since 2015 for all types of lending (Figure 15).

Figure 15: Evolution of coverage of performing loans: consumer lending in comparison with total loans, NFC loans, total household loans and mortgages (%), September 2015 to September 2019



Source: EBA supervisory data.

3.4 Other risks linked with consumer lending

22. In the past, aggressive consumer lending coupled with extremely high interest rates charged for consumer loans have been connected with misconduct and/or misselling practices. Currently, increasing competition (including from other financial institutions and financial technology (FinTech) companies) may also ignite a race to the bottom by encouraging a loosening of credit standards.

23. Information received from competent authorities suggests that the average maturity for consumer loans varies between countries, but it is partly determined by the purpose of the loan (e.g. financing a car purchase). In this regard, competent authorities suggest that the average maturity ranges from 3 years to 7.5 years. Some countries, such as Czechia, Hungary, Italy, the Netherlands, Portugal, and Slovenia, reported a trend towards longer maturities in newly offered consumer loans. Moreover, in some countries banks offer consumer loans with maturities extending to up to 10 years.

24. A similar increasing trend, most evident in eastern European countries, is observed with regard to the average amount of new consumer loans. The value of the average consumer loan differs quite significantly across countries.

25. Based on input received from national competent authorities, consumer associations and other sources, the EBA's 2-yearly consumer trends report¹⁰ identifies several consumer protection issues arising from consumer credit, such as the high cost of short-term consumer credit, misuse of consumer credit, poor creditworthiness assessment practices, over-indebtedness and arrears, insufficient pre-contractual information and inadequate information over the lifetime of the contract.
26. To address these growing risks and to ensure adequate protection for consumers, the EBA, in its Guidelines on loan origination and monitoring, reinforces the consumer protection dimension. In particular, the new guidelines set out requirements for institutions' credit governance arrangements with regard to the design and application of credit granting standards and assessments of borrowers' creditworthiness. This is achieved by establishing specific requirements applicable to lending to consumers.

4. Consumer lending outlook

4.1 Outlook based on surveys

27. The Risk Assessment Questionnaires (RAQs) run by the EBA show an increasing appetite among respondents to increase their exposures to consumer lending. In particular, 80% of the 65 banks participating in the autumn 2019 RAQ planned to increase consumer credit volumes in the next 12 months. By way of comparison, only 65% of respondents to the 2017 questionnaire intended to increase volumes of consumer credit. In fact, in the autumn 2019 RAQ, the number of banks aiming to increase consumer lending exposures came second only to the number of banks aiming to increase exposures to the SME segment (85%).
28. According to the autumn 2019 RAQ results, only 40% of banks expect an improvement in the asset quality of this segment (the second lowest percentage by segment after CRE), while 25% even expect a deterioration in quality. Few banks in CEE countries or Spain indicated plans to increase exposures to consumer lending, but, at the same time, they expect a deterioration in the asset quality of the segment.
29. By contrast, the European Central Bank's Bank Lending Survey (BLS),¹¹ covering the euro area, reveals that in recent quarters (since Q3 2018), credit standards applied to the approval of consumer credit and other lending to households have tightened, following an extended period of easing. In particular, the net percentage¹² in Q4 2019 stood at 3%, mainly as a result of banks' decreased risk tolerance. The result was particularly driven by Spanish banks, perhaps owing to

¹⁰ <https://eba.europa.eu/sites/default/documents/files/documents/10180/2551996/75e73a19-d313-44c9-8430-fc6eca025e8b/Consumer%20Trends%20Report%202018-19.pdf?retry=1>

¹¹ https://www.ecb.europa.eu/stats/ecb_surveys/bank_lending_survey/html/index.en.html

¹² The difference between the percentage of banks reporting that credit standards applied to loan approval have been tightened and the percentage of banks reporting that they have been eased.

increased scrutiny on the part of the Spanish authorities of the relatively high growth in loans to consumers, which may have affected banks' risk tolerance.

30. The BLS also reveals that terms and conditions for consumer credit have eased slightly compared to previous quarter as a result of a decrease in margins on average loans. This follows previous quarters in which terms and conditions eased significantly. This was also as a result of decreasing margins on average loans. These were particularly evident in France and Germany, whereas in Spain increasing collateral requirements were particularly evident. It should also be noted that the rejection rate has continued its increasing trend.

31. Finally, according to the BLS, net demand for consumer credit increased in Q4 2019 to a net percentage of 10%, from 8% in Q3 2019. In fact, net demand has been positive for the past 2 years, driven by spending on durable goods, the general level of interest rates and consumer confidence. Looking at the largest euro area countries, banks in Germany, France and the Netherlands reported a positive contribution on the part of the general level of interest rates to demand for consumer credit.

4.2 Measures undertaken by countries to tackle growth in consumer lending

32. A number of countries – including Croatia, Cyprus, Hungary, Norway, Poland, Portugal, Romania, Slovakia, Slovenia, Sweden – have implemented various measures to tackle increased growth in consumer lending. Such measures include limitations on debt service, income ratios and the maturity of consumer loans, interest rate ceilings to protect consumers, and recommendations on prudent assessments of repayment ability.

5. Conclusion

33. Consumer lending is a growing segment in most of the countries of the EU. Owing to increases in both demand and supply, this segment has recorded a significant increase across many countries in recent years. Demand has been driven mainly by GDP growth and decreasing unemployment, whereas supply has been driven by low interest rates and a search for increased margins by banks.

34. In September 2019, consumer lending exposures as a proportion of all loans were small compared with other segments: less than 6% of total loans and advances were loans to consumers. However, there is significant dispersion of consumer lending as a proportion of total lending, as in some countries more than 15% of total lending consists of consumer lending. At the same time, data show that banks are aggressively extending credit to consumers and that consumer lending is growing faster than any other lending segment. In addition, it should be noted that consumer lending is provided extensively not only by banks but also by non-banking financial companies. While in the majority of jurisdictions non-banking financial companies are

subject to an equivalent prudential supervisory regime to banks, in some cases they are subject to a different and often less rigorous supervisory regime.

35. Aggressive lending coupled with extremely high interest rates may also give rise to consumer detriment and lead to increased conduct risk and conduct costs for banks, in the form of litigation costs, redress, compensation and/or fines imposed by supervisors. Increasing competition (including from other financial institutions and FinTech companies) may also ignite a race to the bottom by encouraging a loosening of credit standards, despite the conduct requirements set out in the EU Consumer Credit Directive.
36. Supervisors should note the sensitivity of consumer lending exposures to economic cycles given Europe's sluggish economy. This exists in parallel with the growing appetite of banks to increase their exposures to consumer credit despite its intrinsic riskiness (e.g. in the case of unsecured loans with no collateral and historically high NPL ratios). Data show that consumer credit loans have above average NPL ratios, but also that they have a higher coverage ratio than any other lending segment. In this regard, aggressive lending and fast growth in consumer lending should be monitored closely and duly scrutinised.
37. Supervisors should also keep in mind the requirement in the upcoming EBA Guidelines on loan origination and monitoring regarding internal governance arrangements for loan origination and creditworthiness assessment of borrowers, in particular consumers. The guidelines aim to improve institutions' loan origination practices to ensure that newly originated loans are of high credit quality.



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