Box 9

EVOLUTION OF EURO AREA BANKS' CUSTOMER FUNDING GAP

The customer funding gap is an indicator that is defined as net loans (i.e. gross lending to the non-financial sector minus provisions for non-performing loans) minus customer deposits. It shows whether banks have enough deposits to cover the expansion of their lending activities or whether they have to tap the money and capital markets to finance these activities. A customer funding gap can lead to funding risks in case liquidity unexpectedly ceases to be available, conditions experienced in autumn 2008 as well as the first half of 2010. This box looks at the development of the aggregated liabilities and at the evolution of the funding gap of the set of euro area banks that participated in the EU-wide stress-test exercise. The customer funding gap for this sample has increased in both absolute and relative (i.e. as a percentage of total assets) terms since 2005, although it declined in 2009 (see Chart A).

Publicly available balance sheet data for both the end of 2009 and the first six months of 2010 are available though for only 33 out of the 77 euro area banks considered. These 33 banks nevertheless represent approximately 74% of 2009 full euro area sample total assets. Total liabilities [1] increased by 9.7% over the first six months of 2010. This increase reflected a very

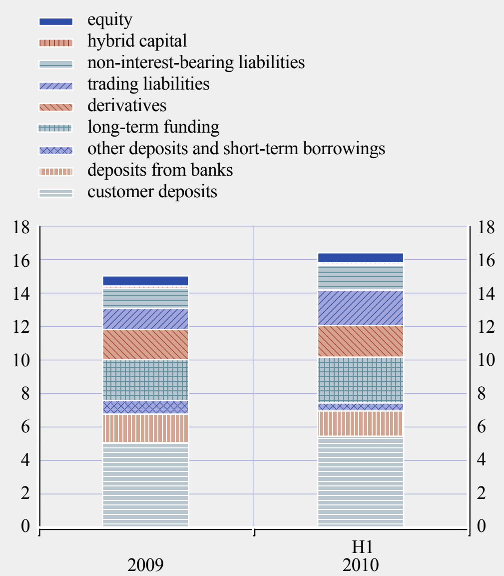
1 The balance sheet categories referred to in this box rely on Bureau van Dijk (Bankscope) classifications. Total liabilities correspond to the liabilities side balance sheet total minus hybrid capital and equity. Total funding includes deposits, money market and short-term funding, long-term funding (i.e. senior debt maturing after one year and subordinated borrowing, as well as other funding), derivatives and trading liabilities. Total liabilities equal total funding plus non-interest-bearing liabilities.

Chart A Evolution of euro area banks' customer funding gap

Source: Bureau van Dijk (Bankscope).
Note: Sample of euro area banks that participated in the EU-wide stress-test exercise.

Chart B Breakdown of euro area banks' liabilities and equity

(EUR trillions)



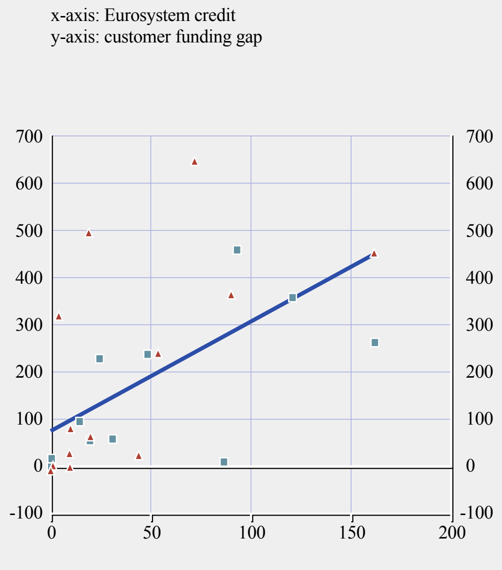
Source: Bureau van Dijk (Bankscope).
Note: Sample of 33 of the 77 euro area banks that participated in the EU-wide stress-test exercise, for which data are available for both 2009 and the first six months of 2010.

divergent development of different types of liabilities (see Chart B). Taken together, trading deposits from banks (-11%), which include central bank credit, and other short-term borrowing (-40.5%), lost around 4.6 percentage points in the share of total assets, to the benefit of trading liabilities (+67.2%) (which include the negative fair values arising from derivative financial instruments, and thus reflect the volatility in financial markets) and non-interest-bearing liabilities (e.g. accounts payable or taxes (+24.3%)). The latter two categories together increased their relative share of total assets by 5.6 percentage points. The decreases of trading deposits and other short-term borrowings are indicative of reduced activity in interbank markets, and (possibly) of banks' difficulties in rolling over short-term debt. The shares of customer deposits (+7.4%) and long-term funding (+11.7%) in total assets remained constant in relative terms. Hybrid capital (-8.5%) and equity (+0.5%) decreased by a total of half a percentage point in relative terms, compared with total assets. As the total assets of this sub-sample grew by 9.2%, mainly on account of an increase in net loans (+4.4%) and in securities (+20.3%), the customer funding gap declined by 1.5 percentage points relative to total assets in comparison with end-2009 and represented 10.8% of total assets at the end of the first half of 2010. The narrowing customer funding gap, together with the fact that both customer deposits and long-term funding exhibited higher growth rates than net loans, points to structural adjustment aimed at reducing future funding risks.

As illustrated in Chart C, the higher the banks' funding gap, the higher on average their demand for Eurosystem credit. In view of the presumably gradual normalisation of Eurosystem liquidity

Chart C Euro area banks' customer funding gap versus Eurosystem credit outstanding

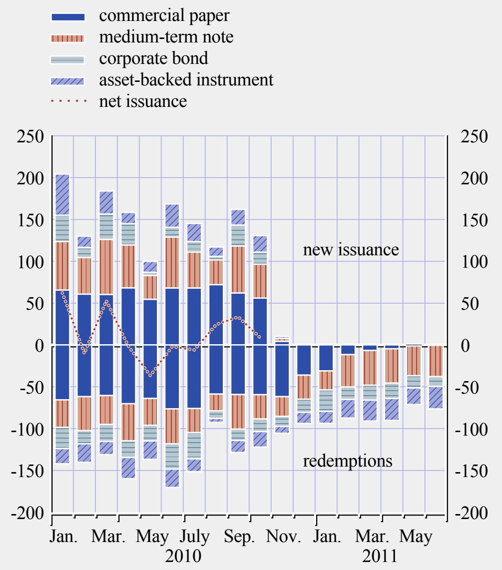
(EUR billions)



Sources: ECB and Bureau van Dijk (Bankscope).
Note: The data points represent figures (where available) for euro area banks that participated in the EU-wide stress-test exercise, aggregated at the country level for end-2009 (triangle) and the first half of 2010 (square).

Chart D Issuance profile of euro area banks

(EUR billions)



Source: Dealogic.
Notes: The underlying sample consists of the euro area banks that participated in the EU-wide stress test. Net issuance is the total new issuance minus scheduled redemptions. Dealogic does not trace instruments following their issuance and therefore some of these instruments might have been redeemed early. The asset-backed instrument category encompasses ABSs, MBSs and covered bond instruments.

operations in the period ahead, banks which currently rely excessively on liquidity from the Eurosystem in covering their funding gaps should start to take the necessary steps to reduce their dependence on Eurosystem financing.

The publication of the EU-wide stress-test exercise results is likely to have been helpful in this respect. As a matter of fact, net issuance by participating euro area banks turned positive after the stress-test results were published (Chart D), a factor that should have a supporting effect in the adjustment process. However, the aggregate figures do not reflect the discrepancies in the funding situations of individual banks and national banking sectors, as some banks in the euro area continue to face difficult funding situations and are therefore relying largely on Eurosystem financing.