

# How Did CESEE Households Weather the Crisis? Evidence from the OeNB Euro Survey

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*During the crisis period from 2008 to 2013 household disposable income deteriorated significantly in Central, Eastern and Southeastern Europe (CESEE), forcing households to adjust their consumption plans. Against this background, the present paper sheds some light on households' consumption smoothing behavior based on microdata supplied by the OeNB Euro Survey for ten countries in CESEE. We find that households reacted to stagnating and in some countries falling income mostly by cutting back on everyday consumption and reducing or postponing large expenditures, while other households coped by reducing the amounts they were setting aside as savings or by drawing on existing savings, overdrawing their current accounts and increasing work hours. Moreover, we find that macroeconomic forecasts by the European Commission, the wiiw and the OeNB are broadly in line with economic sentiment among CESEE households. Finally, Euro Survey results revealed that not all households were able to borrow as much as they would have liked to and that the share of households planning to take out a loan fell between 2008 and 2013.*

*JEL classification: D12, D14, E21, G01*

*Keywords: economic and financial crisis, consumption smoothing, household debt, survey data, Central, Eastern and Southeastern Europe*

During the financial and economic crisis the financial situation of CESEE households deteriorated significantly. Stagnating and in some countries falling disposable income forced households to adjust their consumption plans quite substantially, not least because social security systems in CESEE are still less advanced than in many Western European countries. Against this background this short study presents OeNB Euro Survey<sup>2</sup> data in order to explore three issues.

First, how did CESEE households weather the crisis? In order to shed some light on households' strategies for cushioning the decline in disposable income, the 2013 fall wave of the OeNB Euro Survey included questions on households' actual consumption smoothing behavior during the crisis period from 2008 to 2013.

Second, due to the weak recovery in the main export markets of the CESEE countries, recovery decisively hinges on the pick-up of domestic demand, i.e. private investment and private consumption. The expected rebound of private consumption is partly related to households' expectations regarding their financial situation and the national economy. Are recent macroeconomic forecasts warranted in light of the microeconomic evidence on the financial situation of CESEE households? Drawing from earlier work by Beckmann and Moder (2013) on the leading properties of household sentiment, the present short study discusses the improvement in household expectations regarding the national economy evident in the 2013 fall wave. We find that the macroeconomic forecasts of the European Commission, the wiiw and the OeNB are broadly in line with household economic sentiment.

Finally, given that the crisis was preceded by a credit boom in some CESEE countries the assessment of households' financial situation requires a closer look at household deleveraging. The legacy of the crisis might reduce households' ability

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<sup>2</sup> For more information on the OeNB Euro Survey see box below or [www.oenb.at](http://www.oenb.at).

and/or willingness to borrow for the purpose of smoothing consumption over the life cycle. Presented Euro Survey evidence allows some insights into whether actual levels of household debt correspond to the desired level of household debt. Furthermore, OeNB Euro Survey data allow a first look at borrowing constraints households are faced with – to provide a starting point for further research.

This study is structured as follows: Section 1 shows the impact of the crisis on the financial situation of households based on macroeconomic indicators. Section 2 presents survey evidence as to what extent the economic and financial crisis has affected CESEE households. In particular, this section will discuss a comprehensive set of strategies employed by households to cushion the effects of the crisis-induced decline in disposable income on consumption, savings and leisure. Section 3 briefly discusses improved household sentiment regarding the national economy as observed in fall 2013. Section 4 compares actual and desired levels of household debt as well as CESEE households' plans for borrowing and presumed access to credit; section 5 summarizes and concludes.

## **1 Financial Situation of CESEE Households Deteriorated Substantially between 2008 and 2013**

During the five years preceding the economic and financial crisis real GDP growth was quite impressive, ranging from 2.7% in Hungary to 8.5% in Bosnia and Herzegovina in average annual terms (see table 1). CESEE households profited from this development through rising real income and employment. Higher real incomes led to both higher private consumption expenditures and larger savings. Several years of rising household income and the expectation of being better off in the future may have influenced households' willingness to borrow against future income. Bank loans to CESEE households soared with two-digit growth rates for several years – partly because the stock of outstanding credit to households started from low levels (Backé and Zumer, 2005; Barisitz, 2005). Nevertheless, the rapid credit growth in the region during these years would have been impossible without the market entry of foreign banks with cheap funding and rather aggressive business models (EIB, 2013). Central banks and financial supervisory authorities responded, in part already before 2008, by tightening monetary policy and introducing macroprudential measures in order to mitigate the ongoing credit boom and to contain the associated buildup of vulnerabilities, in particular with respect to foreign currency lending to unhedged households (EIB, 2013; IWF, 2012).

In the course of the economic and financial crisis the financial situation of CESEE households deteriorated substantially. According to the EBRD's Transition Report 2011 households in the CESEE region were hit much harder by the crisis than those in Western Europe. Compared to precrisis levels private consumption declined on average in seven out of ten CESEE countries between 2009 and 2013. The slump in private consumption growth was particularly pronounced for households in Southeastern Europe, where real income on average stagnated or even decreased over the five observed years.<sup>3</sup> Consequently, average annual growth

<sup>3</sup> *The EBRD's Transition Report 2011 stressed that cross-country comparisons of Western Europe and CESEE based on macroeconomic indicators tend to lead to an underestimation of the impact of the crisis on the transition region, in particular in countries that are dependent on remittances or exhibit a high proportion of informal employment.*

### The OeNB Euro Survey – Comprehensive Information on the New OeNB Website

The mission of the OeNB includes the economic analysis of the countries of Central, Eastern and Southeastern Europe (CESEE). To this end, the OeNB regularly conducts a survey of households in CESEE: The OeNB Euro Survey provides a unique and comprehensive source of information about the foreign currency assets and liabilities of households in CESEE, as well as respondents' economic opinions, expectations and experiences.

The harmonized design of the survey allows comparisons not only across countries, but also across sociodemographic groups. The microdata supplied by the OeNB Euro Survey complement aggregate statistics and allow us to move the level of analysis from macroeconomic data to responses obtained directly from households. The analysis affords useful insights into the determinants of household behavior, e.g. euroization, thus providing important input for macroprudential monitoring as well as academic discussion.

Surveys are conducted twice a year, in spring and in autumn, in the following ten countries: EU Member States: Bulgaria, Croatia, the Czech Republic, Hungary, Poland, Romania.

Non-EU Member States: Albania, Bosnia and Herzegovina, the Former Yugoslav Republic of Macedonia, Serbia.

Further information on the OeNB Euro Survey and a new set of selected results can be found on the OeNB's website under:

<http://www.oenb.at/en/Monetary-Policy/Surveys/OeNB-Euro-Survey.html>

Table 1

### Main Economic Indicators of the Household Sector

	BG	CZ	HR	HU	PO	RO	AL	BiH	FYROM	RS
<i>Average annual change in %</i>										
GDP at constant prices (2004–2008)	6.5	5.5	4.1	2.7	5.4	6.8	6.1	8.5 <sup>1</sup>	5.0	5.5
GDP at constant prices (2009–2013)	–0.4	–0.5	–2.4	–0.9	2.7	–0.3	2.8	–0.5	1.5	–0.1
Private consumption (2004–2008)	7.1	3.6	3.8	1.2	4.5	12.0	7.5	6.5 <sup>1</sup>	7.2 <sup>1</sup>	6.8
Private consumption (2009–2013)	–0.5	–0.2	–2.4	–2.2	2.0	–1.4	2.2	–1.0	0.3	–1.7
Compensation per employee (real, whole economy, 2004–2008)	4.3	2.9	1.6	2.1	1.1	13.0	..	..	–0.9	..
Compensation per employee (real, whole economy, 2009–2013)	3.4	0.2	–0.4	–2.9	1.7	–3.4	..	..	1.1	..
Monthly net wages (real, 2009–2013)	..	..	..	..	..	..	1.4	0.4	..	–0.3
<i>Average level 2009–2013</i>										
Unemployment rate (LFS, %, 15–64 years)	10.8	7.0	13.8	10.9	9.8	7.5	13.8	27.4	31.3	23.9 <sup>2</sup>
<i>Average annual change in %</i>										
Deposits of households and NPISH (2004–2008)	26.5	8.7	11.6	9.5	10.2	34.4	13.2	22.2	21.6	40.9
Deposits of households and NPISH (2009–2013)	11.4	4.6	4.3	–0.4	10.3	9.4	11.0	9.6	12.2	17.9
Loans to households and NPISH (2004–2008)	49.5	30.0	18.6	26.8	31.0	71.1 <sup>1</sup>	60.8	27.5	45.8	72.0
Loans to households and NPISH (2009–2013)	0.7	6.5	–0.2	–2.1	8.6	0.8	1.1	1.1	6.6	9.5

Source: European Commission, Eurostat, national statistical offices, *wiiv*.

<sup>1</sup> The average growth rate refers to the period 2005–2008.

<sup>2</sup> Average level 2011–2013.

Note: LFS = labor force survey; NPISH = nonprofit institutions serving households.

rates of household deposits at banks slowed remarkably and even turned negative in Hungary. Furthermore, average annual growth of loans to households came to a halt in six out of ten countries – reflecting deleveraging needs of both households and banks (IMF, 2014). In the Czech Republic, FYR Macedonia<sup>4</sup>, Poland and Serbia the effect was less pronounced with average annual growth of household borrowing falling below 10%.

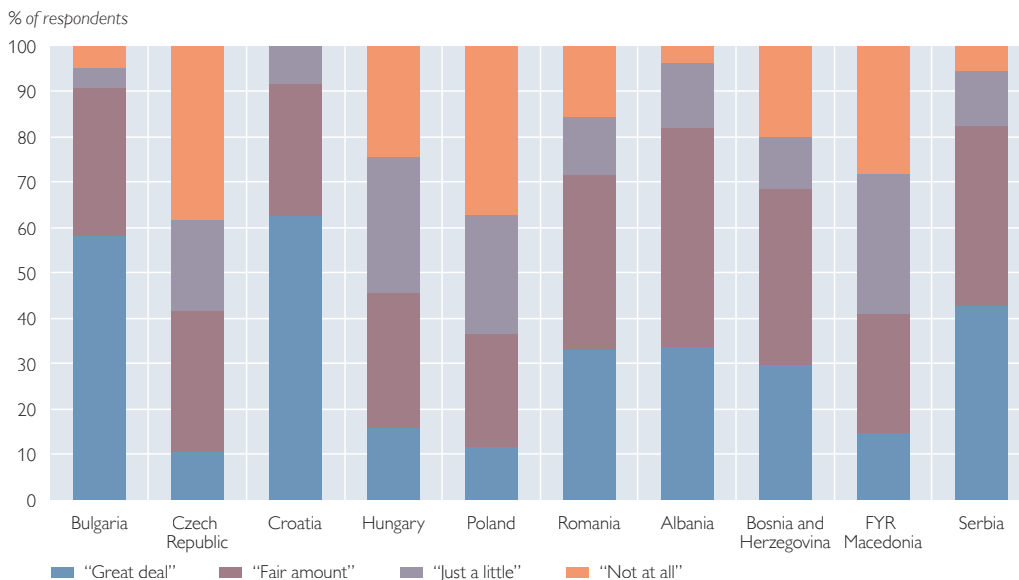
## 2 How Did Households React to the Decline in Disposable Income?

In the 2013 fall wave of the OeNB Euro Survey respondents were asked how much, if at all, the economic crisis had affected their households since 2008.<sup>5</sup> Chart 1 shows that roughly 40% of respondents in Central and Eastern Europe admit to have been affected a “great deal” or “fair amount,” whereas the share for Southeastern European households ranges from 70% to 90%. Households in FYR Macedonia were hit less hard by the crisis (41%). This result is in line with the macroeconomic development of FYR Macedonia.

The question on how households subjectively perceived the impact of the crisis, the results of which are shown in chart 1, had already been asked in fall 2010 in the EBRD’s Life in Transition Survey II. The fall 2013 Euro Survey revealed that, compared with the EBRD results, the proportion of respondents who stated that the crisis had affected them “a great deal” or “a fair amount” had decreased by 17 percentage points on average in FYR Macedonia and Hungary, while in the

Chart 1

### How Much, If At All, Has the Economic Crisis Affected Your Household Since 2008?



Source: OeNB Euro Survey.

Note: Respondents who answered “Don’t know” or indicated “No answer” have been excluded.

<sup>4</sup> Former Yugoslav Republic of Macedonia.

<sup>5</sup> Note that data of the 2013 fall wave for Croatia might be flawed due to a change in the interviewer team. Since mainly inexperienced interviewers were deployed in the latest survey wave the share of rather poor and unemployed respondents turned out disproportionately high.

remaining countries the share of households affected by the crisis had increased (+12 percentage points on average), in particular in Albania (+24 percentage points) and Croatia (+36 percentage points).

Based on economic theory one would expect that a household which has been hit by an adverse disposable income shock in combination with high uncertainty will react by reducing consumption and/or amounts set aside as savings. If households perceive the income shock to be temporary, economic agents will – in absence of credit constraints – try to smooth consumption by borrowing against future income (or drawing on savings). If households regard the reduction in disposable income as permanent, an adjustment of household expenditure will result – *ceteris paribus* – in a lower consumption level over the whole life cycle. By contrast, households which are affected by higher uncertainty but experience no disposable income shock may increase their (precautionary and/or buffer-stock) savings in order to insure themselves against a potential higher risk of an adverse income shock (Carroll et al., 1992), reinforcing business cycle swings as a result.

When asked what measures households took as a result of a decline in income or other economic difficulties during the crisis, respondents were allowed to give multiple answers (see chart 2).

The most frequent answer involved reduced consumption. On average 81% of households that indicated that they had been affected by the economic crisis reduced everyday consumption. Interestingly, variation across countries is rather small. Three in four affected households reported a reduction or postponement of large expenditures. As expected only few households (CESEE average: 2.7%) were forced to move; only Albanian households recorded a significantly higher share (16%).

As an alternative to cutting back on expenditures a household may want to smooth its consumption over time, either by reducing amounts set aside for new savings out of disposable income or by drawing on prior savings. Survey results show that respondents more frequently chose to reduce new savings (51%) than to dissave or sell assets (29%). In Croatia and Serbia both measures of consumption smoothing turned out to be of similar importance. Interestingly, across almost all countries surveyed these two consumption smoothing strategies are less frequently mentioned than measures for reducing consumption. This may be related to two stylized facts concerning CESEE households which limit the scope for consumption smoothing. First, the ability to save out of current income is rather low; and second, several households have no savings at all.

Most of the measures discussed so far reflect the income effect associated with a decrease in disposable household income. Yet, on average, 26% of CESEE households also substituted leisure for additional working hours to counteract the initial decline in disposable income. In particular, households in Albania, Bulgaria, Croatia and Hungary increased working hours or took up additional work in order to cushion the impact of the crisis on their financial situation. Furthermore, in these four countries financial help from family and friends supplemented households' disposable income more frequently than in the remaining countries surveyed (16% on average). Interestingly, financial help from family and friends seems to be more important for CESEE households' finances than social benefits.<sup>6</sup>

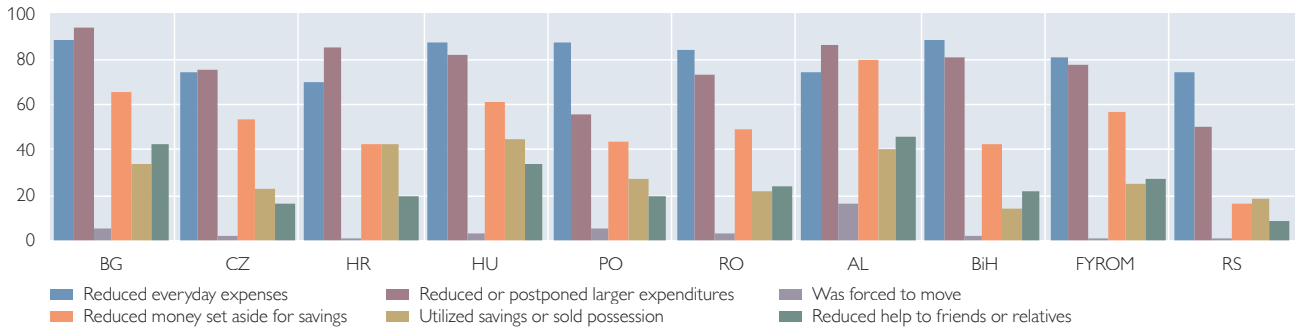
<sup>6</sup> The EBRD's *Transition Report 2011* presented evidence that the (successful) access to unemployment protection is better in Western Europe than in CESEE EU Member States and much better than in (potential) candidate countries.

Chart 2

## How Has the Household Reacted to Lower Disposable Income?

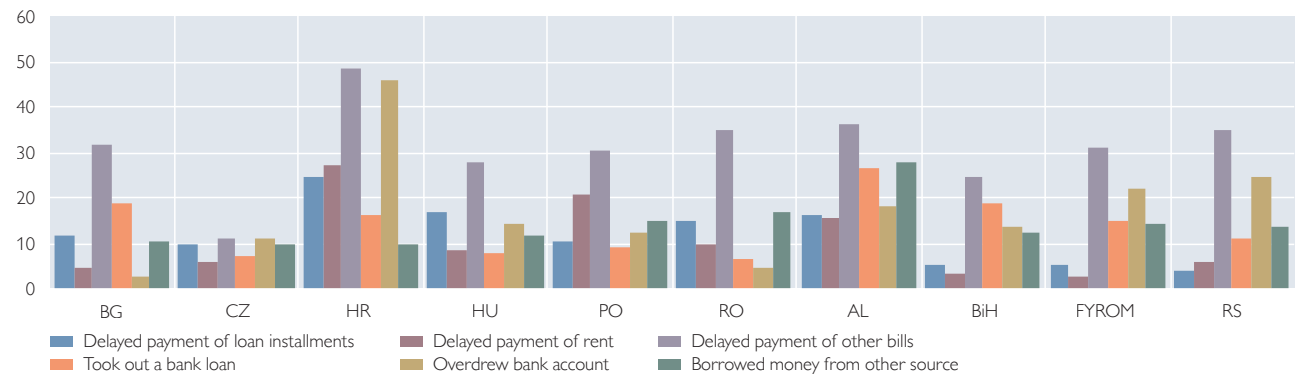
### Reduced Consumption Expenditures, Savings or Help

% of respondents who admit having been affected by the economic crisis since 2008



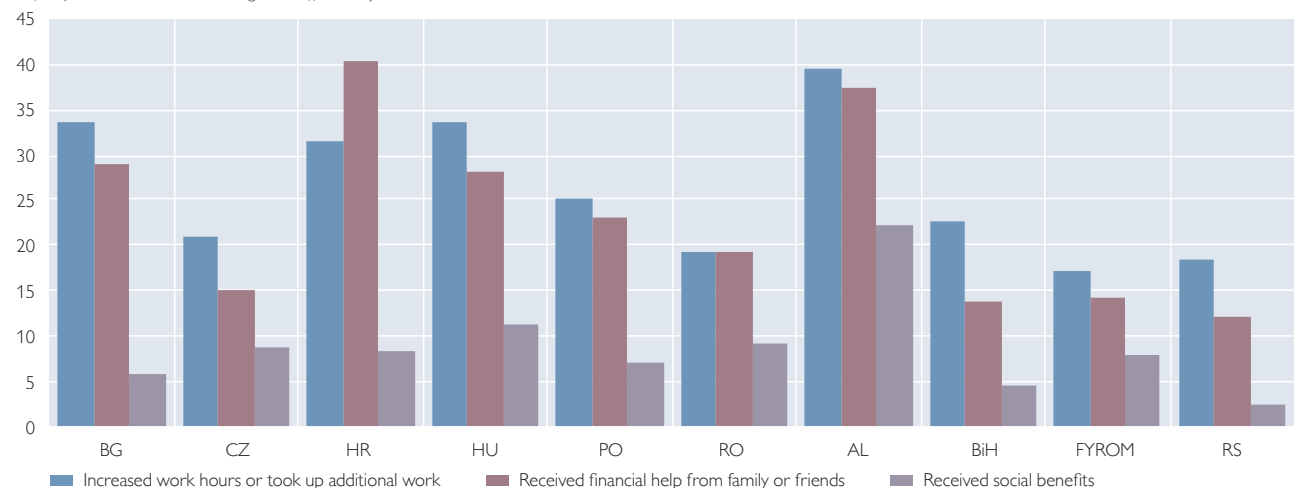
### Postponed Payments or Increased Borrowing

% of respondents who admit having been affected by the economic crisis since 2008



### Increased Work Hours, Received Financial Help or Social Benefits

% of respondents who admit having been affected by the economic crisis since 2008



Source: OeNB Euro Survey (fall 2013).

Note: Respondents who answered "Don't know" or indicated "No answer" have been excluded.

Despite substantial differences across countries, it is possible to sum up that in general households reacted to the crisis and the subsequent reduction in disposable income mainly by reducing consumption and smoothing consumption through

direct or indirect borrowing against future income. Against the background of these findings one may expect that rising disposable income will translate into both rising consumption expenditures and savings in the course of the ongoing recovery. This expectation is supported by research findings published by Beckmann et al. (2013), who examined the determinants of households' savings based on OeNB Euro Survey data and showed that the life-cycle hypothesis holds for CESEE households.

### 3 Survey Data on CESEE Households' Expectations Broadly Support Recent Macroeconomic Outlooks for 2014

Current forecasts by the European Commission, the wiiw and the OeNB<sup>7</sup> stress the importance of private consumption for continued recovery in the CESEE region. All three institutions expect only moderate real GDP growth for 2014. Although private consumption growth should accelerate compared to 2013, growth rates will be still below average precrisis levels (table 1) and less dynamic than real GDP growth (see chart 3). Private consumption growth estimates range from 0.4% in the Czech Republic to 2.5% in FYR Macedonia. In Croatia and Serbia private consumption is expected to shrink again in 2014.

Are these forecasts warranted in light of the microeconomic evidence on the financial situation of CESEE households? Using evidence from the OeNB Euro Survey, Beckmann and Moder (2013) find a positive correlation between households' expectations regarding the national economy and actual future GDP and consumption growth. Hence survey answers on household sentiment might complement recent macroeconomic forecasts.

Chart 4 shows that households' expectations regarding the national economy are still in the negative territory for all countries, except for Albania. Compared to autumn 2012, the fall 2013 wave showed quite a substantial improvement of economic sentiment in the Czech Republic, Hungary, Poland and Albania, whereas

Chart 3

#### Growth Outlook for Real GDP and Private Consumption in CESEE

Annual change in %



Source: European Commission winter forecast, wiiw March 2014 forecast.

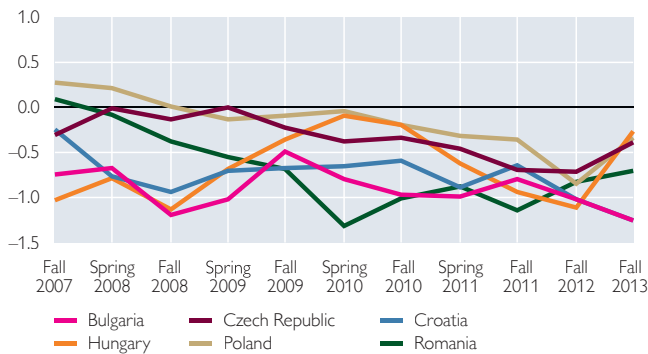
<sup>7</sup> For details see the OeNB's Outlook for Selected CESEE Countries in this issue.

Chart 4

### Consent to the Statement: “Over the Next Five Years the Economic Situation of My Country Will Improve”

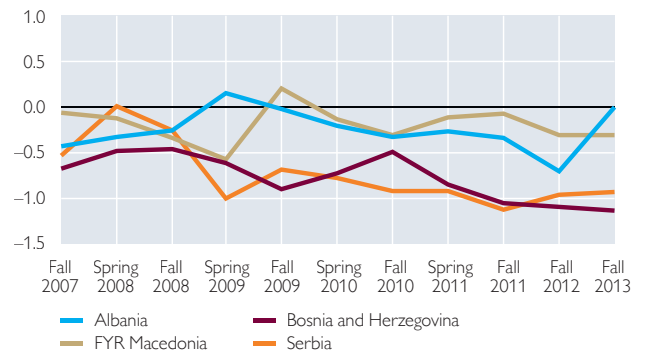
#### EU Member States

Normalized sample means per country (-2.5: fully disagree, 0: neutral, +2.5: fully agree)



#### (Potential) Candidate Countries

Normalized sample means per country (-2.5: fully disagree, 0: neutral, +2.5: fully agree)



Source: OeNB Euro Survey.

Note: Respondents were asked whether they agreed or disagreed with the statement above on a scale from 1 (“fully agree”) to 6 (“fully disagree”). Respondents who answered “Don’t know” or indicated “No answer” have been excluded. This question was not asked in spring 2012 and spring 2013.

sentiment deteriorated further in Bosnia and Herzegovina and particularly in Croatia and Bulgaria.<sup>8</sup>

Summing up, CESEE households’ expectations and macroeconomic forecasts of private consumption point in the same direction in eight out of ten countries. The exceptions are Bosnia and Herzegovina and Bulgaria, where respondents expect things to get worse while the forecasts predict an increase in growth rates for private consumption.

## 4 Will Private Sector Deleveraging Put a Brake on Future Private Consumption?

Some CESEE countries experienced a credit-financed boom in the run-up to the crisis and consequently need to adjust leverage ratios of banks, companies and/or households (European Commission, 2014; IMF, 2014; Vincelette et al., 2013). Thus, apart from a recovery of disposable income, private consumption expenditures will also hinge on the current household debt burden and households’ ability and/or willingness to borrow in order to smooth consumption over the life cycle. OeNB Euro Survey data allow a closer look at the household debt burden and the significance of borrowing constraints.

### Household Debt Burden Still Elevated in Some CESEE Countries

The share of households that have taken out a loan varies considerably across CESEE countries, in part reflecting different stages in financial deepening (see chart 5, left-hand panel). Concerning the self-reported debt position, two-thirds of indebted households in the Czech Republic, Croatia, Poland and FYR Macedonia report that they have the right amount of debt and do not anticipate any problems

<sup>8</sup> Chart A1 in the annex shows a similar pattern for households’ expectations regarding their financial situation. Note that Beckmann and Moder (2013) found that CESEE households are more optimistic about their own financial situation than about the outlook for the whole economy.



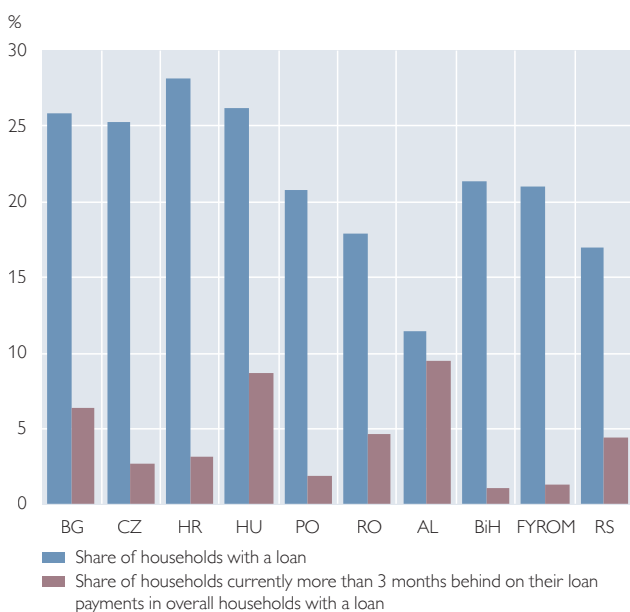
with their debt (see chart 5, right-hand panel).<sup>9</sup> By contrast, almost half of Bulgarian and Hungarian households with a loan admitted having too much debt at the moment and that they might experience difficulties paying it off. Furthermore, around 40% of Albanian, Bosnian, Romanian and Serbian households consider their household debt level to be too high. This self-assessment is partly reflected in the share of nonperforming loans.<sup>10</sup>

Beckmann et al. (2012) studied the determinants of loan arrears of CESEE households. Using OeNB Euro Survey data on the reasons behind households' financial difficulties, the authors showed that income shocks exert a strong and significant impact on loan delinquency rates in CESEE economies. Against the background of widespread foreign currency lending in the region, the authors furthermore confirmed an additional – though weaker – impact of foreign currency borrowing on higher loan delinquency rates in depreciation countries.<sup>11</sup>

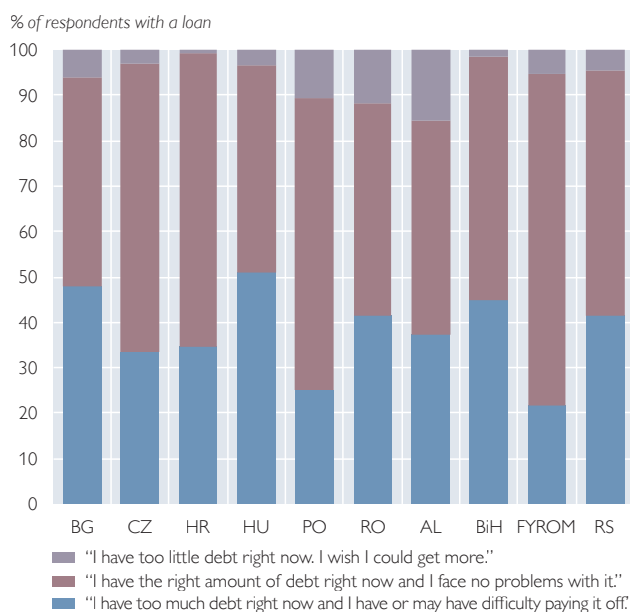
Chart 5

## Current Debt Stock of CESEE Households

### Households with Loans and Current Loan Arrears



### Self-Assessment of the Current Debt Position



Source: OeNB Euro Survey.

Note: Respondents who answered "Don't know" or indicated "No answer" have been excluded. Figures of the left-hand panel are averages of spring wave and fall wave 2013. Figures of the right-hand panel refer to fall 2013.

<sup>9</sup> The question on the self-assessment of the current debt position originates from a survey on debt literacy from Lusardi and Tufano (2009). The wording of the question has been adopted literally. For comparison purposes, Lusardi and Tufano found that in November 2007, before the financial crisis hit the U.S. economy, 26% of respondents in the U.S. said that they were having or might experience difficulties paying off debt, while 61% reported having the right amount and 20% too little debt. Another 11% were unable to judge whether they had too much or too little debt – compared to less than 2% on average for CESEE.

<sup>10</sup> Loans are referred to as nonperforming if households are more than three months behind with their loan payments. The ratio of nonperforming loans derived from survey answers is highly correlated with nonperforming loan ratios from national supervisory statistics ( $R^2 = 0.93$ ).

<sup>11</sup> See also EBRD (2011).

### Do Households Face Borrowing Constraints?

The survey results illustrated in chart 5 (right-hand panel) indicate that some indebted CESEE households wish their debt level were higher. This implies that not all households were able to borrow the amount of money they intended to in the past. Looking forward, one might ask whether households' intentions to take out a loan might be frustrated by borrowing constraints. Although there is no direct survey evidence pointing to the prevalence of credit constraints, household responses indicate that not every household that needs credit actually gets it.

Chart 6 (left-hand panel) shows that the share of households planning to take out a loan has decreased substantially since 2008. Three out of five households that are still planning to take out a loan within the next 12 months assumed in fall 2013 that they would "probably" or "almost certainly" have the possibility to borrow a significant amount from a bank (see chart 6, right-hand panel).<sup>12, 13</sup> Interestingly, they assigned similar probabilities to obtaining a significant amount of money from family or friends. Due to a lack of historical data on this question, this first glimpse at the data does not allow a final assessment of the extent of credit constraints and their dampening impact on the recovery of private consumption in CESEE countries.

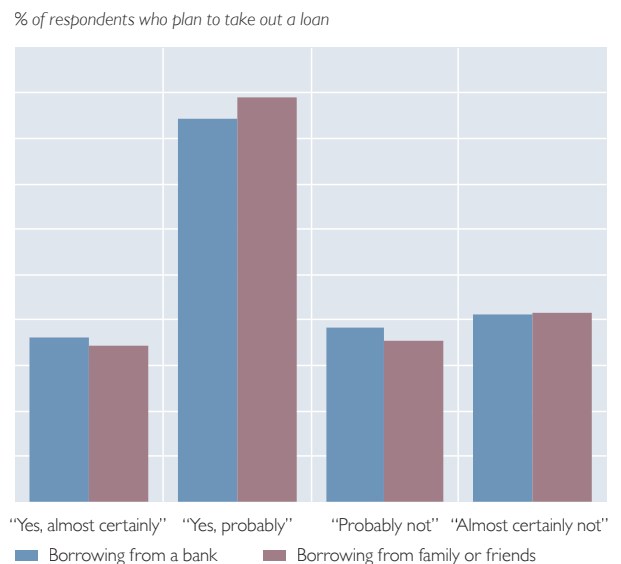
Chart 6

### Planned Loans and Presumed Access to Credit

#### "Do you plan to take out a loan within the next 12 months?"



#### "Do you have the possibility to borrow a significant amount of money?"



Source: OeNB Euro Survey.

Note: Respondents who answered "Don't know" or indicated "No answer" have been excluded. Figures of the right-hand panel refer to fall 2013.

<sup>12</sup> Pessimistic views on the ability to borrow a significant amount from a bank prevail in Bulgaria and Croatia, which coincides with continued deleveraging in these countries. By contrast, three out of four households in the Czech Republic and Poland expect that a bank would grant them a loan of significant amount, which reflects improving financing conditions in the Czech Republic and continued favorable financing conditions in Poland (see CESEE-7 forecast in the OeNB's Outlook for Selected CESEE Countries in this issue).

<sup>13</sup> The wording of the question on borrowing possibilities was inspired by similar questions in the EBRD Life in Transition Survey II and the Household Finance Survey 2008 of the Banco de España.

## 5 Summary

Over the last five years (2008 to 2013) CESEE households were forced to adjust their consumption plans quite substantially as disposable income stagnated and in some countries even fell (in aggregate terms). In order to shed some light on the measures taken by households to cushion the decline in disposable income, the 2013 fall wave of the OeNB Euro Survey included some questions on households' actual consumption smoothing behavior during the crisis period from 2008 to 2013.

The strategy most frequently employed by households affected by the economic crisis was cutting back on everyday consumption followed by reducing or postponing large expenditures. Alternatively, some households saved smaller amounts of their disposable income and, less frequently, households reported to have drawn on their savings. These results suggest that CESEE households had only limited scope for consumption smoothing. Several households' ability to save out of current income was rather limited or they did not have any savings at all. Furthermore, CESEE households reported that when they borrowed against future income in order to smooth consumption, they mainly did so by overdrawing their current accounts. Finally, one in four households indicated having substituted leisure for additional working hours to counteract the initial decline in disposable income.

Against the background of these findings one may expect that rising disposable income in the course of the ongoing recovery will translate into both rising consumption expenditures and savings. Recent macroeconomic forecasts expect private consumption growth to resume in some CESEE countries in 2014, in particular in countries with improving financing conditions. These expectations seem warranted based on information derived from the OeNB Euro Survey. Overall, our analysis shows that a relatively optimistic macroeconomic outlook on private consumption for a specific country coincides with national survey results pointing to improved economic sentiment, a manageable household debt burden and a higher perceived likelihood that a bank would grant a household a significant loan.

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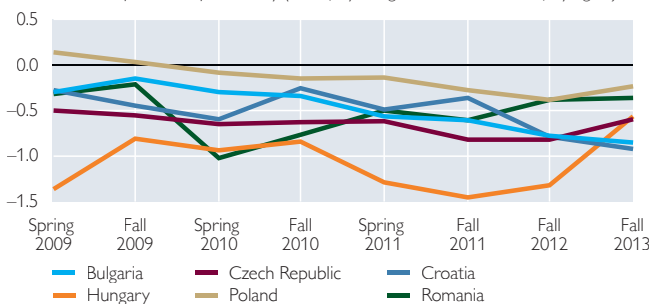
## Annex

Chart A1

### Consent to the Statement: “Over the Next Twelve Months I Expect the Financial Situation of My Household to Get Better”

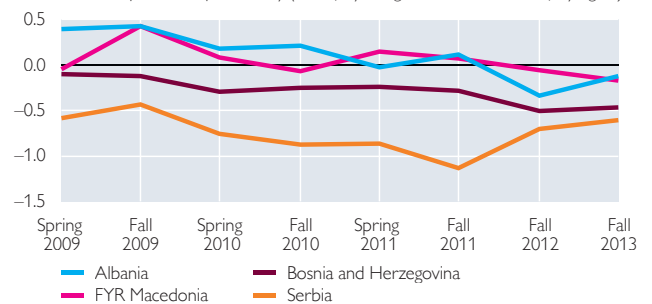
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#### (Potential) Candidate Countries

Normalized sample means per country (–2.5: fully disagree, 0: neutral, +2.5: fully agree)



Source: OeNB Euro Survey.

Note: Respondents were asked whether they agree or disagree with the statement above on a scale from 1 (“fully agree”) to 6 (“fully disagree”). Respondents who answered “Don’t know” or indicated “No answer” have been excluded. This question was not asked in spring 2012 and spring 2013.