CESEE-Related Abstracts from Other OeNB Publications

The abstracts below alert readers to studies on CESEE topics in other OeNB publications. Please see *www.oenb.at* for the full-length versions of these studies.

Austrian Subsidiaries' Profitability in the Czech Republic and Slovakia – CESEE Margins with an Austrian Risk Profile

Stefan Kavan,
Daniela Widhalm

The Czech Republic and Slovakia belong to the small and increasingly concentrated group of countries in Central, Eastern and Southeastern Europe (CESEE) whose banking markets have continued to generate substantial profits for Austrian banks also after the outbreak of the financial crisis in 2008. This short study sheds light on why Austrian subsidiaries have been able to maintain their profitability in these two countries especially when compared to those in other CESEE countries. We find that the strong quality of their asset portfolios is the main contributing factor; also, the Czech and Slovak markets now offer net interest margins well above Austrian levels, while the credit risk level is close to that in Austria. By contrast, several other CESEE markets have recorded worsening credit quality and, consequently, dwindling returns. Despite some downside risks related to the low interest rate environment, the openness of the Czech and Slovak economies and a potential intensification in competition, it seems that, from a current perspective, Czech and Slovak subsidiaries can be considered the most stable earnings generators in Austrian banks' international portfolio.

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The Euroization of Bank Deposits in Eastern Europe

Martin Brown,
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In Eastern Europe a substantial share of bank deposits are denominated in foreign currency. Deposit euroization poses key challenges for monetary policy and financial sector supervision. On the one hand, it limits the effectiveness of monetary policy interventions. On the other hand, it increases financial sector fragility by exposing banks to currency risk or currency induced credit risk. Policymakers disagree on whether Eastern European countries should tackle deposit euroization with "dedollarization" policies or should rather strive to adopt the euro as their legal tender. Assessing the potential effectiveness of "dedollarization" policies requires a clear understanding of which households hold foreign currency deposits and why they do so.

Based on survey data covering 16,375 households in ten countries in 2011 and 2012, we provide the first household-level analysis of deposit euroization in Eastern Europe. We examine how households' preferences for and holding of foreign currency deposits are related to individual expectations about monetary conditions and network effects. We also examine to what extent monetary expectations, network effects and deposit euroization are the legacy of past financial crises or the outflow of current policies and institutions in the region.

Our findings suggest that deposit euroization in Eastern Europe can be partly tackled by prudent monetary and economic decisions by today's policymakers. The preferences of households for euro deposits are partly driven by their distrust in the stability of their domestic currency, which in turn is related to their assessment of current policies and institutions. However, our findings also suggest that a stable monetary policy may not be sufficient to deal with the hysteresis of deposit euroization across the region. First, we confirm that the holding of foreign currency deposits has become a "habit" in the region. Second, we find that deposit euroization is still strongly influenced by households' experiences of financial crises in the 1990s.

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Spillovers from Euro Area and U.S. Credit and Demand Shocks: Comparing Emerging Europe on the Basis of a GVAR Model

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We examine the international effects of adverse loan supply and aggregate demand shocks originating in the euro area and the U.S.A. For that purpose, we use a global vector autoregressive (GVAR) model and isolate disturbances stemming from loan supply from those of four other macroeconomic shocks by means of sign restrictions. Our general results are as follows: Domestic and international responses of total credit and output to an adverse loan supply shock are substantial. They are more pronounced than the responses to an aggregate demand shock. Under both types of shocks, total credit decreases considerably more strongly than output in the long run, implying a reduction in financial deepening. This deleveraging process is particularly pronounced in the case of loan supply shocks. Taking a regional angle, Central, Eastern and Southeastern Europe (CESEE) and even considerably more the Commonwealth of Independent States (CIS) are the most strongly affected regions, and their total credit and output responses are stronger than in the country of shock origin. This is true for both types of structural shocks in the euro area and in the U.S.A. Last, historical decompositions of deviations from trend growth show that for the euro area developments, foreign shocks originating in the U.S.A., the UK and the CESEE and CIS regions feature most prominently, while for the U.S. developments, foreign shocks emanating from the euro area and China play a considerable role.

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