

## Study on Austria: Banking market retains growth prospects

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- Outlook: Annual credit growth rate of 3 percent as of 2010, deposits up by 5 percent
- Erste Bank CEO Bleyleben-Koren sees a window of opportunity and expects further organic growth for savings bank segment

In the past business year, the domestic banking market tended to draw international attention with bad news. However, something that everyone has almost lost sight of is that in international comparison Austria is considered as a stable, consumer-friendly European banking market. Nowhere in Europe – except possibly in Spain – are there more branch offices for customers. And nowhere else in Europe are interest rate changes passed on to customers as rapidly as in Austria. Despite harsh competition and low earnings margins, Austria's banks are profitable: they rank fifth in the euro zone after Finland, Spain, Italy and Ireland. As regards savings, Austrians are the leaders. At a savings ratio of 12%, the rate in the Alpine republic is around twice as high as the EU average. These are the findings of a study carried out by Macro Consult on behalf of Erste Bank. For Erste Bank head Elisabeth Bleyleben-Koren, the study also reveals the growth prospects for the business model of the savings bank.

The author of the study, Josef Christl firmly believes that “if a competition were to be held in Europe for the consumer-friendliest bank, Austria would certainly win”. Christl, a former chief economist at the Ministry of Finance and director on the board of the central bank, investigated the banking market and its prospects in Austria on behalf of Erste Bank. Austria is considered ‘overbranched’ as regards density of branch offices and as a ‘weak margin’ market as regards earnings potential. Nonetheless, Austria's banks are well supplied with equity capital and show an ‘average profitability’. “A fact that may be discouraging as a location factor for profit-hungry bankers is quite pleasing for consumers,” said Christl. The average banking margin, i.e., the spread between the key lending rate and the credit interest rate on a consumer loan was recently 6.19% (October 2009) in the euro area. In Austria, the spread is 4.44%, which is 1.75%-points less. This ratio is similar for loans to companies. Therefore, loans are cheaper in Austria than in the big market of Germany – which is one reason why German citizens gladly come to do business with Austrian banks. “Moreover, changes to key lending rates are passed on to consumers more quickly than in other countries,” according to the author of the study.

### High density of branch offices

There are 867 credit institutions in Austria with 80,300 employees and 4,251 branch offices. This means that coverage in Austria is one bank branch office for every 1,625 inhabitants, which is an extremely high ratio in international comparison. In Holland, for example, at 5,386 inhabitants per branch office three times as many people use one branch. The average in the euro zone is 1,832 persons per branch office.

“One reason why Austrian banks are able to run their businesses so profitably is the high level of cost awareness,” according to Christl. Since 1995, the measure of this factor, the so-called cost/income ratio, has been sinking continuously: It had been almost 70% in the mid-1990s, while today it is below 60%. This means that for every EUR 100 earned, over EUR 40 are booked as operating expenses.

### Austrians are the savings champions in Europe

While the ratio of indebtedness is below average at 83.8% in international comparison, the study confirmed a fact well known in the country: Austrians love to put away money in savings accounts. The savings ratio, i.e., the ratio between disposable income and money that goes into savings is 12%. The average in the euro zone is around 9.3%

and in the EU-27 around 6.2%. This is also one of the reasons why the World Savings Day is of special importance in Austria.

### **Crisis changed investment behaviour and growth prospects for banks**

The high propensity to save is not the only reaction of domestic investors to the crisis though. It has significantly changed investment behaviour among Austrians. The share of total deposits increased from 43% (2006) to 47% (2009) as measured by financial wealth. The volume of cash on hand also increased from 3% to 4%. By contrast, the share of investment certificates declined from 11% to 8%, and among shares, the drop was even steeper from 5% to 2%. In contrast, the savings deposits of private households grew gradually, but steadily, by around 3.5% per year. "They form a secure, crisis-resistant basis for the refinancing of the financial system," said Christl.

### **Future to bring slowing dynamic, but nonetheless growth in savings deposits and loans**

A slower economic growth rate would, of course, also check the dynamic in lending and deposits. Nonetheless, the study expects an increase in credit volume of around 3% over the next five years and a growth rate for deposits of around 5% per year. Inflation is expected to stay unchanged at a low level over the long term.

"The next few years, will not become easier for domestic banks," Josef Christl summarized in his prognosis and added "that credit growth will remain dampened, liquidity will become more expensive to obtain, the requirements for equity will be tighter and the wave of write-offs is not yet over." Therefore, what banks need is "clear business model and a secure funding structure". "To survive, it will be critical to know your customers and thus their credit risk," added Christl.

### **Erste Bank sees a window of opportunity for savings bank model**

"For a long time, international banks condescendingly smiled at the concept of savings bank, but now it is quite modern again," said Elisabeth Bleyleben-Koren, CEO of Erste Bank der oesterreichischen Sparkassen. By sticking to the business model of savings bank, Erste Bank feels well equipped to deal with the coming years. "The high density of the regional offices makes it possible for us to know our customers very well and they trust us," said Bleyleben-Koren. "During the year of the liquidity crisis, deposits grew from the end of 2008 to the end of September 2009 within the savings bank group from EUR 50.4bn to EUR 51.2bn, while the entire market shrunk during this period from EUR 276bn to EUR 268bn. We acquired 35,000 new customers alone in the first three quarters of 2009."

Bleyleben-Koren describes the business model of savings banks as follows: "We collect savings deposits and invest these funds primarily into the domestic economy rather than into structured financial products lacking transparency. Our competitive edge is mainly that we know our customers and the possibility of reaching regional decisions. This is why we will not close any branch offices. The bank function of a basic service is an essential part of our business model," said Bleyleben-Koren.

Erste Bank and the savings banks operate around 1,060 branch offices throughout Austria – and they run a profitable business. With the exception of the 4<sup>th</sup> quarter 2008 – this is when the financial crisis broke out and higher volumes had to be written off – every quarter has been clearly positive with an average of EUR 25m profit after taxes. "Our business model is resistant to crises and our group is growing – not at a revolutionary pace, but evolutionary," was the final comment by the head of Erste Bank.

[Study from Macro-Consult \(only German\)](#)

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