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Focus on: Credits
4 March 2022

European banks: War in Ukraine clouds outlook - mainly due to indirect effects

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Since last week's dramatic escalation in the Russia-Ukraine conflict, valuations of bank equities and bonds have come under severe pressure. In the months leading up to the crisis, the sector had been buoyed by well-founded hopes of a fairly manageable turnaround in monetary policy. However, this optimism has meanwhile given way to concern over a deterioration in the business environment, especially due to rising energy prices. This is compounded by fears of a gloomier outlook for earnings from capital market and securities business in a market environment that may remain weak for an extended period of time.

According to data from the Bank for International Settlements (BIS), banks' direct exposure to borrowers in Ukraine amounted to a relatively manageable USD 13.5 billion in September 2021, while their Russian exposure stood at approx. USD 122 billion - only very few international banks operate subsidiaries there. Consequently, the impact here for the industry as a whole is also limited, albeit some individual institutions are more heavily exposed than others.

On the other hand, the indirect effects of the crisis could prove costly to banks' profit forecasts, with the spotlight on heightened macroeconomic fears and uncertainty about the implications for interest rates. The main negative factors for borrowers are higher energy prices and pressure on trade relations with Eastern Europe.

So, for the time being, hopes of a long-term increase in net interest income have receded. Recently, for instance, the rating agency S&P forecast a 7 to 10% rise in net interest income across the banking industry assuming a parallel shift in the yield curve of 100 bps. When it published its annual financial statements two weeks ago, Commerzbank held out the prospect of additional interest earnings of just over EUR 1 billion for 2024 compared to its current budget - if market expectations of 4 February for interest rates should materialise. Even when factoring in the pricing of deposits and favourable ECB funding conditions in 2021, this would still have represented a hefty gain of around 10%. Since the beginning of February, however, the market has already revised expectations for interest rates downwards.

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