



1. Systemic risk indicators and financial market conditions

Systemic risk as perceived by markets ticked upward in 2016. The composite indicator of systemic risk (CISS) and its sub-indicators have grown steadily since the beginning of the year. Similarly, the global risk aversion indicator turned positive in 2016, signalling increase in investors' risk aversion (indicator 5.1). Meanwhile, high-yield corporate bond spreads and interbank interest rate spreads widened (indicators 3.9 and 4.1).

2. Macro risk

Economic recovery in the European Union continues, as EU real GDP rose by 1.8% in 2015 (indicator 2.1). In addition, the labour market is improving gradually, as unemployment in the EU fell below 9.0% in January (indicator 2.4).

However, debt sustainability in the public and non-financial private sectors remains a concern (indicator 2.5). The aggregated EU and euro area current public sector debt-to-GDP ratio remain above 60% (indicator 2.6). On the positive side, the fiscal deficit of most EU countries is expected to stay or fall below the 3% Maastricht threshold in 2016 (indicator 2.7).

3. Credit risk

Bank lending to the private sector continued on a path of gradual recovery, supported by lower cost of borrowing and credit standards. Annual growth rates of loans to the household and corporate sector increased compared to the same time last year, although highly heterogeneous across countries (indicators 3.1 and 3.2). Most noticeable is the recent growth of MFI loans to the Romanian private sector, compared to the previous year. However, Romania's level of private sector indebtedness is among the lowest in the EU (indicator 2.10). At the same time, borrowing costs of the euro area non-financial private sector continued to decline, and banks' credit standards were eased (indicators 3.3 to 3.8).

4. Banks

The recent increased risk aversion affected bank funding. Since the beginning of the year, credit spreads between senior and subordinated debt widened (indicator 4.9). This widening of spreads is in line with the increased risk aversion in markets (indicator 5.1). Meanwhile, bank debt issuance patterns shifted towards covered bonds (indicator 4.7).

Bank balance sheet repair continues (indicator 6.2). EU Banks' capital ratios further increased, as median CET1 ratio reached 14.5% in Q4 2015. Over the same period, quality of loan portfolios also improved.

However, banks' profitability remains a challenge. The second half of 2015 was marked by the seasonal decline of return on equity, while cost-to-income ratio increased (indicator 6.1).

5. Investment funds and other financial institutions

Footprint of the non-banking and non-insurance segment of the financial sector continues to grow (indicator 7.3). The total assets, net of valuation effects, of the investment funds and the OFIs have been growing steadily relative to the total assets of credit institutions (indicator 7.4). Over the last four quarters, non-MMF investment funds and OFIs have showed the largest nominal growth (indicator 7.5).

However, investment funds risk-taking increased. Exposure to non-euro area residents continued to increase and now account for 50% of investment funds' total assets (indicators 1.8 and 1.9).