Slovakia

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IN A NUTSHELL

→ Real estate prices stabilised by year end after a fall of about 10%.

→ Mortgage rates stabilised in Q4 at roughly 4.5%.

→ New production of mortgages suffered significantly due to increased rates and cooled real estate market.

→ Loan-to-deposit ratio above 100% mitigated by covered bonds.

MACROECONOMIC OVERVIEW

Despite the challenges, the economy has continued to grow, at 1.6% for 2023. While household consumption declined, investment revived after a weak 2022. Increased foreign trade also contributed to growth.

The labour market remained in good shape with the average unemployment rate falling to 5.8%, below 6% for the first time in history. Nominal wage growth accelerated to almost 10%.

Inflation peaked at 15.4% in Q1 and has since fallen. The base effect eased gradually during the year, while pressures from food prices also faded Inflation reached 6.6% as of December 2023 while the average rate during the year was 11%. Energy prices for households were capped at favourable levels with virtually no increase also for 2024, pushing the inflation below 3% in Q1 2024.

The public debt ratio, consistently well below the Euro area average and the Maastricht criteria, declined further by almost 2 pps due to inflation to 56%.

Household indebtedness finally stopped growing after years of steep increases. The growth of retail loans slowed significantly while nominal GDP increased at high pace. The ratio of retail loans to GDP thus decreased from 46% in 2022 to 43% as of year-end 2023. Although it is still well above peer CEE countries, stabilisation or further decline is expected in coming years.

HOUSING MARKET

Slovakia has the second highest homeownership rate in Europe (behind Romania) with 93.6% of the population owning houses, exceeding by far the EU long-term average of around 70%.

In the Bratislava region, which has the country's most expensive housing, residential property prices fell by 7.9% to EUR 3,077 per m2, after rising by more than 50% over the previous three years. Prices stabilised in Q1 2024. In general, regions with higher price increases in 2019-2022 had a more significant correction:

- The largest drop was in Presov region with 17% y-o-y decline (to EUR 1,786 per m^2)
- Banska Bystrica and Kosice, where prices more than doubled in the previous three years, experienced similar price decreases of about 12%.
- Zilina with -9% y-o-y change became the third most expensive region in Slovakia with EUR 1,874 per m2, overtaking Presov.
- Prices in the three remaining regions (Nitra, Trencin and Trnava) experienced prices falls of 6-7% y-o-y.

Price growth prior to the correction was fuelled by low interest rates, robust development in the labour market and low supply of new flats/houses. Increased mortgage rates, lower demand for investment by private individuals and general uncertainty caused the prices to drop by a tenth from the peak in Q3 2022. Prices of newly build projects fell less than those of older dwellings. Developers preferred to freeze the official advertised prices as their liquidity position was sound due to a more cautious approach compared to the market crash after the financial crisis of 2008. Although there have been certain special offers in terms of subsidised mortgages by the developer or "furnishing for free" discounts, number of sold flats in new projects was extremely low in 2023.

As a result, the number of new building permits and housing starts as well as completions declined further and have reached the lowest levels since 2014. Housing starts fell by 12% and a slightly lesser drop was seen in new permits, suggesting lagging supply in years to come. The number of completions increased by 3%, due to strong building activity seen several years ago.

Affordability fell substantially after years of favourable conditions. Financing is now much more costly as interest rates on new mortgages went up significantly and real estate prices declined relatively mildly. Some improvement in affordability was seen in Q4, as real wages started to grow again, and interest rates stabilised. Real estate will become even more affordable with expected mortgage rates decreases and continuing improvement of households' financial situation.

MORTGAGE MARKET

Note that the volume of mortgages outstanding was heavily affected by methodological changes in reporting to the Central Bank. While the quality of reported data increased substantially, comparison with the previous periods is difficult and sometimes it is not possible to calculate correct adjusted y-o-y changes. The underlying annual growth of mortgages outstanding decelerated gradually to its lowest ever level of about 3% y-o-y (adjusted for one-offs). For comparison, the long-term average was above 10% p.a. in the past decade. The volume of new mortgages declined sharply to roughly 40% of exceptional ly high years 2021 and 2022, and about 50% down compared to years 2017-2020. However, the comparison might be affected negatively by the change in reporting.

Higher rates caused significantly lower refinancing which was common both internally (renegotiation) and externally (switching banks). This makes less sense given higher interest rates.

Mortgage interest rates largely stabilised at the end of 2023, with only a small increase in Q4. The average rate was just below 1% in January 2022, above 3.5% in December 2022 and continued to rise, although at lower pace, to 4.6% as of year-end 2023. The increase was among the largest in the Eurozone – while Slovaks enjoyed the third lowest rates in the Eurozone in 2021, they were the fourth most expensive by end of 2023, behind the three Baltics countries.

The market was dominated by fixed rate periods (3 to 5 years) for several years, usually for approximately 90% of new mortgages. But for several months, due to anticipated rates hikes, the share of longer fixings (above 5 years) increased to 40% at the beginning of 2022. In 2024 there was a mild increase in 1-year fixed periods approaching 10% of new production in April, from a typical 2-3%. Variable rate mortgages are virtually non-existent.

The average maturity of new mortgage contracts was around 26 years, almost the same as a year ago. More than half of new housing loans (volume wise) had the maximum possible maturity of 30 years and less than 17% chose a maturity of 20 years or less. The trend of stretching the maturity has been present already for several years but it seems that it has gradually reached its limits.

Although the volume of NPLs experienced a mid-single-digit increase y-o-y, it matched reported annual growth of mortgages outstanding. The NPL ratio thus remained at 1.1% throughout the year. The asset quality deterioration has not materialized despite the economic outlook.

A prominent feature of the market is a high share of new loans intermediated by financial advisors. In 2023, 64% of total lending volume was via such external sales network. The share was only slightly lower than a year ago. The National Bank of Slovakia (NBS) considers intermediated loans as somewhat riskier and sees intermediaries as too aggressive, pushing clients to the maximum level of indebtedness allowed.

Due to the NBS's limits on the maximum LTV ratio, the average has stabilised in recent years at around 70%. The share of new loans that can have an LTV ratio between 80% and 90% is 20% of new production and new loans with an LTV greater than 90% are not allowed. Other measures to fight increases in household indebtedness, which are currently in place, are limits on DTI, set at 8 times in mid-2018 and DSTI, defined as a minimum reserve which must be left aside out of monthly net income after deduction of debt repayments and minimum living costs. The reserve has to be at least 40% since mid-2020. The limits were not changed during the pandemic nor amid the increasing rates as NBS considers the development of declining indebtedness measures favourable for the sector (at least temporarily).

LOOKING AHEAD

The mortgage market did not live up to general expectations in the first half of 2024. The real estate market failed to gain momentum as interest rates remained elevated. While rates declined in other Eurozone countries in line with expectations of ECB's easing, Slovak commercial banks kept rates mostly unchanged. The first reason was newly introduced higher tax rate for banks which pushed the effective income tax rate of banks from around 22% to above 40%. The tax rate (on top of the regular income tax, paid from pre-tax profit) is set to decrease gradually from 30% in 2024 to 15% in 2027, when banks should pay "regular tax for companies operating in regulated industries" which is currently set at 4.4%. The second negative effect was uncertainty about the state budget deficit as the government could not for some time present credible consolidation measures for coming years. As a result, spreads on Slovak government bonds remained high compared to other Eurozone countries. This had also a negative effect on the cost of financing for commercial banks. Strong revival of housing loans is therefore not expected until at least Q3 2024.

MORTGAGE FUNDING

Deposits are, for banks, one main source and for the building societies, the only source of funding for mortgages. Short-term deposits and current accounts have offered stable, low-cost funding for banks and building societies for a long time. Retail deposits had borne virtually 0% interest rates for some time, they rose to around 0.5% in 2023. Current accounts continued to pay 0% while average interest rate on term deposits was already at 1.8% at the end of 2023. Higher rates, together with improving real wage growth, pulled annual growth of retail deposits to more normal levels of 5% as of Q1 2024. More noticeable growth was seen in corporate deposits at 10%.

Loan-to-deposit ratio therefore declined slightly from 109% to 107% in 2023. Such high loan-to-deposit ratio is still seen as acceptable since banks can fund their lending by issuing covered bonds. Covered bonds are an attractive funding tool for Slovak banks as they are typically cheaper than senior unsecured bonds, as they are asset-backed, highly rated (triple A or slightly lower, depending on the actual over-collateralisation), therefore are perceived as lower risk by investors. TLTRO funding was successfully used by the largest banks, mostly due to its positive effect on profitability rather than as a necessary source of funding. As of year-end 2023, almost the entire volume had been repaid.

	SLOVAKIA 2022	SLOVAKIA 2023	EU 27 2023
MACROECONOMIC VARIABLES			
Real GDP growth (%) (1)	1.9	1.6	0.4
Unemployment Rate (LSF), annual average (%) (1)	6.1	5.8	6.1
HICP inflation (%) (1)	12.1	11.0	6.4
HOUSING MARKET			
Owner occupation rate (%) (1)	93.0	93.6	69.2
Gross Fixed Investment in Housing (annual change) (1)	7.2	-14.5	-3.1
Building Permits (2015=100) (2)	108.8	95.9	94.0
House Price Index - country (2015=100) (2)	212.9	200.1	170.2*
House Price Index - capital (2015=100) (2)	198.2	184.9	165.1*
Nominal house price growth (%) (2)	21.3	-6.0	3*
MORTGAGE MARKET			
Outstanding Residential Loans (mn EUR) (2)	41,602	39,035	6,782,375
Outstanding Residential Loans per capita over Total Population (EUR) (2)	7,655	7,190	15,114
Outstanding Residential Loans to disposable income ratio (%) (1) (2)	59.6	51.4	71.3
Gross residential lending, annual growth (%) (2)	-14.6	-59.7	-26.6
Typical mortgage rate, annual average (%) (2)	1.9	4.3	4.7

* Please note that this value is a simple average of the available values in 2023.

Sources:
(1) Eurostat.
(2) European Mortgage Federation - Hypostat 2024, Statistical Tables.

SLOVAKIA FACT TABLE

Which entities can issue mortgage loans in your country?	Housing finance is raised from banks, building societies and State funds with only minimum volume provided.
What is the market share of new mortgage issuances between these entities?	Majority of new mortgages is issued by commercial banks (over 95%), followed by building societies (~3-4%) and state funds contributed with just marginal volumes.
Which entities hold what proportion of outstanding mortgage loans in your country?	Banks had a market share of 94%, building societies of 6% and the state funds just 0.1%.
What is the typical LTV ratio on residential mortgage loans in your country?	In 2023, the average LTV for newly provided mortgages was about 70%. Maximum LTV ratio of 90% is possible although only up to 20% of all newly provided mortgage can have an LTV between 80% and 90%. However, the share of mortgages with LTV between 80% and 90% is just 10% of the total new production.
How is the distinction made between loans for residential and non-residential purposes in your country?	NBS regulations define the purpose and eligible cover (i.e. residential property – flat, house, apartment house or land designed for housing construction) for residential loans. Non-residential loans cannot be included in the cover pools of the covered bonds.
What is/are the most common mortgage product(s) in your country?	Most mortgage loans taken out are loans with rates fixed for period of 3 or 5 years which typically constitute up to 90% of the newly provided housing loans. Loans with floating rate are virtually non-existent.
What is the typical/ average maturity for a mortgage in your country?	Average maturity of a new mortgage loan was about 26 years in 2023. Mortgage loans can have maturity of at least 4 years and maximum of 30 years. There are certain exceptions (e.g. for some Building societies' products the maximum maturity can be extended to 40 years) to these rules, but these are applied only to a fraction of volumes provided.
What is/are the most common ways to fund mortgage lending in your country?	For banks, deposits are one main source and for the building societies the only source of funding for their mortgage market activities. Banks also fund their lending activities through issuance of covered bonds.
What is the level of costs associated with house purchase in your country (taxes and other transaction costs)?	Relatively low. Legal, notarial and registration costs are in the order of hundreds to thousands of euros (depending on property value and specifics of the transaction). No special taxes are payable. Real estate agents' fees are typically 3% - 6%.
What is the level (if any) of government subsidies for house purchases in your country?	Subsidies are provided in two main forms: • Mortgage loan for young – tax bonus of 50% of interest costs, up to EUR 400 per annum, eligibility limited by income and age of debtor. • State Housing Development Fund - providing loans with lower interest rates. But the volume of state loans is low, and conditions apply. New measures by the government were introduced for 2024 as a compensation for increased debt service due to higher interest rates: • Tax return for 2023: tax bonus of 75% of an instalment increase due to higher interest rate, up to EUR 150 per month (EUR 1,800 per annum) • For 2024: - Direct payment of 75% of an instalment increase, up to EUR 150 per month (EUR 1,800 per annum) - Mortgage loan for young – maximum tax bonus increased to EUR 1,200 per annum; debtor's income limit was increased; maximum loan volume was abandoned.