GLOSSARY

Balance-sheet liquidity The ability of an institution to meet its obligations in a corresponding volume and term structure.

Balance-sheet recession A situation caused by the efforts of market participants to reduce their debt, a resulting drop in demand for loans, and a limited ability to stimulate economic activity through monetary policy. The onset of a balance-sheet recession usually follows a sharp decline in asset prices, when the balance sheets of market participants can record negative equity, i.e. the value of assets is lower than that of balance-sheet liabilities. A typical example is the period following the bursting of the stock and property bubble in Japan during the 1990s.

Bank Lending Survey (BLS) A survey of bank lending conditions for non-financial corporations and households in the Czech Republic, the pilot round of which took place in 2012 Q1. The survey aims to obtain qualitative information on current perceptions of the situation on both the supply and demand side of the credit market.

Basel III A new regulatory framework issued by the Basel Committee on Banking Supervision in 2010 which sets standards for capital adequacy of banks and now also for their liquidity. Overall, Basel III introduces stricter rules than the previous framework and came into existence mainly as a reaction to the financial crisis.

Breakdown of banks by total assets
In some charts and tables in the FSR, banks are assigned to groups based on the amount of their total assets. The breakdown of banks into groups is revised at the end of each calendar year. In 2007 and 2008, banks having total assets of over CZK 150 billion were regarded as large banks, banks having total assets of over CZK 50 billion and up to CZK 150 billion were regarded as medium-sized banks and banks having total assets of less than CZK 50 billion were regarded as small banks. In 2009 the total amount of assets necessary for inclusion in the group of large banks was increased to CZK 200 billion and the range for medium-sized banks was changed to CZK 50 billion–CZK 200 billion. The range for small banks was unchanged. As from 2012, the breakdown of banks by total assets is as follows: large banks have total assets of over CZK 250 billion, medium-sized banks have total assets of over CZK 50 billion and up to CZK 250 billion and small banks have total assets of less than CZK 50 billion.

Capital ratio The ratio of regulatory capital to total risk-weighted assets. The Tier 1 capital ratio is the ratio of Tier 1 capital to total risk-weighted assets (see also Tier 1).

Capital requirement The capital requirement is the amount of capital a bank has to hold so as to cover all the risks it undertakes.

Collective investment funds (CIFs)
Mutual and investment funds whose sole business activity is collective investment, i.e. collecting funds from investors and investing them. CIFs are broken down by investor type into funds intended for the public (dominated by open-ended mutual funds) and funds for qualified investors, and by asset risk into money market, bond, equity, mixed and real estate funds and funds of funds. Sometimes the category of funds of funds is not listed separately, but is included in the other categories according to the type of funds in which they invest.

Common Reporting Framework (COREP)
A common reporting framework in the EU, prepared by the European Banking Authority (EBA) for data reporting in accordance with prudential requirements (under CRR). It covers the areas of capital, capital adequacy, risk exposures, operational risk, market risk and credit risk.

Consumer credit Credit used to finance household consumption. It also includes bank overdrafts and debit balances and credit card credit.

Countercyclical capital buffer
A macroprudential tool designed to increase the banking sector's resilience to cyclical risks associated with fluctuations in lending.

Debt deflation A situation where the real value of the debt of corporations and households rises as a result of falling prices and incomes. This happens primarily in a situation where the decrease in nominal interest rates is insufficient to offset the fall in the rate of growth of incomes.

Debt service-to-income (DSTI)
The ratio of total debt service to the net income of the loan applicant.

Debt-to-income The ratio of debt to the net income of the loan applicant.

Default Default is defined as a breach of the debtor's payment discipline. The debtor is in default at the moment when it is probable that he will not be able to repay his obligations in a proper and timely manner, without recourse by the creditor to settlement of the claim from the security, or when at least one repayment (the amount of which deemed by the creditor to be significant) is more than 90 days past due.

Default rate The 12-month default rate is the ratio between the volume of liabilities of debtors which defaulted over a 12-month reference period and the volume of liabilities of all entities existing at the start of that period. The default rate can also be defined analogously in terms of the number of entities which defaulted over the reference period.

Deleveraging A process consisting in the reduction of leverage, i.e. the reduction of indebtedness, which decreases the profitability of economic agents, but also the degree of risk associated with them.

Eligible collateral An asset accepted to ensure fulfilment of an obligation to the central bank.

Financial Reporting Framework (FINREP)
A common reporting framework in the EU, prepared by the European Banking Authority (EBA) for data reporting in accordance with prudential requirements (under CRR). It covers the area of financial data of individual institutions, in particular the balance sheet and the profit and loss account.

Gross government borrowing requirement
The net government borrowing requirement plus redemptions and repurchases of government bonds maturing in the given year, repayments of EIB loans, repurchases and exchanges of government bonds maturing in future years, and revaluation of funding reserves.

Herfindahl-Hirschman index (HHI)
The sum of the squares of the market shares of all entities operating on a given market. It expresses the level of concentration in the market. It takes values between 0 and 10,000. The lower the HHI, the less concentrated the market.

Household insolvency A situation where a household is unable to cover its current expenditures by its current income and the sale of its asset holdings. Insolvency is defined in legal terms in Act No. 182/2006 Coll., on Insolvency and Methods of Resolution Thereof.

IFRS 9 The financial reporting standard IFRS 9 *Financial instruments*, the final version of which was introduced in July 2014 by the International Accounting Standards Board (IASB), took effect on 1 January 2018 pursuant to Commission Regulation (EU) 2016/2067, replacing the previously valid IAS 39 standard. IFRS 9 lays down requirements for the recognition, valuation, impairment and derecognition of financial assets and financial liabilities and general hedge accounting. It aims to provide financial statement users with relevant information for assessing the size, timing and uncertainty of an entity's future cash flows.

Institutional investor Either (a) a bank executing trades in investment instruments on its own account on the capital market, a management company, an investment fund, a pension fund or an insurance company, or (b) a foreign entity authorised to carry on business in the same fields in the Czech Republic as the entities listed under (a).

Interest margin The difference between a bank's loan rate and its deposit rate.

Interest rate spread Also interest rate differential; the spread between the interest rate on a contract (deposit, security) and a reference interest rate.

Interest rate transmission channel
One of the channels of the monetary policy transmission mechanism. It acts such that, for example, an increase (decrease) in monetary policy interest rates leads first to an increase (decrease) in interest rates on the interbank market. Consequently, there is an increase (decrease) in the interest rates announced by banks for the provision of loans and the acceptance of deposits. The result is a downturn (upturn) in investment activity as a part of aggregate demand and ultimately a decrease (increase) in inflation pressures.

Leverage See Leverage ratio.

Leverage ratio The new CRD IV/CRR rules define the leverage ratio as capital to risk-weighted assets. The term leverage is also often used in financial economics. There, however, capital is the denominator in the ratio (e.g. assets/capital or debt/capital). When we say that a bank has high leverage, we generally refer to the definition consistent with the assets/capital ratio. However, such a bank has a low leverage ratio.

Liquidity coverage ratio A requirement to cover net liquidity outflows over a 30-day time horizon with liquid assets. It is calculated as the ratio of the liquidity buffer to the net liquidity outflow.

Loan for house purchase A loan intended for the acquisition of residential property.

Loan service-to-income The ratio of loan-related debt service to the net income of the loan applicant.

Loan-to-income (LTI) The ratio of the amount of a loan to the net income of the loan applicant.

Loan-to-value (LTV) The ratio of the amount of a loan to the value of collateral.

Loss given default (LGD) The ratio of the loss on an exposure in the event of counterparty default to the amount owed at the time of default.

Macroprudential policy A key component of financial stability policy. It focuses on the stability of the financial system as a whole. Its main objective is to help prevent systemic risk.

Market liquidity The ability of market participants to carry out financial transactions in assets of a given volume without causing a pronounced change in their prices.

Minimum Requirement for Own Funds and Eligible Liabilities (MREL)

A sufficient volume of eligible liabilities is necessary for a failed bank to be recapitalised using internal funds (bail-in). In the event of a crisis, the CNB writes off or converts these liabilities. A sufficient MREL together with the application of a suitable combination of resolution tools thus enables a failed institution to be resolved without the use of public money.

Mortgage refinancing The process whereby a mortgage debtor accepts a new loan from a different lender than the one from which he received the original loan and uses it to repay the original loan. He thus becomes a debtor of the other lender, but usually under more favourable conditions. This is usually possible only at the end of the original loan's fixation period.

Mortgage refixation The process whereby at the end of the fixation period of a mortgage loan the debtor selects the length of the new fixation period and negotiates new conditions for this period with the creditor. In this case, the identity of the creditor does not change.

Natural population increase The difference between the number of live births and the number of deaths in the same period of time in a given area.

Net financial assets The difference between the sum of financial assets and the sum of liabilities.

Net stable funding ration (NSFR)

A structural liquidity requirement monitored over a one-year time horizon. It is defined as the ratio of available stable funding to required stable funding.

Non-performing loans A loan is non-performing if at least one of the following two situations occurs: a) the debtor is unlikely to pay its credit obligations in full without recourse to actions such as realising security, b) the debtor is past due more than 90 days on a credit obligation. For details, see Article 178 of Regulation (EU) No 575/2013 of the European Parliament and of the Council. Non-performing loans are broken down into substandard, doubtful and loss loans. Also called loans in default or default loans.

Overnight indexed swap A term contract between economic agents consisting in the mutual exchange of interest payments corresponding to a fixed rate and a floating overnight financial market reference rate.

Pension funds In the Czech environment, pension funds are transformed and participation funds which are managed by pension management companies. Participation funds are further classed into obligatory conservative funds and other funds. Obligatory conservative funds are only allowed to invest in a significantly restricted group of assets.

Pillar 1 The first part of the CRD directive, focused on the determination of minimum capital requirements for all credit institutions to cover credit, market and operational risks.

Pillar 2 The second part of the CRD directive, requiring credit institutions to assess whether the Pillar 1 capital requirement is sufficient to cover all the risks to which they are exposed. This assessment process is reviewed by the supervisory authority under the supervisory review and evaluation process (SREP). The supervisory authority then can apply a wide range of instruments, including setting an additional capital requirement, for example to cover concentration risk.

Prague InterBank Offered Rate (PRIBOR)
The reference interest rate on the interbank deposit market for deposit sales. Reference banks quoting the PRIBOR must be important participants in the interbank market.

Price-to-income (PTI) The ratio of the price of an apartment (68 m^2) to the sum of the annual wage in a given region over the last four quarters.

Price-to-rent (PR) The ratio of the price of an apartment to the annual rent. The price-to-rent ratio is the inverse of the rental return.

Property asking prices Property sale asking prices in estate agencies. Asking prices should be higher than transaction prices. Property asking prices in the Czech Republic are published, for example, by the CZSO and the Institute for Regional Information (which also publishes data on market rent supply prices).

Property developers/developments
Companies/projects whose aim is to build a complex of residential and commercial property. Property developers' work includes choosing an appropriate site, setting up a project, obtaining the necessary permits, building the necessary infrastructure, constructing the buildings and selling the property. Developers also often organise purchase financing for clients and frequently lease or manage the property once it is built (especially in the case of commercial property). Given the combination of construction activity and speculative property purchases, developers' results are strongly dependent on movements in property prices.

Property price gap The deviation of the price of property from its estimated equilibrium value.

Property transaction prices
Prices of actual transactions on the property market, which should be the closest to actual market prices. The CZSO has been publishing two types of data on property transaction prices since 2011. Prices based on Ministry of Finance statistics from property transfer tax returns and published by the CZSO are the older source. These data contain time series from 1998 and are available in a relatively detailed breakdown (by region, degree of wear and tear and type of property). On the other hand, they do not include transactions which are not subject to property transfer tax (i.e. primarily transactions in new property) and the index is published with a lag of at least half a year. The second, new source of data on property transaction prices is data from CZSO surveys in estate agencies. They cover new property, but are not available in such a long time series and such a detailed breakdown.

Quantitative easing A method for implementing monetary policy in a situation where the central bank is no longer able to lower its monetary policy rate because it has already reduced it almost to zero. Quantitative easing involves the central bank buying assets from commercial banks and

thereby creating a sizeable stock of free reserves with those banks. The purpose of this type of policy is to strengthen the balance-sheet and market liquidity of the banking system and minimise the risk of growth in interest rates due to insufficient liquidity. In the past ten years, quantitative easing has been applied in Japan and the USA. A similar policy is now being pursued, for example, by the ECB.

Rental return The ratio of the annual supply rent to the asking price of the apartment. It is the inverse of the price-to-rent ratio.

Return on assets (RoA) The ratio of pre-tax profit and interest to total assets of a firm.

Return on equity (RoE) The ratio of net profit to equity of a firm.

Risk premium The risk premium an investor demands on investments in riskier financial instruments.

Saving rate (households) A flow indicator showing the ratio of savings to gross disposable income of households. In simplified terms, savings are the part of income not spent on consumption in a given period.

Search for yield A situation where economic agents attempt to make up for generally low asset yields by seeking riskier-than-usual investments that yield a premium in return for the increased risk. Such behaviour may increase the future risks to the financial system.

Secondary market The market on which existing securities are traded.

SKEW An index of expectations of extraordinary events (tail risk) for US stock (S&P 500 index), derived from market prices of options traded at the Chicago Board Options Exchange. The calculation is based on options with a significantly lower strike price than the current value of the stock index. SKEW typically ranges from 100 to 150, with a higher value indicating a higher probability that the stock market will fall sharply and such options will be exercised.

Solvency (insurance companies)

Solvency in the insurance sector is the ability of an insurer to meet its insurance obligations, i.e. to settle eligible insurance claims arising from insured losses.

Solvency II A European regulatory framework (directive) for European insurance companies and reinsurers laying down quantitative and qualitative requirements and prudential rules, including requirements to comply with market discipline and disclosure duties. It entered into force in 2016, when it replaced the Solvency I regulatory framework.

Solvency ratio The ratio of the own funds of an insurance company to the minimum capital requirement necessary to cover all the risks it undertakes.

Sovereign risk The risk that a government will default on its obligations, leading to national bankruptcy or restructuring of government debt.

Systemic risk The risk of the entire financial system or market collapsing.

Technical interest rate The interest rate used by insurance companies to calculate premiums in life insurance. The technical interest rate represents the increase in the value of life insurance provisions to which the customer is entitled under the policy (the guaranteed share in the returns on financial investment). The maximum technical interest rate is laid down in a decree.

Tier 1 The highest quality and, for banks in the Czech Republic, also the most significant part of regulatory capital. The dominant components of Tier 1 are equity capital, retained earnings and mandatory reserve funds.

VIX An index of expected 30-day volatility of US stocks (S&P 500 index), derived from market prices of options traded at the Chicago Board Options Exchange. A higher value indicates higher expected volatility of the stock index, and therefore higher market uncertainty.

Yield spread Also yield differential; the spread between the yield on a bond and the yield on a reference ("benchmark") bond.