

# Flash Comment

## Euroland: Credit tightening is slowing

- The Euroland Bank Lending Survey shows that banks are continuing to tighten credit standards significantly, in respect of both enterprises and households, in the first quarter of this year, but not as much as in fourth quarter of last year.
- The reason behind the tightening with regard to enterprises is primarily concern about general economic activity and industry/firm-specific outlook. The importance of banks' cost of funds and balance sheet constraints diminished – but are still at high levels.
- Banks expect further credit tightening in the second quarter, but at a substantially slower pace. We believe that we could see stabilisation, or even an easing of credit standards, before the end of the year.
- Banks also indicated that recapitalisation support and state guarantees have already had a positive affect on their access to funding and are expected to further ease access to funding in the second quarter of 2009.
- Net demand for loans from both enterprises and households continued to decline, but demand for loans for house purchases declined much less than in previous quarters. This is a first sign that the very low interest rate level is now helping to stabilise housing demand.

### Details:

The net percentage of banks that tightened credit standards for loans to enterprises declined from 63% in Q4 08 to 43% in Q1. Just 28% of banks (net) expect to tighten further in Q2. In this respect it is noteworthy that the expectations have been quite precise in recent quarters.

The factors contributing to credit tightening to enterprises were primarily “industry or firm specific outlook” and “expectations regarding general economic activity”. Whereas in Q4 general economic activity was most important, now it is the industry-specific outlook. This may reflect that banks are now getting a more detailed picture of the crisis and this should increase the likelihood that sound enterprises can get access to finance. The tightening factor “access to finance” is at its best level in more than a year. This is a very important signal that financial market conditions are improving. We are now moving from an emphasis on the financial crisis to the economic crisis that has followed in its aftermath.

Credit standards were primarily tightened by margin increases – in particular on riskier loans. The tightening continues to be stronger for loans to large enterprises than for loans to small and medium-sized enterprises.

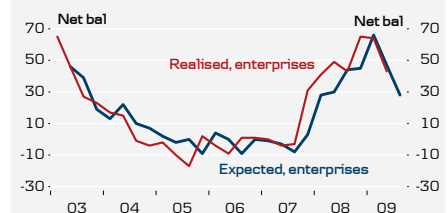
Banks also indicated that government announcements of recapitalisation support and state guarantees for debt securities issued by banks had a positive impact on banks' access to funding in Q1 and is expected to further ease access to funding in Q2. Nevertheless, banks access to funding remained limited in Q1 as a result of the financial crisis. Only in the case of very short-term funding did a majority of reporting banks indicate that access was not hampered in the first quarter of 2009.

### Credit tightening (1<sup>st</sup> quarter 2009)

	Act	Con	Last
Enterprises	43 %	-	68 %
House purchase	28 %	-	42 %
Consumer credit	26 %	-	42 %

Source: ECB

### Credit tightening on loans to enterprises



Source: EcoWin

### Credit tightening on loans for house purchase



Source: EcoWin

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The net percentage of banks that tightened credit standards for loans to households for house purchase declined from 42% in Q4 08 to 28% in Q1. 20% of banks (net) expect to tighten further in Q2. The expectations are generally quite precise and thus give a good indication that we will see further tightening, but the pace of tightening continues to decline. The credit tightening to households for house purchase is primarily driven by concerns regarding general economic activity and housing market prospects. Housing market prospects are being used much less as a reason for credit tightening than in Q4.

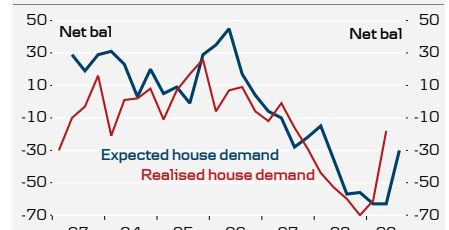
Demand for loans for house purchase has declined much less in Q1 than in each of the past four quarters. 20% of banks actually experienced increasing demand for loans for house purchases in Q1. This could signal a turning point for the European housing markets, but we believe that it is too early for that as yet. Nevertheless we should expect to see the current very low interest rate level give some support to housing demand and some stabilisation of the housing market could well take place in the coming quarters.

The continued credit tightening and decline in loans demand was also reflected in annual money supply growth, which was also published yesterday. Money supply growth (M3) and loans to the private sector continued to decline in March. The annual growth rate of loans to the private sector decreased to 5%, from 6.1% in the previous month and the annual rate of growth of lending for house purchases declined to 0.1% in March, from 0.4% in February. We expect to see continued decline in the annual growth rates for some months to come, as credit tightening and decline in loans demand continue, albeit at a slower pace. In Q3 we could well see a stabilisation of annual money growth and we would not be surprised to see some initial increases in annual growth rates in Q4.

The annual growth rate for M1 it has been on an increasing trend since September last year, but declined slightly in March. The increase in M1 growth signals that we should see a substantial increase in GDP growth in the coming quarters. It should, however, be noted that the increase in both overnight deposits and currency in circulation (the two items in M1) may have been affected by structural developments.

All in all the signals from the bank lending survey and money growth confirm our view that we may not be at the bottom yet. However, the economy is no longer in free fall and we begin to see the first signs of stabilisation and a turning point in the tightening cycle. We believe that we could see stabilisation or even an easing of credit standards before the end of the year.

### Demand for loans for house purchase



Source: Ecwin

### Credit growth still in decline



Source: Ecwin

### Growth in M1 signals GDP growth



Source: Ecwin

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