



**August 1999**

## **Senior Loan Officer Opinion Survey on Bank Lending Practices**

*Note: Some data for the May 1999 survey were slightly revised after their May 21 release, but the survey's overall conclusions were not affected. The summary of the May survey currently available on this web site reflects the revised results.*

The August 1999 Senior Loan Officer Opinion Survey on Bank Lending Practices focused primarily on changes over the past three months in the supply of and demand for bank loans to businesses and households. Additional questions addressed Year 2000 (Y2K) issues and loan quality. Loan officers from fifty-six large domestic banks and twenty-two U.S. branches and agencies of foreign banks participated in the survey. The responses suggest that banks became somewhat more cautious lenders over the past quarter but show no widespread reduction in credit availability.

The results indicate a continued slight firming of business lending practices. For domestic banks, this has taken the form more of a tightening of terms on C&I loans, particularly risk premiums and loan rate spreads, as only a few reported that they had strengthened underwriting standards. In contrast, large proportions of the branches and agencies tightened both standards and terms on C&I loans. Similarly, for commercial real estate loans, a small fraction of domestic banks and a larger fraction of branches and agencies raised standards.

The survey found little evidence of any changes in standards and terms on loans to households. A small net fraction indicated greater willingness to make consumer installment loans, and virtually no banks indicated any change in standards for or terms on credit card and other consumer loans. Demand for consumer loans was also reported to be about unchanged, but many banks said that demand for home mortgages had decreased.

To a large extent, respondents said they were willing to extend special contingency lines of credit over year-end, at least to existing customers, but most had not received requests for such lines. The banks were not, in general, tightening terms and standards on renewals of existing lines over year-end. Those banks limiting credit lines over year-end were chiefly concerned about Y2K effects on borrowers' repayment prospects, although several were also worried about the effects of borrowing on capital ratios, and about possible difficulties they might encounter in funding draws on credit lines over year-end. A large majority of the respondents appeared willing to use the Federal Reserve's recently announced Special Liquidity Facility. Those expressing reluctance to use the facility cited as reasons difficulties with collateral procedures and a resistance by senior management to borrowing at the discount window.

A number of respondents indicated that over the past year the performance of their business loan portfolios had become more sensitive to a period of economic weakness, primarily because of a weaker financial condition of borrowers, but also because of eased lending

standards and terms. Banks assessed the sensitivity of their household loan portfolio to an economic slowdown to have changed little over the past year.

## **Lending to Businesses**

(Table 1, questions 1-7; Table 2, questions 1-7)

About 5 percent of domestic bank respondents said that over the past three months they had tightened standards on C&I loans to large and middle-market borrowers (down from 10 percent in May), and nearly 25 percent of the branch and agency respondents said that they had tightened (about the same as in May). The survey found virtually no change, on net, in standards on loans to small businesses. On net, about a fourth of the domestic banks and more than half of the branches and agencies reported tightening terms on C&I loans, particularly risk premiums, spreads of loan rates over the banks' cost of funds, and costs of credit lines. The net percentages tightening terms increased a bit relative to those recorded on the May survey. However, in the case of both standards and terms, the net percentages tightening are significantly lower than those reported last fall. Loan officers most commonly cited a worsening of industry-specific problems, a less favorable or more uncertain economic outlook, and a reduced tolerance for risk as reasons for having tightened.

On net, no domestic bank respondents said that demand for C&I loans had changed over the preceding three months (neither from large and middle-market firms nor from small businesses). The branch and agency responses also showed virtually no change in demand. Those respondents reporting a change in demand generally attributed it to variation in their customers' merger and acquisition and plant and equipment financing needs.

As in May, less than 10 percent of domestic bank respondents, on net, reported tighter standards on commercial real estate loans. By contrast, nearly 40 percent of branch and agency respondents tightened standards on these loans, a larger percentage than in May. About 10 percent, on net, of the domestic bank respondents said that demand for commercial mortgages had increased over the past three months; branch and agency respondents also reported little change in demand. Only about half of the foreign bank respondents answered the questions on commercial real estate loans, likely reflecting the departure of many of the branches and agencies from this line of business.

## **Lending to Households**

(Table 1, questions 8-15)

As in recent quarters, banks appear not to have made any significant adjustments to their consumer lending policies following the pronounced tightening that began in the mid-1990s. About 10 percent of the respondents, on net, said their willingness to make consumer installment loans had gone up over the preceding three months. Only two banks tightened standards on credit cards; and three, on net, tightened standards on other consumer loans. Terms on these loans were also reported as little changed. About 10 percent of the banks, on net, reported stronger demand for consumer loans.

The survey also found little evidence of changed standards for home mortgages, with one bank, on net, easing. A large net percentage--35 percent--said that demand for home mortgages had decreased, whereas in May respondents had reported increased demand. Even though the question specifically asks about demand for mortgages for purchasing homes as opposed to refinancing existing mortgages, the reported decrease in demand still may reflect, in part, a decline in refinancing activity.

## Year 2000

(Table 1, questions 16-27; table 2, questions 8-19)

The respondents reported continued progress toward mitigating the Year 2000 risks posed by their customers. More than 90 percent of the domestic banks, up from 70 percent in May, had evaluated the Y2K preparedness of at least 90 percent of their material business customers. About 80 percent of branches and agencies had evaluated 90 percent of their customers, up only a little from May. About 95 percent of the banks surveyed stated that less than 5 percent of their customers that had been evaluated were not making satisfactory progress toward achieving Y2K preparedness.

The survey results indicate that requests for Year 2000 contingency lines of credit have been limited to date. Relatively small percentages of the domestic bank respondents had received requests for such lines from nonfinancial and financial firms--10 percent and 20 percent, respectively. These percentages, however, are about twice as large as those found in May. Branch and agency respondents were less likely to have received requests for such lines. Requests for contingency lines came from many different types of financial firms, with the largest number of respondents having received requests from domestic commercial banks, followed by finance companies, mutual funds, securities dealers and brokerages, and savings and loans. Some of the loan officers noted that although they have received relatively few requests to date for contingency lines, the requests they had received were, in some cases, substantial, and they thought that more requests may be forthcoming.

All the domestic bank respondents were willing to extend Y2K contingency lines, but nearly two-thirds--a larger fraction than in May--would do so only for existing customers. About a third of the branches and agencies were unwilling to extend contingency lines; the remainder were willing to extend such lines only to existing customers. A fourth of the domestic banks, up from about 15 percent in May, had tightened standards or terms on renewals of existing lines that extended into next year but were not specifically meant to meet year-end funding needs. Those banks that were tightening policies on renewals were raising spreads or fees, tightening standards, requiring a rate premium for advances around year-end, or pricing lines off of their own cost of funds rather than off independent indexes (such as LIBOR). By contrast, two-thirds of the branches and agencies were adjusting policies on renewals, including limiting the usage of lines over year-end. Those respondents (domestic and foreign) that were unwilling to extend Year 2000 contingency lines of credit, were limiting such lines to existing customers, or had tightened standards or terms on renewals of existing lines gave a variety of reasons for their reluctance. Most commonly, they were concerned about Y2K effects on borrowers' repayment prospects, difficulty funding draws on credit lines over year-end, the effect of borrowing on capital ratios, and also about credit quality generally.

Several questions addressed the willingness of respondents to use the Century Date Change Special Liquidity Facility (SLF), which will make discount window credit readily available to depository institutions in sound financial condition at a 150 basis point premium over the FOMC's target federal funds rate between October 1, 1999, and April 7, 2000. Nearly 70 percent of the domestic and foreign respondents said they would not be likely to borrow overnight funds in the market at a rate greater than that charged by the SLF. Of the institutions that would pay more for funds to avoid borrowing from the SLF, a third thought it likely they would pay more than 50 basis points in excess of the SLF rate to do so. Those that would be willing to pay a premium to avoid borrowing at the SLF cited as the reasons difficulties with collateral procedures and limitations on the amount of collateral the institution has available to pledge, resistance by senior management to borrowing at the discount window, and concern that use of the facility would be viewed negatively either by bank regulators or by market participants.<sup>1</sup> Over 80 percent of the respondents said that the

existence of the SLF had not changed their willingness to extend Year 2000 contingency lines of credit.

## Loan Quality

(Table 1, questions 28-29; table 2, questions 20-21)

Two special questions addressed changes in loan quality over the past year. On net, the domestic respondents said that the delinquency and charge-off rates of their credit card and other consumer loans had not become more sensitive to a period of economic weakness over the past year, although a few said their residential real estate loans had become more sensitive. A small net percentage of the domestic and foreign respondents, about 15 percent, judged their commercial real estate loans to have become more sensitive to a downturn. However, about a third of the domestic and foreign respondents, on net, said that their C&I loan portfolios had become more sensitive. Domestic banks most commonly attributed the heightened sensitivity of their C&I loan portfolios to borrowers' greater financial leverage, and also noted borrowers' narrower profit margins and banks' eased lending standards and terms. Branches and agencies stressed in addition a shift in the composition of borrowers toward riskier credits.

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1. As noted in the questionnaire, absent signs of financial trouble, use of the Special Liquidity Facility will not be taken as an indication of underlying problems and will not trigger intensified oversight by supervisory authorities. As also noted, the Federal Reserve treats information on individual bank borrowing at the discount window as confidential.

The report, with charts and tables, is available in Acrobat (PDF) format. <a href="#">Obtaining the Acrobat Reader</a>
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### **Charts** ([17 KB PDF](#))

Measures of lending practices from current and previous surveys

**Chart data** ([ASCII](#))

### **Table 1** ([31 KB PDF](#))

Summary of responses from U.S. banks

### **Table 2** ([21 KB PDF](#))

Summary of responses from branches and agencies of foreign banks

### **Full report** ([82 KB PDF](#))

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