Box 2

THE RESULTS OF THE JULY 2006 BANK LENDING SURVEY FOR THE EURO AREA

This box describes the main results of the July 2006 bank lending survey for the euro area carried out by the Eurosystem.[1] In the second quarter of 2006, credit standards on loans to enterprises remained broadly unchanged in net terms[2] compared with the previous quarter. At the same time, banks continued to ease credit standards applied to both loans to households for house purchase and consumer credit and other loans. During the second quarter of 2006, net loan demand,[3] as perceived by banks, continued to rise for loans to enterprises and loans to

1 A comprehensive assessment of the results of the July 2006 bank lending survey for the euro area was released on 4 August 2006 and can be found on the ECB's website.
2 The net percentage refers to the difference between the proportion of banks reporting that credit standards have been tightened and the proportion of banks reporting that they have eased. A positive net percentage would indicate that banks have tended to tighten credit standards ("net tightening"), whereas a negative net percentage would indicate that banks have tended to ease credit standards ("net easing").
3 The term "net demand" refers to the difference between the proportion of banks reporting an increase in loan demand and the proportion of banks reporting a decline.

households for consumption and other purposes, whereas it decreased further for loans to households for house purchase, although remaining in positive territory.

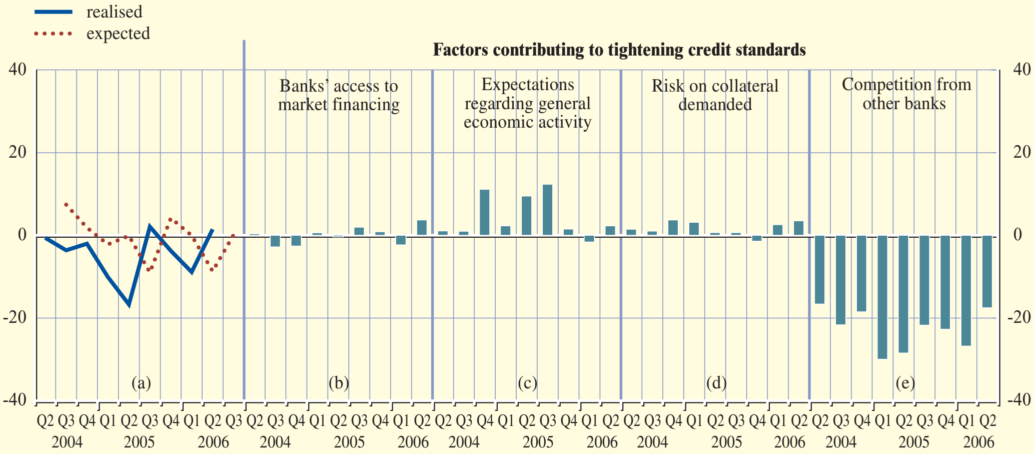
For the third quarter of 2006, banks expected credit standards applied to loans to enterprises and loans to households for house purchase to remain unchanged and forecast a further net easing for consumer credit and other lending to households. On the demand side, banks expected an increase in net demand for loans to both enterprises and households for the period from July to September 2006.

Loans or credit lines to enterprises

Credit standards: For the second quarter of 2006, banks reported broadly unchanged credit standards applied to loans or credit lines to enterprises (1%, from -9% in the previous quarter; see Chart A, panel a). The costs related to bank capital, banks' ability to access market financing and the increased perceived risks regarding the industry or firm-specific outlook contributed to a tightening of credit standards (see Chart A, panels b and d). At the same time, competition from other banks continued to militate in favour of an easing of credit standards (see Chart A, panel e), while expectations regarding general economic activity, as in previous quarters, affected credit standards in a neutral manner (see Chart A, panel c). As regards the terms and conditions of credit, there was a narrowing of margins on average loans and a lengthening of the maturity of loans or credit lines, while, as in previous quarters, a widening of the margins on riskier loans was observed corresponding to the perceived higher risks concerning the industry or firm-specific outlook.

Chart A Changes in credit standards applied to the approval of loans or credit lines to enterprises

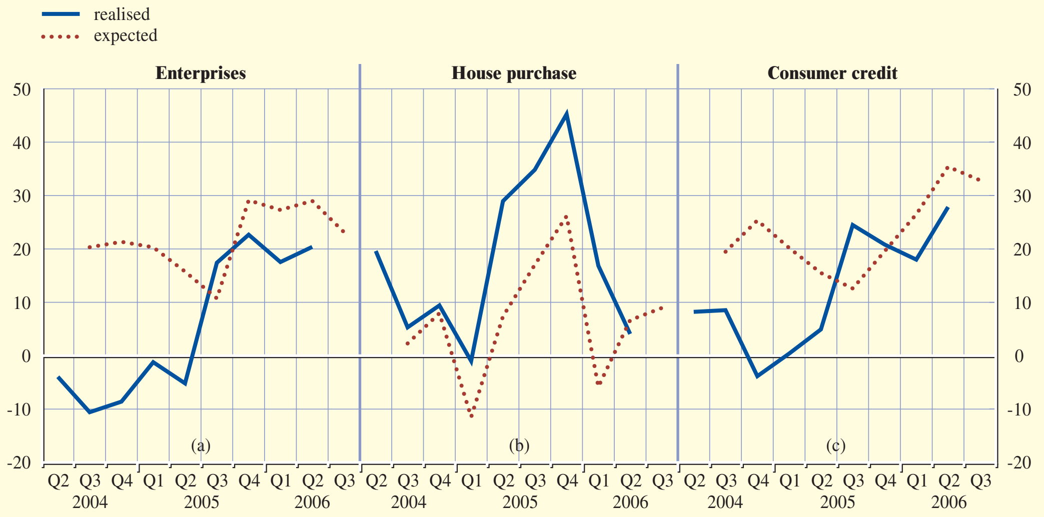
(net percentages)



Notes: The net percentages refer to the difference between the sum of the percentages for "tightened considerably" and "tightened somewhat" and the sum of the percentages for "eased somewhat" and "eased considerably". The net percentages for the questions related to the factors are defined as the difference between the percentage of banks reporting that the given factor contributed to tightening and the percentage reporting that it contributed to easing. "Realised" values refer to the period in which the survey was conducted. "Expected" values are the net percentages calculated from the responses given by the banks in the previous survey. For instance, "expected" values for the third quarter of 2006 were reported by banks in the July 2006 survey.

Chart B Changes in the demand for loans or credit lines to enterprises and households

(net percentages)



Notes: The net percentage refers to the difference between the sum of the percentages for "increased considerably" and "increased somewhat" and the sum of the percentages for "decreased somewhat" and "decreased considerably". "Realised" values refer to the period in which the survey was conducted. "Expected" values are the net percentages calculated from the responses given by the banks in the previous survey. For instance, "expected" values for the third quarter of 2006 were reported by banks in the July 2006 survey.

In terms of the borrower's size, credit standards applied both to small and medium-sized enterprises and to large enterprises remained broadly unchanged in the second quarter of 2006, compared with the previous quarter. As regards the maturity of loans, banks reported a net easing of credit standards applied to both short-term and long-term loans.

Loan demand: Net demand for loans to enterprises continued to be very strong (20% in July, compared with 18% in April; see Chart B, panel a). A similar pattern was recorded for loan demand by small and medium-sized enterprises, while the net loan demand of large corporations declined slightly.

According to the respondent banks, these developments were mainly related to increased financing needs for fixed investment, while financing for mergers and acquisitions and corporate restructuring, inventories and working capital, and debt restructuring continued to support loan demand as well. At the same time, the availability of other funding sources – such as internal financing and loans from other banks – helped to moderate net loan demand somewhat.

Expectations: For the third quarter of 2006, banks expect credit standards applied to loans or credit lines to enterprises (see Chart A, panel a) to remain unchanged, irrespective of the borrower's size. As regards loan maturity, banks expect a net tightening of credit standards on long-term loans in the third quarter of 2006, while they expect a slight net easing of credit standards on short-term loans.

Loans to households for house purchase

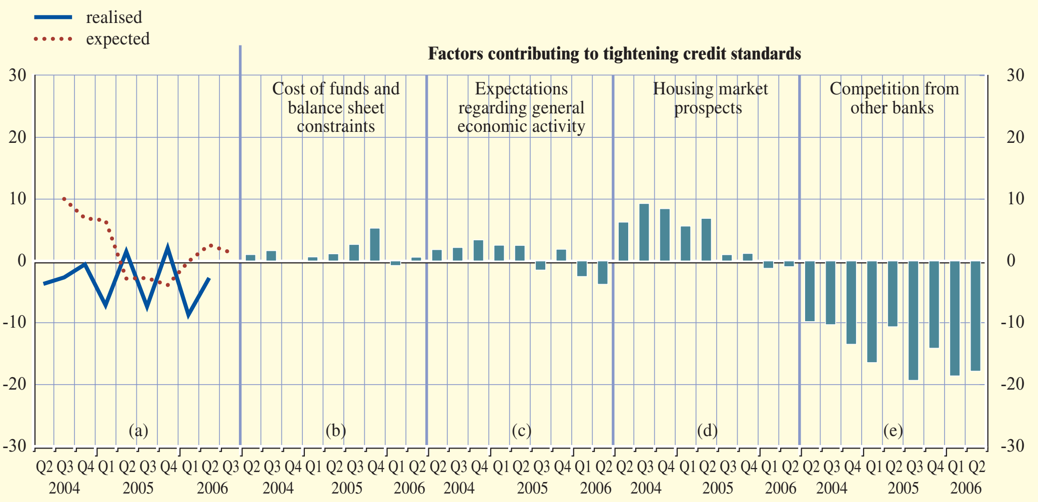
Credit standards: Banks continued to ease credit standards applied to housing loans in the second quarter of 2006 (-3% in July, from -9% in April; see Chart C, panel a). Competition from other banks continued to contribute to this net easing (see Chart C, panel e). A lower perception of risk in terms of both expectations regarding general economic activity and housing market prospects (see Chart C, panels c and d) also provided support for this development. The net easing for housing loans was mainly implemented by reducing the margins on average loans and lengthening loan maturities. At the same time, margins on riskier loans narrowed for the first time since the launch of the survey (-3% in the second quarter of 2006, from 9% in the previous quarter).

Loan demand: While still being reported as positive, net demand for housing loans stood at a much lower level in the second quarter of 2006 than in the previous quarter (4% in July, compared with 17% in April; see Chart B, panel b). This decrease was mainly the result of competition from other banks and, to a lesser extent, of non-housing-related consumption expenditure. At the same time, housing market prospects continued to support net loan demand.

Expectations: For the third quarter of 2006, respondent banks expect credit standards applied to loans to households for house purchase (see Chart C, panel a) to remain basically unchanged, whereas banks expect a slight increase in net demand over the same period (see Chart B, panel b).

Chart C Changes in credit standards applied to the approval of loans to households for house purchase

(net percentages)



Notes: The net percentages refer to the difference between the sum of the percentages for "tightened considerably" and "tightened somewhat" and the sum of the percentages for "eased somewhat" and "eased considerably". The net percentages for the questions related to the factors are defined as the difference between the percentage of banks reporting that the given factor contributed to tightening and the percentage reporting that it contributed to easing. "Realised" values refer to the period in which the survey was conducted. "Expected" values are the net percentages calculated from the responses given by the banks in the previous survey. For instance, "expected" values for the third quarter of 2006 were reported by banks in the July 2006 survey.

Loans for consumer credit and other lending to households

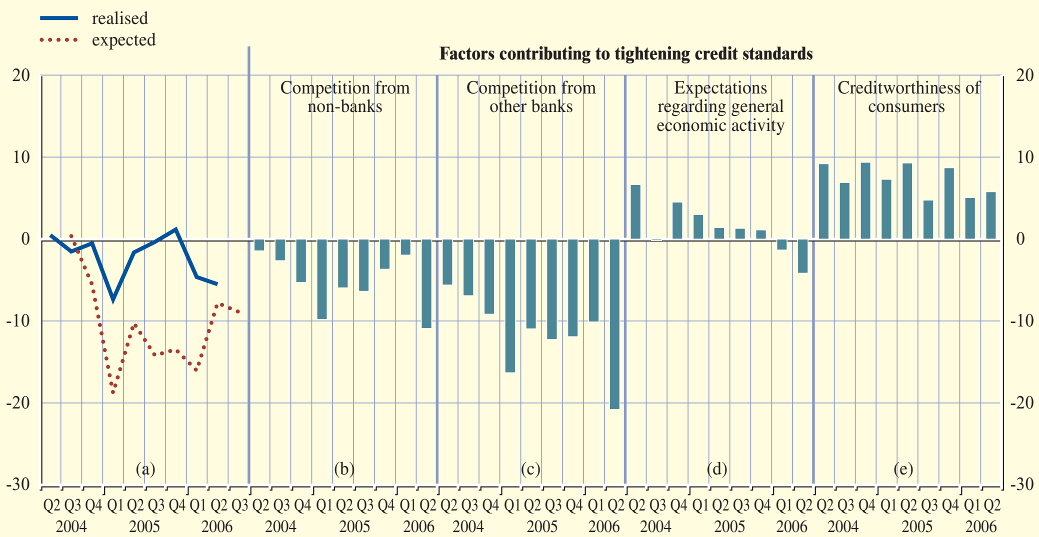
Credit standards: In the second quarter of 2006, credit standards applied to the approval of consumer credit and other lending to households continued to ease on a net basis (-6% in July, from -5% in April; see Chart D, panel a). According to the respondent banks, the net easing of credit standards was driven by competitive pressures from both other banks and non-banks (see Chart D, panels b and c). More favourable expectations regarding general economic activity also contributed to the net easing (see Chart D, panel d). With regard to terms and conditions, the easing of credit standards for consumer credit and other lending to households was mainly implemented by changing pricing conditions. In particular, margins on average loans were significantly eased, while margins on riskier loans tightened slightly. All other terms and conditions remained basically unchanged compared with the previous quarter.

Loan demand: Net demand for consumer credit and other lending to households continued to increase in the second quarter of 2006 (28%, from 18% in April 2006; see Chart B, panel c). This development was mainly related to spending on durable consumer goods and, to a somewhat lesser extent, a positive contribution from consumer confidence.

Expectations: For the third quarter of 2006, banks expect a continuation of the net easing of credit standards (see Chart D, panel a), as well as a further increase in net demand for these loans (see Chart B, panel c).

Chart D Changes in credit standards applied to the approval of loans for consumer credit and other lending to households

(net percentages)



Notes: The net percentages refer to the difference between the sum of the percentages for "tightened considerably" and "tightened somewhat" and the sum of the percentages for "eased somewhat" and "eased considerably". The net percentages for the questions related to the factors are defined as the difference between the percentage of banks reporting that the given factor contributed to tightening and the percentage reporting that it contributed to easing. "Realised" values refer to the period in which the survey was conducted. "Expected" values are the net percentages calculated from the responses given by the banks in the previous survey. For instance, "expected" values for the third quarter of 2006 were reported by banks in the July 2006 survey.

Ad hoc question on loans to households secured by real estate

For the first time, the July 2006 bank lending survey includes an ad hoc question which aims to address some of the reasons behind the noticeable developments in loans for house purchase in a large number of countries. The question focuses on loans to households secured by real estate and used for purposes other than the acquisition of a principal residence. In particular, the question distinguishes between loans used for the purchase of second homes or homes for investment purposes ("buy to let") and those used for other purposes, such as consumption, financial investment and redemption of debt. Since there is anecdotal evidence of a growing phenomenon in this respect, at least in a number of countries, this ad hoc question is aimed at gathering some qualitative and quantitative information directly from banks.

The ad hoc question is divided into two parts.[4] The first part quantifies the phenomenon. Hence, banks are asked to quantify the volume of the outstanding amount of loans to households secured by real estate used for purposes other than the acquisition of a principal residence and to indicate this as a percentage of all mortgage loans. For this, two categories of purpose were provided: loans to households secured by real estate used for the purchase of second homes or for investment purposes, and such loans used for other purposes.[5] The second part relates to recent developments: banks are asked to indicate whether the shares of these loans have changed over the past 12 months by comparison with the previous 12-month period. The majority of the banks were able to respond to the ad hoc question.

Almost 50% of the banks participating in the survey said that less than 10% of their mortgage loans were used for the purchase of second homes or homes for investment purposes. At the same time, 27% considered the share of such loans to be relatively significant (between 10% and 20%), while 12% said that the share was considerable (more than 20%). The indication given by banks is that the share of loans to households secured by real estate used for other purposes (such as consumption and financial investment) is relatively low. More specifically, 64% of banks indicated that the share of loans secured by real estate and used for other purposes was less than 10%.

With regard to the second part of the ad hoc question, banks reported an overall net increase over the past 12 months both in the share of loans to households secured by real estate to purchase second homes or for investment purposes and in the share of such loans used for other purposes (14% in both cases).

4 The specific formulation of the ad hoc question can be found in the report on the results of the July 2006 survey published on the ECB's website.
5 This category covers, for example, consumption, financial investment and redemption of debt, as well as borrowing for the purpose of transferring the funds to a son or daughter for a house purchase.