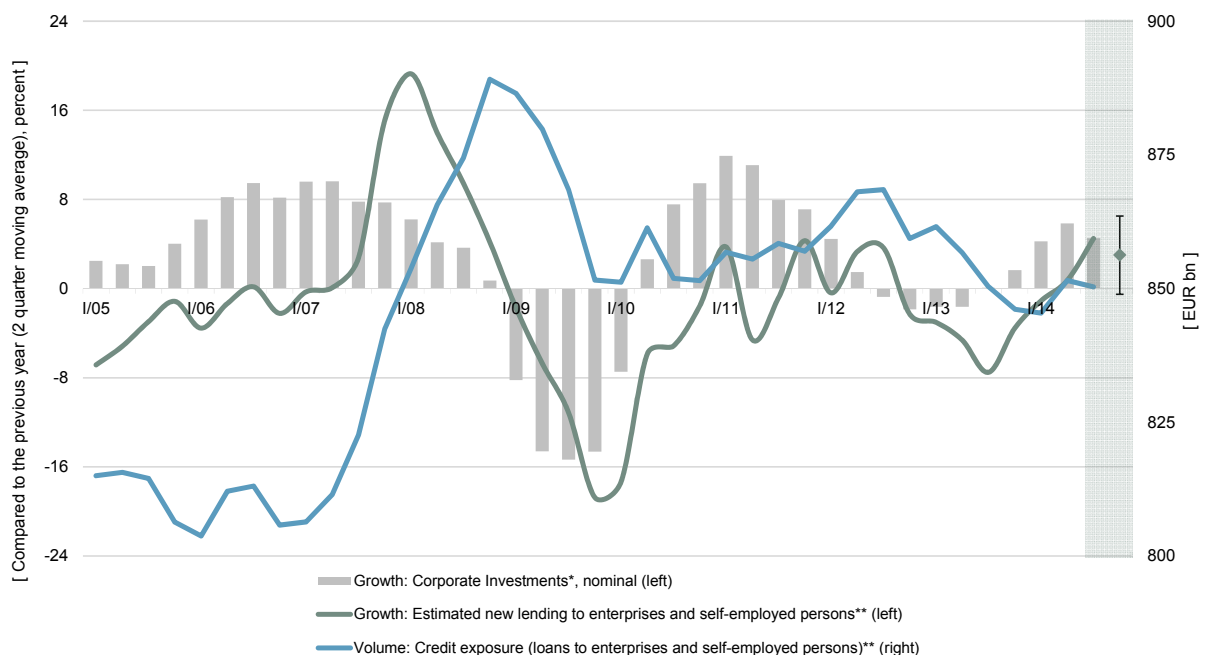


KfW Credit Market Outlook December 2014

New lending: Interim high rather than a sustained upswing

- *The estimated new lending for the third quarter 2014 rose 4.5% over the previous year's level.*
- *A partial reduction of this increase looks likely during the winter half-year.*



* non-public investments in equipment, commercial buildings and other plants

** excludes commercial building loans and loans to insurance and financial institutions (excluding MFIs)

New lending of credit institutions to companies and the self-employed as estimated by KfW grew by 4.5% in the third quarter of 2014 compared to the same quarter in the previous year. This was aided by significant growth in long-term loans with a duration of more than five years. We expect to see lower additional growth in the final quarter. New lending in the fourth quarter should come out roughly 3% above the previous year's level (moving average of growth rate over two quarters).

Weak previous year and large companies driving growth

There were two main reasons for the substantial rise in new lending in the third quarter. (1) A statistical base effect: New lending in the third quarter of the previous year was extremely weak. (2) Loan demand on the part of large companies actually increased (see Bank Lending Survey of the German banks). Among other factors, companies relied less on alternative methods of financing than before – the volume of outstanding corporate bonds has declined slightly since the start of the year.

An estimated rise in corporate investment by a mere 1.1 % in the fourth quarter of 2014 compared to the same quarter of the previous year also contributes to the decline of the growth in new lending at the end of this year, compared to the previous year, to about 3 %. This is also reflected in the banks' expectations. They anticipate a slight drop in demand for corporate loans in the current quarter.

There are hardly any changes on the supply side. Financial resources are still plentiful. The Ifo credit constraint indicator rose slightly in November but is still at only 18.3 %. Fewer than one in five companies surveyed are under the impression that lending from banks is restrictive. Loan conditions were eased further in the third quarter.

Outlook: Interim high rather than an upswing

We expect low growth in new lending at best for the coming year. Germany's economy will start off 2015 with low dynamism and is only expected to become more stable over the course of the year. We expect a similar picture for corporate investment, which should show much weaker growth (0.5 %) in 2015, following an increase of 3.5 % in 2014. This means demand for investment loans on the part of companies will remain weak. Uncertainty over interest rates on bank deposits should give some companies an additional incentive to pay as much of their expenses as possible with cash, as opposed to requesting a loan.

Conclusion

New lending posted considerable growth rates in the second half of the year, primarily for statistical reasons. Nothing has changed fundamentally, however, with regard to the weakness of the German lending market. A sustainable revival would require a significant rise in corporate investment, of which there are no signs at the moment.

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Appendix

The structure of the KfW Credit Market Outlook:

New lending business is determined by adding to the quarterly variation of existing loans (data from the Deutsche Bundesbank on loans extended by German banks to domestic enterprises and self-employed professionals without housing construction loans and without loans to financial institutions and the insurance industry) a simulated on-schedule repayment behaviour (per quarter). The publication is presented in the form of the thus determined new lending business variation rate against the prior-year quarter, with the variation rate expressed as the moving two-quarter average.

The forecast of new lending business is performed on the basis of a VAR model in which the GDP, the twelve-month money market rate and business investments are taken into account as the most important explanatory variables. Business investments comprise all non-public investment in equipment, industrial buildings and other facilities. They are calculated by KfW quarterly on the basis of the national accounts data from the Federal Statistical Office and, using leading financial and economic indicators, are projected into the future with the aid of a vector autoregressive model.