It takes time to overcome the crisis – longer maturities are driving new lending

1 September 2020

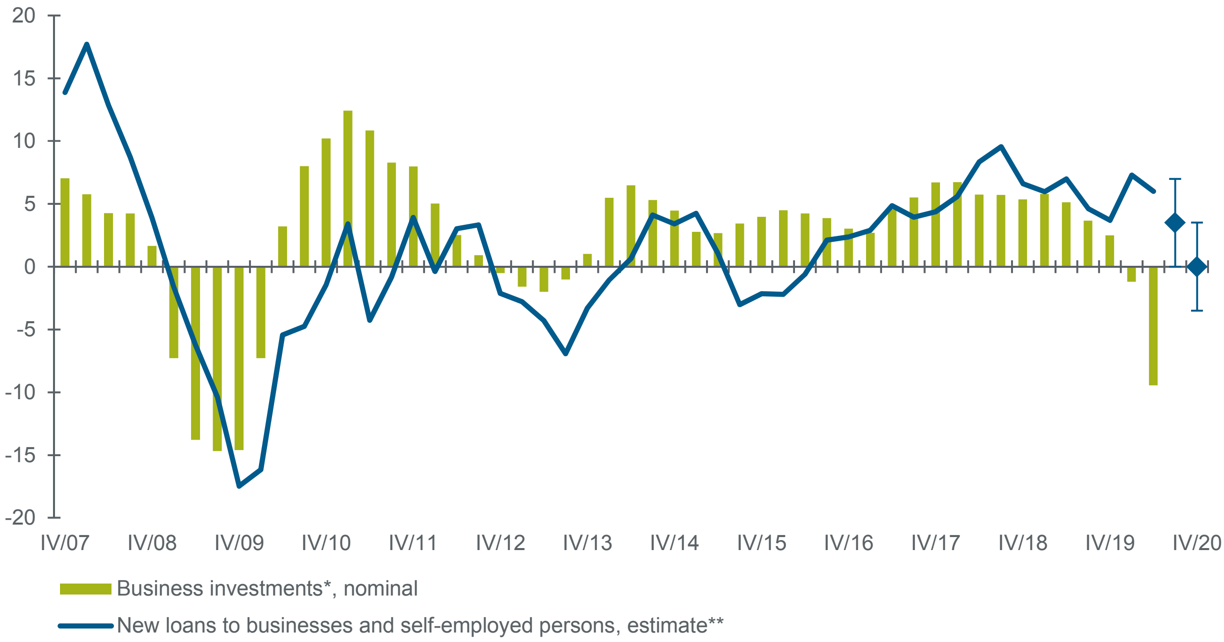
Author: Stephanie Schoenwald, phone +49 69 7431-6446, stephanie.schoenwald@kfw.de
Press contact: Christine Volk, phone +49 69 7431-3867, christine.volk@kfw.de

– New lending to businesses and self-employed persons continued with high momentum in the second quarter of 2020. After the pace of growth doubled to 7.3% in the first three months of the year, new credit commitments increased slightly less in the second quarter, up 6% on the previous year.

– Owing to massive losses in turnover as a result of the pandemic, the financial situation of many enterprises is highly precarious. Along with other instruments, loans play a significant role in bridging liquidity shortages. Unlike in the financial crisis of 2009, access to credit appears to have become only moderately more difficult.

– After resorting to short-term credit instruments at the beginning of the crisis, companies sharply increased their use of loans with longer maturities even as their capital expenditure collapsed. The fact that enterprises are willing and able to secure their business operations for the longer term is good news for the stability of the economic recovery.

Figure 1: New lending by German banks to domestic businesses and self-employed persons*
Variation on the previous year (moving two-quarter average), in per cent



* non-public investment in equipment, industrial buildings and other facilities
** excluding commercial housing loans and excluding loans to financing institutions and insurance industry

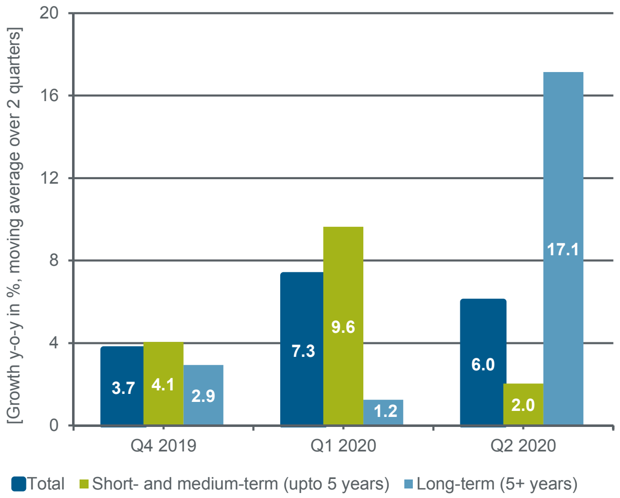
Lending continued at a high level during the peak of the coronavirus crisis

The German economy suffered a deep shock from the pandemic. Economic output contracted by around 10% in the second quarter. The restrictions on public life had serious consequences for businesses. In a supplemental survey conducted by KfW Research,[1] two in three SMEs reported having suffered losses in turnover in May. The resulting liquidity shortages, however, which threatened the existence of many businesses, could also be mitigated through additional lending. According to KfW Research, this is illustrated by the significant increase of new lending to domestic enterprises and self-employed persons. Between April and June, banks extended 6.0% more loans than during the same period last year. The rate of growth has thus hardly slowed since the beginning of the year (+7.3%).

Focus is shifting to longer maturities

A look at the borrowing terms reveals a remarkable change (see Figure 2). At the beginning of the crisis, enterprises first resorted to short-term credit instruments, for example by drawing on existing credit lines. This pattern is typical of an economic downturn. In the past quarter, however, the situation reversed.

Figure 2: New lending business by maturity



Sources: Deutsche Bundesbank, KfW Research

Rising by 17%, long-term loans with maturities of five or more years increased at an exceptionally high rate. The use of state credit guarantees, among them the KfW programmes, is likely to have facilitated this. This is good news for the stability of the economic recovery. Longer maturities give enterprises more financing certainty and allow them to distribute the burden of their losses from the crisis over longer periods. This improves the prospects for the long term continuation of their operations. However, part of this increase is surely also attributable to deferment agreements, while the financing of capital expenditure, which has collapsed dramatically, has probably played a minor role at best.

Criteria for accessing credit have been tightened only moderately so far

Despite the strong growth, the momentum of new lending business has remained slightly below our expectations. Given the businesses' financial hardship and growing risks of default, the question is whether banks are too reluctant to lend and excessively restricting their supply of credit. So far, there are no indications of this. Although credit has become slightly more difficult to access, criteria have so far only been tightened moderately. In the survey conducted for the KfW ifo Credit Constraint Indicator[2] at the end of June, only one fifth of SMEs deplored restrictive lending practices. During the global financial crisis, that share was more than twice as high. The findings of the Bank Lending Survey paint a similar picture. In the July edition, most financial institutions reported having tightened their lending criteria for enterprises. However, the net balance was 9.4 percentage points, far below the 2009 level (37 percentage points). Rather, enterprises followed other pathways to obtain funding besides bank loans, such as tapping into state subsidy programmes or issuing substantially more bonds.

Outlook: Lending momentum is trending downward

The far-reaching relaxation of restrictions has already allowed the economy to recover in the course of the second quarter and liquidity shortages are decreasing. On the other hand, investment activity and associated funding needs are likely to remain weak. New lending business is therefore likely to slow significantly over the remainder of the year and might even decline. Given the unprecedented nature of the coronavirus crisis, it remains to be said that forecast uncertainty is extraordinarily high.

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 the VAR model in which 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.

---

[1] Gerstenberger, J. and Schwartz, M. (2020), **Coronavirus crisis in Germany|s SMEs: Return to full economic activity still far off but gradual opening has eased pressure on liquidity**, Focus on Economics No. 294, KfW Research.

[2] Schoenwald, S. (2020), **KfW ifo Credit Constraint Indicator rises as coronavirus makes banks more cautious,** July 2020, KfW Research.