New lending is down

- Weakness in the corporate lending market worsened in the third quarter of 2015.
- New lending was down 2.9% on the previous year.
- The cause is low demand – weak corporate investment and ample internal resources reduce borrowing requirements.
- The decline will continue into the new year.

According to KfW estimates, new lending from banks to companies and self-employed professionals fell for the first time in one and a half years in the third quarter of 2015. The decline amounted to 2.9% on the same quarter of the previous year (moving growth rate across two quarters). It is becoming apparent that the structurally weak demand for credit by German enterprises is standing in the way of a lasting recovery of the corporate lending market. Also because of unfavourable base effects, we expect positive growth to return mid-year at the earliest but at least the pace of the downturn should not accelerate. In the final quarter of 2015 new lending has likely declined by some 1.5% on the previous year’s level.
Credit demand is returning to old weakness

Companies continue to benefit from bank loans with excellent conditions. On average, borrowing costs in October remained at record-low levels at 2.1%, with the majority of banks indicating in the ECB’s quarterly survey that they had once again adjusted the remaining borrowing terms (e.g. collateral, loan amounts, maturities) in favour of borrowers. The ifo credit hurdle dropped to a historic low yet again in November, with only 14.5% of commercial enterprises reporting borrowing difficulties.

Nevertheless, after gaining momentum in the summer of 2014, the corporate lending market began to sputter again, contrasting sharply with the strong growth of the market for residential construction loans. The decline in corporate investment during the past two quarters (in real terms and adjusted for seasonal effects) is likely to have contributed to this development. Still, the main causes are probably structural, as the growth of German enterprises’ own financial resources – retained earnings and depreciation – has outpaced their investment expenditure since as far back as 2009. In the 12 months since September 2014, for example, new net lending by non-financial corporations amounted to EUR 90 billion.

Conclusion

The structural weakness of German enterprises’ credit demand is proving difficult to overcome. Favourable lending terms alone are insufficient to induce companies to consistently borrow more. Given the excellent financial position of the German business sector, a stable upward trend in new lending to companies cannot be expected until investment activity picks up on a broad and sustained basis.

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

<table>
<thead>
<tr>
<th>The structure of the KfW Credit Market Outlook:</th>
</tr>
</thead>
</table>

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.