February 26, 2018

Economics Group

John E. Silvia, Chief Economist
john.silvia@wellsfargo.com • (704) 410-3275
Harry Pershing, Economic Analyst
harry.pershing@wellsfargo.com • (704) 410-3034
Shannon Seery, Economic Analyst
shannon.seery@wellsfargo.com • (704) 410-1681

Supply Side Credit: U.S. Banks Report Stable Conditions

Supply side credit dynamics point to stable conditions. Recent data suggest business lending demand has improved while consumer demand remains basically unchanged.

Equipment Investment Leads Business Loan Demand

In the January 2018 Senior Loan Officer Opinion Survey (SLOOS), released by the Federal Reserve, we received a snapshot of Q4 credit standards among businesses and households. This report, which surveys banks in the United States, focuses on supply side reporting of credit dynamics.

While banks reportedly continued to ease standards on commercial and industrial (C&I) loans, demand for such loans has picked-up slightly after remaining weak for more than a year (top graph). Increased demand is likely attributable to the rise in business fixed investment, specifically the surge in capital spending in the second half of 2017. With equipment spending up 10.8 percent and 11.4 percent in Q3 and Q4, respectively, the surge in investment likely contributed to the increased demand banks experienced for C&I loans over the period. However, increased competition among lenders was the most cited reason for an easing of credit standards, intimating that businesses have increasingly turned to alternative forms of funding to fuel capital spending.

Weaker demand for commercial real estate (CRE) loans was reported by banks, while banks continued to tighten standards on such loans. Cautious CRE lending has helped keep a fairly tight rein on the supply of credit throughout this recovery.

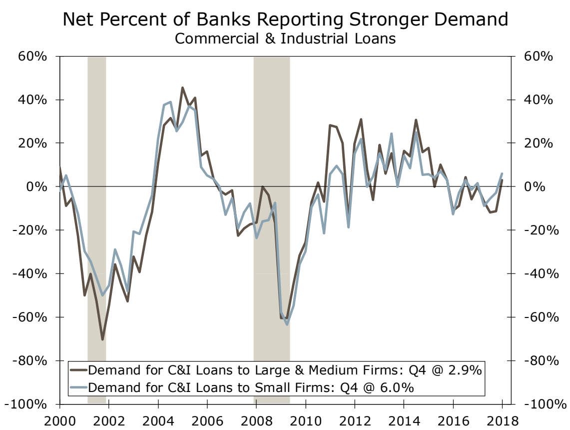
Tightening Consumer Standards as Interest Rates Rise

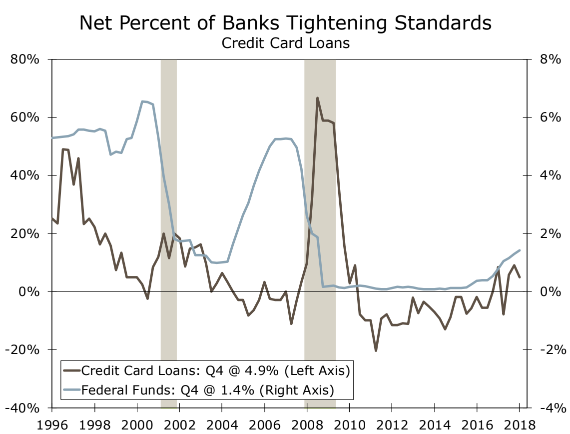
Banks' willingness to make consumer loans continued to slow in the fourth quarter. On net, banks increased the minimum required credit scores to receive a loan, resulting in a modest decrease in loans, which were granted to consumers (middle graph). This overall tightening of standards is expected to persist as interest rates are expected to trend higher, which will likely lead to marginally higher loan delinquency rates. Likewise, after years of near-zero interest rates, demand for consumer loans has weakened as the Federal Reserve continues to tighten monetary policy. Demand for auto and credit card loans weakened in Q4, continuing the downward trending demand for these types of loans over the past couple of years (bottom graph).

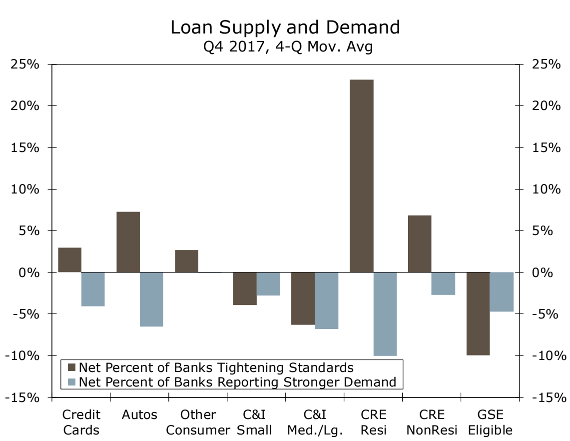
Deteriorating Consumer Performance Ahead?

The SLOOS report included a special section regarding the outlook for credit standards in 2018. Next year, banks expect to ease standards on residential mortgage and C&I loans, while tighten terms on CRE and credit card loans. On net, banks anticipate improved credit performance among businesses, while they expect deteriorating conditions for the consumer.

Continued growth in personal consumption expenditures coupled with modest income gains demonstrates that consumers will continue to take advantage of low-cost borrowing to fund consumption. However, as interest rates continue to rise, and borrowing becomes increasingly more costly, we may see a gradual shift in the credit market.







Source: Federal Reserve Board and Wells Fargo Securities

Wells Fargo Securities Economics Group

Diane Schumaker-Krieg	Global Head of Research, Economics & Strategy	(704) 410-1801 (212) 214-5070	diane.schumaker@wellsfargo.com
John E. Silvia, Ph.D.	Chief Economist	(704) 410-3275	john.silvia@wellsfargo.com
Mark Vitner	Senior Economist	(704) 410-3277	mark.vitner@wellsfargo.com
Jay H. Bryson, Ph.D.	Global Economist	(704) 410-3274	jay.bryson@wellsfargo.com
Sam Bullard	Senior Economist	(704) 410-3280	sam.bullard@wellsfargo.com
Nick Bennenbroek	Currency Strategist	(212) 214-5636	nicholas.bennenbroek@wellsfargo.com
Eugenio J. Alemán, Ph.D.	Senior Economist	(704) 410-3273	eugenio.j.aleman@wellsfargo.com
Azhar Iqbal	Econometrician	(704) 410-3270	azhar.iqbal@wellsfargo.com
Tim Quinlan	Senior Economist	(704) 410-3283	tim.quinlan@wellsfargo.com
Eric Viloria, CFA	Currency Strategist	(212) 214-5637	eric.viloria@wellsfargo.com
Sarah House	Economist	(704) 410-3282	sarah.house@wellsfargo.com
Michael A. Brown	Economist	(704) 410-3278	michael.a.brown@wellsfargo.com
Jamie Feik	Economist	(704) 410-3291	jamie.feik@wellsfargo.com
Erik Nelson	Currency Strategist	(212) 214-5652	erik.f.nelson@wellsfargo.com
Michael Pugliese	Economic Analyst	(704) 410-3156	michael.d.pugliese@wellsfargo.com
Harry Pershing	Economic Analyst	(704) 410-3034	harry.pershing@wellsfargo.com
Hank Carmichael	Economic Analyst	(704) 410-3059	john.h.carmichael@wellsfargo.com
Ariana Vaisey	Economic Analyst	(704) 410-1309	ariana.b.vaisey@wellsfargo.com
Abigail Kinnaman	Economic Analyst	(704) 410-1570	abigail.kinnaman@wellsfargo.com
Shannon Seery	Economic Analyst	(704) 410-1681	shannon.seery@wellsfargo.com
Donna LaFleur	Executive Assistant	(704) 410-3279	donna.lafleur@wellsfargo.com
Dawne Howes	Administrative Assistant	(704) 410-3272	dawne.howes@wellsfargo.com

WELLS FARGO SECURITIES