Trends in Lending

July 2013

BANK OF ENGLAND

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This quarterly publication presents the Bank of England's assessment of the latest trends in lending to the UK economy.(1) It draws mainly on long-established official data sources, such as the existing monetary and financial statistics collected by the Bank that cover all monetary financial institutions, and on newer data collections, established since the start of the financial crisis.

These data are supplemented by discussions between the major UK lenders and Bank staff, giving staff a better understanding of the business developments driving the figures, and this intelligence is reflected in the report.(2) The major UK lenders(3) are Banco Santander, Barclays, HSBC, Lloyds Banking Group, Nationwide and Royal Bank of Scotland and together they accounted for around 70% of the stock of lending to businesses, 75% of the stock of mortgage lending and 55% of the stock of consumer credit (excluding student loans) at end-December 2012. The report also draws on intelligence gathered by the Bank's network of Agents and from market contacts, as well as the results of other surveys including the Bank of England's *Bank Liabilities Survey* and *Credit Conditions Survey*.(4) The focus of the report is on lending, but broader credit market developments, such as those relating to capital market issuance or trade credit, are discussed where relevant.

The report covers data up to May 2013 and intelligence gathered up to end-June 2013. Unless stated otherwise, the data reported cover lending in both sterling and foreign currency, expressed in sterling.

(1) See www.bankofengland.co.uk/statistics/2013.pdf for future publication dates.
(2) For a fuller background, please refer to the first edition of *Trends in Lending* available at www.bankofengland.co.uk/publications/other/monetary/trendsapril09.pdf.
(3) Membership of the group of major UK lenders is based on the provision of credit to UK-resident companies and individuals, regardless of the country of ownership.
(4) The *Bank Liabilities Survey* and the *Credit Conditions Survey* for 2013 Q2 were conducted between 10 and 31 May 2013.

Contents

Executive summary

The annual rate of growth in the stock of lending to UK businesses was negative in the three months to May. The stock of lending to both small and medium-sized enterprises and large businesses also contracted over this period. The annual rate of growth in the stock of secured lending to individuals was broadly unchanged. Mortgage approvals by all UK-resident mortgage lenders for house purchase rose in the three months to May. Total net consumer credit flows were positive over this period.

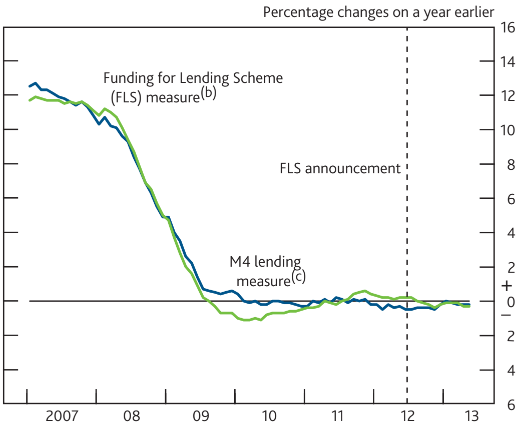
Indicative measures of the spread over relevant swap rates on longer-term wholesale debt decreased in April and May, before increasing during June. According to the Bank of England's *Credit Conditions Survey* 2013 Q2, spreads over reference rates on new lending fell significantly for large businesses, decreased slightly for medium-sized businesses, and were little changed for small businesses. The Bank's measure of the effective mortgage rate on overall new lending fell by around 20 basis points in the three months to May. Effective interest rates on new personal loans and interest-bearing credit cards also fell over this period.

The overall availability of credit to the corporate sector and demand for bank credit increased in the three months to May, according to respondents to the Bank of England's *Credit Conditions Survey*. Lenders in the survey also reported that the availability of new secured credit to households increased over this period. Contacts of the Bank's network of Agents reported that activity in the housing market had continued to strengthen.

1 Lending to UK businesses and individuals

The annual rate of growth in the stock of lending to UK businesses was negative in the three months to May. The stock of lending to both small and medium-sized enterprises and large businesses also contracted over this period. The annual rate of growth in the stock of secured lending to individuals was broadly unchanged. Mortgage approvals by all UK-resident mortgage lenders for house purchase rose in the three months to May. Total net consumer credit flows were positive over this period.

Chart 1.1 Lending to UK households and businesses[(a)]



(a) Twelve-month growth rate in the stock of lending. Lending to the UK household sector and PNFCs, excluding the effects of securitisations and loan transfers. Non seasonally adjusted.
(b) Sterling loans by UK monetary financial institutions (MFIs) and related specialist mortgage lenders. Holdings of securities are excluded from this measure.
(c) Sterling M4 lending by UK MFIs. Holdings of securities are included in M4 lending.

This section presents a summary of the recent data on lending to UK businesses and individuals. The twelve-month growth rate in the stock of lending to UK-resident households and businesses was little changed in the three months to May, and was similar across different lending measures (**Chart 1.1**).

Data from participants in the Funding for Lending Scheme (FLS) indicated that their overall net lending to UK households and private non-financial corporations (PNFCs) was -£0.3 billion in 2013 Q1.[(1)] Within this, there were diverse lending outcomes across different lenders. A majority of the participating groups increased their lending in 2013 Q1. Others contracted their lending, a large proportion of which was accounted for by three large groups. In part, that reflects a desire by several major UK lenders to reduce the scale of their so-called 'non-core' loan portfolios following the financial crisis, or a need to comply with State Aid conditions. Based on conversations with FLS participants, net lending is expected to pick up modestly in the second half of 2013.

Recent aggregate data (non seasonally adjusted) for April and May 2013, on an FLS-consistent basis, indicated that net lending by all UK MFIs and their related specialist mortgage lenders was negative over this period. Net lending (seasonally adjusted) to UK households and PNFCs was around -£4.5 billion in the twelve months to May.[(2)] Within this, net lending to PNFCs was negative, partly offset by positive net lending to households.

Table 1.A Lending to UK businesses[(a)]

	Averages							2013		
	2007	2008	2009	2010	2011	2012	2013 Q1	Mar.	Apr.	May
Net monthly flow (£ billions)	7.4	3.8	-3.9	-2.1	-0.8	-1.5	-0.9	0.6	-1.3	-3.8
Three-month annualised growth rate (per cent)	20.9	10.7	-7.7	-5.2	-2.0	-3.7	-3.8	-2.5	-3.0	-4.1
Twelve-month growth rate (per cent)	16.8	18.0	-1.8	-7.1	-3.3	-3.1	-3.0	-2.5	-2.9	-3.5

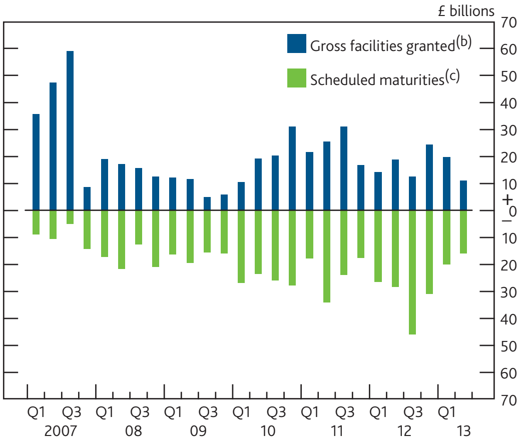
(a) Lending by UK monetary financial institutions to PNFCs. Data cover lending in both sterling and foreign currency, expressed in sterling. Seasonally adjusted.

Lending to UK businesses

Data covering lending by all UK-resident banks and building societies indicated that the stock of lending to businesses contracted by around £4.5 billion in the three months to May (**Table 1.A**). This was broadly similar to the contraction

(1) These data are not seasonally adjusted as quarterly net lending outcomes for individual FLS participants are published. For more details, see 'Funding for Lending Scheme — Usage and lending data', available at www.bankofengland.co.uk/markets/Pages/FLS/data.aspx.
(2) This is based on the M4 lending measure. For more details on the similarities between M4 lending and the FLS definition see the box on pages 7–9 in *Trends in Lending* October 2012, available at www.bankofengland.co.uk/publications/Documents/other/monetary/trendsoctober12.pdf.

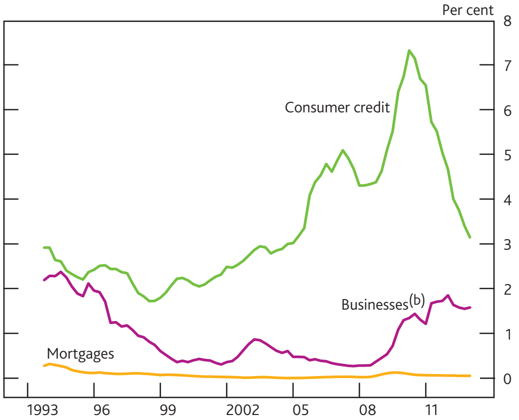
Chart 1.2 Estimates of syndicated lending facilities granted to UK businesses(a)



Sources: Dealogic and Bank calculations.

(a) Defined broadly as PNFCs. Data cover lending facilities in both sterling and foreign currency, expressed in sterling. Data are quarterly. Non seasonally adjusted.
(b) New syndicated lending facilities excluding cancelled or withdrawn facilities.
(c) Scheduled maturities of syndicated lending facilities excluding cancelled or withdrawn facilities. Actual maturities will also reflect the effects of refinancing and prepayments, exchange rate changes and other effects.

Chart 1.3 Write-off rates on lending to UK businesses and individuals(a)



(a) Lending by UK monetary financial institutions. The series are calculated as annualised quarterly write-offs divided by the corresponding loans outstanding at the end of the previous quarter. The data are presented as four-quarter moving averages. Series start in 1993 Q4. Lending in both sterling and foreign currency, expressed in sterling. Non seasonally adjusted.
(b) PNFCs.

Table 1.B Secured lending to individuals(a)

	Averages							2013		
	2007	2008	2009	2010	2011	2012	2013 Q1	Mar.	Apr.	May
Net monthly flow (£ billions)	9.0	3.4	1.0	0.6	0.8	0.7	0.5	0.4	0.7	0.3
Three-month annualised growth rate (per cent)	10.4	4.1	1.0	0.7	0.7	0.7	0.5	0.5	0.6	0.5
Twelve-month growth rate (per cent)	11.0	6.9	1.4	0.9	0.7	0.8	0.6	0.5	0.5	0.5

(a) Sterling lending by UK monetary financial institutions and other lenders to UK individuals. Seasonally adjusted.

in the previous three months. The annual rate of growth in this measure of the stock of lending to businesses has been negative for the past four years.

The stock of lending to both small and medium-sized enterprises (SMEs) and large businesses contracted in the three months to May. The box on pages 7–9 provides more details on recent trends in lending to SMEs.

Larger companies have access to more funding sources than smaller businesses, such as the syndicated lending market. The total value of new syndicated lending facilities granted in the UK market declined in the year to 2013 Q2 (**Chart 1.2**). In recent discussions, most major UK lenders noted that the subdued level of syndicated lending volumes in 2013 Q2 reflected a lack of mergers and acquisitions activity.

Capital markets provide an alternative source of funding for larger companies. Net bond issuance by UK businesses was positive in 2013 Q1 and the largest since 2009 Q2. Monthly net bond issuance continued to be positive in April and May, though was lower on average than in the first quarter of the year. Positive net bond issuance by PNFCs was partly offset by negative net equity issuance, such that net capital market issuance was slightly positive over this period. Despite this positive capital market issuance, a net repayment of bank lending by businesses (**Table 1.A**) meant that total net funds raised by UK businesses from UK monetary financial institutions and capital markets was negative in April and May.

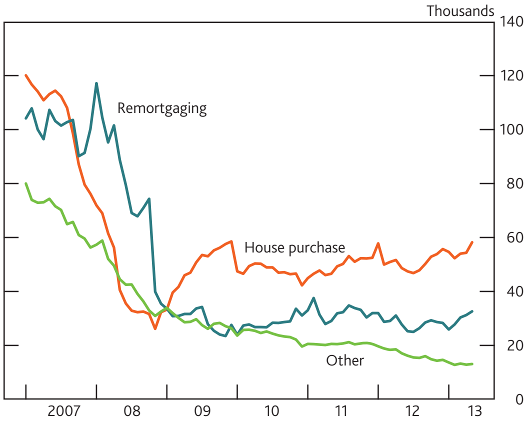
Notwithstanding the recent weakness of bank lending, the majority of respondents to the *Deloitte CFO Survey* for 2013 Q2, which covers large companies, indicated that they still viewed bank borrowing as an 'attractive' source of finance. Bond issuance remained the most favoured source of funding.

Recent indicators of corporate distress were broadly stable. The rate of corporate liquidations was unchanged for the year to 2013 Q1. The corporate write-off rate — the ratio of write-offs on corporate lending to the stock of that lending — was broadly unchanged in 2013 Q1, though remained elevated compared to the pre-crisis period (**Chart 1.3**). In recent discussions, most major UK lenders reported that over the past six months, measures of corporate distress such as insolvencies had performed in line with or slightly better than their expectations at the start of 2013, which had been to remain broadly flat. Looking ahead, most major UK lenders expected measures of corporate distress to improve slightly or to remain unchanged in the second half of 2013.

Secured lending to individuals

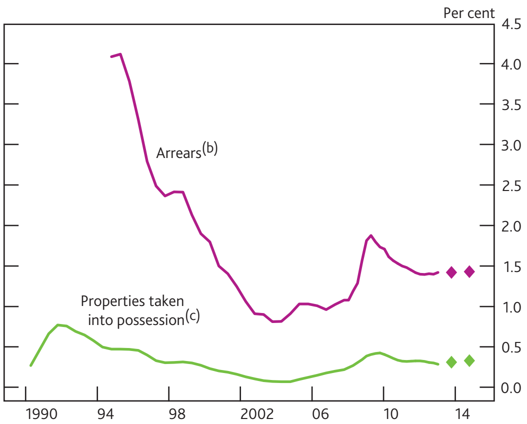
The total flow of net lending in sterling by UK-resident mortgage lenders was positive in the three months to May (**Table 1.B**), with the average monthly flow slightly lower than

Chart 1.4 Approvals of loans secured on dwellings[a]



(a) Data are for monthly number of approvals covering sterling lending by UK monetary financial institutions and other lenders to UK individuals. Approvals secured on dwellings are measured net of cancellations. Seasonally adjusted.

Chart 1.5 Mortgage arrears and possession rates[a]



Sources: CML and Bank calculations.

(a) Series are expressed as the proportion of the number of outstanding mortgages. Non seasonally adjusted.
(b) Mortgages in arrears of 2.5% or more of the outstanding mortgage balance. Data are available from end-1994, are semi-annual up to end-2007 and quarterly since then. The magenta diamonds show the latest CML forecast for end-2013 and end-2014 made in December 2012 and are unchanged to date.
(c) Properties taken into possession over the preceding twelve-month period. Data are semi-annual up to end-2007 and quarterly since then. The green diamonds show the latest CML forecast for end-2013 and end-2014 made in December 2012 and are unchanged to date.

Table 1.C Consumer credit[a]

	Averages							2013		
	2007	2008	2009	2010	2011	2012	2013 Q1	Mar.	Apr.	May
Net monthly flow (£ billions)	0.8	0.6	-0.2	-0.2	-0.1	0.2	0.6	0.6	0.6	0.7
Three-month annualised growth rate (per cent)	5.3	3.9	-1.3	-1.4	-0.5	0.5	4.8	4.4	4.7	4.9
Twelve-month growth rate (per cent)	4.9	5.1	0.8	-1.8	-0.8	-0.3	2.2	2.5	3.0	3.3

(a) Sterling lending by UK monetary financial institutions and other lenders to UK individuals. Consumer credit consists of credit card lending and other loans and advances. Consumer credit data exclude student loans. Seasonally adjusted.

in the previous period. The annual rate of growth in the stock of secured lending was broadly unchanged at 0.5%.

Mortgage approvals by all UK-resident mortgage lenders for house purchase and for remortgaging rose over the three months to May, with the number of house purchase approvals in May the highest since December 2009 (**Chart 1.4**). In recent discussions, most major UK lenders reported that their pipelines of mortgage applications were strong in June. Gross secured lending rose in the three months to May, compared to the previous period. Repayments on lending secured on dwellings also increased slightly.

Recent indicators of mortgage distress were little changed or eased slightly. Data from the Council of Mortgage Lenders (CML) indicated that the mortgage arrears rate was broadly unchanged in 2013 Q1 (**Chart 1.5**). The arrears rate on buy-to-let mortgages fell slightly in this period. The write-off rate on mortgages — the ratio of write-offs on secured loans to the stock of that lending — was little changed in 2013 Q1 (**Chart 1.3**). Claims for possessions issued in the courts were little changed in the year to 2013 Q1. The possessions rate — the ratio of the number of properties taken into possession to the number of outstanding mortgages — was also broadly flat in the year to 2013 Q1.

In recent discussions, the major UK lenders reported that over the past six months, indicators of mortgage distress such as arrears were slightly better than or in line with their expectations at the start of 2013, which had been for them to remain stable over this period. Looking forward, some major UK lenders expected mortgage arrears to fall slightly or to be broadly flat over the remainder of the year.

Consumer credit

Total net consumer credit flows (excluding student loans) were positive in the three months to May (**Table 1.C**). Within this, net flows for other unsecured lending were higher than those for credit card lending.

The annual rate of growth of consumer credit (excluding student loans) was above 3% in May (**Table 1.C**), the highest in over four years. This partly reflected an increase in car finance.

The write-off rate on consumer credit — the ratio of write-offs on unsecured loans to the stock of unsecured lending — fell in 2013 Q1 (**Chart 1.3**). The rate of personal insolvencies, the ratio of the number of insolvencies to the 16+ population, in England and Wales was broadly unchanged in 2013 Q1. In recent discussions, most major UK lenders reported that indicators of distress related to unsecured lending, such as write-offs and arrears, had performed slightly better than or in line with expectations in the first half of 2013.

Recent trends in lending to small and medium-sized enterprises

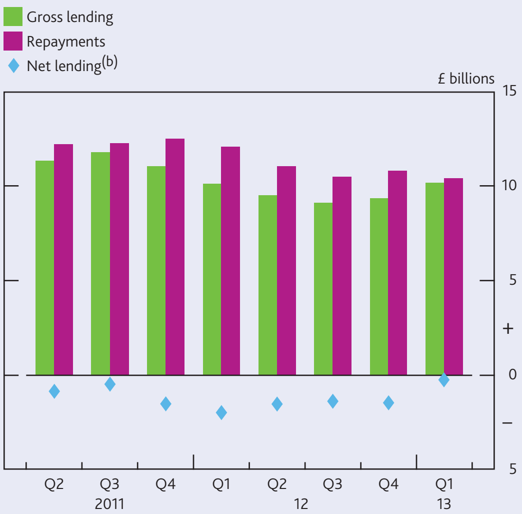
Small and medium-sized enterprises (SMEs) are an important part of the UK economy, accounting for around 60% of private sector employment and half the annual turnover of all private sector businesses.(1) An assessment of developments in lending to SMEs over 2011 was provided in *Trends in Lending* July 2012. This box provides an update on recent developments in this segment, drawing on existing monetary and financial statistics collected by the Bank of England, survey data and wider information.

Credit quantities

The amount outstanding of all currency lending by UK-resident monetary financial institutions (MFIs) to UK SMEs was estimated to be around £170 billion at end-May 2013, according to Bank of England data.(2) Within this, the share of overdrafts was approximately 10%. The stock of lending to SMEs represented around 35% of the stock of lending to all UK non-financial businesses.

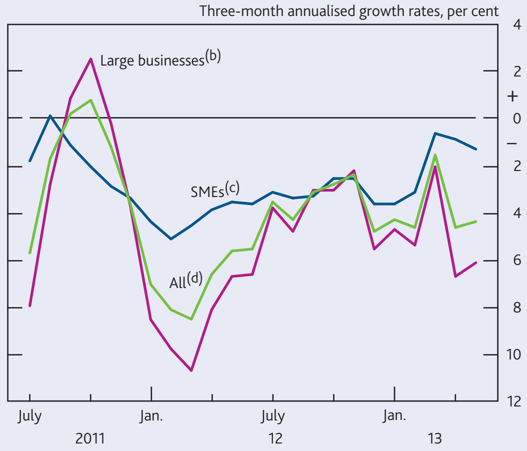
Gross lending to SMEs and repayments by them declined over most of 2012 (**Chart A**). With repayments being higher than gross lending, net lending — defined as gross lending minus repayments — was negative over this period and has been since the series began in 2011 Q2. More recently, gross lending picked up in 2013 Q1, though remained lower than repayments. As a result, while the three-month annualised rate of growth in the stock of lending to SMEs was negative over 2012, the rate of contraction slowed in 2013 (**Chart B**). The stock of lending to large businesses also contracted, though the rate of contraction has been greater than that for SMEs for most of the period since early 2012. This may reflect a greater degree of bank disintermediation by large businesses, which have access to more funding sources than smaller businesses.

Chart A Gross lending to and repayments by SMEs[(a)]



(a) Loans by UK monetary financial institutions to UK non-financial businesses and repayments by them. Data exclude overdrafts. Data cover lending in both sterling and foreign currency, expressed in sterling. SMEs are those with annual debit account turnover on the main business account less than £25 million. Non seasonally adjusted.
(b) Net lending is defined as gross lending minus repayments.

Chart B Lending to non-financial businesses, by size[(a)]



(a) Three-month annualised growth in the stock of lending. Lending by UK monetary financial institutions to UK non-financial businesses. Data exclude overdrafts. Data cover lending in both sterling and foreign currency, expressed in sterling. Non seasonally adjusted.
(b) Large businesses are those with annual debit account turnover on the main business account over £25 million.
(c) SMEs are those with annual debit account turnover on the main business account less than £25 million.
(d) All non-financial businesses are the sum of large businesses and SMEs.

More generally, businesses may have alternative sources of finance to borrowing from banks. Contacts of the Bank's network of Agents recently reported a growing use of non-bank finance by SMEs, albeit from low levels, including from peer-to-peer lending, crowd funding, venture capital funds, and insurance companies and pension funds.

Trade credit is an important source of short-term financing for many businesses. One product through which trade credit can be obtained is invoice finance. The stock of asset-based finance — of which around 80% is pure invoice finance — to businesses with annual turnover under £10 million is small compared to the stock of lending by MFIs. This stock of asset-based finance was slightly higher in 2013 Q1 compared to the same quarter in 2011.(3)

Internal funding sources, such as cash holdings, are an alternative to external finance. SMEs' deposit balances have grown at an annual rate of over 5% since the second half of 2012, according to data from the British Bankers' Association (BBA).(4) Annual growth in deposits from all private non-financial corporations was higher than that for SMEs in 2013 Q1.

Loan pricing

The total cost of bank finance to a business can be decomposed into the fees charged by the lender to provide facilities, the spread over a given reference rate at which loans are offered and the prevailing level of that reference rate in the financial markets.

A survey by the Bank's Agents during February and March 2013 suggested that there had been an increase in loan fees for SMEs in the previous twelve months. Lenders in the Bank of England's *Credit Conditions Survey* reported that fees and commission for SMEs fell slightly in 2013 Q2.

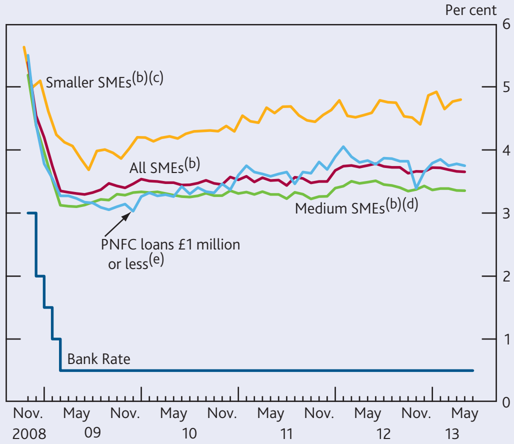
Across various measures, spreads over relevant reference rates on lending to SMEs have remained elevated and little changed over the post-crisis period. A study by the National Institute of Economic and Social Research (NIESR) indicated that, controlling for business characteristics related to firms' risk profiles, lenders' margins for both overdrafts and term loans were significantly higher from 2008–09 onwards compared to the pre-crisis period.[5]

The spread over relevant reference rates that SMEs face on new borrowing can vary widely, taking into account various business-specific risk and credit quality factors. As a result, there is no single definitive measure of loan pricing, though statistical and survey data can provide broad estimates. Indicative median interest rates charged on new and renewed variable-rate credit facilities to SMEs have been little changed since the start of 2012, according to survey data of four major UK lenders from the Department for Business, Innovation and Skills (BIS) (**Chart C**). The Bank's measure of effective rates on new corporate lending for advances of £1 million or less — another indicator of pricing for small business loans — has also been broadly unchanged since the start of 2012.[6] Both these measures may not entirely reflect the true cost of credit facing SMEs, as they do not include the impact of cashback deals or changes in fees. In addition, these rates may be affected by changes in the risk profile of borrowers, which will vary over time. For example, a change in rates could reflect banks' willingness to lend to different types of businesses.

Qualitative survey data also provide an indicator of loan pricing to SMEs. The Federation of Small Businesses' *Voice of Small Business Index* 2013 Q2 reported that the cost of finance for small businesses was lower compared to a year ago, for a second quarter in a row. Respondents to the *Credit Conditions Survey* — which was conducted between 10 and 31 May 2013 — reported that spreads on lending to small businesses had been broadly stable, and had narrowed slightly for medium-sized businesses in the three months to May.

While cost of finance was less likely to be a limiting factor in the decision to invest by firms, the Confederation of British Industry's *SME Trends Survey* April 2013, for SMEs in manufacturing, reported that uncertainty about customer demand was the most cited factor likely to limit capital expenditure authorisations over the coming twelve months.[7]

Chart C Indicative interest rates on lending to SMEs[a]



Sources: BIS, Bank of England and Bank calculations.

(a) These indicative rates do not reflect the impact of cashback deals or fees. Data for Bank Rate are to end-June, and for all other series to end-May. Non seasonally adjusted.
(b) Median by value of SME facilities (new loans, new and renewed overdrafts) priced at margins over base rates, by four major UK lenders (Barclays, HSBC, Lloyds Banking Group and Royal Bank of Scotland). Data cover lending in both sterling and foreign currency, expressed in sterling.
(c) Smaller SMEs are those with annual debit account turnover on the main business account less than £1 million.
(d) Medium SMEs are those with annual debit account turnover on the main business account between £1 million and £25 million.
(e) Weighted average of new lending to PNFCs of all sizes by UK MFIs for advances less than or equal to £1 million. Data cover lending in sterling. The Bank's effective interest rates series are currently compiled using data from 23 UK MFIs.

Demand and supply

The weakness in lending to SMEs over the past 18 months is likely to reflect a combination of demand and supply factors. Earlier editions of *Trends in Lending* noted that demand for credit by SMEs was muted over 2012. The latest *SME Finance Monitor* reported that around three quarters of SMEs surveyed had not applied for a new or renewed credit facility in the year to 2013 Q1, and that nothing had stopped them from doing so.[8] Contacts of the Bank's Agents reported that demand for bank borrowing among smaller firms remained subdued, with many preferring to pay down debt or build cash reserves.

Rejection rates for term loan applications, controlling for risk factors, had been significantly higher between 2008–12 compared to the pre-crisis period, according to analysis by NIESR. They suggested that credit conditions facing SMEs tightened significantly in the aftermath of the crisis. More recently, the availability of credit to SMEs has increased somewhat. During the past quarter, contacts of the Bank's Agents noted that with bond finance and US private placements providing a cheaper source of finance for many large firms, this had recently led to some increase in the availability of credit from UK banks to mid-tier corporates and to some larger SMEs with strong balance sheets.

Overall, while credit conditions for SMEs have improved recently, this improvement has been less marked than for larger businesses.[9] SMEs, which are more dependent on bank finance, have not benefited to the same extent as large companies from the recent reduction in the cost of finance from capital markets. In April 2013, the

Bank of England and HM Treasury announced an extension to the Funding for Lending Scheme, which has been designed in such a way as to provide considerably greater incentives for banks to lend to SMEs.

(1) For more details see *Business Population Estimates for the UK and Regions 2012*, Department for Business, Innovation and Skills. In this context, SMEs are defined as those private sector businesses with 0–249 employees. Available at www.gov.uk/government/uploads/system/uploads/attachment_data/file/80247/bpe-2012-stats-release-4.pdf.

(2) In the context of these lending data, SMEs are defined as those with annual debit account turnover on the main business account less than £25 million. These data include lending to unincorporated businesses and non-profit institutions serving households. For monthly data on lending to SMEs and large businesses, see *Bankstats* Table A8.1, available at www.bankofengland.co.uk/statistics/Documents/bankstats/current/taba8.1.xls.

(3) For more details see *Industry Figures 2013 Q1*, Asset Based Finance Association, available at www.abfa.org.uk/members/statistics.asp.

(4) These data are compiled for a sample of UK lenders. For more details, see *Banks' support for SMEs — Quarter 1 2013*, British Bankers' Association, available at www.bba.org.uk/statistics/article/banks-support-for-smes-quarter-1-2013/small-business/.

(5) For more details see 'Evaluating changes in bank lending to UK SMEs over 2001–12 — ongoing tight credit?', National Institute of Economic and Social Research, available at www.niesr.ac.uk/sites/default/files/publications/dp408.pdf.

(6) It could be that large businesses, defined as those with annual debit account turnover on the main business account of over £25 million, also have borrowing amounts of £1 million or less. The average approval for an SME loan in 2012 was £120,000 according to data from the BBA, suggesting that this measure of effective rates is a reasonable proxy on loan pricing for SMEs.

(7) In this context SMEs are defined as those private sector businesses with 0–499 employees.

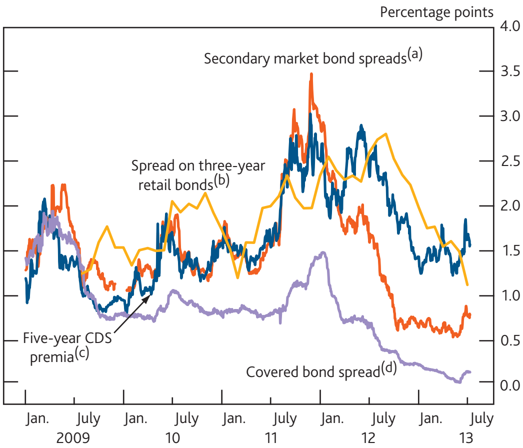
(8) For more details see *SME Finance Monitor Q1 2013*, BDRC Continental, available at www.bdrc-continental.com/EasySiteWeb/GatewayLink.aspx?alId=6345.

(9) Section 3 on pages 13–15 contains more details on lending to larger businesses.

2 Loan pricing

Indicative measures of the spread over relevant swap rates on longer-term wholesale debt decreased in April and May, before increasing during June. According to the Bank of England's *Credit Conditions Survey* 2013 Q2, spreads over reference rates on new lending fell significantly for large businesses, decreased slightly for medium-sized businesses, and were little changed for small businesses. The Bank's measure of the effective mortgage rate on overall new lending fell by around 20 basis points in the three months to May. Effective interest rates on new personal loans and interest-bearing credit cards also fell over this period.

Chart 2.1 Indicative long-term funding spreads



Sources: Bloomberg, Markit Group Limited, Bank of England and Bank calculations.

(a) Constant-maturity unweighted average of secondary market spreads to mid-swaps for the major UK lenders' five-year euro senior unsecured bonds, where available. Where a five-year bond is unavailable, a proxy has been constructed based on the nearest maturity of bond available for a given institution. Where there are gaps in the time series, no suitable bonds were issued in that period. Data are up to 10 July 2013.
(b) Sterling. Spread over the relevant swap rate. The three-year retail bond rate is a weighted average of rates from banks and building societies within the Bank of England's quoted rates sample with products meeting the specific criteria (see www.bankofengland.co.uk/statistics/Pages/iadb/notesiadb/household_int.aspx).
(c) The data show an unweighted average of the five-year senior CDS premia for the major UK lenders, which provides an indicator of the spread on euro-denominated long-term wholesale bonds. Data are up to 10 July 2013.
(d) The data show an unweighted average of the spread between euro-denominated covered bonds and equivalent-maturity swap rates for a selected bond issued by each of the major UK lenders. The selected bonds have residual maturities of between three and seven years. Data are up to 10 July 2013.

This section discusses recent developments in loan pricing for businesses and individuals, based on statistical data, survey evidence and discussions with the major UK lenders.

The total cost of bank finance to a company or individual can generally be decomposed into the fees charged by the lender to provide loan facilities, the spread over a given reference rate (such as three-month Libor or Bank Rate) at which loans are offered, and the prevailing level of that reference rate in the financial markets.

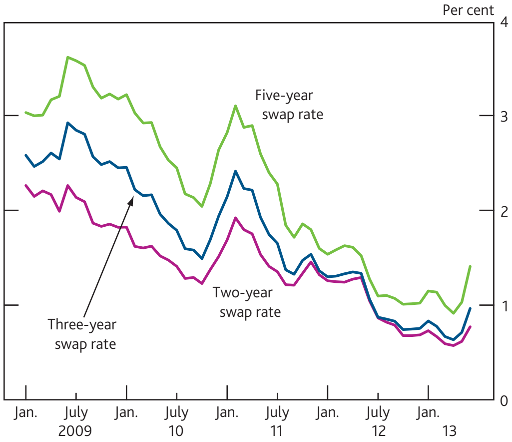
Funding and lending rates to May

Conditions in longer-term wholesale funding markets were broadly stable during April and May 2013. Indicative measures of the spread over relevant swap rates on longer-term wholesale debt decreased (**Chart 2.1**). Some respondents to the Bank of England's *Bank Liabilities Survey* 2013 Q2 — which was conducted between 10 and 31 May — commented that the fall in spreads during the quarter was a result of strong investor demand for wholesale debt issuance relative to the available supply.

Spreads over reference rates on some longer-term retail deposits — such as those over equivalent-maturity swap rates for three-year fixed-rate bonds — fell in the three months to May (**Chart 2.1**). This fall in spreads mainly reflected a fall in deposit rates, as relevant swap rates were little changed in this period (**Chart 2.2**). Broadly consistent with this, respondents to the *Bank Liabilities Survey* reported that spreads on retail funding had fallen significantly in the three months to May.

Respondents to the Bank of England's *Credit Conditions Survey* — which was also conducted between 10 and 31 May — reported that spreads over reference rates on new lending to large businesses tightened significantly in the three months to May (**Chart 2.3**). Some lenders in the survey noted that increased competition had squeezed margins. Respondents to

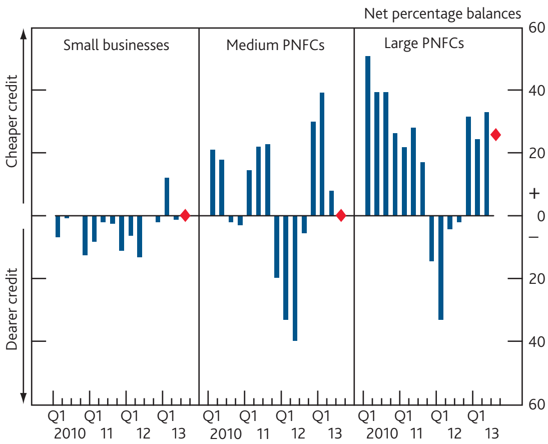
Chart 2.2 Swap rates at different maturities[(a)]



Sources: Bloomberg and Bank calculations.

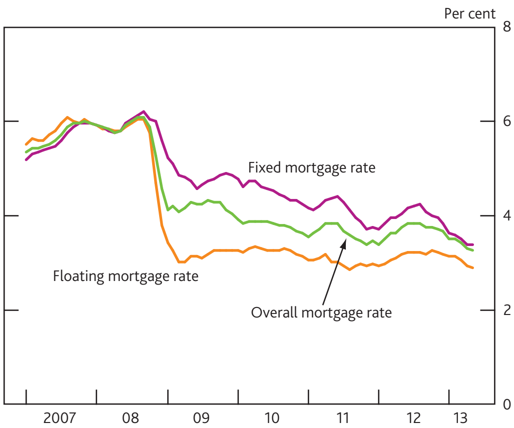
(a) Swap rates are monthly averages of daily data. Data are to end-June 2013.

Chart 2.3 *Credit Conditions Survey*: spreads over reference rates on lending to corporates by firm size[(a)(b)(c)]



(a) Net percentage balances are calculated by weighting together the responses of those lenders who answered the question. The blue bars show the responses over the previous three months. The red diamonds show the expectations over the next three months. Expectations balances have been moved forward one quarter.
(b) Small businesses are defined as those with annual turnover of less than £1 million; medium-sized businesses are defined as those with annual turnover of between £1 million and £25 million; and large businesses are defined as those with annual turnover of over £25 million.
(c) A positive balance indicates that spreads over reference rates have fallen, such that all else being equal it is cheaper for corporates to borrow.

Chart 2.4 Effective interest rates on new mortgage lending[(a)]



(a) Sterling. The Bank's effective interest rates series are currently compiled using data from 23 UK monetary financial institutions. Non seasonally adjusted.

the survey reported that fees and commission fell for large businesses. The balance of respondents in the *Deloitte CFO Survey* 2013 Q2 — which covers large companies — reported the cost of credit to be 'cheap'.

Spreads over reference rates on new lending to medium-sized businesses decreased slightly and were little changed for small businesses in the three months to May, according to the Bank of England's *Credit Conditions Survey* (**Chart 2.3**). Lenders in the survey reported that fees and commission had decreased slightly for both small and medium-sized firms. More generally, indicative measures of the spread over relevant reference rates on lending to small and medium-sized enterprises (SMEs) have been broadly stable in recent months. For more details on loan pricing to SMEs, see the box on pages 7–9.

The Bank's measure of the effective interest rate on new borrowing for businesses was broadly unchanged over the three months to May. Contacts of the Bank's network of Agents reported that pricing for corporate lending had continued to improve slowly. Looking forward in May, respondents to the *Credit Conditions Survey* expected a further significant tightening in spreads for large businesses in Q3, while spreads on lending to small and medium-sized firms were expected to be unchanged (**Chart 2.3**).

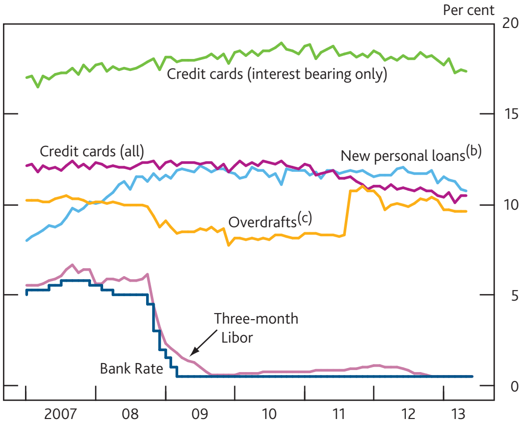
The Bank's measure of the effective mortgage rate on overall new lending fell by around 20 basis points in the three months to May and was lower by 50 basis points than a year ago (**Chart 2.4**). This fall was also reflected in effective rates on new fixed-rate mortgage lending.

The Bank's measures of quoted interest rates on some fixed-rate mortgages fell in April and May. With relevant swap rates broadly unchanged, spreads on these products narrowed by around 20 basis points.

Respondents to the *Credit Conditions Survey* reported that spreads on overall secured lending to households had tightened significantly in the three months to May. Within the total, a significant fall in spreads was reported for both prime and buy-to-let lending. Looking ahead in May, respondents to the *Credit Conditions Survey* expected a significant fall in spreads on overall secured lending in the coming quarter.

Effective interest rates on new personal loans and interest-bearing credit cards fell in the three months to May (**Chart 2.5**). Respondents to the *Credit Conditions Survey* reported that spreads on credit card lending remained unchanged in the three months to May. Spreads had tightened significantly for other unsecured lending, according to lenders in the survey. But spreads between effective rates and Bank Rate and Libor for consumer credit as a whole remained significantly wider than in late 2008, which lenders report partly reflects heightened credit risk on this form of

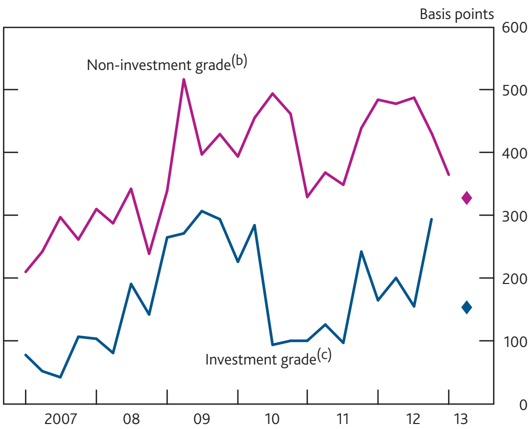
Chart 2.5 Effective interest rates on consumer credit(a)



Sources: BBA, Bank of England and Bank calculations.

(a) Sterling. The Bank's effective interest rates series are currently compiled using data from 23 UK monetary financial institutions. The rate for personal loans is for new business. For the other series the rates shown are for the stock of lending, as comparable data for new lending are not available. Data for Bank Rate and three-month Libor are to end-June, and for effective rates to end-May. Three-month Libor data are monthly averages of daily data. Non seasonally adjusted.
(b) Data cover loans with initial fixation of greater than one year but less than or equal to five years.
(c) The rate rise in September 2011 reflects system improvements and changes to reporting practices by one institution.

Chart 2.6 Average estimated spreads on syndicated loans(a)



Sources: Dealogic and Bank calculations.

(a) Average disclosed spreads over reference rates in the currency in which loan tranches are denominated, weighted by tranche size. Classification may be adjusted if ratings change over the life of the loan providing this is confirmed by the banks involved in the loan. The share of loans for which spread details are disclosed varies over time. Data for 2013 Q2, denoted by diamonds, are based on deal information available at the time of publication. Data are quarterly. Non seasonally adjusted.
(b) Non-investment grade is Dealogic leveraged and highly leveraged categories.
(c) Investment grade is classified by Dealogic as a rating of BBB- or higher, on announcement of the loan. If there is no rating then the loan spread on origination is used as the basis for classification, with any spread up to 250 basis points classified as investment grade. There are no disclosed spreads for investment-grade deals in 2013 Q1 in the current data.

lending. Lenders in the *Credit Conditions Survey* expected spreads on credit cards to fall slightly in the coming quarter, with spreads on other unsecured lending products expected to tighten further.

Funding and lending rates in June

In discussions conducted at the start of July, the major UK lenders reported that conditions in longer-term wholesale funding markets experienced an increase in volatility during June. Market contacts noted that this was consistent with uncertainty about the future path of monetary policy in the United States affecting a broad range of asset prices.

Indicative measures of the spread on longer-term wholesale debt rose in June (**Chart 2.1**). As at the start of July, most major UK lenders did not expect a significant change in these spreads in 2013 Q3.

Spreads over reference rates for three-year fixed-rate bonds continued to fall in June (**Chart 2.1**). This was mostly accounted for by a sharp rise in the relevant swap rate (**Chart 2.2**). In discussions at the start of July, the major UK lenders reported that pricing on some retail deposit products had fallen in 2013 Q2. Some lenders noted that this was at a slower rate than in recent quarters. The major UK lenders also noted that a higher volume of retail deposits had been retained, partly reflecting a compression in rates lessening the incentive for customers to switch between products and lenders. Looking forward, most lenders did not expect significant falls in retail deposit rates in 2013 Q3.

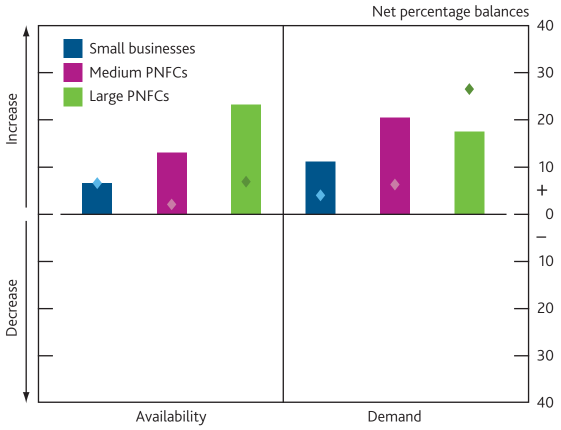
Quoted rates on fixed-rate mortgages were little changed in June. Spreads over swap rates on these fixed-rate products fell further, on average by around 25 basis points, reflecting the rise in swap rates on the month. In recent discussions, the major UK lenders noted that margins on many fixed-rate mortgage products were currently being compressed. Some lenders noted that fixed mortgage rates had not yet risen because of competition in the secured lending market.

Spreads on syndicated lending, which typically apply to large businesses, narrowed for the non-investment grade segment in 2013 Q2, according to Dealogic data (**Chart 2.6**). Spreads also narrowed for the investment-grade segment between 2012 Q4 and 2013 Q2.

3 Credit supply and demand

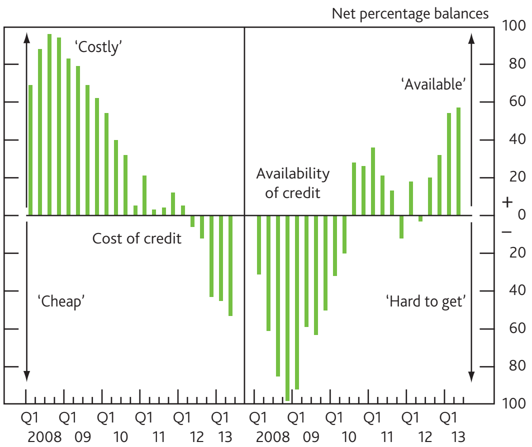
The overall availability of credit to the corporate sector and demand for bank credit increased in the three months to May, according to respondents to the Bank of England's *Credit Conditions Survey*. Lenders in the survey also reported that the availability of new secured credit to households increased over this period. Contacts of the Bank's network of Agents reported that activity in the housing market had continued to strengthen.

Chart 3.1 *Credit Conditions Survey*: availability and demand for credit across firm sizes reported in the 2013 Q2 survey[(a)]



(a) Net percentage balances are calculated by weighting together the responses of those lenders who answered the question. The bars in the chart show the net percentage balance reported over the three months to end-May. The diamonds show the associated expectations for the next three months. In the first panel, a positive balance indicates that more credit is available. In the second panel, a positive balance indicates an increase in demand. See also footnote (b) to **Chart 2.3**.

Chart 3.2 *Deloitte CFO Survey*: cost and availability of credit[(a)(b)]



(a) Net percentage balances for the cost of credit are calculated as the percentage of respondents reporting that bank credit is 'costly' less the percentage reporting that it is 'cheap'. Net percentage balances for the availability of credit are calculated as the percentage of respondents reporting that credit is 'available' less the percentage of respondents reporting that it is 'hard to get'. A positive balance indicates that a net balance of respondents report that credit is 'costly' or credit is 'available'.
(b) The *Deloitte CFO Survey* 2013 Q2 was published on 9 July and is available at www.deloitte.com/assets/Dcom-UnitedKingdom/Local%20Assets/Documents/Research/CFO%20Survey/uk-insights-cfo-survey-2013-q2-full-report.pdf.

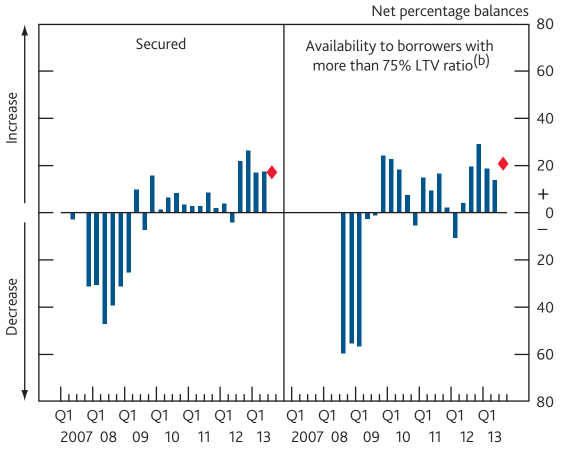
The amount of lending and its price depend on the interaction of demand and supply factors. Disentangling the separate influences of changes in the supply of and demand for credit is difficult, though survey data can help. This section looks at recent trends in credit supply and demand, drawing on surveys, reports from the Bank's network of Agents, and discussions with the major UK lenders.

Credit conditions for businesses

The overall availability of credit to the corporate sector increased in the three months to May, according to respondents to the *Credit Conditions Survey*. Availability increased for small and medium-sized businesses (**Chart 3.1**). Lenders in the survey reported that availability increased significantly for large businesses, the largest increase since 2009 Q3. The most important positive factor for availability was an improvement in the economic outlook. Respondents to the *Deloitte CFO Survey* 2013 Q2 — which covers large companies — reported that credit is cheaper and more easily available now than at any time in the past six years (**Chart 3.2**). Contacts of the Bank's network of Agents noted signs that competition among banks was starting gradually to increase lending appetite beyond the largest companies and strongest credit propositions. Looking forward, lenders in the *Credit Conditions Survey* expected overall credit availability to the corporate sector to be little changed in the coming quarter.

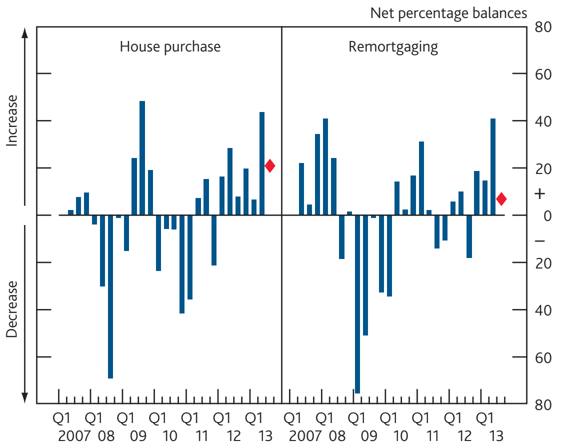
Demand for corporate credit was reported to have picked up across firm sizes in 2013 Q2, according to lenders in the *Credit Conditions Survey* (**Chart 3.1**). The reported increase in demand from small businesses in Q2 followed falls in the previous three surveys. Credit utilisation rates by SMEs were steady over the recent past, with significant headroom of unutilised overdraft facilities outstanding, according to data from the British Bankers' Association. Contacts of the Bank's Agents reported that, overall, demand for bank finance continued to be subdued, though had increased a little in recent months. Demand for credit was expected to be little

Chart 3.3 *Credit Conditions Survey*: availability of secured credit to households[a]



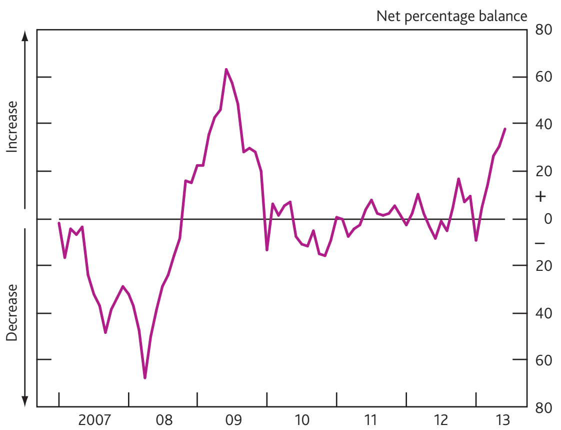
(a) See footnote (a) to **Chart 2.3**. A positive balance indicates that more credit is available.
(b) This question was introduced in 2008 Q3.

Chart 3.4 *Credit Conditions Survey*: demand for household secured lending[a]



(a) See footnote (a) to **Chart 2.3**. A positive balance indicates an increase in demand.

Chart 3.5 *RICS Residential Market Survey*: new buyer enquiries[a]



Source: Royal Institution of Chartered Surveyors.

(a) The net percentage balance for new buyer enquiries is calculated as the proportion of respondents reporting an increase in enquiries over the previous month, less the proportion reporting a decrease. A positive balance indicates an increase in enquiries. Seasonally adjusted.

changed for small firms, increase slightly for medium-sized firms and increase significantly for large firms in 2013 Q3, according to respondents to the *Credit Conditions Survey*.

Credit conditions for households

The availability of new secured credit to households increased in the three months to May, according to respondents to the *Credit Conditions Survey* (**Chart 3.3**). Lenders in the survey reported that the increase in availability was spread across the loan to value (LTV) ratio range. Looking ahead, the availability of secured credit was expected to increase further over the next three months across LTV ratios, according to respondents to the *Credit Conditions Survey*. Maximum LTV ratios were expected to increase a little and lenders expected their willingness to lend at 90% LTV ratios and above to increase in Q3, as it had in Q2.

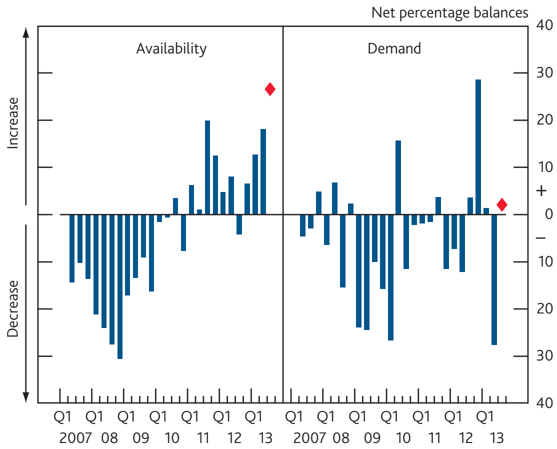
Overall demand for secured lending for house purchase increased significantly over the past quarter, according to respondents to the *Credit Conditions Survey* (**Chart 3.4**). This rise in demand was reported for both prime and buy-to-let lending. Lenders in the survey also reported that demand for remortgaging increased significantly. Some lenders in the survey noted that increased demand for secured lending in part reflected competitive pricing (which in turn was influenced by the Funding for Lending Scheme) and a general improvement in consumer sentiment. The Royal Institution of Chartered Surveyors' new buyer enquiries balance was positive in Q2, indicating an increase in demand for house purchase (**Chart 3.5**). The balance in June was the highest since August 2009. Lenders in the *Credit Conditions Survey* expected overall demand for secured credit for house purchase to increase significantly and for remortgaging to increase slightly in 2013 Q3.

Contacts of the Bank's Agents reported that activity in the housing market had continued to strengthen, partly reflecting the effects of the Government's Help to Buy scheme and a further gradual easing in mortgage terms and pricing. Looking ahead, the major UK lenders expected house prices in the coming months to be little changed or to increase slightly.

Respondents to the *Credit Conditions Survey* indicated that the amount of unsecured credit made available to households rose over the past three months (**Chart 3.6**), driven by a slight increase in risk appetite. The availability of unsecured credit was expected to increase significantly in 2013 Q3, according to lenders in the *Credit Conditions Survey*.

Demand for total unsecured lending fell significantly in 2013 Q2, according to respondents to the *Credit Conditions Survey* (**Chart 3.6**). Within this, demand for credit card lending decreased significantly while demand for other unsecured lending increased slightly. Demand for total unsecured credit was expected to be broadly unchanged

Chart 3.6 *Credit Conditions Survey*: availability and demand for household unsecured lending(a)



(a) See footnote (a) to **Chart 2.3**. In the first panel, a positive balance indicates that more credit is available. In the second panel a positive balance indicates an increase in demand.

in the coming quarter, although demand for other unsecured lending was expected to rise, according to lenders in the survey. Some respondents expected increasingly competitive offers to support demand for other unsecured lending going forwards.

Abbreviations

BBA — British Bankers' Association.
BIS — Department for Business, Innovation and Skills.
CDS — credit default swap.
CFO — chief financial officer.
CML — Council of Mortgage Lenders.
FLS — Funding for Lending Scheme.
Libor — London interbank offered rate (see below).
LTV ratio — loan to value ratio (see below).
MFIs — monetary financial institutions (see below).
NIESR — National Institute of Economic and Social Research.
PNFCs — private non-financial corporations (see below).
RICS — Royal Institution of Chartered Surveyors.
SMEs — small and medium-sized enterprises.

Glossary

Arrears rate The number of loans in arrears divided by the number of loans outstanding.
Bank Rate The official rate paid on commercial bank reserves by the Bank of England.
Businesses Private non-financial corporations.
Consumer credit Borrowing by UK individuals to finance expenditure on goods and/or services. Consumer credit is split into two components: credit card lending and 'other' lending (mainly overdrafts and other loans/advances).
Effective interest rates The weighted average of calculated interest rates on various types of sterling deposit and loan accounts. The calculated annual rate is derived from the deposit or loan interest flow during the period, divided by the average stock of deposit or loan during the period.
Facility An agreement in which a lender sets out the conditions on which it is prepared to advance a specified amount to a borrower within a defined period.
Gross lending The total value of new loans advanced by an institution in a given period.
Headroom Additional committed finance available that has not been drawn down.
Liquidations rate The number of corporate liquidations divided by the number of companies.
Loan approvals Lenders' firm offers to advance credit.
Loan to value (LTV) ratio Ratio of outstanding loan amount to the market value of the asset against which the loan is secured (normally residential or commercial property).
London interbank offered rate (Libor) The rate of interest at which banks borrow funds from each other, in marketable size, in the London interbank market.
Major UK lenders Banco Santander, Barclays, HSBC, Lloyds Banking Group, Nationwide and Royal Bank of Scotland.
Monetary financial institutions (MFIs) A statistical grouping comprising banks and building societies.
Mortgage lending Lending to households, secured against the value of their dwellings.
Net lending The difference between gross lending and repayments of debt in a given period.
Personal insolvency rate The number of individual insolvencies divided by the adult population.
Possessions rate The number of properties taken into possession divided by the number of mortgages outstanding.
Private non-financial corporations (PNFCs) All corporations (and partnerships) whose primary activity is non-financial and that are not controlled by central or local government.
Reference rate The rate on which loans are set, with an agreed margin over the reference rate (typically this will be Bank Rate, Libor or a swap rate).
Remortgaging A process whereby borrowers repay their current mortgage in favour of a new one secured on the same property. A remortgage would represent the financing of an existing property by a different mortgage lender.
Specialist mortgage lenders Providers of mortgage loans for niche markets that generally fall outside the scope of mainstream mortgage lending.
Swap rate The fixed rate of interest in a swap contract in which floating-rate interest payments are exchanged for fixed-rate interest payments. Swap rates are a key factor in the setting of fixed mortgage rates.
Utilisation rate Proportion of the total stock of facilities that has been drawn down.

Symbols and conventions

Except where otherwise stated the source of data in charts is the Bank of England.

On the horizontal axes of charts, larger ticks denote the first observation within the relevant period, eg data for the first quarter of the year.

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