Credit Conditions Review

2016 Q1

BANK OF ENGLAND

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This quarterly publication presents the Bank of England's assessment of the latest developments in bank funding and household and corporate credit conditions. It draws mainly on long-established official data sources, such as the existing monetary and other financial statistics collected by the Bank, and other data sources such as surveys of businesses and data from other organisations. The analysis also draws on the results of the Bank of England's *Bank Liabilities Survey* and *Credit Conditions Survey*.(1)

These data are supplemented by discussions between Bank staff and the major UK lenders; this intelligence is reflected in the report. The major UK lenders(2) are Banco Santander, Barclays, HSBC, Lloyds Banking Group, Nationwide and Royal Bank of Scotland; together they accounted for around 75% of the stock of mortgage lending, 50% of the stock of consumer credit (excluding student loans), and 65% of the stock of lending to businesses at end-December 2015. The *Review* also draws on intelligence gathered by the Bank's network of Agents and from market contacts.

The *Review* covers data and intelligence gathered up to end-March 2016. Unless stated otherwise, the data reported cover lending in sterling and foreign currency, expressed in sterling.

The *Credit Conditions Review* replaced the Bank of England's *Trends in Lending* publication in 2015 Q2.(3) For more details, see the box on page 1 in *Trends in Lending* April 2015, available at www.bankofengland.co.uk/publications/Documents/other/monetary/trendsapril15.pdf.

The publication dates in 2016 for future *Credit Conditions Reviews* are:
2016 Q2 *Review* on 13 July 2016.
2016 Q3 *Review* on 14 October 2016.

(1) The *Bank Liabilities Survey* and the *Credit Conditions Survey* for 2016 Q1 were conducted between 22 February and 11 March 2016. These surveys can be found at www.bankofengland.co.uk/publications/Pages/other/monetary/bls/default.aspx and www.bankofengland.co.uk/publications/Pages/other/monetary/creditconditions.aspx.
(2) 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.
(3) Previous editions of *Trends in Lending* are available on the Bank's website at www.bankofengland.co.uk/publications/Pages/other/monetary/trendsinlending.aspx.

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Executive summary

In 2016 Q1 long-term wholesale funding spreads for UK banks increased. Those higher wholesale funding spreads continued to push up transfer prices in 2016 Q1, according to respondents to the *Bank Liabilities Survey*, although responses were varied and not all lenders reported a rise. Retail deposit rates remained low, and the effective interest rate on household deposits decreased a little further in the three months to February. UK lenders continued to issue wholesale debt in 2016 Q1, and retail deposit growth increased slightly in the three months to February.

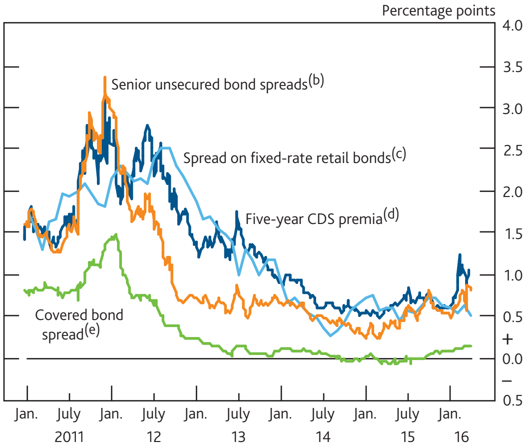
Annual growth in the stock of mortgage lending picked up further in recent months, reaching 3.0% in February. The 2016 Q1 *Credit Conditions Survey* suggested that this rise reflected an increase in demand for secured lending. Some of this strength in demand is likely to have come from the buy-to-let sector ahead of the stamp duty change. But recent discussions with the major UK lenders indicated that mortgage activity in the owner-occupier market had also been strong. Consumer credit continued to grow robustly reflecting both demand and supply factors. An important contributor to the pick up in consumer credit in recent years has been the increased provision of car finance through dealerships.

Net lending to UK non-financial businesses was positive in the three months to February 2016, and annual growth in the stock of lending reached 1.4%. For large companies, the cost of borrowing in UK corporate bond markets increased in 2016 Q1, but surveys suggest that credit availability remains plentiful and the cost of bank lending remains relatively low. Credit conditions facing SMEs were little changed in 2016 Q1, but have improved in recent years.

1 Bank funding

In 2016 Q1 long-term wholesale funding spreads for UK banks increased. Those higher wholesale funding spreads continued to push up transfer prices in 2016 Q1, according to respondents to the *Bank Liabilities Survey*, although responses were varied and not all lenders reported a rise. Retail deposit rates remained low, and the effective interest rate on household deposits decreased a little further in the three months to February. UK lenders continued to issue wholesale debt in 2016 Q1, and retail deposit growth increased slightly in the three months to February.

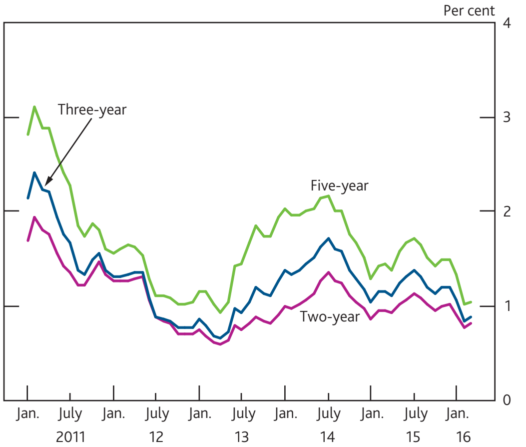
Chart 1.1 Indicative long-term funding spreads(a)



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

(a) Data are to end-March 2016.
(b) Constant-maturity unweighted average of secondary market spreads to mid-swaps for the major UK lenders' five-year euro senior unsecured bonds or a suitable proxy when unavailable.
(c) Unweighted average of spreads for two-year and three-year sterling fixed-rate retail bonds over equivalent-maturity swaps. Bond rates are end-month rates and swap rates are monthly averages of daily rates.
(d) Unweighted average of five-year euro senior CDS premia for the major UK lenders.
(e) Unweighted average of covered bond spreads for the major UK lenders.

Chart 1.2 Swap rates at different maturities(a)



Sources: Bloomberg and Bank calculations.

(a) Data are to end-March 2016 and are monthly averages of daily data. Sterling swap rates.

Funding costs and transfer prices

The cost of bank funding influences the interest rates charged to households and corporates. It can generally be decomposed into the spread over a given reference rate (such as swap rates), and the prevailing level of that reference rate in financial markets.

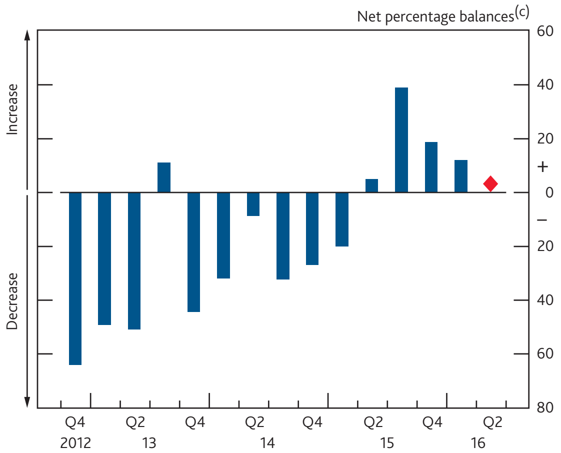
Indicative measures of banks' long-term wholesale funding spreads — such as senior unsecured bond spreads and CDS premia — rose in 2016 Q1 (**Chart 1.1**). Senior unsecured bond spreads were around 30 basis points higher at the end of 2016 Q1 than at the start. Notwithstanding the rise on the quarter, spreads remain much lower than the levels seen in 2011.

In recent discussions, most major UK lenders attributed the widening of spreads in Q1 partly to greater uncertainty about the global economic outlook, as well as weaker investor sentiment about prospects for the banking sector. Prices for certain types of funding instruments such as additional Tier 1 (AT1) securities were particularly volatile. Respondents to the *Bank Liabilities Survey* (*BLS*) expected spreads on 'other' funding, which includes wholesale debt funding and wholesale deposits, to increase further in 2016 Q2.

Higher wholesale funding spreads have been partially offset by decreases in swap rates (**Chart 1.2**). The fall in swap rates likely reflected changes in financial market participants' expectations for the path of Bank Rate.

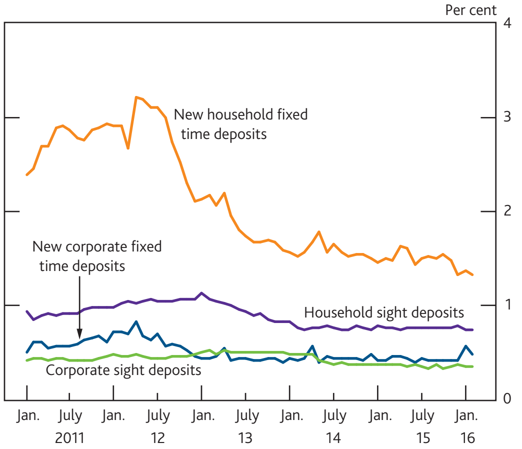
Respondents to the *BLS* reported that higher wholesale funding spreads had continued to push up transfer prices — the internal price charged to banks' business units to fund the flow of new loans — for the third consecutive quarter in 2016 Q1 (**Chart 1.3**). However, responses were varied and not all lenders reported a rise. In recent discussions, some major UK lenders noted that the fall in the cost of retail funding had pushed down a little on their transfer prices. Other lenders

Chart 1.3 *Bank Liabilities Survey*: changes in banks' transfer prices(a)(b)



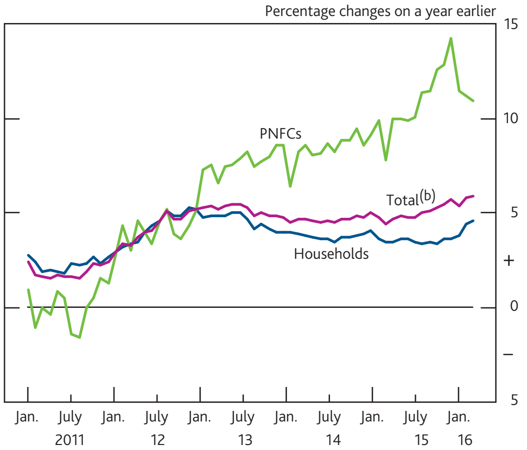
(a) Net percentage balances are calculated by weighting together the responses of those lenders who answered the question. The blue bars show the responses over the previous three months. The red diamond shows the expectation over the next three months. The expectation balance has been moved forward one quarter. Where the *BLS* is discussed, descriptions of a 'significant' change refers to a net percentage balance greater than 20 in absolute terms, and a 'slight' change refers to a net percentage balance of between 5 and 10 in absolute terms.
(b) Question: 'How has the marginal absolute cost of providing funds to business units changed (sometimes referred to as the 'transfer price')?'.
(c) A positive balance indicates an increase in transfer prices.

Chart 1.4 Rates on household and PNFC deposits(a)(b)



(a) Effective rates on sterling household and PNFC deposits. The Bank's effective rate series are currently compiled using data from up to 19 UK monetary financial institutions (MFIs). The effective rate is an average monthly rate. Non seasonally adjusted.
(b) The rates on sight deposits show rates on interest-bearing deposits only.

Chart 1.5 Household and PNFC deposits(a)



(a) Rate of growth in MFIs' M4 liabilities. Seasonally adjusted.
(b) Total is the rate of growth of PNFCs and households deposits together.

noted that they had smoothed through some of the recent volatility in wholesale funding spreads when setting their transfer prices. Interest rates on retail deposits remained low in 2016 Q1, and the rate fell a little for new household fixed time deposits (**Chart 1.4**).

There is little evidence so far of higher transfer prices feeding through to borrowing rates facing households (Section 2) and companies (Section 3).

Funding volumes

Respondents to the *BLS* reported that their total funding volumes increased significantly in 2016 Q1. Within the total, lenders reported that retail funding had remained broadly flat, while wholesale funding had increased significantly. Lenders expected total funding volumes to increase slightly further in 2016 Q2.

Despite the increase in wholesale funding spreads, UK lenders continued to issue wholesale term debt in public markets in 2016 Q1. Issuance was £24.5 billion, slightly higher than levels in 2015 Q1, according to data from Dealogic.

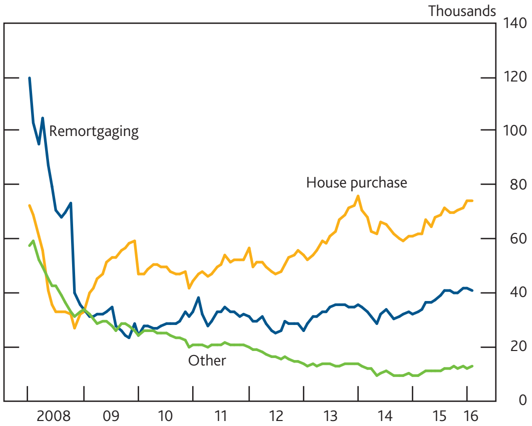
Although rates on retail deposits remained low, annual growth in retail deposits increased a little further in the three months to February, reaching 5.9% (**Chart 1.5**). That recent increase was driven by household deposits, within which sight deposits continue to account for the majority of overall growth. Deposits from private non-financial corporations (PNFCs) fell slightly in the past three months, but the annual growth rate remained strong at 11.0% in February. Similarly, the British Bankers' Association reported that deposits from small and medium-sized companies rose by 7% in 2015.

Capital instruments are a source of bank funding and banks' capital positions will influence their funding costs. Respondents to the *BLS* reported that their total level of capital had decreased in 2016 Q1, having reported increased capital in most quarters since the survey began in 2012 Q4. Lenders reported that investor demand for capital instruments fell significantly in Q1, likely reflecting increased market volatility. Lenders also suggested that market conditions had pushed down the supply of capital from issuers.

2 Household credit conditions

Annual growth in the stock of mortgage lending picked up further in recent months, reaching 3.0% in February. The 2016 Q1 *Credit Conditions Survey* suggested that this rise reflected an increase in demand for secured lending. Some of this strength in demand is likely to have come from the buy-to-let sector ahead of the stamp duty change. But recent discussions with the major UK lenders indicated that mortgage activity in the owner-occupier market had also been strong. Consumer credit continued to grow robustly reflecting both demand and supply factors. An important contributor to the pick up in consumer credit in recent years has been the increased provision of car finance through dealerships.

Chart 2.1 Approvals of loans secured on dwellings(a)



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

Table 2.A Secured lending to individuals(a)

	Averages						2015	2016	
	2013	2014	2015	2015 Q2	2015 Q3	2015 Q4	Dec.	Jan.	Feb.
Net monthly flow (£ billions)	1.1	2.0	2.8	2.4	3.2	3.6	3.2	3.7	3.6
Three-month annualised growth rate (per cent)	1.1	1.9	2.5	2.1	2.8	3.4	3.4	3.4	3.4
Twelve-month growth rate (per cent)	0.9	1.7	2.1	1.9	2.1	2.5	2.6	2.8	3.0

(a) Sterling lending by UK MFIs and other lenders to UK individuals. Seasonally adjusted.

Secured lending to UK households

Housing market activity has continued to pick up gradually in recent months. Mortgage approvals for house purchase rose to around 74,000 in February 2016 (**Chart 2.1**). Recent increases in approvals have fed through to higher net lending (**Table 2.A**). Annual growth in the stock of mortgage lending reached 3.0% in February, the highest since December 2008.

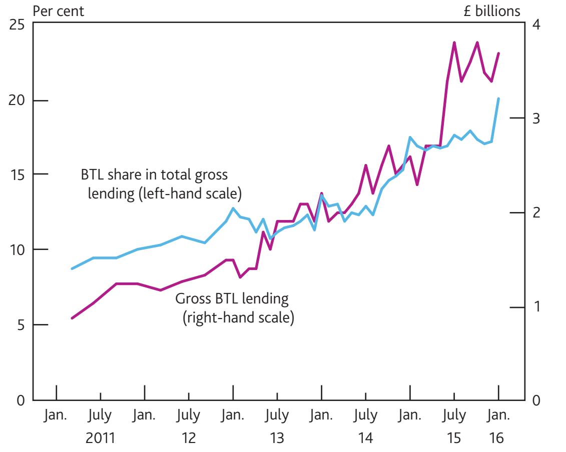
Some of the recent strength in approvals and lending is likely to reflect an increase in buy-to-let (BTL) activity, with some borrowers bringing forward their purchases ahead of the changes to stamp duty implemented on 1 April. Data from the Council of Mortgage Lenders (CML) indicated that the share of BTL in gross lending rose to 20% in January 2016, although the pick-up in BTL gross lending (non seasonally adjusted) was not particularly marked relative to the changes in the recent past (**Chart 2.2**).

The pickup in mortgage approvals also appears to reflect activity outside the BTL sector. Lenders responding to the *Credit Conditions Survey* (*CCS*) reported that demand for prime lending had increased in 2016 Q1, and in recent discussions the major UK lenders reported that mortgage activity in the owner-occupier market had been strong.

While demand for secured lending appears to have increased recently, lenders responding to the *CCS* reported that credit availability and credit scoring criteria were unchanged in the three months to mid-March.

Despite some lenders reporting higher transfer prices (Section 1), two-year fixed mortgage rates at 75% loan-to-value (LTV) ratios have remained broadly flat in recent months, while rates at 90% and 95% LTV fell marginally (**Chart 2.3**). As high LTV mortgage rates have fallen in recent years, and such mortgages have been made more available in

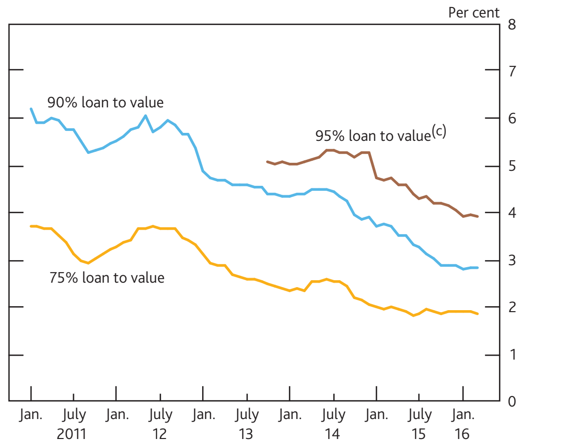
Chart 2.2 Gross buy-to-let lending[a]



Sources: CML, Bank of England and Bank calculations.

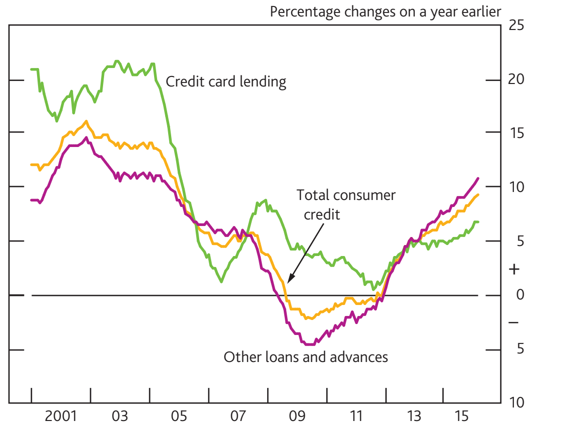
(a) Data are for monthly gross sterling lending from January 2013. Prior to this, the monthly estimates are calculated from quarterly data. Data cover lending for house purchase, remortgaging and other advances. Non seasonally adjusted.

Chart 2.3 Quoted interest rates on two-year fixed-rate mortgages[a][b]



(a) Rates on sterling lending. The Bank's quoted interest rates series are currently compiled using data from up to 19 UK MFIs. Non seasonally adjusted.
(b) The quoted interest rates are end-month rates.
(c) This series was not available between May 2008 and September 2013 as fewer than three products were offered from the sample of lenders in that period.

Chart 2.4 Consumer credit[a]



(a) Sterling lending by UK MFIs and other lenders to UK individuals. Consumer credit consists of credit card lending and other loans and advances and excludes student loans. Seasonally adjusted.

part through government schemes such as Help to Buy, the number taken out has risen. Bank of England data show that the proportion of mortgages with an LTV ratio exceeding 90% has picked up from 1.5% in 2009 Q4 to 3.8% in 2015 Q4.[1] This, however, remains well below the series peak of 16.3% in 2007 Q2.

Looking ahead to Q2, respondents to the *CCS* expected demand for secured credit to increase slightly further and for credit availability to increase as well. In recent discussions, some major UK lenders expected gross secured lending volumes to increase by a similar amount in 2016 as they did in 2015.

Consumer credit

The annual growth rate in the stock of consumer credit (excluding student loans) picked up to 9.3% in February (**Chart 2.4**), the highest since December 2005. Within this, non-credit card loans and advances continued to account for the majority of the net flow.

Car finance through dealerships has been an important contributor to the pickup in non-credit card loans and advances in recent years. Data from the Finance & Leasing Association (FLA) suggested that the gross flow of new advances was in excess of £28 billion in 2015, double that in 2011 (**Chart 2.5**).

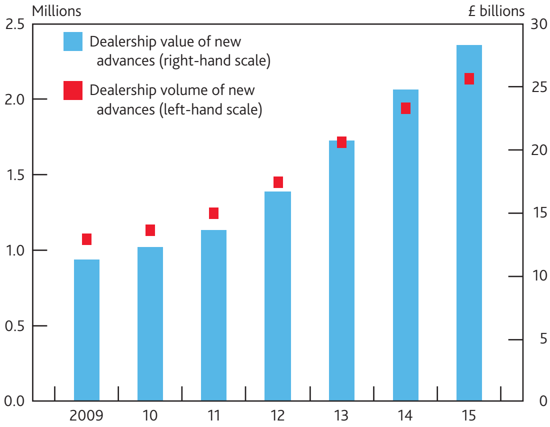
The increase in non-credit card loans and advances is likely to reflect both an increase in demand from borrowers and an increase in supply from credit providers. Demand for non-credit card unsecured lending increased significantly in Q1, and credit scoring criteria loosened significantly, according to the latest *CCS* (**Chart 2.6**). Respondents have reported looser credit scoring criteria for non-credit card lending in eleven out of the past twelve quarters.

Consistent with an increase in credit supply, personal loan rates have fallen markedly over recent years, although rates have been fairly flat at low levels in recent months. Supermarkets have been particularly competitive, offering rates that are well below the average quoted £10,000 personal loan rate (**Chart 2.7**).

Credit card rates have remained broadly stable over the past three months, although competition continued to centre on non-price terms and conditions. The average duration of interest-free balance transfers has increased steadily from around twelve months at the start of 2011 to around two years in the latest data, and market leading offers can be for as long as 40 months. While demand for credit card

(1) Data are for regulated mortgages. See Table 1.31 of the Mortgage Lenders and Administrators Statistics — 2015 Q4; www.bankofengland.co.uk/pra/Pages/regulatorydata/mlar/2015/dec.aspx.

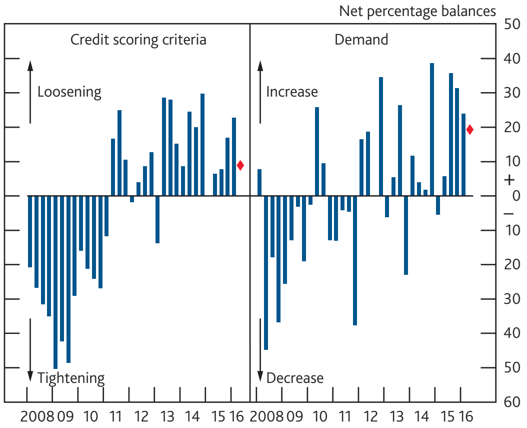
Chart 2.5 Car finance through dealerships by Finance & Leasing Association (FLA) members(a)



Source: Finance & Leasing Association.

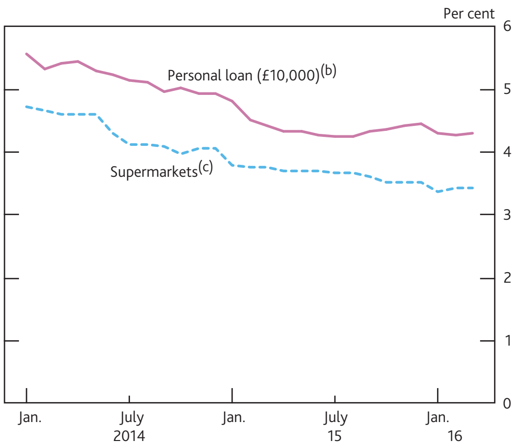
(a) New and used cars bought on finance by consumers through dealerships. Data are from monthly press releases, available at www.fla.org.uk/index.php/category/press-release.

Chart 2.6 *Credit Conditions Survey*: credit scoring criteria and demand for other unsecured lending to households(a)



(a) Net percentage balances are calculated by weighting together the responses of those lenders who answered the question. The bars show the responses over the previous three months. The diamonds show the expectations over the next three months. Expectations balances have been moved forward one quarter. Where the *CCS* is discussed, descriptions of a 'significant' change refer to a net percentage balance greater than 20 in absolute terms, and a 'slight' change refers to a net percentage balance of between 5 and 10 in absolute terms.

Chart 2.7 Personal loan rates(a)



Sources: Moneyfacts, Bank of England and Bank calculations.

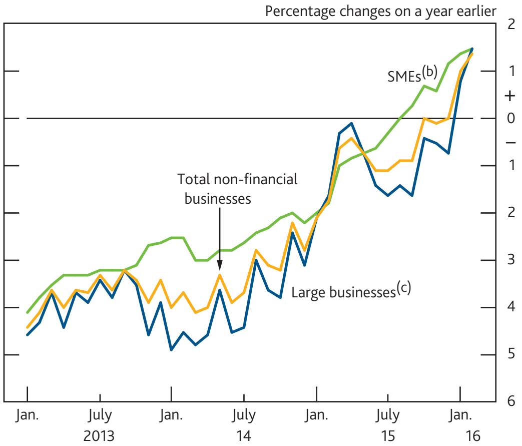
(a) End-month rates on sterling lending.
(b) The Bank's quoted interest rates series are currently compiled using data from up to 19 UK MFIs. Non seasonally adjusted.
(c) Supermarkets are Marks & Spencer, Sainsbury's and Tesco.

lending remained unchanged over the past three months according to the *CCS*, annual growth in the stock of credit card lending picked up to 6.7% in February (**Chart 2.4**).

3 Corporate credit conditions

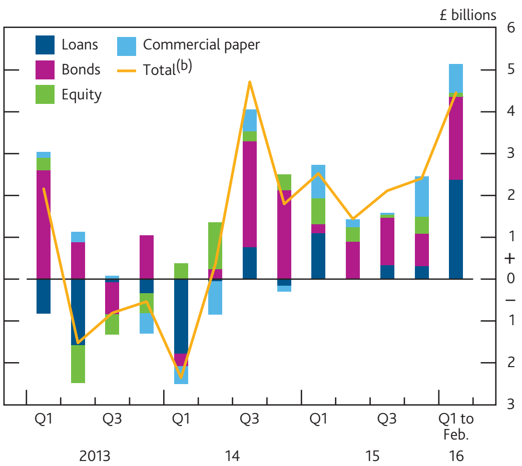
Net lending to UK non-financial businesses was positive in the three months to February 2016, and annual growth in the stock of lending reached 1.4%. For large companies, the cost of borrowing in UK corporate bond markets increased in 2016 Q1, but surveys suggest that credit availability remains plentiful and the cost of bank lending remains relatively low. Credit conditions facing SMEs were little changed in 2016 Q1, but have improved in recent years.

Chart 3.1 Lending to UK non-financial businesses(a)



(a) Rate of growth in the stock of lending. Lending by UK MFIs. Data cover lending in sterling and foreign currency, expressed in sterling. Non seasonally adjusted.
(b) SMEs are those businesses with annual debit account turnover on the main business account less than £25 million.
(c) Large businesses are those with annual debit account turnover on the main business account over £25 million.

Chart 3.2 Net finance raised by UK businesses(a)



(a) Monthly averages presented at a quarterly frequency. Finance raised by PNFCs from UK MFIs and from capital markets. Bonds data cover debt issued by UK companies via UK-based Issuing and Paying Agents. Data cover funds raised in sterling and foreign currency, expressed in sterling. Seasonally adjusted. Bonds, equity and commercial paper are not seasonally adjusted.
(b) Owing to the seasonal adjustment methodology, this series may not equal the sum of its components.

Borrowing by UK businesses

Net lending to UK non-financial businesses was positive in the three months to February 2016, and annual growth in the stock of lending reached 1.4% (**Chart 3.1**). Growth over the past few quarters has been predominantly driven by the distribution and transport and communication sectors, as discussed in the box on pages 12–13.

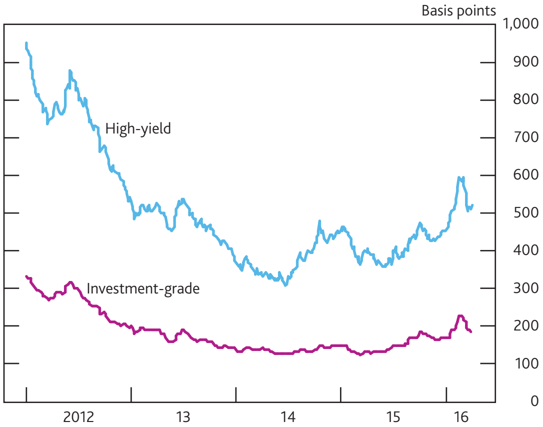
Total net finance raised by UK businesses from banks and capital markets was strong in January and February, averaging £4.5 billion across the two months (**Chart 3.2**). This was primarily accounted for by net bank lending and bond issuance; although a significant amount of the bond issuance in February was by one business.

Large corporates

Credit conditions in corporate bond markets — an important source of finance for some large companies — have tightened in recent months. Spreads rose markedly in the early part of 2016 Q1 before falling back more recently (**Chart 3.3**). Sterling denominated corporate bond spreads widened, on average, by around 20 basis points for investment-grade issuers, and by around 70 basis points for 'high-yield' issuers (those with lower credit ratings), over Q1. Likely reflecting the rise in the cost of issuance, the balance of respondents to the *Deloitte CFO* Survey — which covers large companies — who reported that bond issuance was 'attractive', fell back in 2016 Q1 to 59% from its most recent peak of 79% in 2014 Q4.

But there are few signs that higher borrowing costs in corporate bond markets have spilled over into bank lending. In recent discussions, most major UK lenders reported that lending rates to large companies remained low, although the downward trend in rates had abated. Consistent with this, respondents to the *CCS* noted that spreads on lending to large businesses were unchanged in 2016 Q1, having reported that they narrowed significantly over most of the past three years.

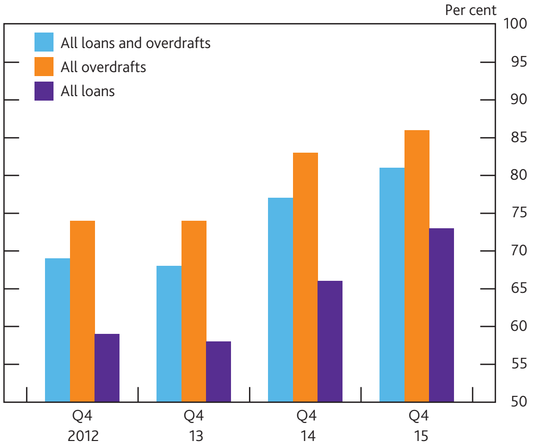
Chart 3.3 Sterling-denominated corporate bond spreads(a)



Source: BofA Merrill Lynch Global Research.

(a) Spreads over UK government bond yields. Sterling-denominated corporate bonds issued in domestic or Eurobond markets. Data are to end-March 2016.

Chart 3.4 *SME Finance Monitor*: successful applications for borrowing facilities(a)



Source: BDRC *SME Finance Monitor*.

(a) Survey question asks SMEs whether they had made an application for a new or renewed loan or overdraft facility in the previous twelve months, and had received a response from the bank. Successful applications are those ending the process with the loan/overdraft facility. Interim data for applications made in 2015. Data are reported in 18 month periods. SMEs are defined as businesses with up to 249 employees. For full descriptions of these series, see *SME Finance Monitor* 2015 Q4, page 127, available at http://bdrc-continental.com/wp-content/uploads/2016/03/BDRCContinental_SME_Finance_Monitor_Q4_2015.pdf.

Overall, credit availability remained plentiful for large companies despite a slight tightening on the quarter. The assessment of the Bank's Agents was that credit availability to large companies remains 'looser than normal',(1) though had tightened slightly in Q1 because of less favourable conditions for capital market issuance. In addition, the net balance of respondents to the *Deloitte CFO Survey* continued to report that credit was available and cheap in 2016 Q1, though these balances had fallen on the previous quarter.

Demand for bank lending from large corporates was broadly unchanged in 2016 Q1, according to lenders in the *CCS*. However, in recent discussions, the major UK lenders suggested that demand had fallen slightly for some firms, partly reflecting less refinancing activity and partly concerns about the global outlook. Some lenders also noted that somewhat weaker demand may partly reflect uncertainty about the forthcoming EU referendum.

Small and medium-sized enterprises

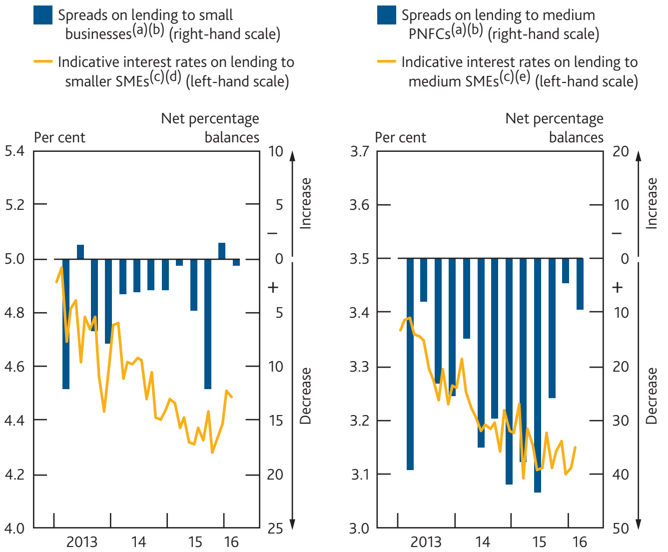
Credit conditions facing small and medium-sized enterprises (SMEs) have eased over the past couple of years. For example, loan and overdraft application success rates have increased steadily according to the BDRC's *SME Finance Monitor* (**Chart 3.4**). Credit availability for SMEs was little changed in 2016 Q1, according to respondents to the *CCS*.

Consistent with this easing in the supply of credit, pricing on lending to SMEs has decreased somewhat. Interest rates on lending decreased by around 40 basis points since the start of 2013 according to survey data from the Department for Business, Innovation and Skills (BIS) (**Chart 3.5**). And spreads on lending to SMEs have narrowed over recent years according to respondents to the *CCS*, although that has been more marked for medium-sized companies than smaller businesses. Looking forward, respondents expected spreads to be little changed in Q2.

Demand for credit from SMEs remained subdued. The proportion of SMEs described as 'happy non-seekers' was 78% in 2015 Q4 according to the latest *SME Finance Monitor*, broadly the same as in recent quarters. Though overall credit conditions were little changed in 2016 Q1, there has been continued growth in lending to SMEs. Net lending by FLS Extension participants was £0.6 billion in the fourth quarter of 2015,(2) and annual growth in the stock of lending by all UK MFIs to SMEs continued its upward trend, reaching 1.5% in February, the highest since the series began in April 2012 (**Chart 3.1**).

(1) For more details, see *Agents' summary of business conditions*, 2016 Q1; www.bankofengland.co.uk/publications/Documents/agentssummary/2016/q1.pdf.
(2) Net lending in the FLS Extension includes lending related to non-bank credit providers. For more details, see 'Funding for Lending Scheme Extension — usage and lending data'; www.bankofengland.co.uk/markets/Pages/FLS/extensiondata.aspx. Non seasonally adjusted.

Chart 3.5 Spreads and indicative median interest rates on lending to SMEs



Sources: BIS, Bank of England and Bank calculations.

(a) See footnote (a) to **Chart 2.6**. Data are quarterly.
(b) Spreads are over Bank Rate or London interbank offered rate (Libor) for small businesses and over Libor for medium-sized companies. A positive balance indicates that spreads have fallen such that, all else being equal, it is cheaper for companies to borrow. Data are on an inverted axis.
(c) These indicative rates do not reflect the impact of cashback deals or fees. Non seasonally adjusted. 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 sterling and foreign currency, expressed in sterling. Data are monthly and are to February 2016.
(d) Smaller SMEs are businesses with annual debit account turnover on the main business account less than £1 million.
(e) Medium SMEs are businesses with annual debit account turnover on the main business account between £1 million and £25 million.

Alternative sources of finance for SMEs — such as asset based finance and crowdfunding — continued to grow in 2015. Peer-to-peer lending grew by 75% to £1.26 billion in 2015 according to the latest *Small Business Finance Markets* report by the British Business Bank.[1] The report also noted that despite this increase it remains less than 3% of gross lending to SMEs by UK MFIs.

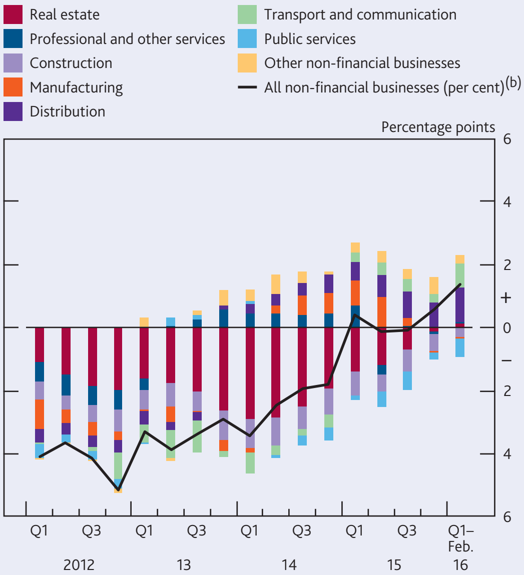
(1) For more details, see *Small Business Finance Markets* report, British Business Bank, February 2016; http://british-business-bank.co.uk/wp-content/uploads/2016/02/British-Business-Bank-Small-Business-Finance-Markets-Report-2015-16.pdf.

Trends in lending, by major industrial sector

This box provides an update of bank lending by major industrial sector to UK non-financial businesses.(1)

The overall growth rate in the stock of bank lending to UK businesses has continued to improve over the past few years and was positive in recent months (**Chart A**). This increase mainly reflects the improvement in net lending to the real estate sector. A number of other industrial sectors have also contributed positively since 2014.

Chart A Lending to UK non-financial businesses by major industrial sector(a)



(a) Lending by UK MFIs to UK non-financial businesses. Data cover lending in sterling and foreign currency, expressed in sterling. Contributions to the annual rate of growth in the stock of lending. Data are quarterly up to end-2015, with 2016 Q1 calculated using monthly data up to February 2016. Non seasonally adjusted. Further details on the series used in the chart are provided in the spreadsheet; www.bankofengland.co.uk/publications/Documents/creditconditionsreview/2016/additionalboxesq116.xlsx.
(b) Annual rate of growth in the stock of lending.

Lending to the real estate sector

The contribution of the real estate sector — which accounted for 30% of the stock of loans to businesses as at February 2016 — to the overall growth rate has become less negative since 2014 and close to zero over recent quarters (**Chart A**). The negative contribution over the past few years is likely to have reflected an active reduction of exposures to commercial real estate companies by banks, including through loan sales.

Gross lending flows (excluding overdrafts) — which are indicative of new activity in lending — to the real estate sector were slightly higher in 2015 compared to previous years (**Chart B**). Repayments decreased in 2015 such that net lending (excluding overdrafts) was close to zero in 2015, having been negative in previous years.

Lending to other industrial sectors

Excluding the real estate sector, the improvement in the overall growth rate since 2014 has been broad-based across industries. But over the past few quarters this has predominantly been driven by contributions from the distribution and transport and communication sectors, while the contribution from the manufacturing sector has declined somewhat (**Chart A**).

The contribution from the distribution sector has continued to increase over recent years, with positive net lending recorded in 2015 (**Chart B**). Gross lending flows have also continued to increase in the professional and other services sector.

Overdrafts

Overdrafts,(2) which are generally used as a form of working capital for businesses, accounted for 9% of the amounts outstanding of loans to UK businesses as at February 2016. This proportion was broadly the same across business sizes, and has been little changed in recent years.(3) According to the BDRC's *SME Finance Monitor*, 16% of SMEs used overdrafts in 2015, down from 22% in 2012.

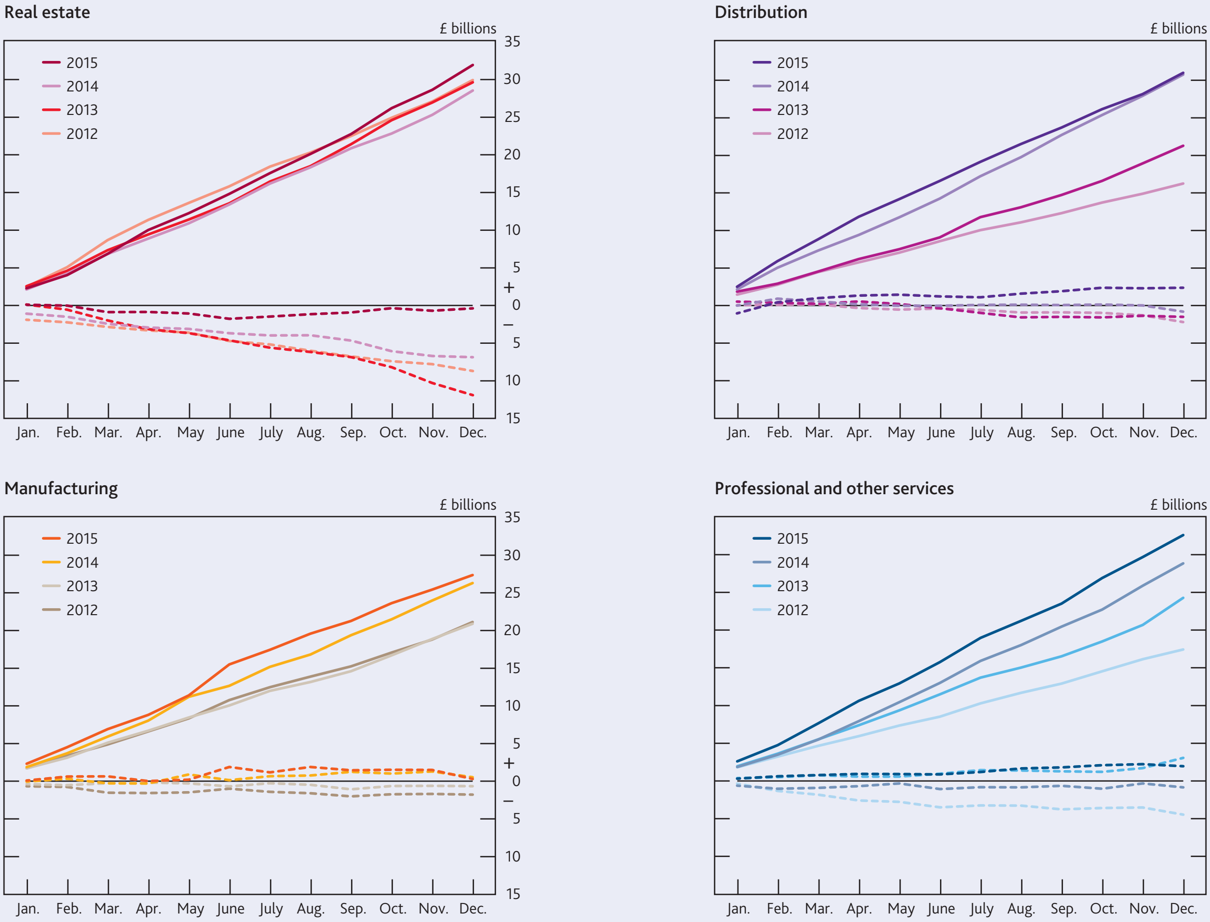
Within the stock of overdrafts, over half was accounted for by the manufacturing, distribution and professional and other services sectors — though these major industrial sectors constituted 30% of the stock of loans (**Chart C**). In contrast, the real estate sector accounted for 6% of overdrafts, despite having the largest single share of loans outstanding.

For SMEs, the agriculture, forestry and fishing sector accounted for a significant proportion of both loans and overdrafts as at end-2015, according to data from a BBA panel of lenders (**Chart C**). For most other major industrial sectors, the shares of the amounts outstanding of loans and overdrafts to SMEs were broadly similar to all non-financial businesses.

The Bank of England started collecting data on lending by UK MFIs split by both business size and major industrial sector in February 2016. Aggregated statistics, based on these data, are expected to be published in the second half of 2016.

(1) For previous updates on bank lending by major industrial sector, see the box in *Credit Conditions Review* 2015 Q2; www.bankofengland.co.uk/publications/Pages/creditconditionsreview/2015/q2.aspx.
(2) Overdrafts are defined as debit balances on accounts which, if in credit, would be classed as deposits. Facilities which involve a high frequency of advance and repayment of credit are also included.
(3) For more details on the amounts outstanding on overdrafts and loans by size of business, see *Bankstats* Table A8.1; www.bankofengland.co.uk/statistics/Pages/bankstats/2016/feb.aspx. Non seasonally adjusted.

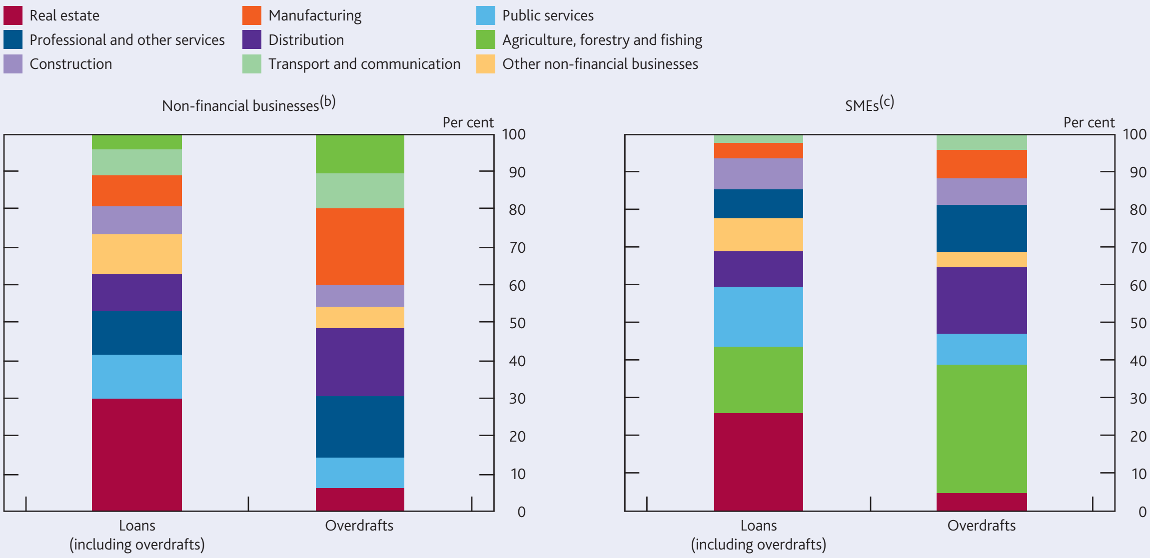
Chart B Cumulative gross and net lending to UK non-financial businesses by major industrial sector[(a)(b)]



Note: Solid lines: gross lending, dashed lines: net lending.

(a) Loans by UK MFIs to UK non-financial businesses. Net lending is defined as gross lending minus repayments. Data exclude overdrafts and cover lending in sterling and foreign currency, expressed in sterling. Non seasonally adjusted.
(b) Further details on the series used in the chart are provided in the spreadsheet; www.bankofengland.co.uk/publications/Documents/creditconditionsreview/2016/additionalboxesq116.xlsx.

Chart C Shares of loans and overdrafts to UK non-financial businesses and SMEs by major industrial sector[(a)]



Sources: BBA, Bank of England and Bank calculations.

(a) Data are as at December 2015. Data cover lending in sterling and foreign currency, expressed in sterling. See footnote (b) to **Chart B**.
(b) Lending by UK MFIs to UK non-financial businesses.
(c) Lending by a BBA panel of lenders to SMEs in Great Britain. SMEs are defined as businesses with turnover up to £25 million. For more details see *Bank support for SMEs — 4th Quarter 2015*, BBA; www.bba.org.uk/news/statistics/sme-statistics/bank-support-for-smes-4th-quarter-2015.

Abbreviations

AT1 — Additional Tier 1.
BBA — British Bankers' Association.
BIS — Department for Business, Innovation and Skills.
BLS — *Bank Liabilities Survey*.
BTL — Buy-to-let.
CCS — *Credit Conditions Survey*.
CDS — Credit default swap.
CFO — Chief financial officer.
CML — Council of Mortgage Lenders.
FLA — Finance & Leasing Association.
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).
MLAR — Mortgage Lenders and Administrators Return.
PNFCs — Private non-financial corporations (see below).
SMEs — Small and medium-sized enterprises.

Glossary

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.

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.

Other funding This refers to wholesale debt funding, wholesale deposits and funding via central bank operations.

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.

Retail funding Funding raised by banks in the form of deposits from households and PNFCs.

Senior unsecured debt Debt securities issued by lenders that pay a coupon, along with a final redemption payment, which are repaid before junior liabilities if a bank becomes insolvent.

Specialist/other 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.

Total funding Retail and other funding, which includes wholesale funding.

Transfer price The marginal absolute cost charged internally to business units for obtaining funding from the treasury unit, ie the cost of funding the flow of new loans.

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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