

BANK LENDING SURVEY**Portugal****INTRODUCTION**

Monitoring developments in credit markets is very important to assess the functioning of an economy, as the conditions prevailing in this market may affect the process of transmission of the monetary policy to economic activity. Aiming at gathering more detailed information on credit markets in the euro area, thus improving the assessment on the role of credit in business cycles and in the monetary policy transmission mechanism, the Eurosystem has launched, in early 2003, a new survey on banks' lending to be conducted quarterly — the Bank Lending Survey (BLS)⁽¹⁾.

The survey consists of a set of qualitative questions which is addressed, at the beginning of each quarter, to a predefined sample group of banks, located in the 12 countries of the euro area. The aim of the survey is to extend available statistics on interest rates and bank credit, providing additional information on non-interest rate conditions as well as on the factors affecting loan demand in the euro area. The results of the Survey will support the assessment of the ECB Governing Council on monetary and economic developments in the euro area, becoming, in the future, a further important tool to monetary policy decision-making.

The first bank lending survey took place in January 2003, followed by a second operation carried out in April. The Banco de Portugal has decided to disclose the results for the five Portuguese banking groups that participate in the sample group of the BLS. Thereby, the results for Portugal will be available, on a quarterly basis, following the ECB release of the corresponding aggregated results for the euro area (available on the ECB's website, at www.ecb.int).

What is the purpose of a bank lending survey?

Banks have an important role in the functioning of economies, as they do most of the financial intermediation between households and enterprises that are net savers and those that have net financing requirements. This role of the banks is especially important for those borrowers whose access to capital markets is limited, usually households and small and medium-sized enterprises.

Normally, credit supply is determined by the general economic outlook that affects banks' risk assessment and by banks' own financial situation. This latter is reflected in either tighter or easier credit standards, conditions and terms as applied by the banks to the approval of loans. Actually, the aggregate amount of loans provided by the banks is dependent on such factors as the price of credit (the interest rate) and other non-interest rate credit conditions or terms.

Over the business cycle, changes in financing conditions faced by the non-financial private sector are normal and they do not raise particular concerns if they correspond to smooth adjustments to economic activity developments. On the contrary, if they give rise to sudden and severe restrictions on the liquidity and solvency conditions of a considerable part of the economy, the efficient allocation of resources to valuable investment projects may be difficult, thereby hindering the respective implementation. Although rare, when these situations occur they may result in serious repercussions on economic developments. These situations are characterised by a very strict bank policy of credit rationing, where lending decisions relies more heavily on non-price conditions (credit crunch). This credit rationing reflects both the expression of extreme banks' risk aversion in the presence of an economic downturn and/or a deterioration of banks' own financial position. As a result banks' capacity to provide the adequate financing of the economy may be seriously restricted.

The value of a bank lending survey derives from the fact that the information is obtained directly from the lenders — i.e. the banks — who are at the best place to know whether they are relying more heavily on non-price conditions or not, for approving loans, and the reasons underlying their decisions.

The Bank Lending Survey has been developed precisely to provide specific information on credit conditions for both enterprises and households. Therefore, one purpose is to gather information on non-interest rate conditions and terms as applied to the approval of loans. The survey also aims at obtaining information on various factors affecting loan demand.

In addition to the importance of bank credit to the financing of the economy through the business cycle, changes in credit availability have an effect on the monetary policy transmission process — i.e. the way in which monetary policy decisions affect the economy in general and the price level in particular.

Besides extending the information on bank lending, available at present in the Eurosystem, the BLS results will also make easier to understand existing statistics on credit conditions. Additionally, information from the BLS, in particular regarding expected changes in credit standards and loan demand, should provide a better insight into future developments and thus facilitating the preparation of economic projections. Experience with bank lending surveys conducted by other central banks since some time ago — as the Federal Reserve System in the United States and the Bank of Japan — has shown that they provide important information for the assessment of past and future economic developments.

The questionnaire

The questionnaire is addressed to those responsible for the lending policy of the banks — usually at the board level. The questions — all of a qualitative nature — are intended to remain constant over time, thus keeping the reporting burden for the banks relatively low.

The survey includes 18 questions on past and expected developments in the credit market. The questions are organized according to the two borrower sectors that are the central focus of the survey: non-financial corporations and households. The definitions

(1) See the article "A bank lending survey for the euro area", in the April 2003 issue of the ECB's Monthly Bulletin p.65-75.

and classifications used in the survey are consistent with other ECB statistics. For both sectors, the questionnaire covers loan demand and loan supply factors.

Among the factors affecting loan supply, special attention is given to credit standards and credit conditions and terms as applied to the approval of loans, as well as to the various factors potentially responsible for the changes⁽²⁾. On the whole, ten questions are about supply factors, of which seven focus on credit standards and three on terms and conditions. Of the questions on credit standards, three give banks the opportunity to point out specific factors that have an effect on their current credit standards, as applied to the approval of loans to both enterprises and households.

Concerning loan demand, various factors that potentially affect it, namely related to financing needs and the use of alternative sources of finance, are mentioned. Seven questions are explicitly targeted on loan demand, of which three focus on demand of enterprises and four on demand of households.

Overall, the questionnaire includes thirteen backward and four forward-looking questions, in order to capture both recent and expected developments. Concerning past developments, the questions refer to the quarter before the reporting month while the questions on expected changes look at the next three months⁽³⁾.

The survey concludes with an open-ended question aimed at capturing any interesting development in the euro area credit markets that have not been covered by the other questions.

The sample group

In setting up the sample of banks to participate in the BLS, the Eurosystem took into consideration the qualitative nature of the information to be reported, the voluntary basis for participation and the need to adequately capture the specific features of the banking system in each country. Other crucial issue of concern was ensuring the confidentiality of information provided by the individual banks.

Given the differences in banking structures across individual countries and given that small and specialised banks have an important role in some countries, the BLS could not be concentrated just on the largest banks in the euro area. Therefore, the sample group has been drawn up taking into account the specific characteristics of the national banking structures in order to ensure the best possible representation of the sector.

At present, the sample is composed of 86 banks, five of them — each considered at the level of the banking group — are located in Portugal.

Naturally, the group of banks participating in the survey is subject to adjustments, as a result of changes in either the credit markets or the characteristics of the individual banks (e.g. in case of mergers). The sample group is also influenced by the need to remain representative of bank lending markets and loan categories at the euro area level. In order to identify any changes that make necessary an adjustment in the BLS sample, the Eurosystem and the National Central Banks (NCBs) will monitor attentively developments in the national banking sectors and credit markets.

Implementation procedures and aggregation of the results, at the euro area level

The Eurosystem has established a set of internal procedures to ensure confidential treatment of the individual results, at each step of the process by which responses are transmitted from participating banks to the ECB. The NCBs are responsible for contacting with the banks participating in the survey in their country and compiling the replies to the questionnaire. Then the NCBs transmit the responses to the ECB in such a way to fully protect their confidentiality and the anonymity of the banks. It is worth mentioning that the specific list of banks participating in the survey is confidential.

Quarterly, and after completing the final quality checks of the Survey, the ECB will publish the aggregated results of the euro area. The national results are disclosed by the NCBs, if they decide to do so, as the Banco de Portugal has started doing from now on.

Since the size of the sample differs from country to country depending on national banking structures, national results are aggregated at the euro area level using different country weights. These weights are the national shares in the total amount of the euro area outstanding lending to euro area residents, taking into account only the market segments considered in the survey — loans and credit lines to enterprises (non-financial corporations), lending to households for house purchase, consumer credit and other lending to households. The country weights will be updated every quarter. In aggregation of the April 2003 survey's results, the weight used for Portugal was 2.58 per cent.

(2) Credit standards are the internal guidelines or criteria that guide a bank's loan policy. The terms and conditions of a loan refer to the specific obligations agreed upon by the lender and the borrower, such as the interest rate, collateral required and maturity.

(3) The surveys take place, each quarter, at the beginning of January, April, July and October.