kcFED Small Business Lending Survey

New Small Business Lending Declines as Credit Standards Continue to Tighten

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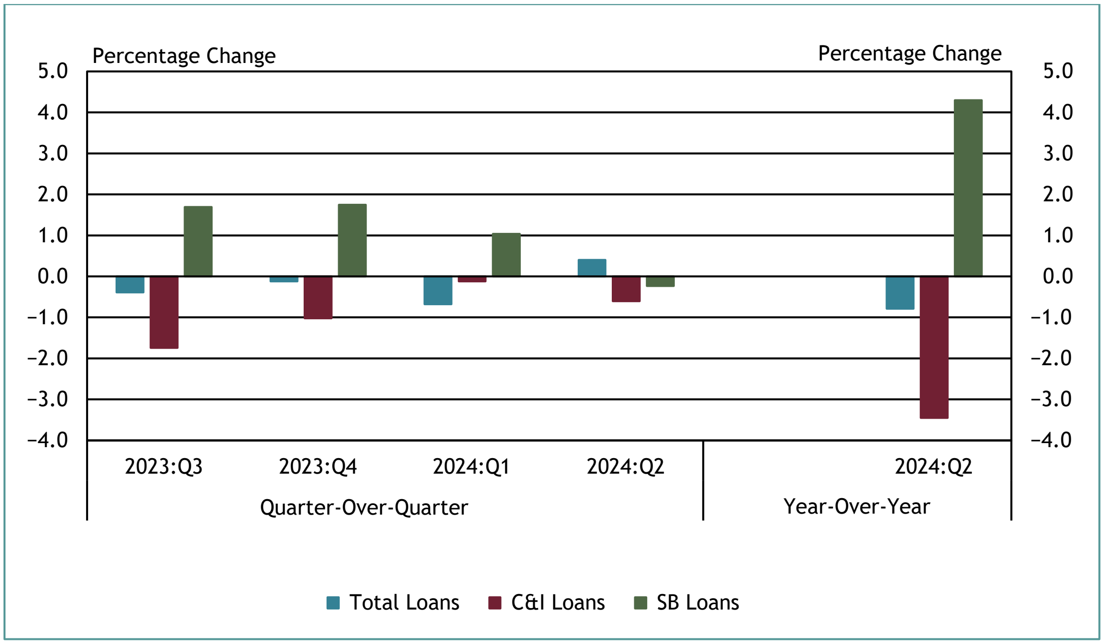
In the second quarter, new small business lending[1] decreased by 9.0 percent when compared to the same period in 2023 and 2.0 percent when compared to the previous quarter. Although new lending decreased, outstanding loan balances increased by 4.3 percent when compared to the same period in 2023. Interest rates for variable term loans increased, while rates on lines of credit offered at urban and rural banks began to converge.

With over $75 billion in small business loans reported, the 179 survey respondents reported credit standards tightened for the eleventh consecutive quarter and credit quality decreased. Credit line usage among all bank sizes[2] continued to increase, citing changes in borrowers' business revenue or other business-specific conditions. Loan demand decreased for the ninth consecutive quarter, and loan application approval rates decreased among all bank sizes.

[1] Small business lending refers to commercial and industrial lending to organizations generally defined as having less than five million in gross annual revenue, unless otherwise noted.
[2] Small banks have total assets of $1 billion or less, midsized banks have total assets between $1 billion and $10 billion and large banks have total assets greater than $10 billion.

Chart 1: Outstanding Small Business (SB) Loans Increase Year-over-Year

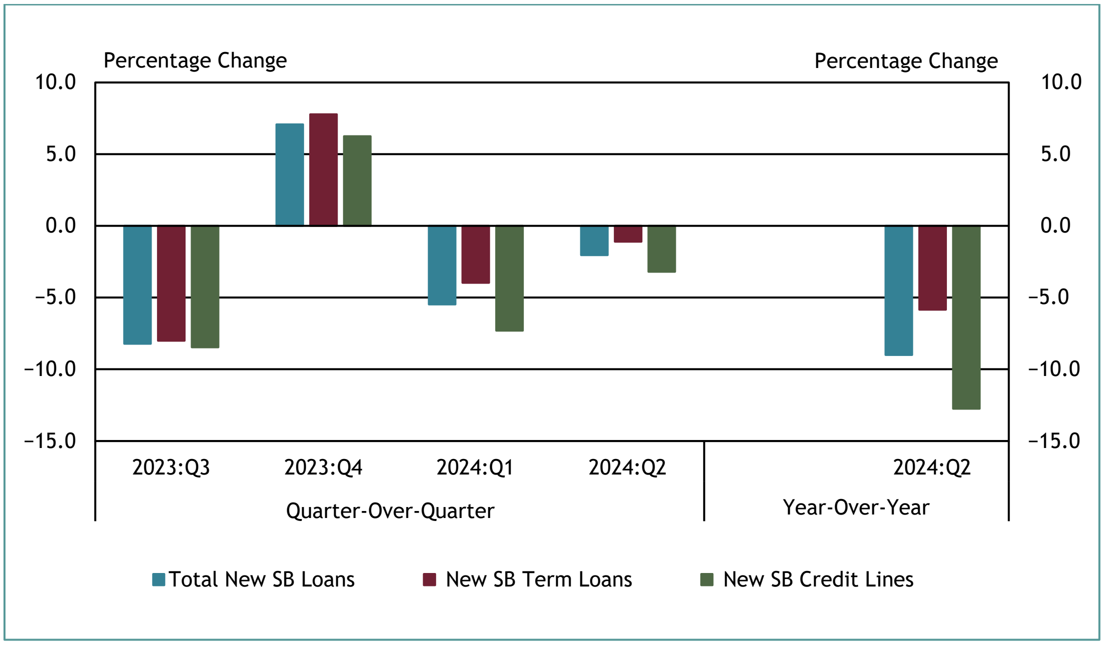


Note: Items are calculated using a subset of 119 respondents that completed the FR 2028D for the last five quarters surveyed.

Sources: Call Report, Schedule RC-C Part I, items 4. Commercial and Industrial Loans and 12. Total Loans and Leases Held for Investment and Held for Sale, and FR 2028D, items 5.b and 6.c.

When compared to second quarter 2023, small business loan balances increased by 4.3 percent, C&I loans decreased by 3.4 percent, and total loans decreased by 0.8 percent. The year-over-year increase in SB loans was comprised of increases in loans at large and midsized banks, while small banks reported decreases. Quarter-over-quarter, all loan categories remained relatively stable.

Chart 2: New Small Business Lending Declines

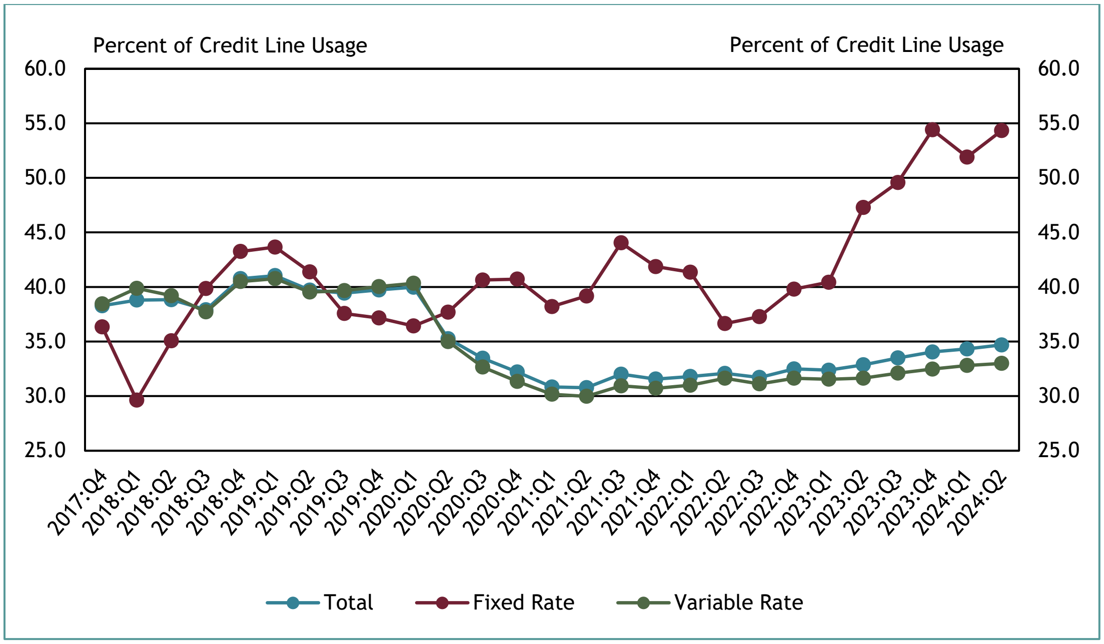


Note: Items are calculated using a subset of 119 respondents that completed the FR 2028D for the last five quarters surveyed. All loan types referenced in Chart 2 refer to small business lending.

Source: FR 2028D, items 7.b and 8.c.

Year-over-year, total new loans decreased by 9.0 percent, including a 5.9 percent decrease in new term loans and a 12.8 percent decrease in new credit lines. Quarter-over-quarter, total new small business loan balances decreased by 2.0 percent, including a 1.1 percent decrease in new term loans and a 3.2 percent decrease in new credit lines.

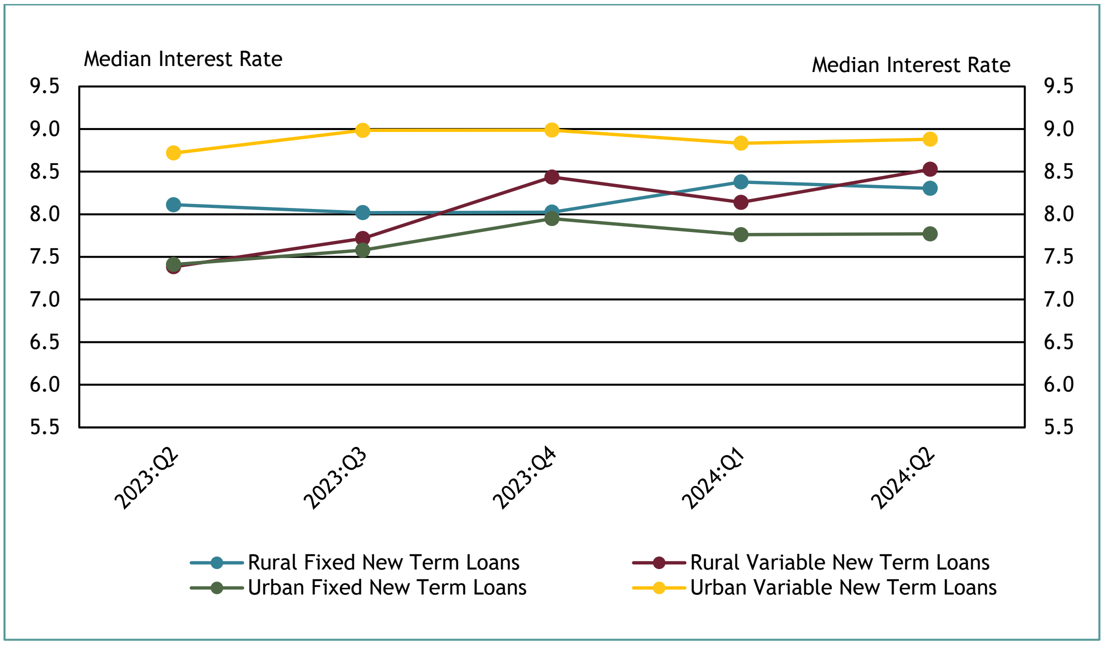
Chart 3: Credit Line Usage Continues Upward Trend



Source: FR 2028D, items 6.b and 6.c.

Usage of total small business credit lines continued an increasing trend for the fifth straight quarter. Although small businesses are utilizing 55 percent of fixed rate lines of credit compared to 33 percent of variable rate lines of credit, variable rate lines make up a larger portion of credit lines issued by banks. Respondents have consistently indicated that variable rate lines make up about 88 percent of total credit line usage.

Chart 4: Variable Rates on Term Loans Increase



Note: Items are calculated using a subset of 119 respondents that completed the FR 2028D for the last five quarters surveyed.

Source: FR 2028D, item 7.c.

Median interest rates increased for variable rate small business term loans in second quarter 2024, while fixed rates decreased slightly. The highest reported rates remained variable rate loans offered at urban banks. The lowest reported continued to be fixed rates offered at urban banks. The largest change was a 39-basis point increase in variable rates offered at rural banks. Urban banks make up about 89 percent of the subset of 119 respondents.[3]

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[3] Urban and rural classification is determined exclusively by the bank's head office location and [US Census Population] data.

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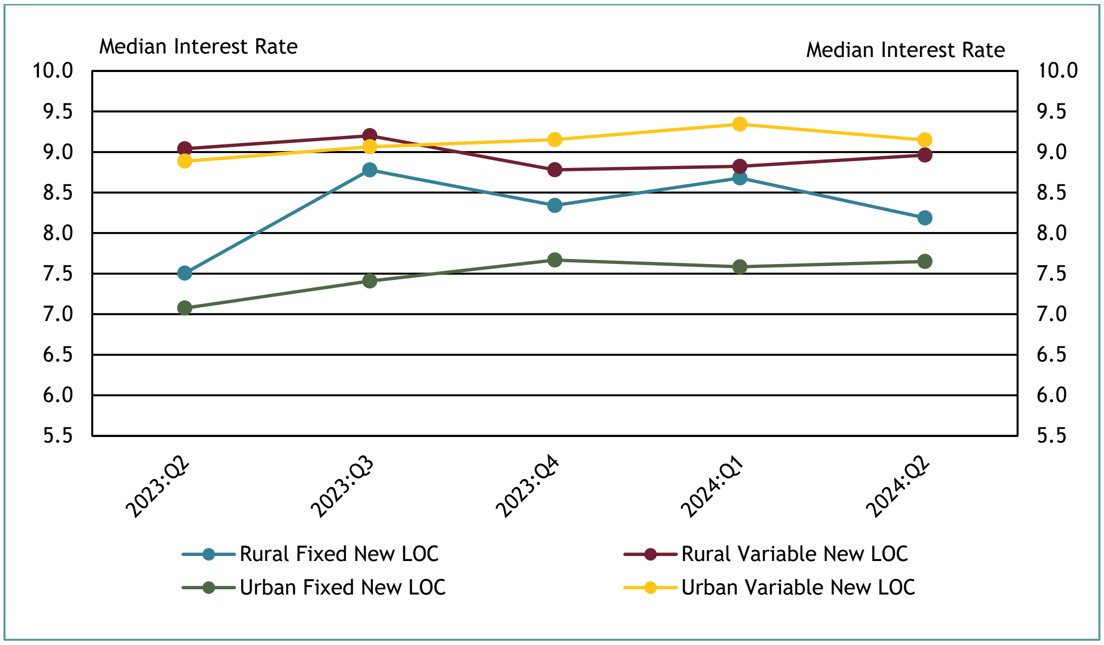
Chart 5: Rural and Urban Rates on Lines of Credit (LOC) Begin to Converge

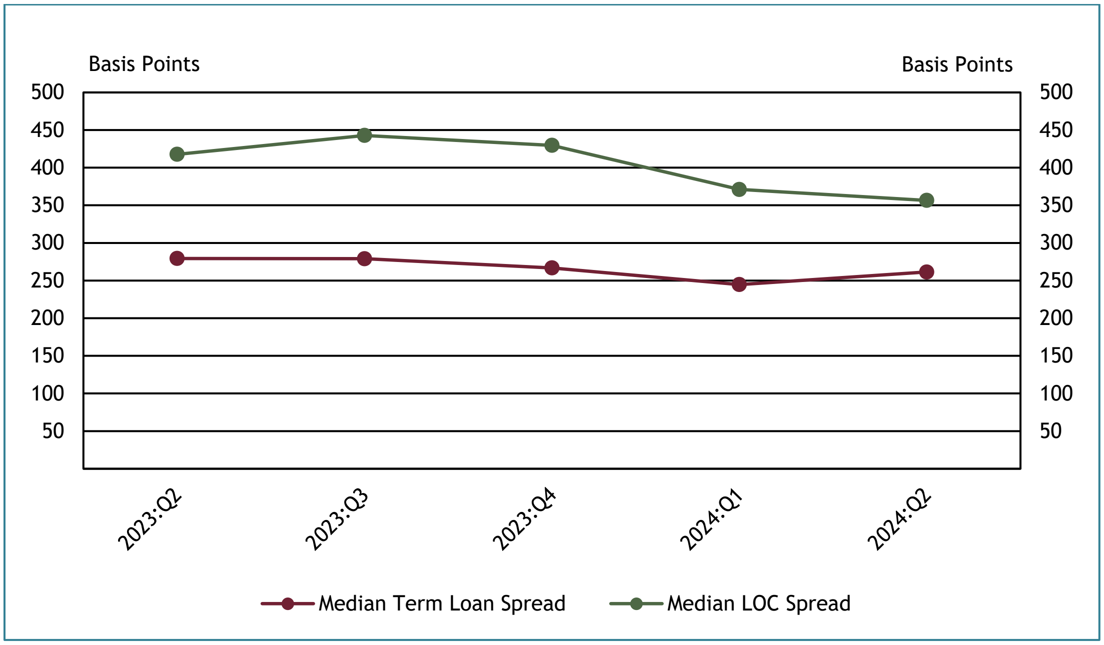


Note: Items are calculated using a subset of 119 respondents that completed the FR 2028D for the last five quarters surveyed.

Source: FR 2028D, item 8.d.

Median interest rates for rural and urban banks moved closer together in second quarter 2024. Variable rates offered at urban banks decreased to 9.2 percent, while rural rates increased to 9.0 percent. Fixed rates offered at rural banks decreased to 8.2 percent, while urban rates increased to 7.7 percent. Urban banks make up about 89 percent of the subset of 119 respondents.

Chart 6: Interest Rate (IR) Floor Spreads Increase for Term Loans and Decrease for Lines of Credit

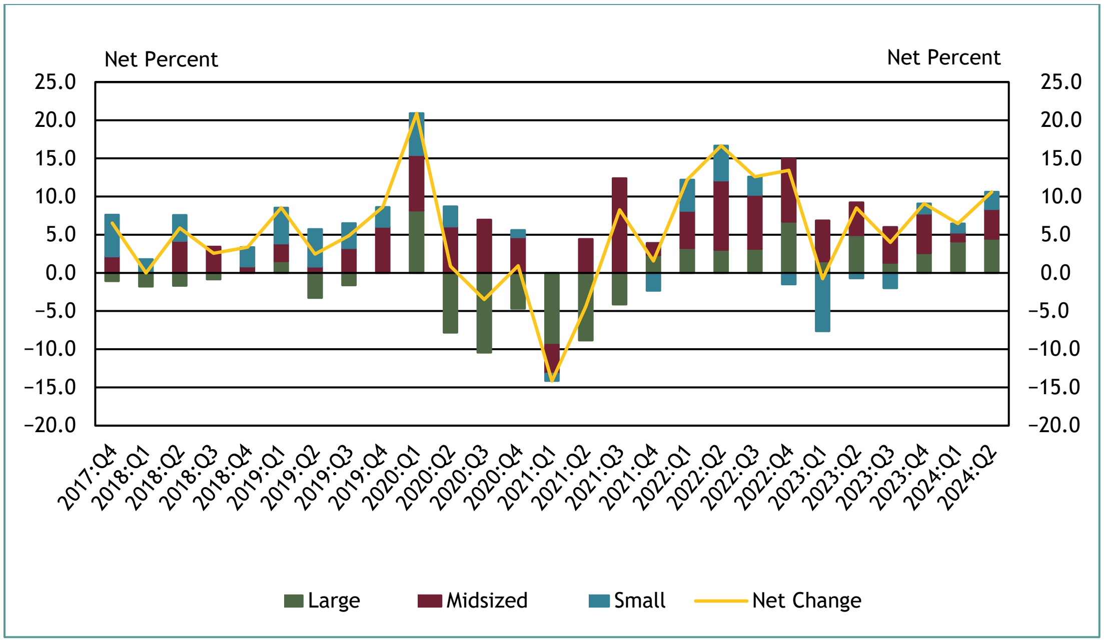


Note: Spread refers to the distance between the weighted average nominal interest rate and the weighted average interest rate floor.

Sources: FR 2028D, items 5.c, 5.h, 6.d, 6.g

Interest rate floor spreads increased on outstanding term loans and decreased on lines of credit in second quarter 2024. The median spread on term loans increased to 261-basis points, a 17-basis point increase. The median spread on lines of credit decreased to 357-basis points, a 15-basis point decrease.

Chart 7: All Bank Sizes Report Increases in Credit Line Usage



Note: Chart 7 shows diffusion indexes for credit line usage. The diffusion indexes show the difference between the percent of banks reporting decreased credit line usage and those reporting increased credit line usage. Net percent refers to the percent of banks that reported having decreased ("decreased somewhat" or "decreased substantially") minus the percent of banks that reported having increased ("increased somewhat" or "increased substantially").

Source: FR 2028D, items 9 and 10.

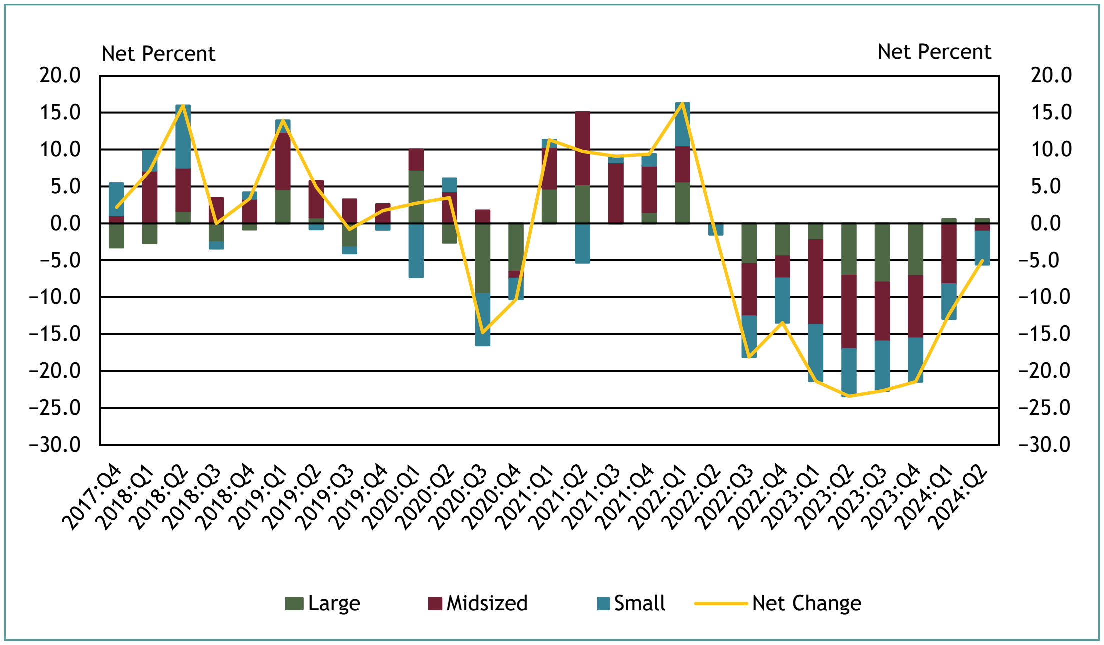
In second quarter 2024, 28 percent of respondents reported a change in credit line usage. Ten percent of respondents, on net, indicated that credit line usage increased, up from 6 percent last quarter.

On net, all bank sizes reported an increase in credit line usage for the third straight quarter. Of the banks reporting an increase, about 40 percent cited changes in borrowers' business revenue or other business-specific conditions and 29 percent cited changes in local or national economic conditions as very important reasons.

The reported increase in credit line usage is consistent with a shift to increased debt financing observed in other key indicators such as elevated consumer credit card debt.[4] Total household credit card debt continues to increase each quarter.[5]

[4] Source: FRED, Consumer Loans: Credit Cards and Other Revolving Plans.
[5] Source: FRBNY Consumer Credit Panel/Equifax

Chart 8: Respondents Report Declines in Loan Demand for the Ninth Consecutive Quarter



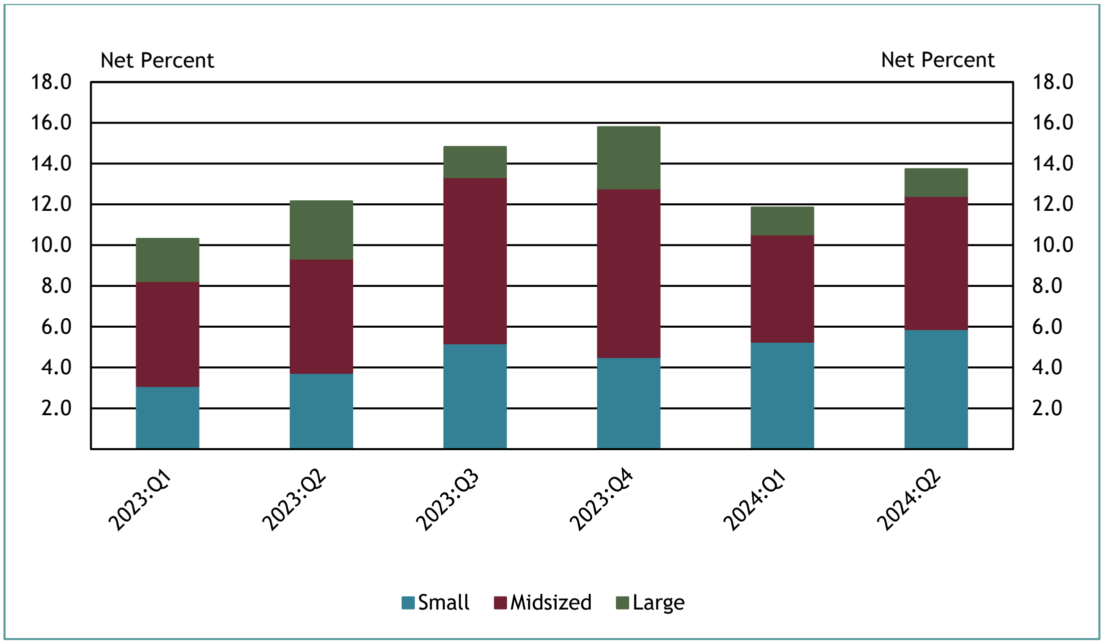
Note: Chart 8 shows diffusion indexes for loan demand. The diffusion indexes show the difference between the percent of banks reporting weakened loan demand and those reporting stronger loan demand. Net percent refers to the percent of banks that reported having weakened ("moderately weaker" or "substantially weaker") minus the percent of banks that reported having stronger loan demand ("moderately stronger" or "substantially stronger").

Source: FR 2028D, item 11.

About 39 percent of respondents reported a change in small business loan demand in second quarter 2024. On net, about 5 percent of respondents indicated weaker loan demand across all bank sizes. This marks the ninth consecutive quarter of respondents reporting a net decline in loan demand. However, large banks, on net, reported an increase in loan demand for the second consecutive quarter.

The timing of softer loan demand aligns with the Federal Reserve's tightened monetary policy since 2022. It is also consistent with the July 2024 Federal Reserve Senior Loan Officer Opinion Survey (SLOOS), where about 20 percent respondents reported weaker C&I loan demand from small firms (annual sales of less than $50 million) over the prior three months.

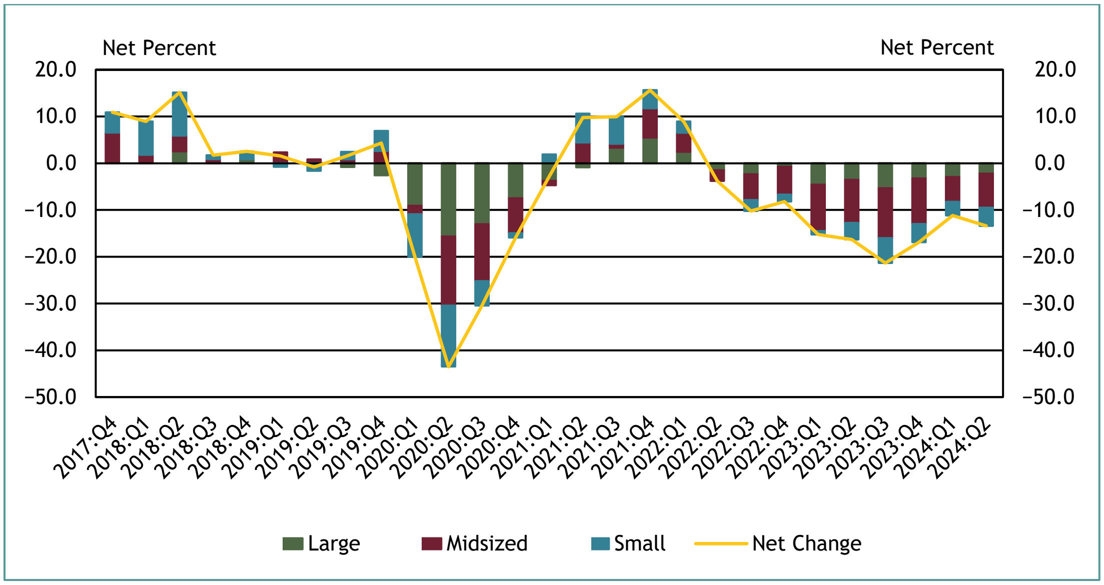
Chart 9: Banks Indicating Constrained Lending Increases



Source: FR 2028D, Special Question.

About 14 percent of all respondents indicated their lending to small businesses was constrained by the availability of liquidity in the market. This is an increase of about 1 percent from second quarter 2023 and 2 percent from the previous quarter. Most respondents reporting a constraint were small and midsized banks. For the sixth consecutive quarter, all respondents who indicated lending was constrained cited greater competitive pressures for deposits.

Chart 10: Overall Credit Quality Declines for the Ninth Consecutive Quarter



Note: Chart 10 shows diffusion indexes for credit quality of applicants. The diffusion indexes show the difference between the percent of banks reporting a decline in credit quality and those reporting improvement in credit quality. Net percent refers to the percent of banks that reported declining credit quality ("declined somewhat" or "declined substantially") minus the percent of banks that reported improving credit quality ("improved somewhat" or "improved substantially").

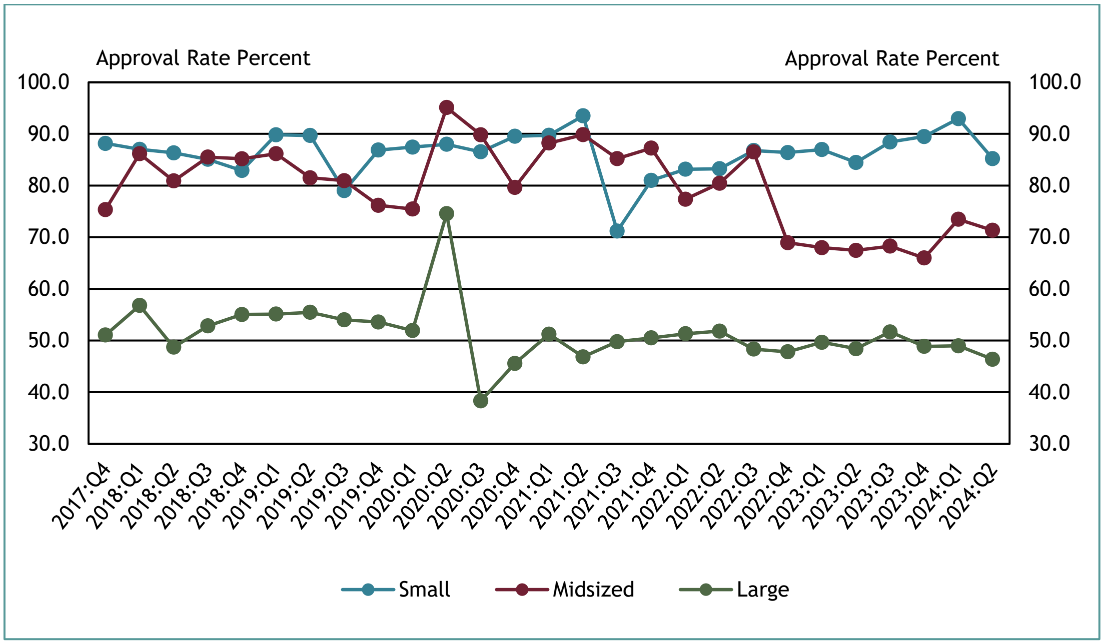
Source: FR 2028D, items 18 and 19.

About 13 percent of survey respondents, on net, reported a decrease in applicant credit quality. This is the ninth consecutive period in which respondents of all bank sizes, on net, reported a decrease. Of the respondents reporting a change in credit quality, whether an increase or decrease, 56 percent cited the liquidity position of business owners as a very important reason for a change. Other commonly cited reasons for a change include debt-to-income level of business owners, recent business income growth, and quality of business collateral.

The decrease in applicant credit quality reported by firms is consistent with the negative outlook of loan availability reported by small businesses in the July 2024 NFIB Survey of Loan Availability. In addition, declining credit quality for small businesses stands in contrast to measures of credit quality for large businesses. Corporate bond spreads[6] are currently near a decades low, which could suggest that small businesses may be under more strain when compared to their large counterparts.

[6] Source: FRED, ICE BofA US High Yield Index Option-Adjusted Spread.

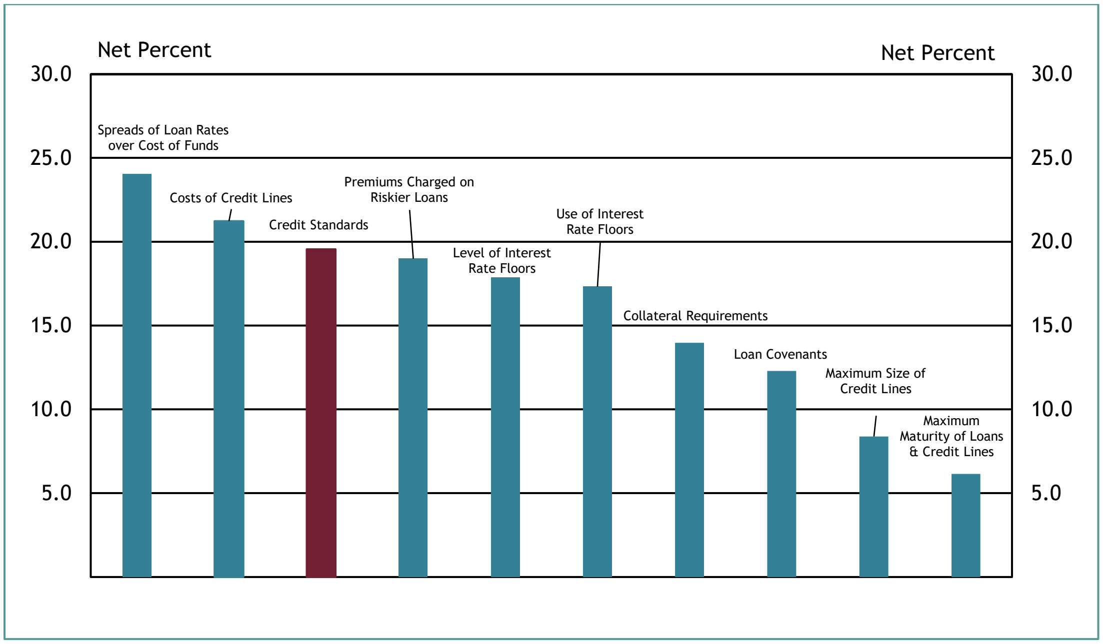
Chart 11: Loan Approval Rates Decrease for All Bank Sizes



Source: FR 2028D, items 12.a and 13.

Application approval rates decreased for all respondents in second quarter 2024. About 70 percent of respondents indicated borrower financials as the most common reason for denying a loan. Other commonly cited reasons were borrower credit history and collateral.

Chart 12: Respondents Report Tightening Credit Standards for the Eleventh Consecutive Quarter



Note: Chart 12 shows diffusion indexes for credit standards (red bar) and various loan terms. The diffusion indexes show the difference between the percent of banks reporting tightening terms and those reporting easing terms. Net percent refers to the percent of banks that reported having tightened ("tightened somewhat" or "tightened considerably") minus the percent of banks that reported having eased ("eased somewhat" or "eased considerably"). Source: FR 2028D, items 14, 15, 16 and 17.

About 20 percent of respondents, on net, reported tightening credit standards (red bar) in second quarter 2024. This is the eleventh consecutive quarter that respondents have reported tightening credit standards and is consistent with the tightening credit standards reported in the July 2024 Senior Loan Officer Opinion Survey on Bank Lending Practices.

On net, respondents indicated that all loan terms tightened. About 86 percent of respondents cited less favorable or more uncertain economic outlook as a somewhat important or very important reason for the tightening. Other commonly cited reasons were worsening of industry-specific problems and reduced tolerance for risk.

Other contributors to the release include Alli Baranski, Lauren Bennett, Nicholas Bloom, Sophie Burge, Nicholas Courtney, Daniel Harbour, and Stewart Pozzuto.