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Economics Group

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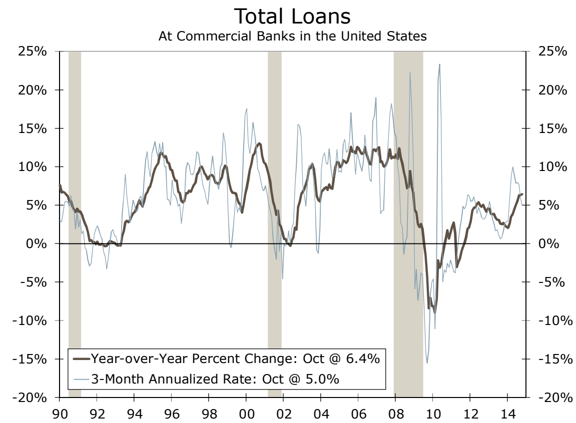
Bank Lending Supports Growing Economy

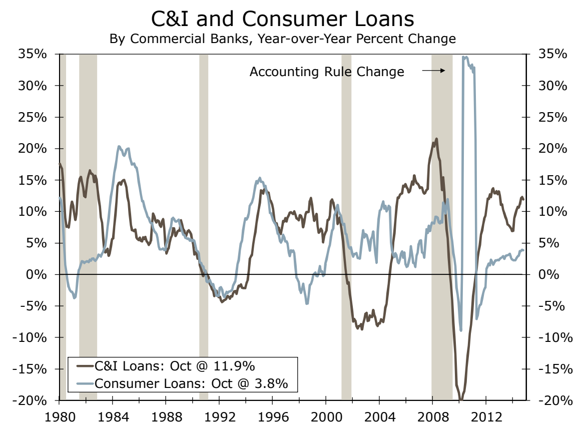
U.S. commercial banks continue to increase lending to both businesses and consumers, with commercial and industrial lending leading the way. Consumer lending has shown signs of pick up, as sentiment has improved.

Business Lending Continues to Outpace Consumer Lending

Loan growth continues to support a U.S. economy that is currently the main driver of global growth, in an environment where other major economies are facing considerable headwinds. Total loans at commercial banks were up at a year-over-year rate of 6.4 percent in October, continuing a strengthening trend that started in the beginning of 2013 (top chart). Despite recent strength, these rates of growth still remain below the 8 to 9 percent rates averaged in the last expansion. We see room for continued growth. Bank lending has continued to grow as banks have reportedly been easing standards following the strict tightening that occurred in the wake of the global financial crisis. However, the Fed's Senior Loan Officers' Opinion Survey showed a bit of pause to this trend in the fourth quarter, as the net percent of banks tightening standards edged up slightly, but remains in negative territory (i.e. net easing on balance).

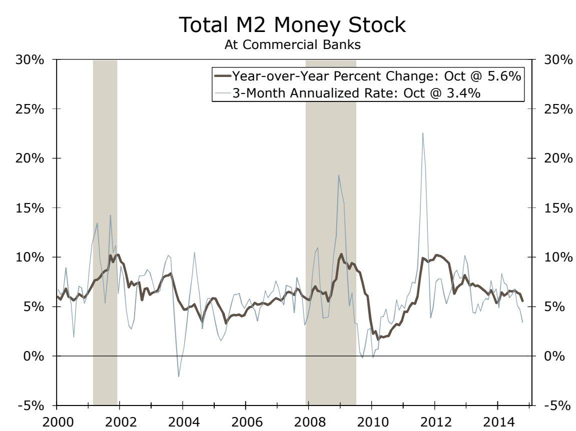


Growth in total lending has been underpinned by growth in commercial and industrial (C&I) lending throughout this recovery. C&I lending was up yet again in October at a solid rate of 11.9 percent year-over-year, while consumer lending has lagged behind (middle chart). Consumer lending has experienced relatively low rates of growth throughout this recovery, somewhat mirroring the behavior we have seen in revolving consumer credit. We have recently seen growth in revolving credit increase, to cycle-highs in excess of three percent year-over-year, while consumer loans reported by the Fed's H8 report were up 3.8 percent in October. This is encouraging news for economic growth going forward, as the consumer seems to be getting more and more comfortable engaging in spending through borrowing, whether it be through credit-card use (revolving credit) or otherwise. These measures of growing credit and loans outstanding are also consistent with recent consumer confidence surveys which continue to reach new highs for the current expansion.



Increased Lending Should Lead to Money Supply Growth

Overall lending growth has been picking up, driven primarily by C&I lending, but consumer lending is also beginning to increase. We expect this momentum to continue, and it should have a positive effect on growth in the money stock. We have seen growth in the M2 money stock fall on a year-over-year basis since the beginning of 2012, even as the Fed had been purchasing assets, expanding the monetary base. However, the key factor that has kept money stock growth subdued in the recent past has been the relatively muted growth in lending. As lending continues to gain momentum in a strengthening U.S. economy, we expect to see a rise in money stock growth, as the monetary base is set to remain elevated. With a meaningful rise in the money stock, inflation could experience upward pressure over the medium term.



Source: Federal Reserve Board and Wells Fargo Securities, LLC

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