# The Dramatic Tightening in Lending Standards to Reinforce the Projected 2023 Growth Slowdown

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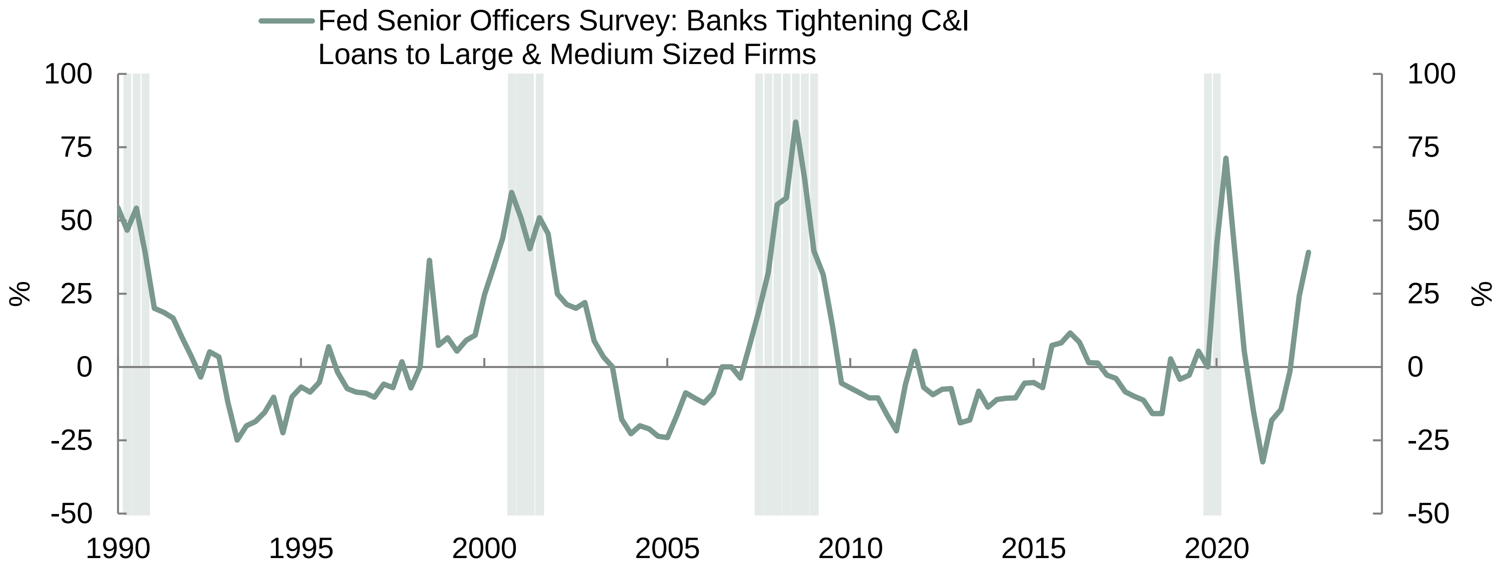
# C&I Lending Highly Cyclical

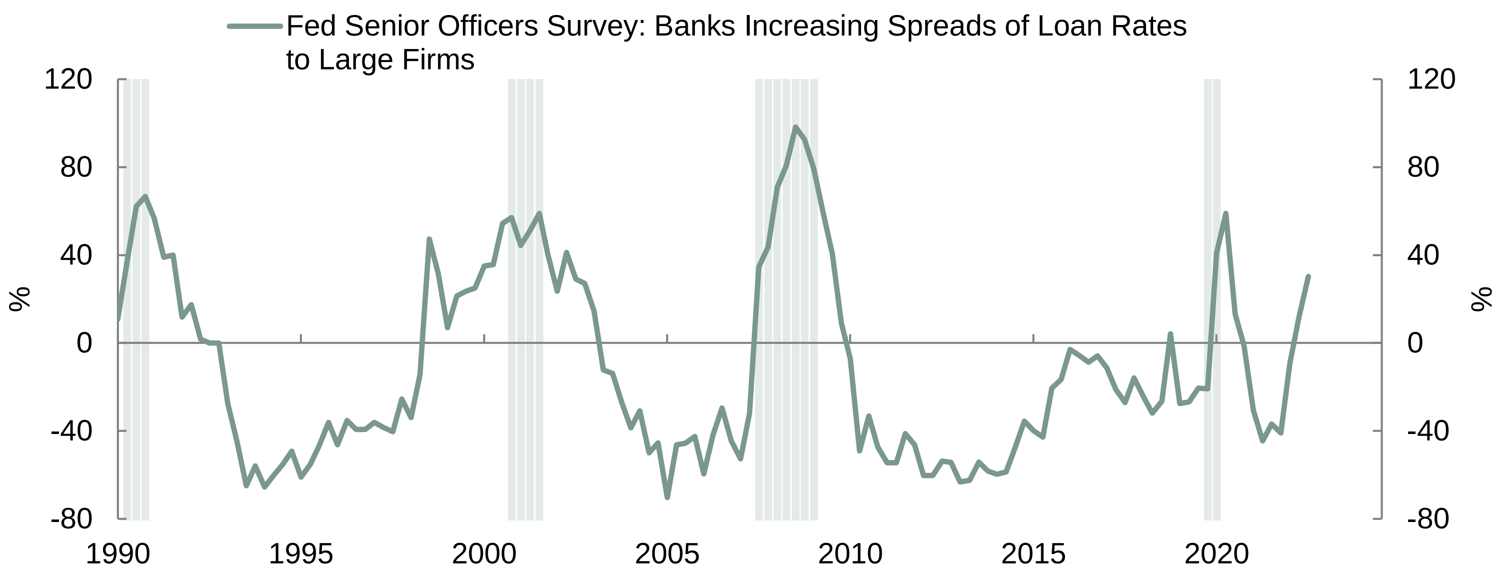
**The Fed's Senior Loan Officer Survey (SLOS) showed a dramatic tightening in lending standards this quarter for commercial and industrial loans (C&I). These loans are correlated with activity in the highly cyclical factory sector. Notably, C&I standards have tightened 41 points in the last two quarters to their highest non-pandemic reading since Q2 2008. The current level has always been associated with recession. Will this time be different?**




Source: Bloomberg, Federal Reserve, SMBC Nikko

# Tightening on CRE Loans Even More Dramatic

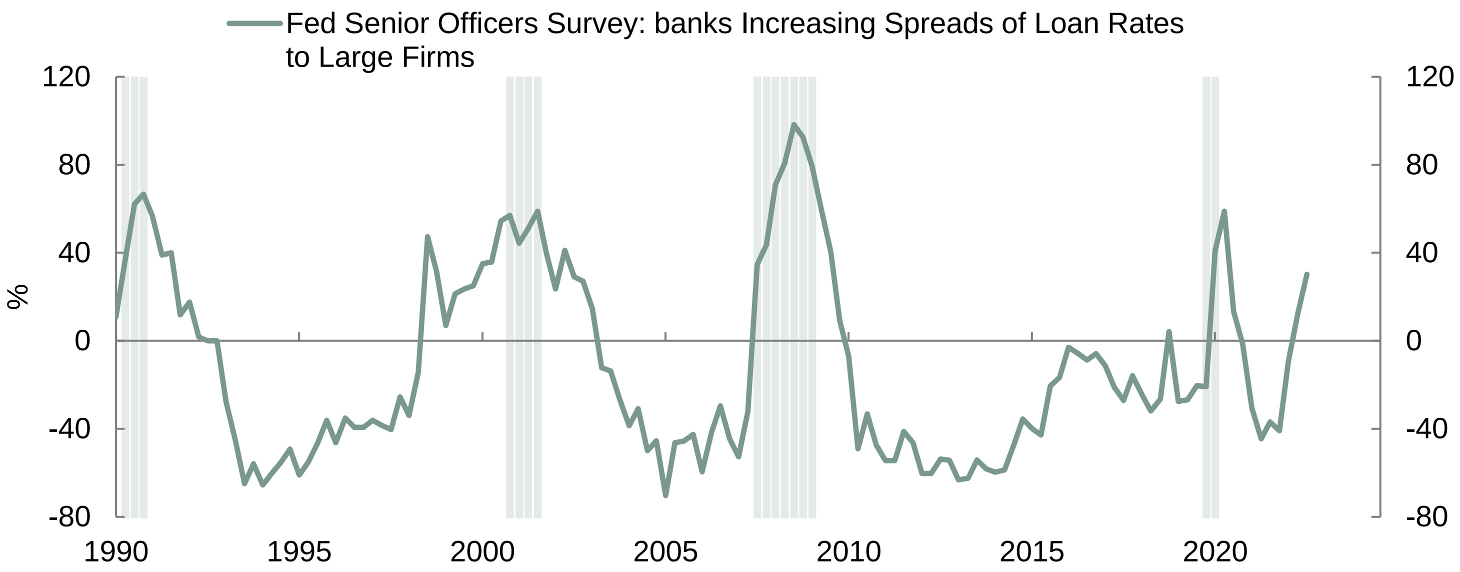
**The tightening in commercial real estate (CRE) standards has been even more dramatic, with the SLOS showing nearly 52 points of tightening in the last two quarters to the highest non-pandemic level since Q1 2008. Trends in the CRE market often lead changes in the broader economy.**




Source: Bloomberg, Federal Reserve, SMBC Nikko

# Charging More Because of Repayment Risk

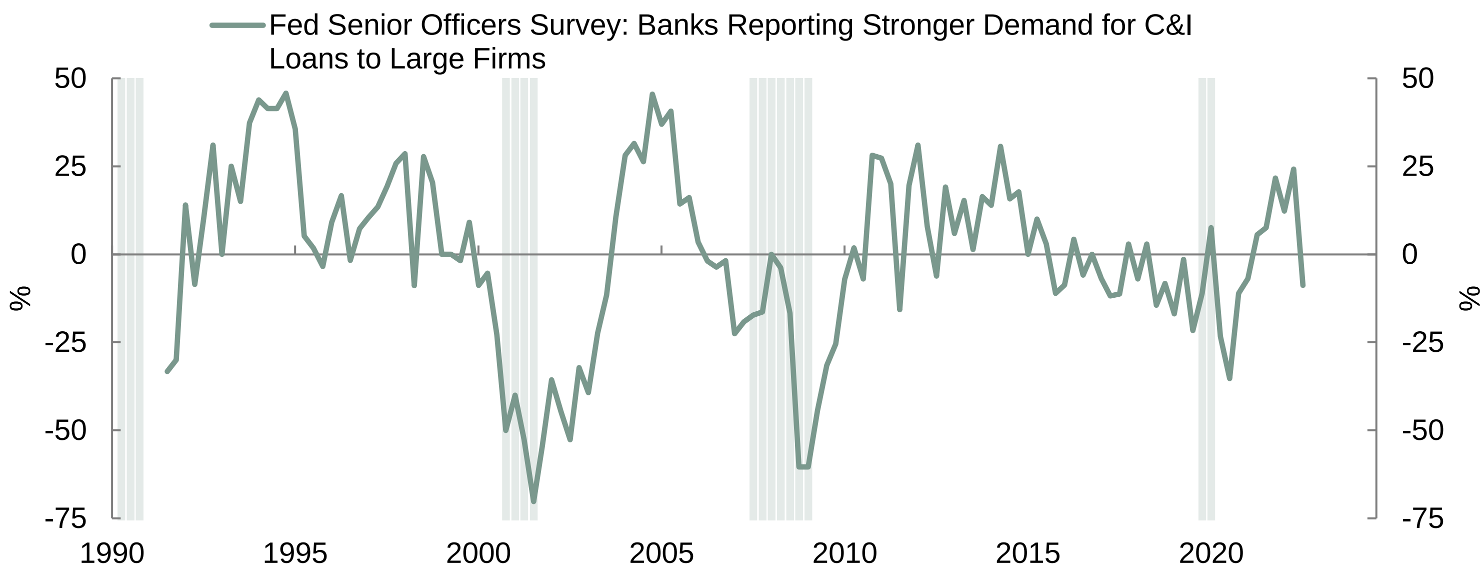
**Why the tightening? The tightening in lending standards partially reflects lending officers' concerns about weakening economic growth prospects. Essentially, bankers are charging higher loan spreads to compensate for the possibility of rising default risk. Unfortunately, caution among bankers can be self-fulfilling, helping to produce a downturn.**




Source: Bloomberg, Federal Reserve, SMBC Nikko

# Higher Costs Leads to Less Demand

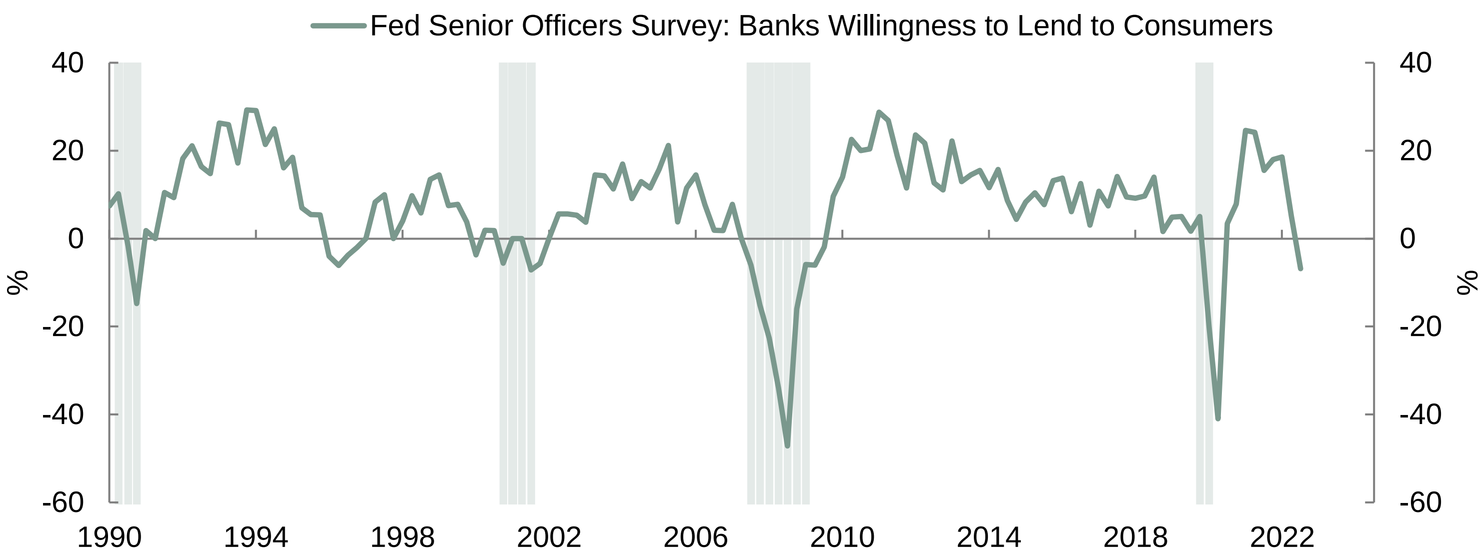
**Not surprisingly, a high cost of funding is leading to less demand. Indeed, the SLOS shows a negative reading for C&I loans. This leaves us wondering if a sharp pullback in manufacturing hiring and production is on the near-term horizon. We think so.**




Source: Bloomberg, Federal Reserve, SMBC Nikko

# Reining in Consumer Credit

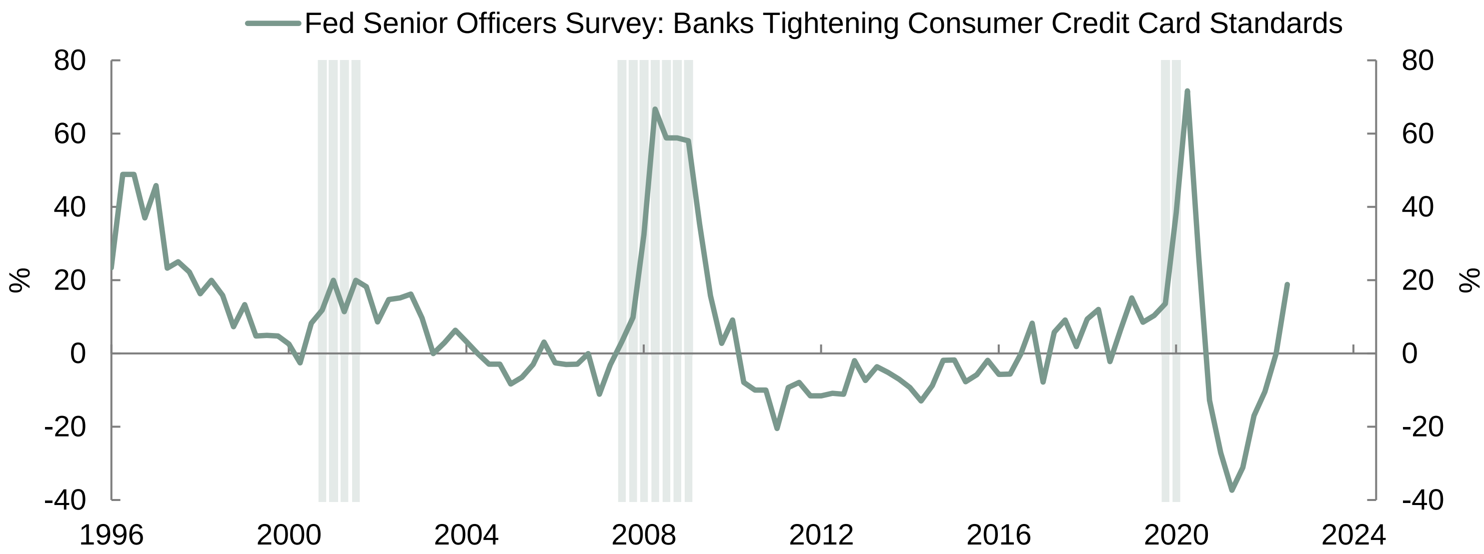
**The tightening in standards has not just been limited to businesses. Banks are also tightening standards on households. Banks' willingness to make consumer loans has declined to its lowest non-pandemic reading since Q1 2009. Since consumption accounts for a near-record high 71% of GDP, less of credit means less spending.**




Source: Bloomberg, Federal Reserve, SMBC Nikko

# Too Much Debt

**One of the areas banks are tightening standards is credit cards which went from -17.0% in Q1 20222 to +18.8% in Q4 2022. Outside of the pandemic, this is the largest three-quarter increase since Q4 2008 immediately following the Lehman Brothers bankruptcy. The bottom line: The Q2 2022 SLOS is showing a sharp tightening in credit provisioning thereby reinforcing tighter monetary policy and headwinds to 2023 GDP growth.**




Source: Bloomberg, Federal Reserve, SMBC Nikko

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