



TD Economics

Observation

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CANADIAN BANK LENDING TO HOUSEHOLDS AND FIRMS IN MAY

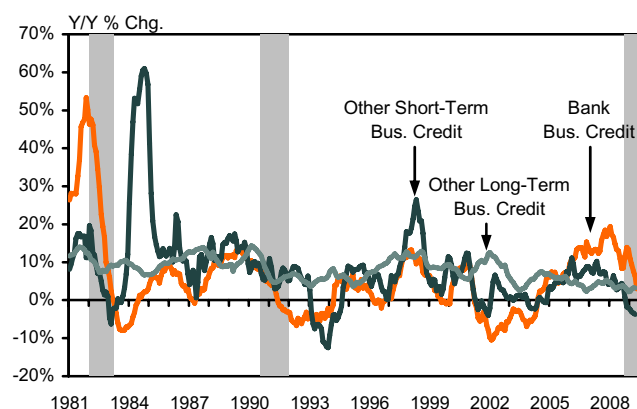
In May 2009, Canadian bank credit to households and non-financial firms expanded at 9.9% Y/Y and 3.0% Y/Y, respectively. Household credit rose relatively robustly on a monthly basis; however, a strong advance in household borrowing is usually witnessed in May – a consequence of pre-summer purchases and high volumes of home sales. Nonetheless, with house prices nation-wide showing surprising resilience in the midst of the recession and house re-sales on par with those in May 2008, borrowing through mortgages and lines of credit remained robust. However, with homebuilding down over 40% Y/Y, mortgage growth should continue to moderate in the coming months.

Year-over-year growth in bank-provided business credit has slowed – from a 13.9% pace in November 2008 to its 3.0% gain in May – and this is consistent with decreased demand for short-term business credit as firms seek to

HIGHLIGHTS

- **Bank credit to households and firms grew by 9.9% Y/Y and 3.0% Y/Y in May, respectively.**
- **Household credit growth was particularly supported by borrowing through mortgages and lines of credit. Slower homebuilding and reduced retail spending will certainly continue to moderate household credit growth in the months ahead.**
- **Bank business credit growth is slowing, but this reflects deteriorating business conditions – and especially the draw-down of inventories – as well as an easing of earlier re-intermediation pressures: many firms have now returned to financial markets for long-term debt, shown by the exceptional corporate bond issuance in May.**

BUSINESS CREDIT GROWTH BY TYPE



Source: Bank of Canada

draw-down inventories. Historically low levels of capacity utilization and heightened inventory-to-sales ratios imply diminished production and demand for operating funds. As well, the appreciation of the Loonie has shrunk the Canadian-denominated value of foreign-denominated loans. Improved conditions on bond and equity markets have enabled corporations to raise capital in financial markets and shift to longer-term debt, easing the demand for short-term business credit.

Credit to Households

Household credit from banks rose robustly by 0.9% M/M in May. A strong advance of household credit is often

observed in May, owing to pre-summer retail purchases and the prime home-buying season. Mortgage lending grew swiftly, but the data continues to show a greater pace of percentage growth in lines of credit, reflecting the popularity of home equity lines of credit (HELOCs) as substitutes for traditional mortgages. Banks expanded their balance sheet mortgages in May, and securitization of bank mortgages under the NHA MBS program was relatively flat on the month.

Credit card lending and personal loans also saw solid monthly gains, reflecting typical seasonally elevation in retail sales during the month of May. The percentage advance in credit card balances was ahead of that in May 2008 but slower than in Mays of previous years. Retail sales during May were likely tepid (data has not been published), consistent with Canadians' "shift to thrift". A continuing contraction in "other loans" reflects the wallop to auto sales and lessened demand for auto-finance. Lending by auto finance companies has been impaired by much diminished market appetite for their securitized loans, and banks have gained market share in vehicle financing. However, overall auto sales (-17% Y/Y in April) are still in sharp decline, reducing demand for bank-provided auto-related credit.

Credit to Businesses

The pace of bank business credit has moderated to 3.0% Y/Y. Particularly during the autumn, bank-provided business credit filled the financing gap. This reflected a rush to re-intermediated credit, as securitized lending froze and corporate bond spreads widened, making market debt cost prohibitive. The result was an expansion of bank business credit at a faster pace relative to other forms of business credit. Moreover, short-term business credit demand tends to rise sharply early in a recession as firms, hit by falling sales, accumulate undesired inventories. Now, as corpo-

rate spreads subside and firms return to bond markets, the monthly decline in bank-provided business credit is unsurprising. The value of corporate bonds outstanding increased by a net \$7.5 billion in May – a record monthly advance. The fall in bank-provided loans to businesses partially reflects the Loonie's appreciation, which reduced the Canadian-denominated value of loans issued in foreign currencies.

Nonetheless, the year-over-year pace of business loans has subsided with the reduced demand for short-term business credit. This is consistent with the inventory pressures faced by manufacturers and wholesalers, and the ongoing rapid reductions in inventories. We forecast a roughly \$20 billion reduction in nominal non-farm inventories during 2009 (effectively, a return to the nominal inventory levels of 2006). This anticipates a steeply decline in demand for short-term business credit during this year, and only tepid recovery during 2010. During May, the outstanding value of bank-provided business loans declined and outstanding Bankers' Acceptances (BAs) fell, but the value of Commercial Paper (CP) shrank on the month as well. In the context of deteriorating economic conditions, these trends are consistent with overall diminished demand for short-term business borrowing – even with attractive short-term interest rates. Even as financial conditions normalize, economic conditions – especially inventory draw-down and rising spare capacity – will continue to drag down demand for business credit.

Looking ahead, bank credit growth will moderate further, with the dominant theme being a reduction in demand for financing. Household credit will slow in a lagged response to soft consumer spending and the past decline in real estate. Business borrowing looks likely to contract as businesses draw down inventories, and more capacity is idled.

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FINANCING BY BANKS TO CANADIAN HOUSEHOLDS							
	Personal Loans	Credit Cards	Lines of Credit	Other	Consumer Credit	Total Mortgages*	Household Credit
Outstanding Amount (CDN millions)							
Feb/2009	48154	51643	175336	20493	295,626	669,164	964,790
Mar/2009	48190	51278	178777	20895	299,140	666,013	965,153
Apr/2009	48500	51685	181015	20773	301,973	673,324	975,297
May/2009	49201	52423	184624	20601	306,849	677,241	984,090
Month-over-Month Percentage Change							
Feb/2009	1.0%	-1.6%	1.4%	-1.1%	0.7%	0.2%	0.3%
Mar/2009	0.1%	-0.7%	2.0%	2.0%	1.2%	-0.5%	0.0%
Apr/2009	0.6%	0.8%	1.3%	-0.6%	0.9%	1.1%	1.1%
May/2009	1.4%	1.4%	2.0%	-0.8%	1.6%	0.6%	0.9%
Year-over-Year Percentage Change							
Feb/2009	9.9%	8.6%	20.9%	-6.6%	14.4%	10.0%	11.3%
Mar/2009	9.1%	8.3%	20.6%	-8.3%	13.9%	8.6%	10.2%
Apr/2009	8.1%	8.9%	20.4%	-6.6%	14.0%	8.8%	10.3%
May/2009	9.4%	9.3%	20.4%	-11.1%	13.9%	8.1%	9.9%
* Mortgages include both those on banks' balance sheets and estimated securitization by banks							
Source: Bank of Canada, Canadian Mortgage and Housing Corporation							

FINANCING BY BANKS FOR BUSINESSES RESIDENT IN CANADA					
	Bus Loans* (ex. Interbank)	Non-Res. Mortgages	Leasing Receivables	Bankers' Acceptances	Total
Outstanding Amount (CDN millions)					
Feb/2009	230,488	24,985	8,228	68,423	332,124
Mar/2009	230,921	25,042	8,110	67,007	331,080
Apr/2009	224,175	25,212	8,146	68,929	326,462
May/2009	215,303	25,284	8,142	66,392	315,121
Month-over-Month Percentage Change					
Feb/2009	-0.2%	0.5%	-0.4%	-2.6%	-0.6%
Mar/2009	0.2%	0.2%	-1.4%	-2.1%	-0.3%
Apr/2009	-2.9%	0.7%	0.4%	2.9%	-1.4%
May/2009	-4.0%	0.3%	0.0%	-3.7%	-3.5%
Year-over-Year Percentage Change					
Feb/2009	12.5%	12.7%	3.0%	-0.3%	9.4%
Mar/2009	10.2%	12.1%	4.2%	-1.9%	7.5%
Apr/2009	7.0%	12.1%	4.5%	2.8%	6.4%
May/2009	3.3%	11.3%	4.5%	-1.0%	3.0%
* Includes loans to Canadian businesses in Canadian dollars and in foreign currencies					
Source: Bank of Canada					

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