Senior loan officer opinion survey

on bank lending practices and credit conditions

3rd quarter 2008

Warsaw, July 2008

Summary of the survey results

Corporate loans

- Lending policy: the banks did not change the standards of granting loans for enterprises. The year-long upward trend of loan spreads was still present, which was related to the worsening of the banks' capital position. In the case of a few small banks, the increase in spreads was related to the situation of the capital group.
- Demand for loans: an increase in demand was recorded, which was stronger in the segment of long-term loans than in the segment of short-term loans. Demand for short-term loans was revived. The growing financing needs for fixed investment and for working capital and inventories were the main reasons for the growth in demand.
- Expectations for the third quarter of 2008: the banks expect a slight tightening of lending policy towards large enterprises and an easing of the policy towards small and medium-sized enterprises. According to the banks, the demand for corporate loans will continue to grow.

Housing loans

- Lending policy: changes in the standards of granting housing loans were insignificant. The banks increased their loan spreads again, mainly due to capital constraints and high costs of raising capital.
- Demand for loans: the demand for housing loans grew strongly, which the banks attributed to the situation on the housing market, rising household income and changes in consumer spending.
- Expectations for the third quarter of 2008: around half of the banks forecast a tightening of lending policy in this segment. A further slight increase in the demand for housing loans is expected.

Consumer loans

- Lending policy: the standards of granting consumer loans were tightened. The banks raised their loan spreads in connection with the worsening of the economic outlook and NBP interest rates' increases.
- Demand for loans: the second quarter of 2008 saw a marked increase in demand for consumer loans, which – as the banks assessed – had resulted from the on-going improvement in the financial standing of households, the growing demand for financing durable goods and promotional campaigns.
- Expectations for the third quarter of 2008: the banks expect a slight tightening of lending policy. At the same time, they expect a slight increase in demand for consumer loans.

Results of the survey – overview

The objective of the survey is to define the direction of changes in the lending policy, i.e. the standards and terms of granting loans, as well as changes in the demand for loans in the Polish banking system. The standards of granting loans are understood as the minimum standards of creditworthiness that the borrower is required to meet in order to obtain a loan, which are set by the bank. The terms of granting loans are the features of the loan agreement agreed by the bank and the borrower, including spread, non-interest loan costs, maximum loan size, collateral requirements and maximum loan maturity.

The survey is addressed to the chairpersons of banks' credit committees. Banks' responses may not take account of the opinions of the banks' divisions other than the credit division. This survey was conducted at the turn of June and July 2008 among 24 banks whose total share of claims on enterprises and households in the banking sector portfolio amounts to 75.9%.

The aggregation of the data behind the results consisted in the calculation of weighted percentages of responses and the net percentage, i.e. the difference between the structures presenting opposite trends. In line with the adopted methodology, words describing quantities (majority, half, considerable, significant, percentage of the banks, etc.) refer to the weighted percentages and not to the number of banks. Thus, the phrase "the majority of the banks" should be understood as "the asset-weighted majority of the banks". Details concerning the calculation methodology are presented in Appendix 1.

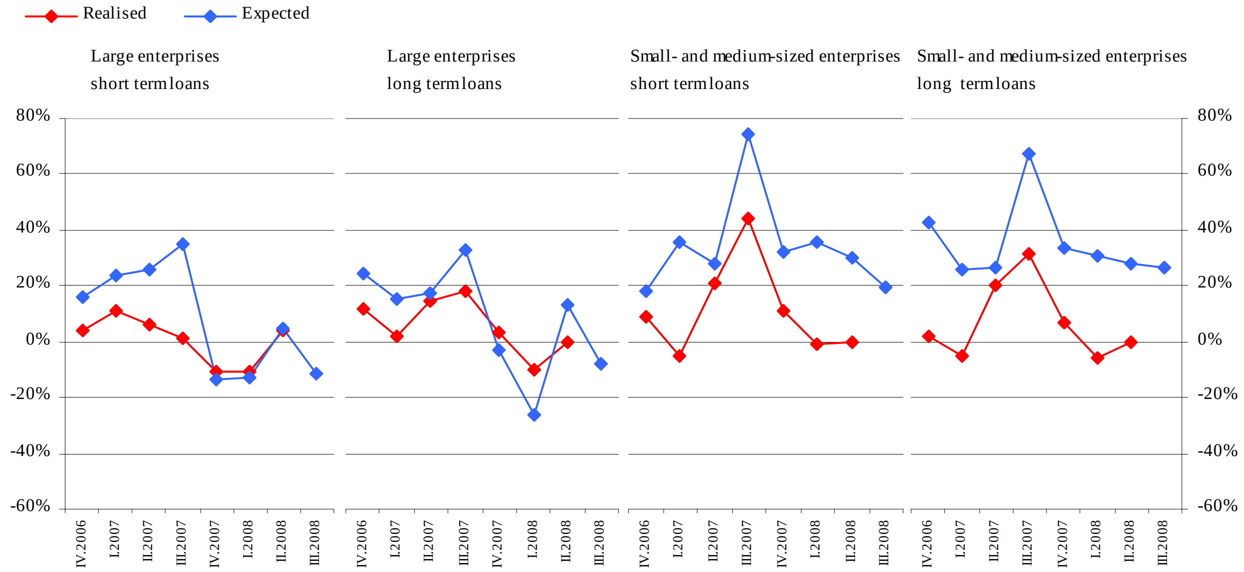
The following section presents tendencies regarding the bank's lending policy and changes in demand in the second quarter of 2008, as well as the banks' expectations for the third quarter of 2008.

Corporate loans

The standards of granting corporate loans did not change in the second quarter of 2008. In the case of large enterprises, this was in line with expectations expressed in the first quarter of 2008. Expectations concerning the easing of standards of granting loans to small and medium-sized enterprises were not met (see Figure 1).

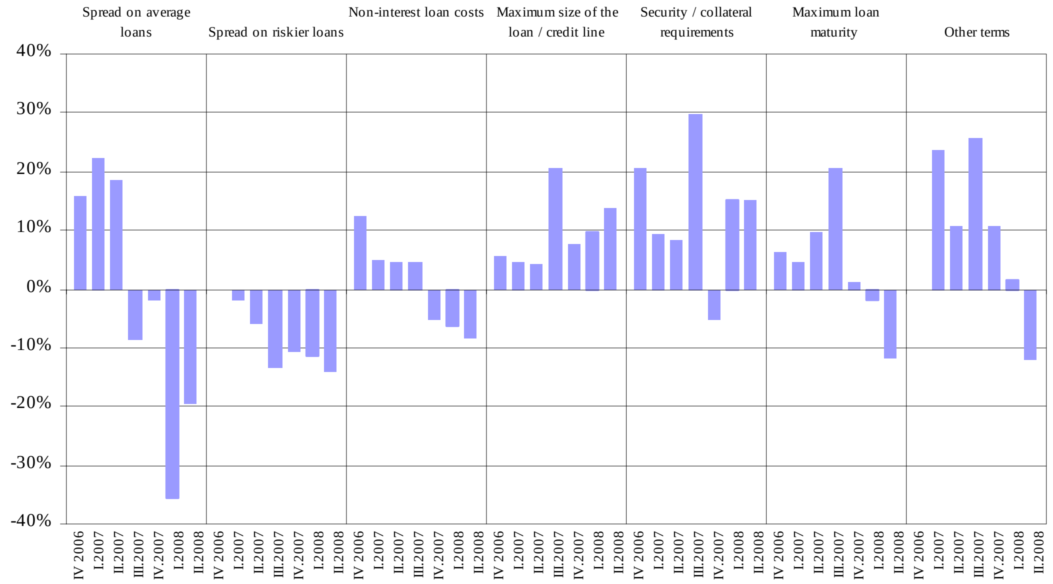
The terms of granting loans to enterprises were tightened. Approximately 20% of the banks raised their loan spreads (see Figure Figure 2). These were mostly the banks that in the first quarter of 2008 had expected a tightened lending policy towards large enterprises. The tendency to raise loan spreads dates back to the third quarter of 2007. A small group of banks increased non-interest loan costs. Around 14% of the banks increased spreads on higher risk loans. The changes related primarily to loans to small and medium-sized enterprises, with one bank considering it as representing a strong tightening of lending policy. The banks continued to ease the collateral requirements for corporate loans and to increase available loan sizes. Over 10% of the banks cut short the maximum corporate loan maturity.

Figure 1
Corporate credit standards



Note: the Figures included in this study present the net percentage. A positive value of net percentage should be interpreted as the easing of lending policy or the growth in demand for loans, and a negative value of net percentage – as the tightening of lending policy or a fall in demand for loans. Details concerning the calculation methodology are presented in Appendix 1.

Figure 2
Terms on corporate loans

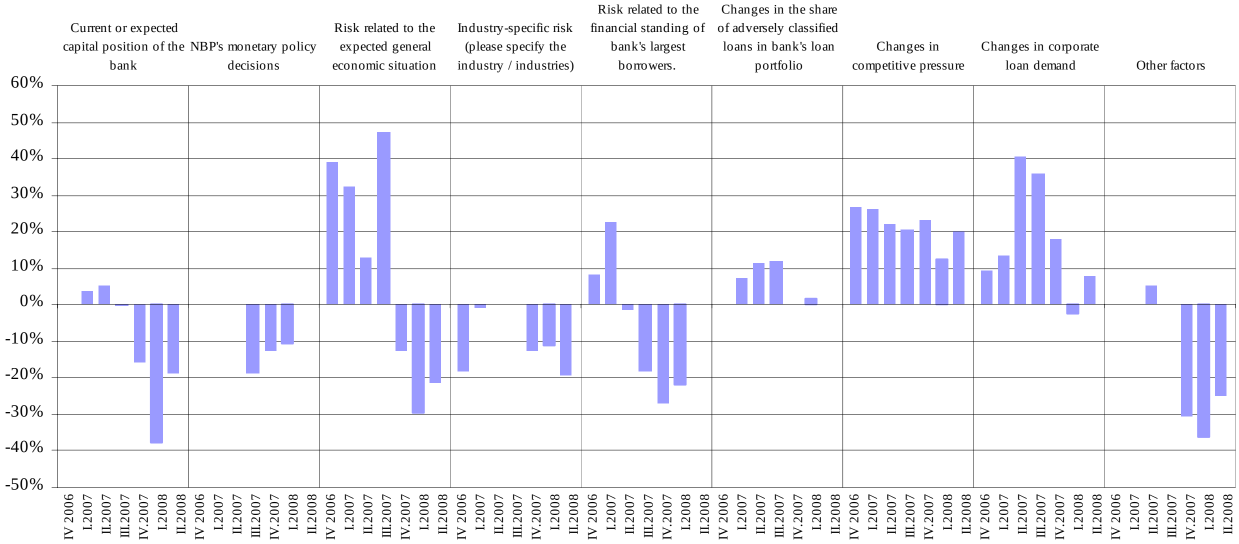


The banks' deteriorating capital position was the primary reason for the tightening of lending policy towards enterprises (see Figure 3). Two of the banks that cited the cause said it had considerably influenced the tightening of their lending policies.[1] This may reflect the deteriorating capital position of some parent entities of Polish banks, which curbs lending not only in the home markets of the parent entities but also in the Polish market. **Nearly one fourth of the banks assessed that the economic prospects had justified the introduction of more**

[1] The banks have a possibility of grading the influence of factors on lending policy. In the survey, the banks choose among the following options: considerably influencing the tightening of lending policy, somewhat influencing the tightening of lending policy, not influencing lending policy, somewhat influencing the easing of lending policy, considerably influencing the easing of lending policy.

rigorous terms of granting loans to enterprises. These banks assessed the risk of economic slowdown to be the most pronounced in the segment of small and medium-sized enterprises. A similar number of banks decided to tighten their lending policies in response to the growing risk of the specific industries, and these banks indicated the property sector as particularly risky. Among other factors impacting the tightening of lending policy, the banks cited the drive to improve their profitability, the policy of the capital group and the rising cost of capital. **The influence of the situation of the parent entities of the surveyed banks on the tightening of lending policy was visible only in small banks.**

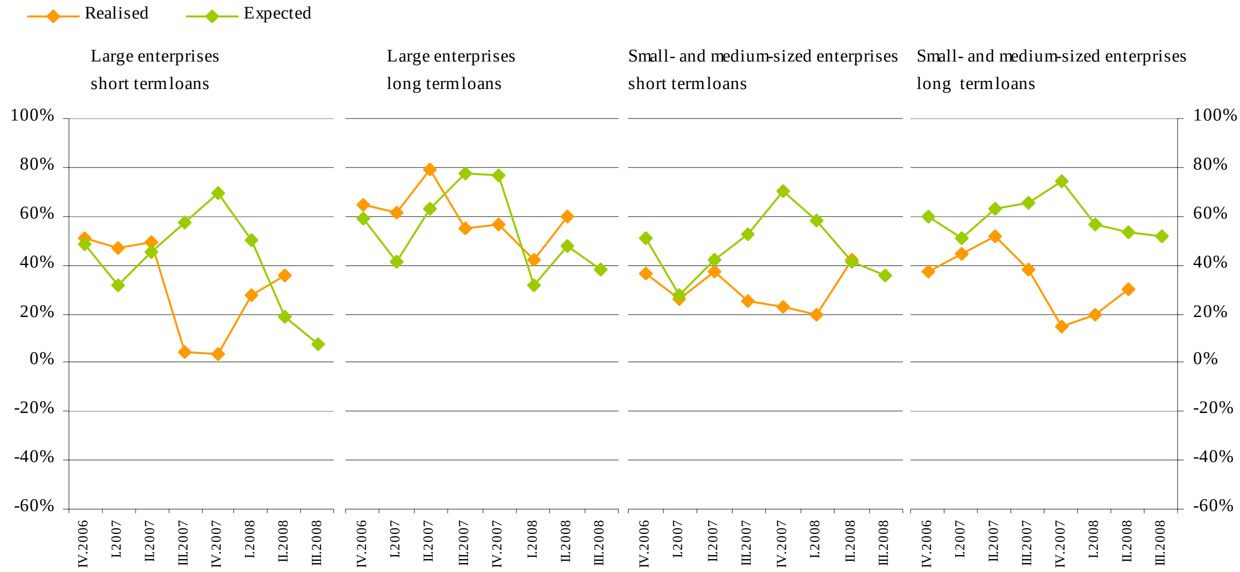
Figure 3
Factors influencing changes in lending policies



The banks recorded the growth in demand for loans to enterprises in the second quarter of 2008. It was strongest in the segment of long-term loans to large enterprises. However, the banks' opinions were discrepant: 68% of the banks reported an increase in demand for lending, while a decrease in demand was noted by 8% of the banks. The demand for short-term loans will continue to grow, although approximately 15% of the banks reported a falling demand in this market segment. The segment of long-term loans to small and medium-sized enterprises exhibited a relatively smallest growth in demand (see Figure 4).

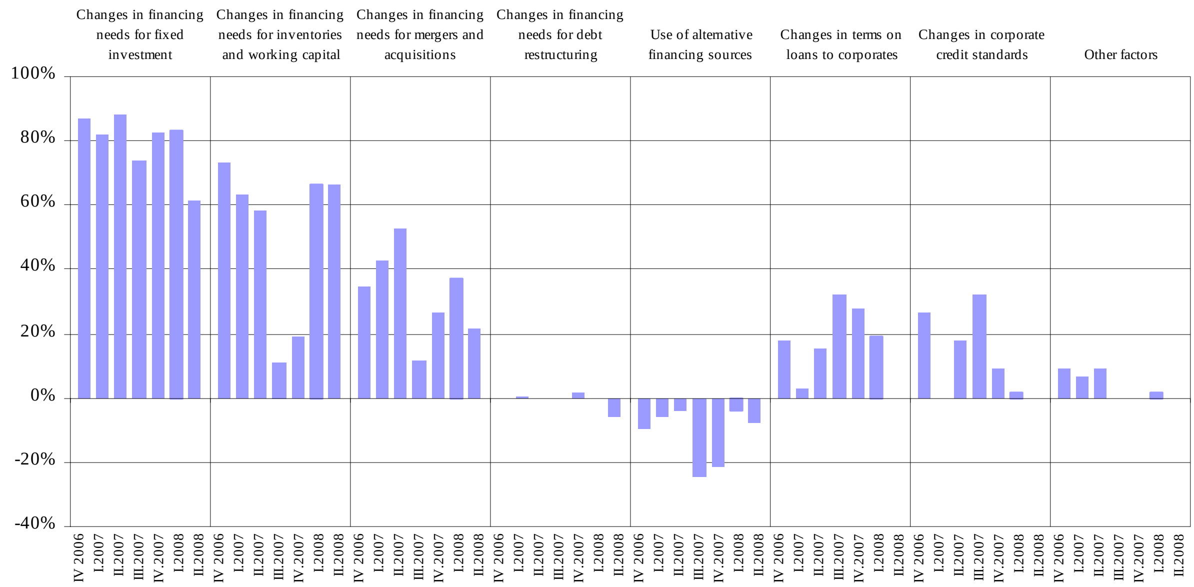
According to two thirds of the banks, growing financing needs for enterprises' fixed investment, inventories and working capital were the major factors stimulating the growth in demand for corporate loans (see Figure 5). Presumably, the first of the categories also covers the financing of purchases of real estate by enterprises. The importance of this factor considerably diminished, reaching its lowest level since the end of 2005. Around 13% of the banks regarded the impact of financing of enterprises' fixed investment on the demand for loans as negative. The upturn in the market of short-term loans was linked to the strongly growing financing needs for enterprises' inventories and working capital. The role of mergers and acquisitions as a factor influencing the demand for loans was insignificant.

Figure 4
Corporate loan demand



The impact of competition from the alternative sources of finance for enterprises on the demand for loans was low (see Figure 5). The opinion that the demand for loans offered by a given bank is curbed by the competition was shared by fewer than 20% of the banks. It may imply that given a high demand for loans and the emergence of supply constraints in some of the banks, competitive pressure on the market is being eased. Despite the fall in the number of IPOs and the relative stock price of the newly-listed firms on the Warsaw Stock Exchange in comparison with the previous year, 25% of the banks regarded the availability of capital on the share market as contributing to a fall in demand for corporate loans.

Figure 5
Factors influencing changes in corporate loan demand



The banks expect lending policy towards large enterprises to be somewhat tightened in the third quarter of 2008. They are mainly the same banks that had tightened their lending policies in the second quarter. Merely one bank intends to ease lending policy towards large enterprises. One third of the banks expect the lending policy towards the segment of small and medium-sized enterprises to be eased (see Figure 1). A few small banks that tightened their lending policies in the second quarter due to their capital position plan to further tighten their lending policies towards these enterprises.

In the third quarter of 2008, the banks expect a further increase in demand for corporate loans (see Figure 4). This growth is to be slightly stronger in the segment of loans to small and medium-sized enterprises than in the segment of loans to large enterprises. The banks forecast that the change in demand for short-term loans to large enterprises will be very small.

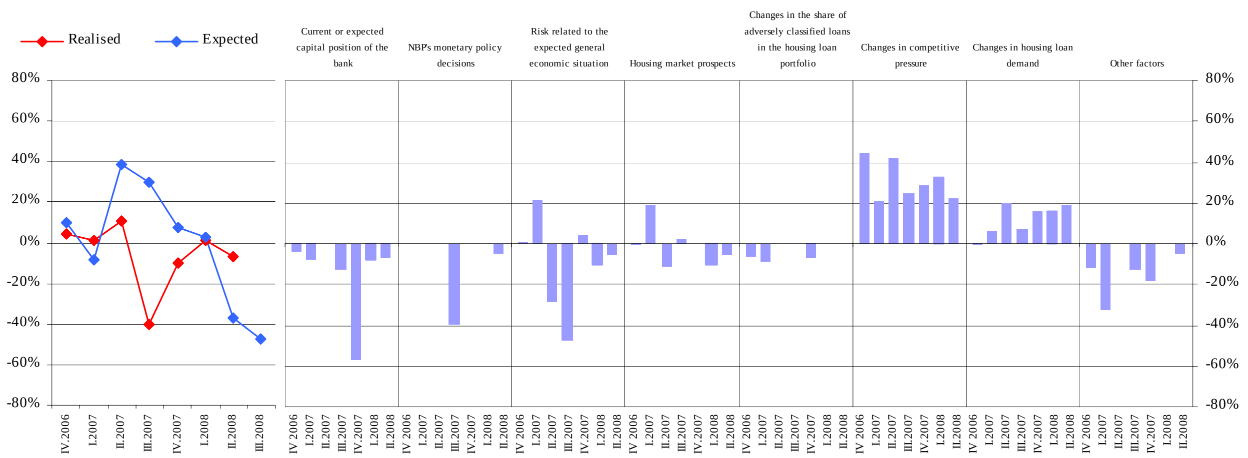
Housing loans

As in the previous two quarters, **in the second quarter of 2008 the banks slightly changed the standards of granting housing loans** (see Figure 6). Two banks tightened the standards, of which one bank regarded the changes as considerably tightening its lending policy. One bank slightly eased its standards of granting housing loans.

The tendency to raise loan spreads on housing loans, observed since mid-2007, **was still present** (see Figure 7). The banks that tightened the standards of granting housing loans were also increasing their loan spreads. Some banks chose to lower their loan spreads, and in one case this reduction was considerable. Around one fifth of the banks resolved to reduce non-interest housing loan costs. Other changes of the terms of granting housing loans were very insignificant.

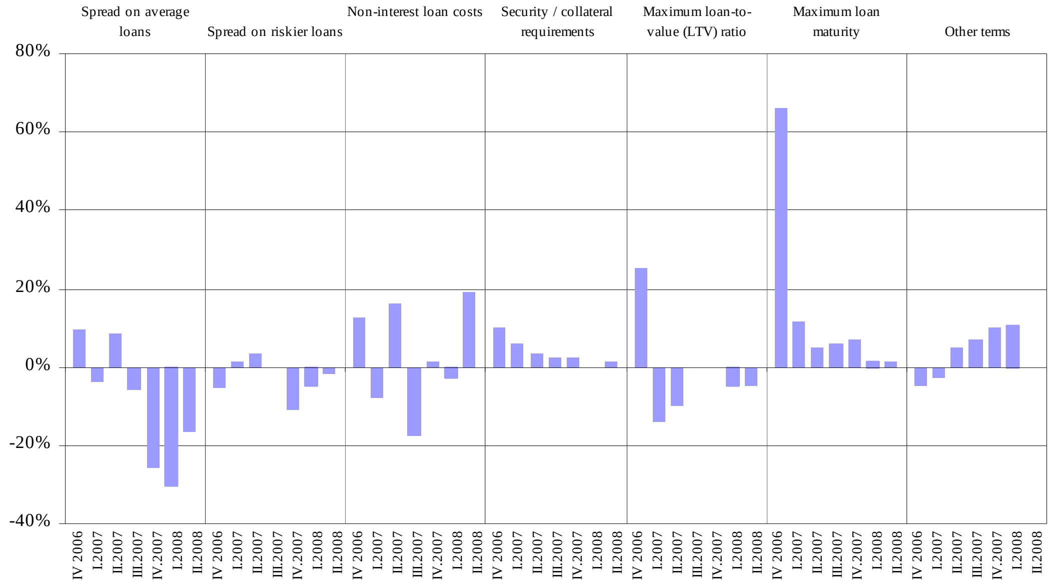
The banks' decisions regarding their lending policies in the segment of housing loans diverged from expectations from the first quarter of 2008 when they expected a strong tightening of lending policy.

Figure 6
Lending policy and factors influencing its changes – housing loans



The banks indicated NBP interest rate increases, deterioration of bank's capital position, risk related to the economic outlook as well as an increase in costs of raising capital as reasons of their decisions to tighten their lending policies (see Figure 6). However, these reasons were cited by individual banks and none of them was a dominant factor. **The banks that were easing the terms and standards of granting housing cited growing competitive pressure as the rationale behind their policy decisions**. One bank justified its decision to ease its lending policy by citing not only strong competition but also favourable economic developments and decisions taken by the Monetary Policy Council.

Figure 7
Terms on housing loans



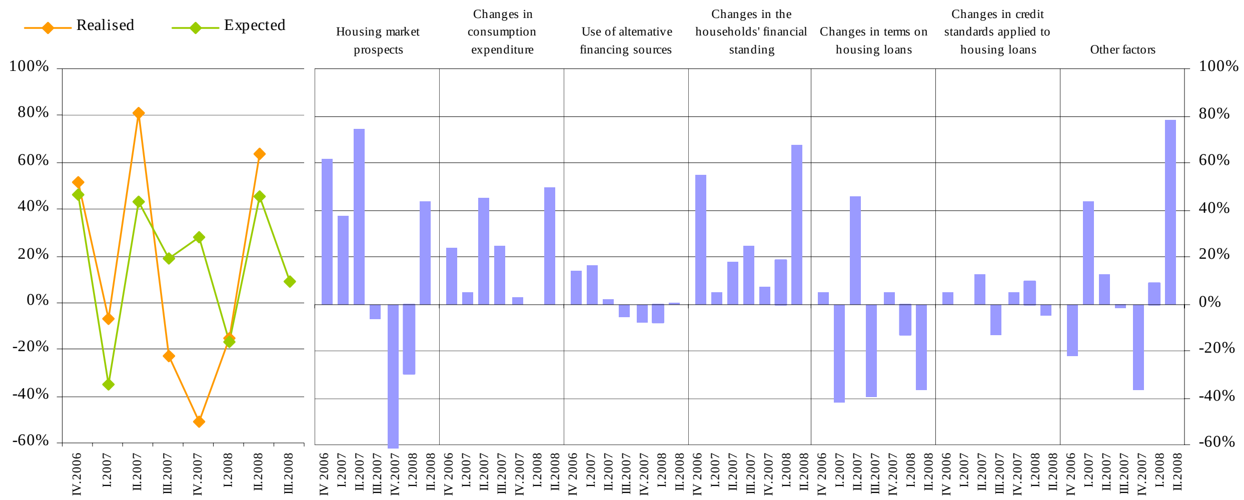
In the second quarter of 2008, over two thirds of surveyed banks reported an increase in demand for housing loans (see Figure 8), including around 15% of the banks in which the increase was regarded as significant.[2] Two small banks reported a decrease in the demand. Increased demand, which was primarily related to Swiss franc-denominated loans, was mostly reported by large universal banks. The increase in demand was stronger than expectations presented in the first quarter of 2008.

Changes in the structure of household expenditure and an increase in households' income were the main reasons of the growing demand for housing loans. According to the majority of the banks that reported increased demand for housing loans, this increase was supported by the projections of developments in the housing market (see Figure 8). Thus, a long period of price stabilisation of dwellings might have forced many prospective borrowers who put off their dwelling purchase decisions to go ahead with the transaction. **The widening disparity between the interest rates in Poland and in Switzerland was another factor influencing the increased demand**. According to the banks, this development supported the growth in demand for foreign currency loans. Some banks also said that the demand in loans had been spurred by intensive advertising campaigns. The banks that noted a decrease in demand for housing loans attributed the fall to tightened loan standards and terms.

Over half of the banks expect a strong tightening of lending policy in the segment of housing loans in the third quarter of 2008. At the same time, approximately 10% of the banks intend to ease the terms or standards of granting the loans. Among the banks planning to tighten their lending policies, the banks that eased their housing loan standards in the second quarter prevail. **A slight increase in demand for housing loans is expected** (see Figure 8) mostly by banks with a small market share. Most of them plan to ease their lending policies in the third quarter of 2008, which may reflect intention to increase their market shares. Large banks expect the demand for loans to remain at the present level.

[2] The banks have a possibility of grading changes in demand. In the survey, the banks choose among the following options: demand increased considerably, demand somewhat increased, demand remained unchanged, demand somewhat decreased and demand decreased considerably.

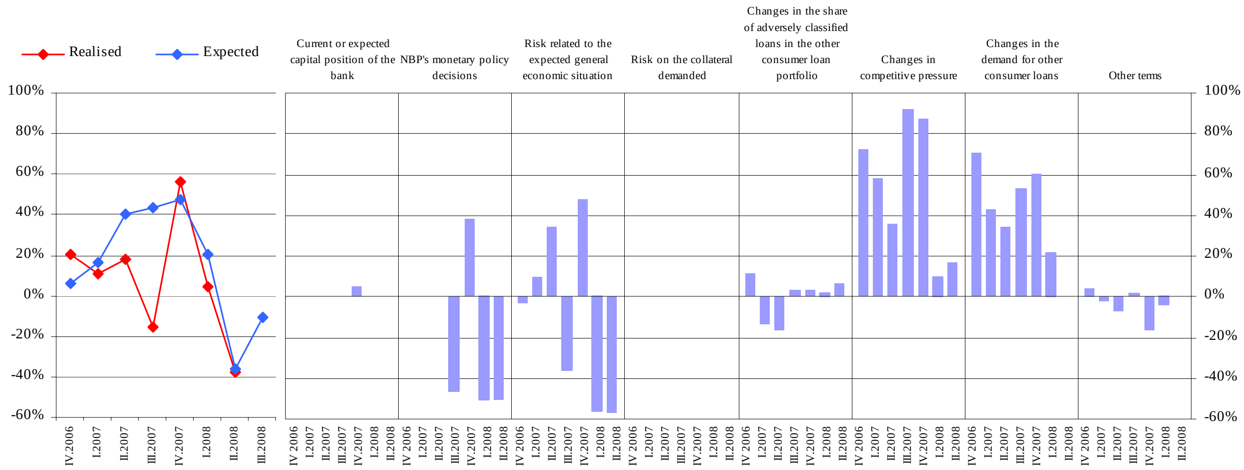
Figure 8
Demand for housing loans and factors influencing its changes



Consumer loans

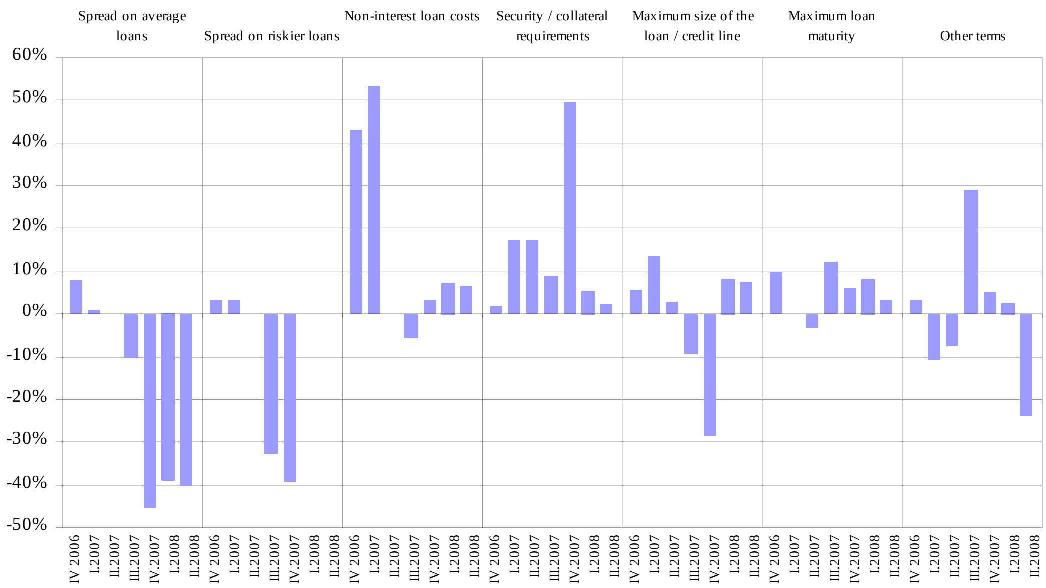
In the second quarter of 2008, the standards of granting consumer loans to households were tightened (see Figure 9). On the one hand, 11% of the banks eased the standards, but nearly half of the banks decided to tighten them. The net tightening of lending policy in the segment of consumer loans was in line with the banks' forecasts from the end of the first quarter of 2008.

Figure 9
Lending policy and factors influencing its changes – consumer loans



Increasing the credit price was the major change of lending policy in the segment of consumer loans in the second quarter of 2008. Similarly as in the first quarter of 2008, around 40% of the banks increased loan spreads on consumer loans (see Figure 10). These were mostly the banks that did not change their consumer loan standards. The spreads' increase did not involve higher risk loans. Just below 25% of the banks introduced higher requirements on the borrower's income statements or increased the minimum disposable income for the borrower to obtain a loan. Other consumer loan terms included in the survey were slightly eased. In particular, over 6% of the banks reduced their non-interest loan costs. A few banks lowered loan collateral requirements, increased maximum loan sizes or extended the maximum loan maturity.

Figure 10
Terms on consumer loans



In the second quarter of 2008, the NBP interest rate increases and the worsening perception of the risk related to the future economic situation were the main factors influencing the tightening of lending policy in the segment of consumer loans (see Figure 9)**.** Thus, these were the same reasons behind the banks' decisions to tighten their lending policies in the previous quarter. Although the abovementioned factors were indicated as contributing to the tightening of lending policy only by two and three banks respectively, then the fact that banks with a high market share were present in the group determined the relatively high importance of these responses. However, it should be noted that unlike in the first quarter of 2008, in the second quarter of the year the banks that indicated the significance of the NBP interest rate increases as contributing to the tightening of lending policy regarded this factor as having little impact on their decisions. However, it is worth noting that this factor is mentioned exclusively within the context of changes in the lending policy with regard to consumer loans.

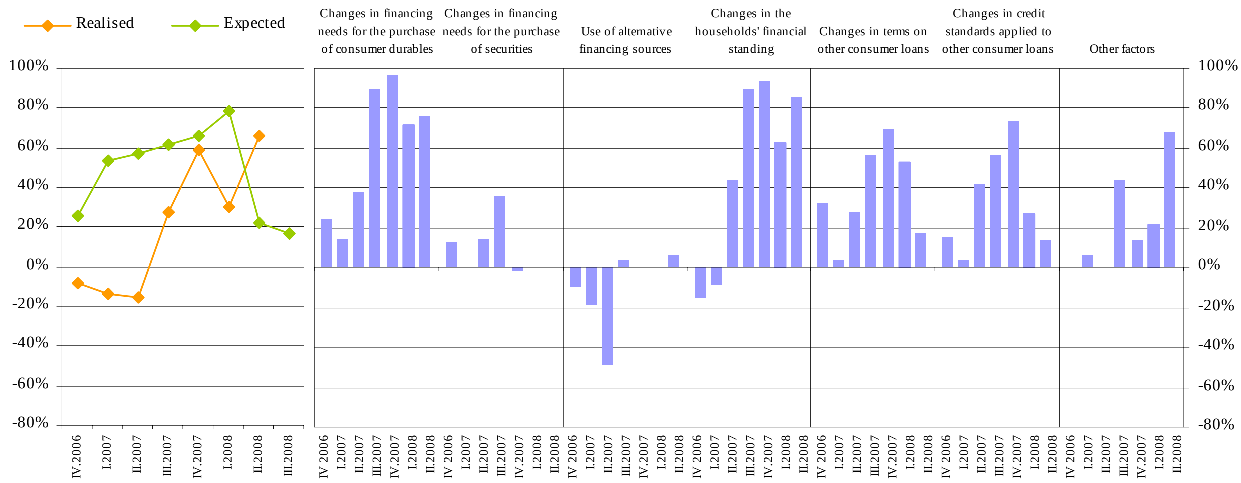
Around 16% of the banks indicated competitive pressure from other financial institutions as the factor influencing their decisions to ease lending policy. These banks adjusted their offers to market requirements mainly with regard to maximum loan maturity, maximum loan size and collateral requirements. Competitive pressure from other peer banks offering consumer loans was primarily significant.

The growth in demand for consumer loans in the second quarter of 2008 was reported by over 65% of the banks being surveyed. Over 10% of the banks noted a significant increase in the demand for consumer loans. At the end of the first quarter of 2008, the banks expected the demand to grow, but on a markedly smaller scale (see Figure 11).

An improvement in the financial standing of households and an increase in financing needs for the purchases of durable goods were the two major causes of the growth in demand for consumer loans. These factors were indicated by the majority of the banks that recorded demand growth (see Figure 11). With the exception of one bank, these were other banks than the ones that justified the tightening of consumer loan standards or terms, citing a worsening economic outlook. Two banks stated that the growth in demand had been supported by their promotional campaigns.

In the third quarter of 2008, the banks expect the lending policy in the segment of consumer loans to be further tightened (see Figure 9). These expectations concern a smaller percentage of banks than in the second quarter of 2008. Over 20% of the banks expect the policy to be slightly tightened while approximately 10% of the banks expect it to be eased. **At the same time, approximately 17% of the banks expect the demand for consumer loans to continue to grow** (see Figure 11).

Figure 11
Demand for consumer loans and factors influencing its changes



Appendix

Methodology

The results of surveys are presented in the form of structures, i.e. the percentages of banks, which chose a given option in response to particular questions. Banks' responses are weighted with the share of the given bank in the market segment to which a given question relates. Weighing of responses is a solution frequently applied in preparation of results of qualitative surveys.[2]

The importance of particular banks in a given market segment is represented by the share of loans outstanding of a given bank in the loan portfolio of all 24 banks responded to the survey, broken down by particular types of loans. The following table presents the market segment to which particular questions refer, and the type of loans outstanding which was used to calculate the shares of particular banks in a given market segment.

Table 1

Market segment and the respective type of loans taken into consideration in calculation of the weights

Questions no.	Market segment	Type of loans
1, 4, 6, 7	Short-term corporate loans	Loans outstanding from state-owned enterprises and companies, private enterprises and companies as well as cooperatives and sole traders with the basic term to maturity of up to one year, together with the outstanding on the current account
	Long-term corporate loans	Loans outstanding from state-owned enterprises and companies, private enterprises and companies as well as cooperatives and sole traders with the basic term to maturity above 1 year
2, 3, 5	Total corporate loans	Total amount of loans outstanding from state-owned enterprises and companies, private enterprises and companies as well as cooperatives and sole traders
8, 9, 10, 13, 14, 16, 17	Housing loans to households	Housing loans to persons
8, 11, 12, 13, 15, 16, 17	Consumer and other loans to households	Total loans outstanding from persons less housing loans to persons

Note: All types of claims relate to residents only. In the case of corporates the distribution between large enterprises and small and medium-sized enterprises was not retained, due to a lack of relevant data in banking statistics.

Source: NBP.

Thus a weight, corresponding to a given bank's share in a given market segment is assigned to particular responses. At the calculations of weights the average amount of claims of a given type in the two first months of the period covered by the survey, was taken into account.[3] Where a bank marked "*Not applicable*" in the response options, a weight of 0 was assigned. Thus while calculating

[2] Cf.: M. Bieć *„Business survey: Methods, techniques, experience"*, Papers and Materials of the Research Institute for Economic Development, No. 48, Warsaw School of Economics, pp. 71-114.

[3] No data on claims loans of particular banks in the third month of the period are available at the time of analysing the results of the survey, due to an about three-week delay in reporting.

the structures for particular questions, only banks being active in a particular market segment were taken into account.

Apart from structures, the so-called net percentage was calculated for each response, that is the difference between the percentages of responses showing opposing directions of changes. This magnitude indicates a general tendency in the specific market segment. The method of calculating the net percentage for particular questions is presented in the following Table 2.

Table 2

Method of calculating the net percentage

Questions no.	Definition of net percentage
1, 2, 8, 9, 11	The difference between the percentage of responses „Eased considerably” and „Eased somewhat” and the percentage of responses “Tightened considerably” and “Tightened somewhat”. A negative index indicates a tendency of tightening the credit standards.
3, 10, 12	The difference between the percentage of responses “Contributed considerably to the easing of lending policies” and “Contributed somewhat to the easing of lending policies” and the percentage of responses “Contributed considerably to the tightening of lending policies” and “Contributed somewhat to the tightening of lending policies”. A negative index indicates a given factor’s greater contribution to the tightening than to the easing of lending policies.
4, 13	The difference between the percentage of responses „Increased considerably” and „ Increased somewhat” and the percentage of responses „Decreased considerably” and „Decreased somewhat”. A positive index indicates an increase in demand.
5, 14, 15	The difference between the percentage of responses „Contributed considerably to higher demand” and „Contributed somewhat to higher demand” and the percentage of responses „Contributed considerably to lower demand” and „Contributed somewhat to lower demand”. A positive index means that a given factor contributed to an increase in demand, and a negative one – to a decrease in demand.
6, 16	The difference between the percentage of responses „Ease considerably” and „Ease somewhat” and the percentage of responses „Tighten considerably” and „Tighten somewhat”. A positive index indicates the expected easing of the lending policies.
7, 17	The difference between the percentage of responses „Increase considerably” and „Increase somewhat” and the percentage of responses „Decrease considerably” and „Decrease somewhat”. A positive index indicates the expected increase in demand.

Source: NBP.