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Box B: QB 3 – July 2021

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Spending, credit, and deposits: An update on Irish household and business activity

By Statistics Division

Nearly a year and a half after the beginning of the Covid-19 pandemic, which has had a profound impact on the global economy and societal norms, the rollout of vaccinations is growing at pace throughout Europe. Domestically, after a prolonged period of stringent public health measures, a phased easing of restrictions has begun. Non-essential retail has reopened, with some hospitality and other services industries also recommencing, providing a boost to employment and reducing reliance on certain government supports. Despite the more positive domestic health environment, a number of uncertainties around spending and the path of reopening, among others, may materially impact the economic outlook. This Box provides an update on the development of Irish households' and firms' spending, savings and borrowing activities at an aggregate level.

Household Spending

As Daily Credit & Debit Card Statistics[1] demonstrate, the Covid-19 pandemic has had a significant impact on Irish household aggregate spending, the reallocation of spending between sectors and the method by which spending occurs. Following the contraction in spending after the Christmas period, when card spending declined by 10 per cent in January in year-on-year terms, spending quickly rebounded and by late-February activity had recovered to 2020 levels and remained relatively stable throughout the opening months of 2021. From mid-April, spending began to increase again, reflecting both the improvement in consumer sentiment[2] that has accompanied the acceleration of the national vaccination programme and the announced phased easing of public health restrictions.

[1] Further information on the Daily and Monthly Credit & Debit Card Statistics is available here and here.
[2] See the latest KBC Consumer Sentiment Index available here.

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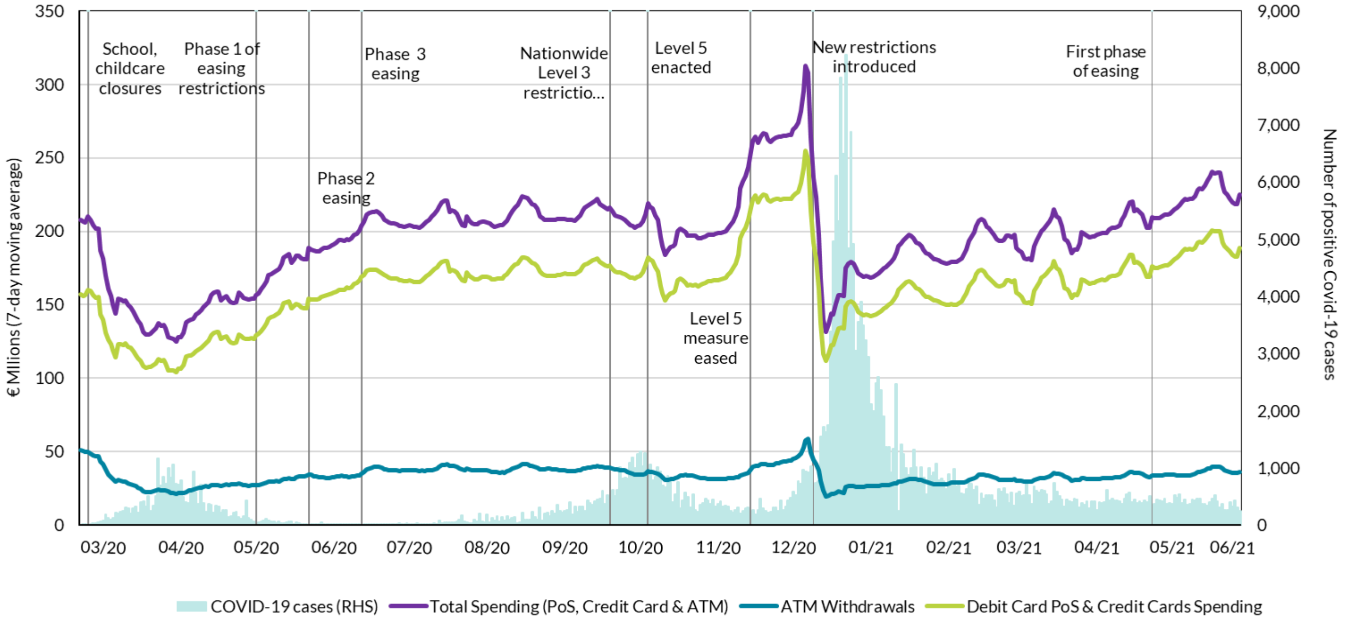
Figure 1: Changes in daily card spending and cash withdrawals[3]

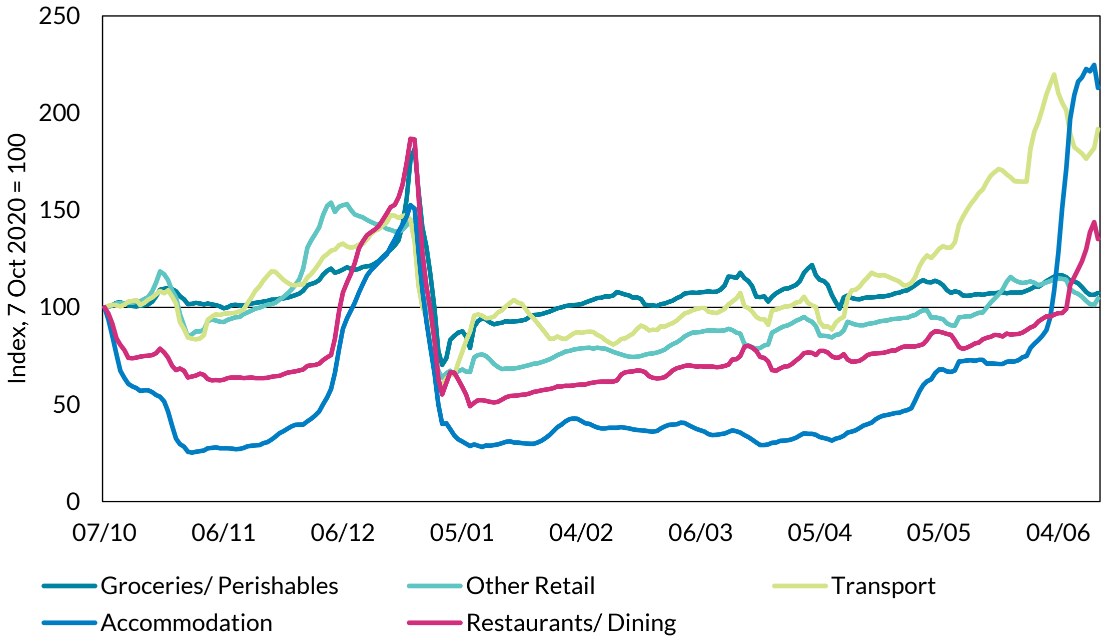


Source: Central Bank of Ireland

Analysis of the monthly Credit and Debit Card Statistics[1], which provides a less timely but more granular breakdown of the daily data, indicates that while aggregate card spending for February 2021 (the last month for a pre vs post pandemic comparison) was largely unchanged in year-on-year terms, however there was a substantial reallocation of spending since the beginning of the pandemic compared with previous long-established spending patterns. For example, the significant decline in spending in sectors such as restaurants, accommodation and transport was in part offset by increases in the retail sectors of groceries, electrical goods and hardware.

[3] The sharp contraction in spending immediately after Christmas was driven by a number of factors in addition to the introduction of public health measures. These included seasonal factors, the impact of weekends and public holidays; all of which contribute to the significantly lower spending. Chart uses daily data from 7 March 2020 to 7 June 2021.

Figure 2 – Changes in Daily Sectoral Card Spending



Source: Central Bank of Ireland

On a sectoral level, daily data indicates that spending remained relatively stable during the first few months of 2021, with the restaurant and accommodation sectors reverting to levels observed in late-October and November last year, when similar Level 5 public health restrictions were in place (Figure 2). Since late-April, spending in the two sectors most impacted by the public health restrictions, the accommodation and transport sectors, has increased markedly, coinciding with increased optimism due to the accelerating vaccine rollout and the government announcement outlining the proposed path for easing restrictions. While more recently, as restrictions in the hospitality sectors were eased in early-June, accommodation and restaurants spending rose sharply. Meanwhile, spending on groceries has proven largely resilient to the changes regarding public health measures as spending relocated from outside to inside the home, and remains significantly higher than pre-pandemic levels.

The proportion of card spending conducted online rose to 57 per cent in January, up from a monthly average of 39 per cent in 2019, as the public health restrictions limited opportunities for in-person spending. Despite restrictions remaining unchanged until early-May, the proportion of in-store spending rose steadily to nearly 49 per cent over the intervening period. A number of factors likely contributed to this increase; including seasonality, greater public mobility[4] as the health environment improved, and the increasing adaptability of businesses. Once non-essential retail reopened in early-May, in-store spending rose sharply and once again became the primary venue for card spending.

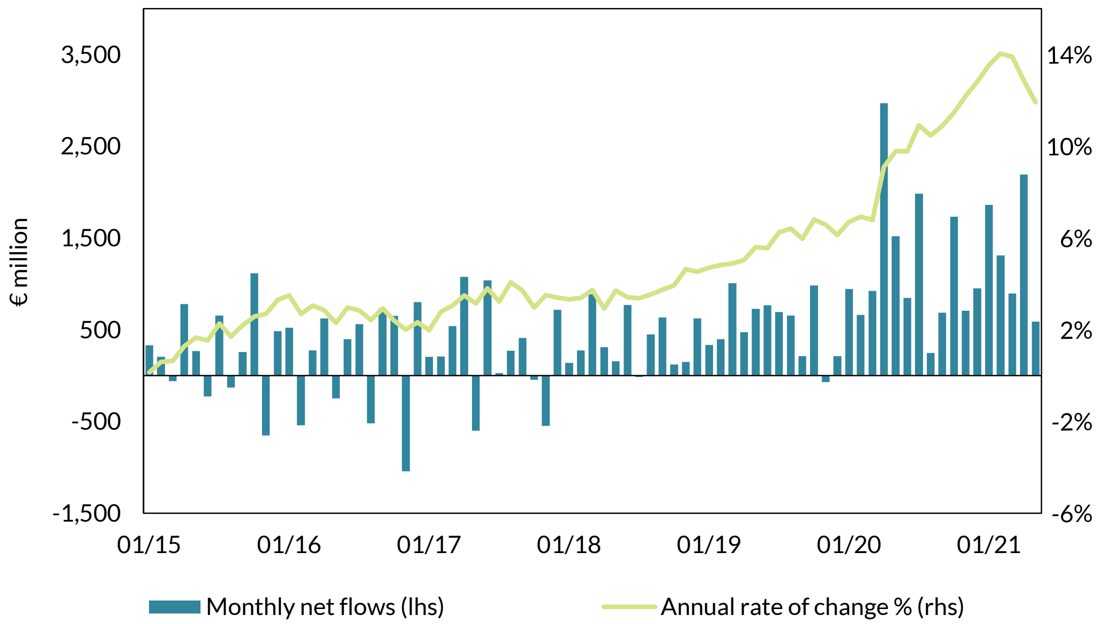
[4] See latest google mobility report here.

Household Credit & Deposits

Household savings have continued to rise at pace since the beginning of the Covid-19 pandemic and the introduction of the associated public health measures. This continued growth likely reflects an increase in precautionary and forced savings due to the curtailed consumption opportunities[5], while government income supports and other intervention measures have helped, to a certain extent, to mitigate household income shocks.

The latest Credit and Banking Statistics[6], shows that household deposits continue to post new record highs and stood at €131.5 billion at end-May. Lodgements exceeded withdrawals by €14 billion in the twelve months to end-May, a growth rate of 11.9 per cent (Figure 3). However, comparing March, April and May 2020 at the beginning of the pandemic with the same months this year, lodgements exceeded withdrawals by a lesser extent than in 2020 indicating that while there was a forced element to savings due to curtailed consumption opportunities, a certain proportion of savings may also be described as precautionary[7]. What happens with these accumulated savings will be an important factor in determining the path for the economy in the coming years, and this issue is discussed further in Box D.

Figure 3 – Deposits from Households; developments in net flows, and annual rate of change



Source: Central Bank of Ireland

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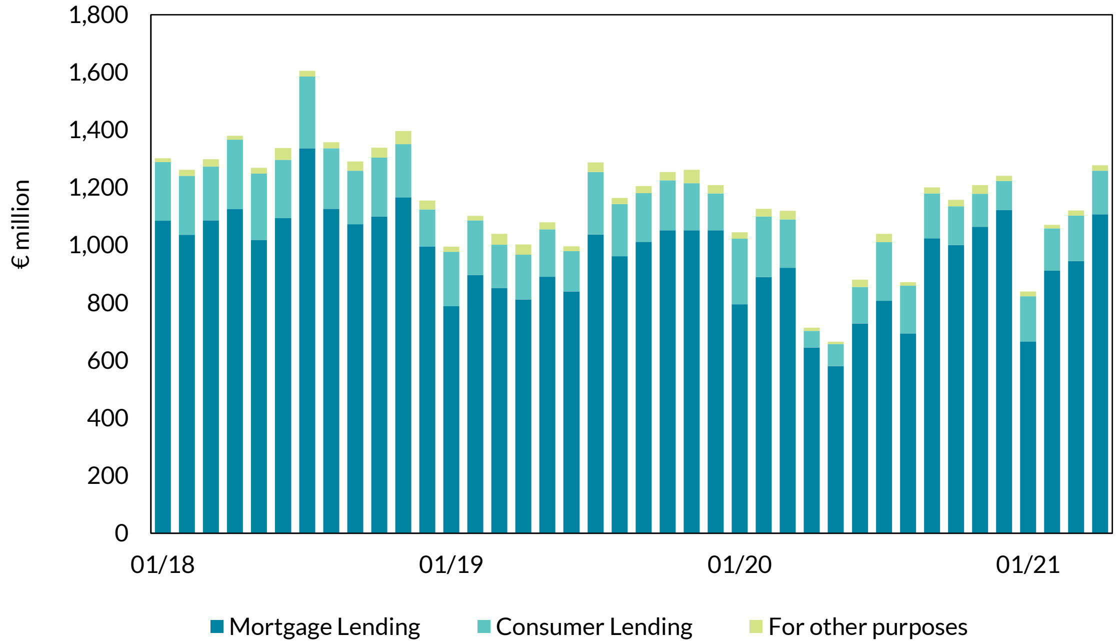
[5] For a detailed discussion of the impact of the pandemic on consumption and savings, see Byrne, S., Hopkins, A., McIndoe-Calder, T., and Sherman, M. The Impact of COVID-19 on Consumer Spending. Central Bank of Ireland Economic Letters. Vol 2020. No 15.

[6] The latest Credit and Bank Statistics are available here.

[7] For a more detailed discussion on savings and the potential effect on future spending, see Reamonn Lydon & Tara McIndoe-Calder. Saving during the pandemic: Waiting out the storm? Central Bank of Ireland Economic Letters. Vol 2021. No 4.

Analysing household credit by purpose of lending reveals differing trends in lending for house purchases, which accounts for the vast majority of household credit, and shorter-term lending for consumption and other purposes (Figure 4). In total, new lending to households contracted by 8 per cent in the first quarter compared to the corresponding quarter of 2020, while lending strengthened in April.

Figure 4 – New Lending to Households by Purpose



Source: Central Bank of Ireland

There was a significant decline in new mortgage lending (ex. renegotiations) at the beginning of the pandemic. Recent analysis has shown that the biggest factor shaping credit outcomes appeared to have been falling credit demand, while only some tightening was observed in credit supply conditions[8]. The beginning of 2021 got off to a subdued start, with new mortgage lending down almost 7 per cent year-on-year in January. Lending has since recovered, with the latest data indicating the volume of new mortgage lending was only slightly lower than in April 2019.

According to the latest Bank Lending Survey[9], demand for house purchase loans was largely unchanged compared to the previous survey but demand for consumer credit and other lending declined. Increases in demand for the latter two categories of lending are expected during the second quarter, while the credit standards on household loans are also expected to be loosened.

[8] Credit Conditions for Irish Households and SMEs, available here.
[9] Central Bank of Ireland's latest Bank Lending Survey, available here.

The average interest rates on all new mortgage agreements have remained largely unchanged at around 2.79 per cent since January[10]. The rate on fixed rate agreements, which account for nearly four in every five new mortgages agreements, continues to edge lower and currently stands at 2.63 per cent in April, its lowest level since the series began and down 16 bps since the beginning of 2020. Ireland currently has the second highest average rate in the euro area, however the composition of loan types and risk characteristics are different in each country, making like-for-like comparisons difficult[11].

New consumer lending remains subdued, contracting sharply during the first quarter. The latest data for April shows this subdued trend has continued, although it is significantly higher than the lows associated with the beginning of the pandemic. Looking to the months ahead, as consumer credit is largely driven by car purchases, holidays and credit cards, any increase in new lending for consumption purposes is unlikely until consumer confidence and activity returns[12]. The sharp increase in consumer lending seen in summer of 2020, highlights that the flow of consumer credit can pick up quickly and sharply to support the recovery when health restrictions ease.

Business Credit & Deposits

Data on lending to non-financial corporations (NFCs) shows that repayments exceeding drawdowns by €2.2 billion in the twelve months to end-May.

The trend of subdued new lending to NFCs continued in the first two months of this year before rising sharply in March, with loans over €1 million, which are mainly driven by large enterprises, contributing the majority of the increase. April's data shows slightly lower levels of new lending compared to March, but remains higher in year-on-year terms.

New lending advanced to Irish resident SMEs[13] stood at just over €1 billion in the first quarter of 2021, a decline of 24 per cent compared to the final quarter of 2020. New lending varied considerably across sectors, with the property investment/development and primary industries recording the largest levels of new lending in the quarter, while hotel and restaurant sectors were significantly lower than pre-pandemic levels.

[10] Central Bank of Ireland. Retail Interest Rate Statistics April 2021.

[11] https://www.centralbank.ie/news/article/blog-monetary-policy-and-interest-rates-in-ireland

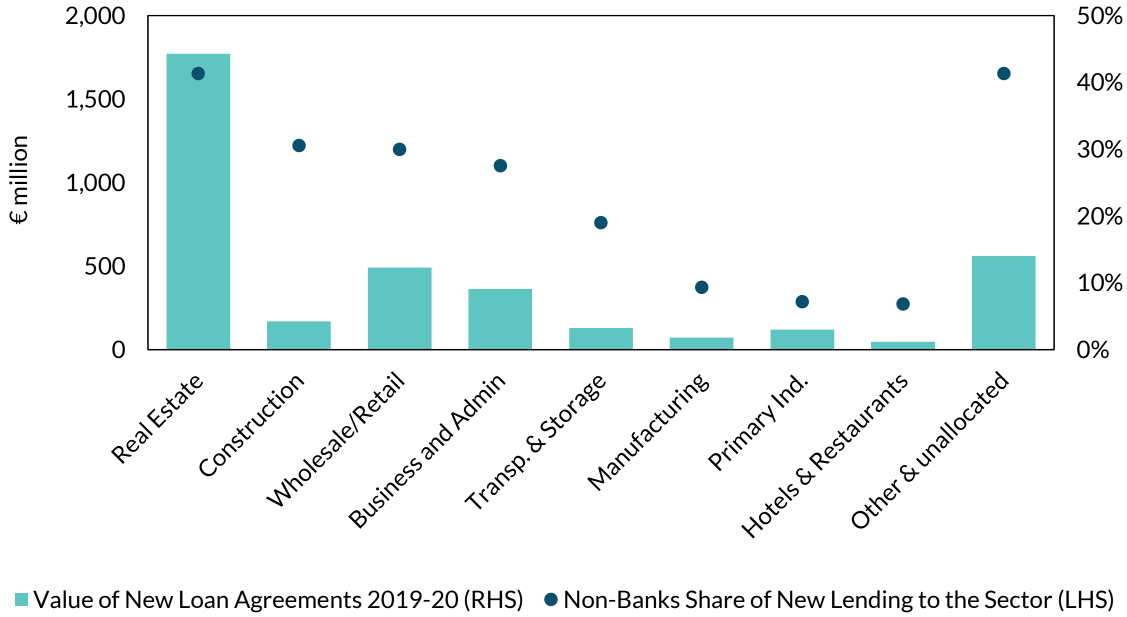
[12] Byrne, S., Hopkins, A., McIndoe-Calder, T., and Sherman, M. The Impact of COVID-19 on Consumer Spending. Central Bank of Ireland Economic Letters. Vol 2020. No 15.

[13] Data on lending to SMEs is available here.

According to recent analysis on household and SME credit conditions[14], the decline in of new lending to SME's does not appear to be driven by factors that relate to bank balance sheet constraints, such as capital, access to funding or liquidity. Looking at firms' demand for credit, the latest ECB SAFE survey[15], covering the six months to March 2021, shows that the percentage of euro area SMEs applying for bank loans declined compared to the previous six months, with a significant proportion citing sufficient availability of internal funds. In Ireland, the extensive set of policies introduced, focusing on wage subsidisation, tax and payment deferrals, grants and direct cost supports as well as lending facilities has helped support firms' liquidity, with some sectors more heavily reliant on these supports than other sectors. The survey also highlights that the financial vulnerability of euro area SMEs remains high, with almost 10 per cent of SMEs encountering major difficulties in running their businesses and servicing debts.

Forward-looking risks to the supply of credit to businesses remain, including the possibility that supply will not meet firm demand for credit as the government liquidity supports are phased out as the economy reopens. While the possibility of an unexpected deterioration in credit quality also exists, which may lead to a tightening of risk appetite by lenders and individual lender decisions, leading to a collectively sub-optimal outcome[10].

Figure 5: Sectoral use of non-bank lending



Source: Central Bank of Ireland Statistics, Central Credit Register, CRO, RIAD and Central Bank of Ireland calculation

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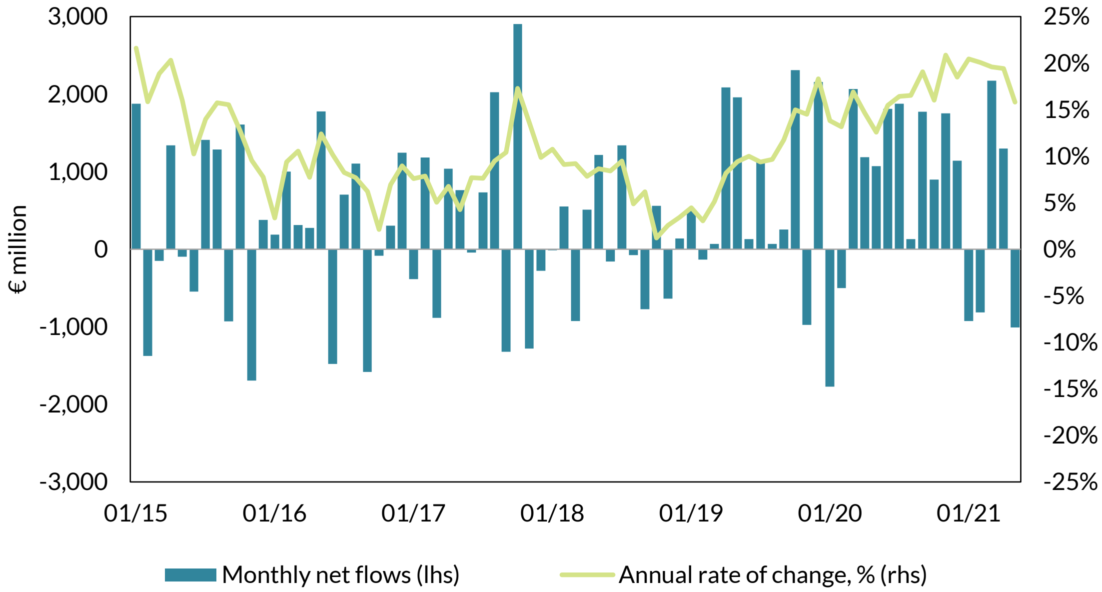
[14] Credit Conditions for Irish Households and SMEs, available here.
[15] https://www.ecb.europa.eu/stats/ecb_surveys/safe/html/ecb.safe202106~3746205830.en.html#toc18

The non-bank sector provides a growing and important source of credit for Irish SMEs, recent analysis using the Central Bank's Central Credit Register[16], shows that SMEs borrowed in excess of €1.6 billion from non-bank lenders in 2020. Overall, SMEs had outstanding debts of circa €4.3 billion owed to non-bank lenders at the end of 2020, compared to €19.8 billion owed to banks. The real estate sector received the largest share, at 41 per cent, of their total borrowing from the non-bank sector, which amounted to €1.8 billion between 2019 and 2020 (Figure 5). Non-banks also account for a high share of funding in the wholesale and retail sector, which is heavily concentrated in stocking finance for car dealers, and was one of the few sectors to see a growth in lending in 2020.

Figure 6: Deposits from NFCs; developments in net flows, and annual rate of change



Source: Central Bank of Ireland

Similarly to households, NFCs have significantly increased their aggregate holdings of deposits. The most recent data, to end-May, shows that the annual increase in NFC deposits has risen by an average of 19 per cent each month since the beginning of the year (Figure 6). Since the beginning of the Covid-19 pandemic in March last year, NFCs deposit lodgements has exceeded withdrawals by €14.4 billion, the vast majority of which are overnight deposits.

Summary

Irish households and NFCs have continued to adapt their financing activities in response to the evolving nature of the COVID-19 pandemic and the corresponding public health measures. As restrictions began to ease in early-May, and supported by the rising consumer sentiment, spending in

[16] For more detail on latest Behind The Data, 'The role of non-bank lenders in financing Irish SMEs', see Tiernan Heffernan, Barra McCarthy, Rory McElligott and Conall Scollard.

sectors most impacted by the public health restrictions rose strongly, although remain well below their pre-pandemic levels. Online spending accounted for the majority of card payments over the period January to early-May, however, as non-essential retail reopened, in-store spending rose sharply and once again became the primary venue for card spending.

Irish households' net worth rose to a record high at the end of 2020, boosted by the rise in aggregate household deposits and increases in housing assets. The latest monthly data shows that household deposits continued to record fresh highs at end-May, while net new lending remains negative. New mortgage lending, despite getting off to a subdued start at the beginning of this year, has since recovered with the latest data for April indicating it was only marginally lower than April 2019.

Net new lending to NFCs also contracted at end-May, while similarly to households since the beginning of the pandemic, their aggregate holdings of deposits has significantly increased. Recent analysis has shown that non-bank lenders are becoming an increasingly important alternative source of credit for Irish SMEs, especially in the real estate, wholesale and retail sectors. Despite the lack of constraints in banks' balance sheets for providing new lending, as the economy reopens and government liquidity supports are gradually phased out, forward-looking risks to the supply of credit to businesses remain, including the possibility that supply may not meet firm demand for credit or the possibility of an unexpected deterioration in credit quality.