

*kcFED* **Small Business Lending SURVEY****Small Business Lending Demand Continues to Decline**

Outstanding small business commercial and industrial (C&I) loan balances<sup>1</sup> increased year over year for the first time since the first quarter of 2021, despite remaining stable in the last two quarters. Although outstanding balances have increased, new lending continued to decline in the third quarter, decreasing 18.1 percent from the same period in 2022 and 16.4 percent from the previous quarter.

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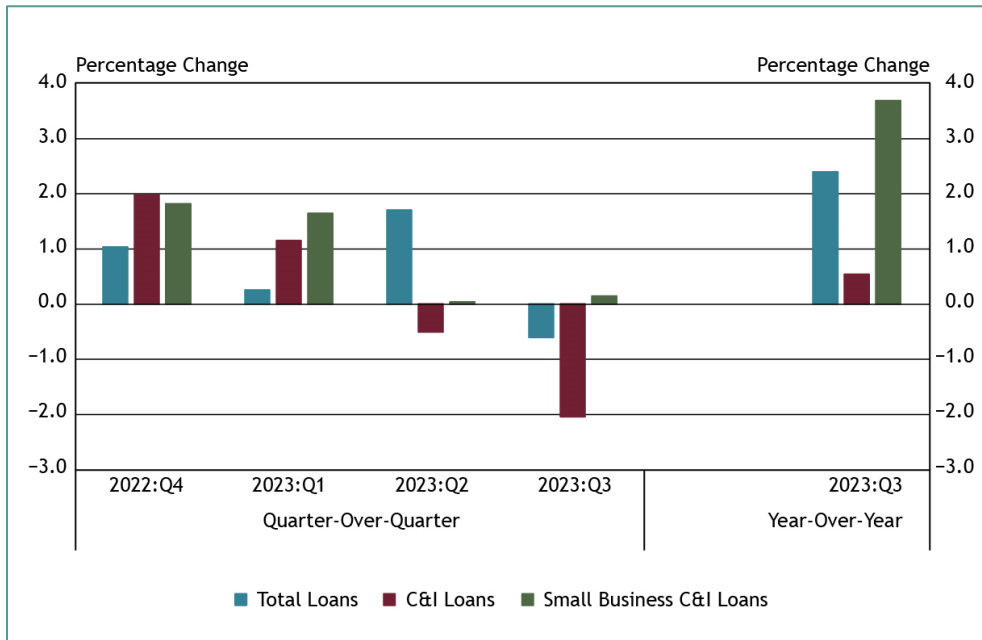
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Respondents reported declining loan demand for the sixth consecutive quarter, despite a minimal increase in loan approval rates. With over \$65 billion in small business loans reported, the 150 respondents to the survey indicated that credit standards tightened while credit quality continued to decrease, and interest rates generally rose, consistent with the current rate environment. Most respondents indicated that lending to small businesses was unconstrained by available liquidity, and the primary respondents reporting any constraints were small and midsized banks.

<sup>1</sup> Small business lending refers to commercial and industrial lending to organizations generally defined as having less than five million in gross annual revenue, unless otherwise noted.

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**Chart 1: Outstanding Small Business Loans Increase Year-over-Year**



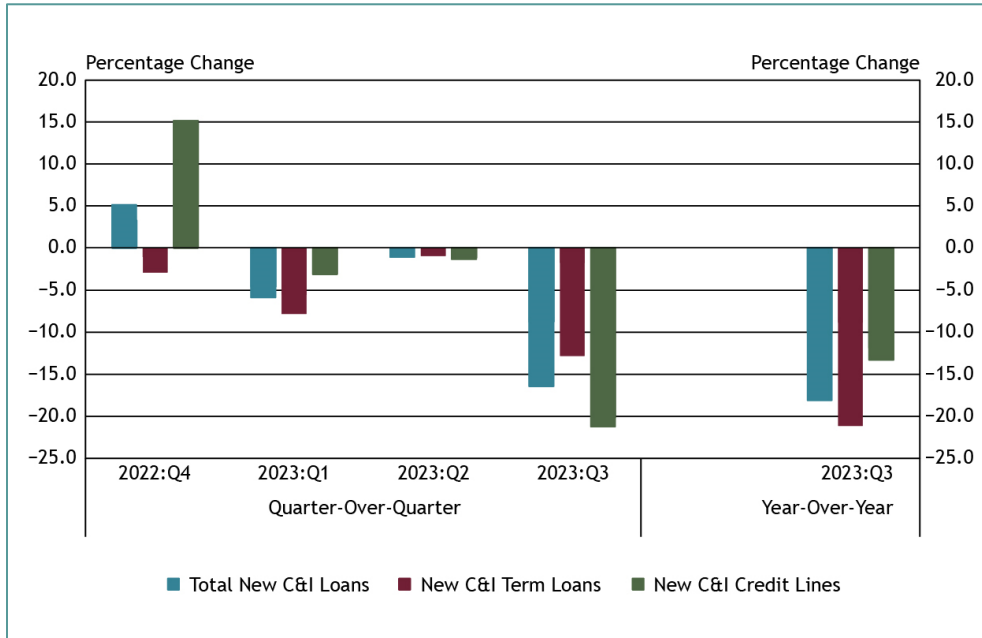
Note: Items are calculated using a subset of 102 respondents that completed the FR 2028D for the last five quarters surveyed.

Sources: Call Report, Schedule RC-C Part I, items 4. Commercial and Industrial Loans and 12. Total Loans and Leases Held for Investment and Held for Sale, Small Business Administration, and FR 2028D, items 4.b and 5.c.

When compared to the third quarter of 2022, small business C&I loan balances increased by 3.7 percent, C&I loan balances increased by 0.5 percent, and total loan balances increased by 2.4 percent. This is the first year-over-year increase in small business loans since the first quarter of 2021. Quarter-over-quarter, small business loan balances remained stable, while C&I loan balances decreased by 2.0 percent and total loan balances decreased by 0.6 percent.

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**Chart 2: New Small Business Lending Declines**



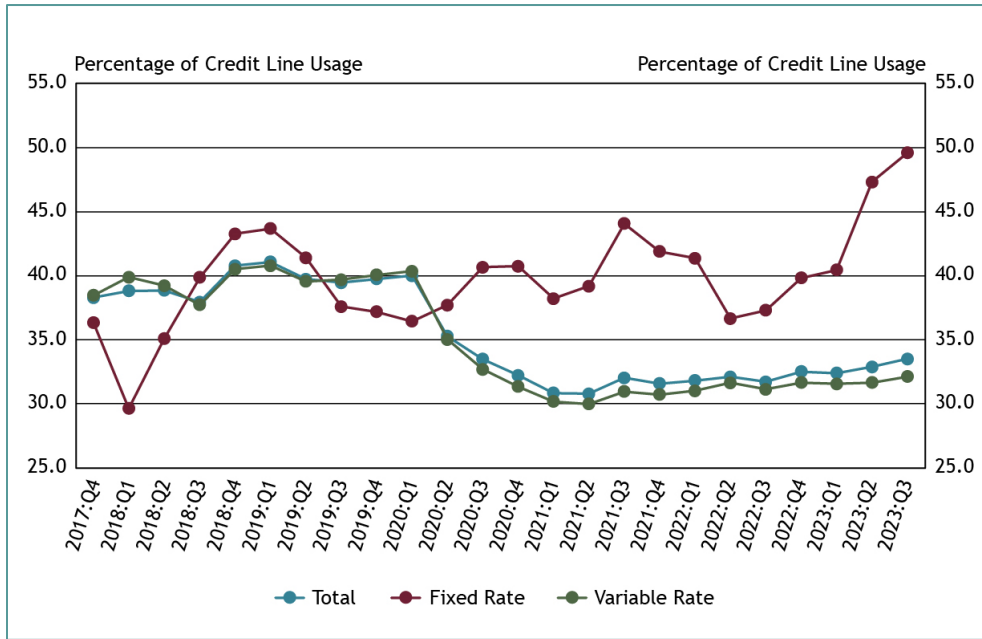
*Note: Items are calculated using a subset of 102 respondents that completed the FR 2028D for the last five quarters surveyed. All loan types referenced in Chart 2 refer to small business lending.*

*Source: FR 2028D, items 7.b and 8.c.*

Compared to third quarter 2022, total new small business loan balances decreased 18.1 percent, driven by a 21.1 percent decrease in new term loans and a 13.2 percent decrease in new lines of credit. The year-over-year decline in new small business lending is consistent with weaker loan demand and tightening credit standards reported by survey respondents. Total new small business lending declined by 16.4 percent quarter-over-quarter, due to reduced lending by large banks. Small and medium banks both reported increases in new lending from the previous quarter.

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**Chart 3: Credit Line Usage Remains Stable**

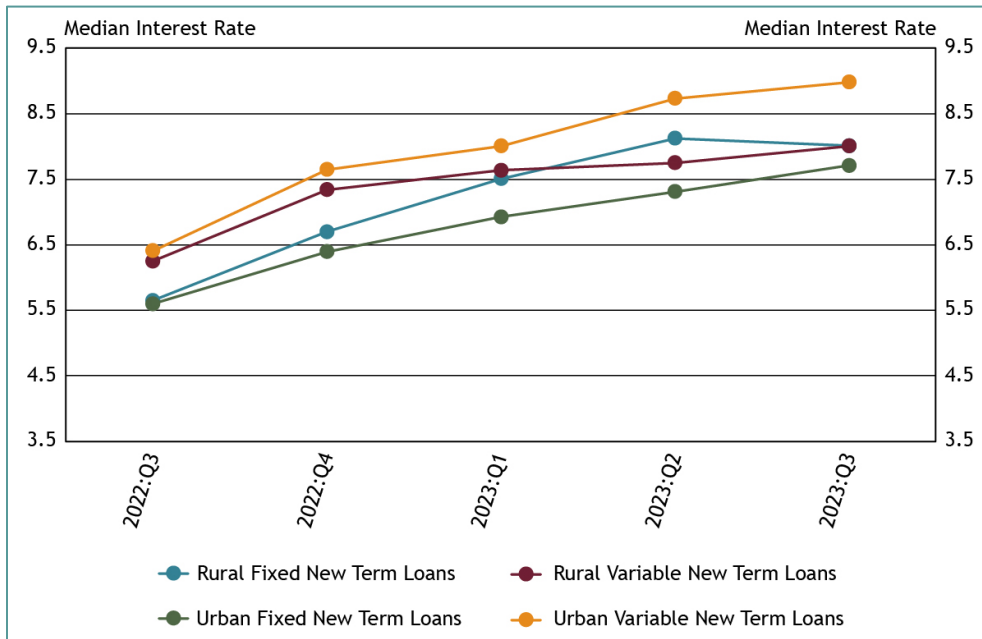


Source: FR 2028D, items 5.b and 5.c.

Usage of small business credit lines remained stable in the third quarter at 33 percent, despite a slight increase in the utilization of fixed rate credit lines. As of third quarter 2023, respondents indicated variable rate lines make up about 90 percent of total credit line usage.

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**Chart 4: Most Rates Increase on New Term Loans**



Note: Items are calculated using a subset of 102 respondents that completed the FR 2028D for the last five quarters surveyed.

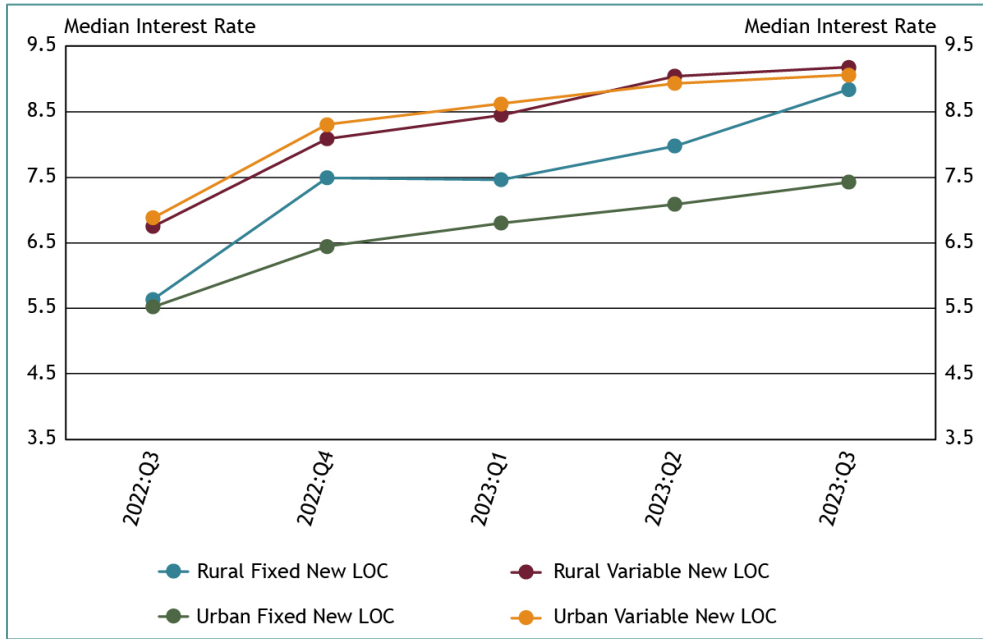
Source: FR 2028D, item 7.c.

Median interest rates increased for new small business term loans in the third quarter 2023. The highest reported rates were for variable rates offered at urban banks, regardless of asset size, which were reported as 9.0 percent, a 25-basis point increase from the second quarter 2023. The lowest reported rates were for fixed rates offered at urban banks, which were reported as 7.7 percent.<sup>2</sup>

<sup>2</sup> Urban and rural classification is determined exclusively by the bank's head office location and [US Census Population](#) data.

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**Chart 5: Rates Increase on New Lines of Credit**



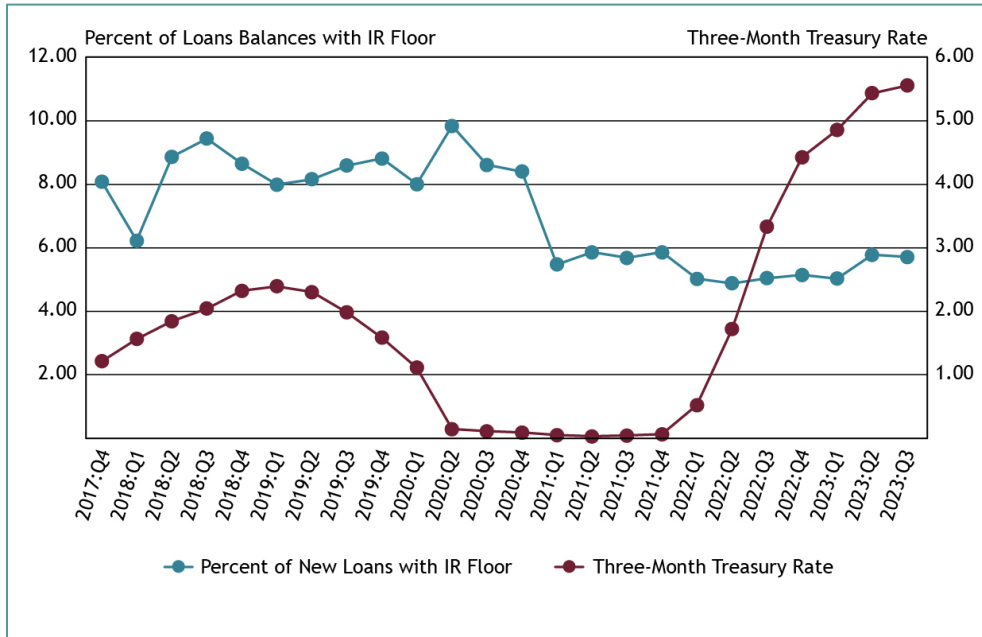
Note: Items are calculated using a subset of 102 respondents that completed the FR 2028D for the last five quarters surveyed.

Source: FR 2028D, item 8.d.

Median interest rates on new small business lines of credit increased in the third quarter 2023, which is directionally consistent with the increase of 12 basis points for the three-month Treasury rate and the 25-basis point increase in the Federal Funds Rate in the same period. The highest were variable rates offered at rural banks, which were reported as 9.2 percent, a 14-basis point increase from the second quarter 2023. The lowest were fixed rates offered at urban banks, which were reported as 7.4 percent.

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**Chart 6: New Loans with Interest Rate (IR) Floors Remain Stable**

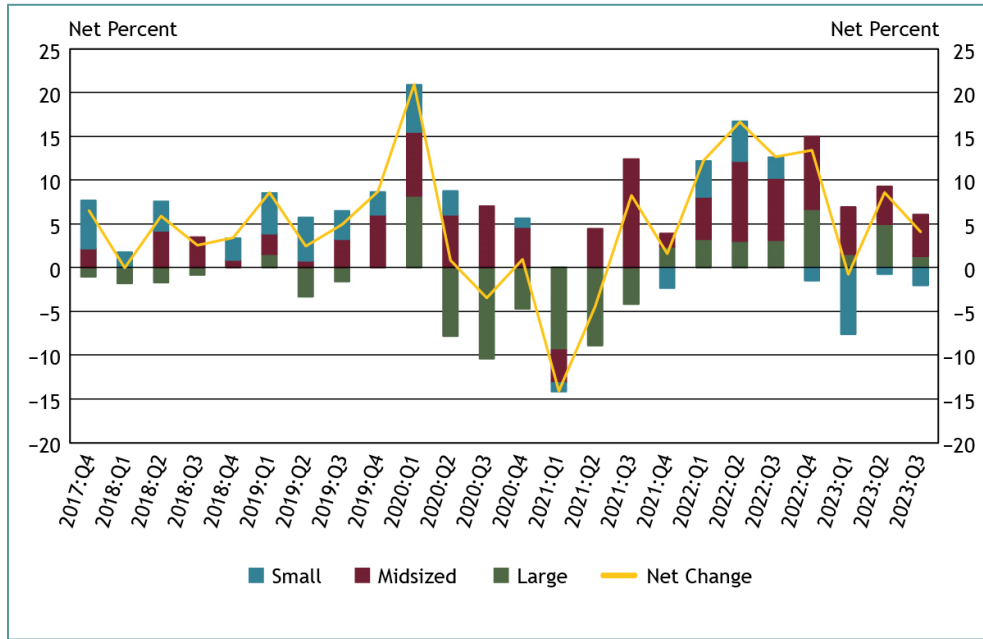


Sources: FR 2028D, items 7.a, 7.f, 8.a, 8.e and Federal Reserve Bank of St. Louis, 3-Month Treasury Constant Maturity Rate.

While the three-month Treasury rate continues to increase, the percentage of new variable-rate loans with interest rate floors remain generally stable dating back to first quarter 2021.

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**Chart 7: Large and Midsized Banks Report Increase in Credit Line Usage**



Note: Chart 7 shows diffusion indexes for credit line usage. The diffusion indexes show the difference between the percent of banks reporting decreased credit line usage and those reporting increased credit line usage. Net percent refers to the percent of banks that reported having decreased (“decreased somewhat” or “decreased substantially”) minus the percent of banks that reported having increased (“increased somewhat” or “increased substantially”).<sup>3</sup>

Source: FR 2028D, items 11 and 12.

In the third quarter, 30 percent of respondents reported a change in credit line usage. Four percent of respondents, on net, indicated that credit line usage increased, which is down from 8 percent last quarter. On net, about 5 percent of midsized banks and 1 percent of large banks reported an increase, despite 2 percent of small banks reporting a decrease. Of the banks reporting an increase, 46 percent cited changes in local or national economic conditions as a very important reason, while 35 percent cited changes in borrowers’ business revenue or other business-specific conditions as very important reasons. Of the banks reporting a decrease, 47 percent cited changes in pricing (rates, fees, etc.).

The reported increase in credit line usage is consistent with a shift to increased debt financing observed in other key indicators such as elevated consumer credit card debt.<sup>5</sup> Total household credit card debt continues to increase each quarter.<sup>6</sup>

<sup>3</sup> Small banks have total assets of \$1 billion or less, midsized banks have total assets between \$1 billion and \$10 billion and large banks have total assets greater than \$10 billion.

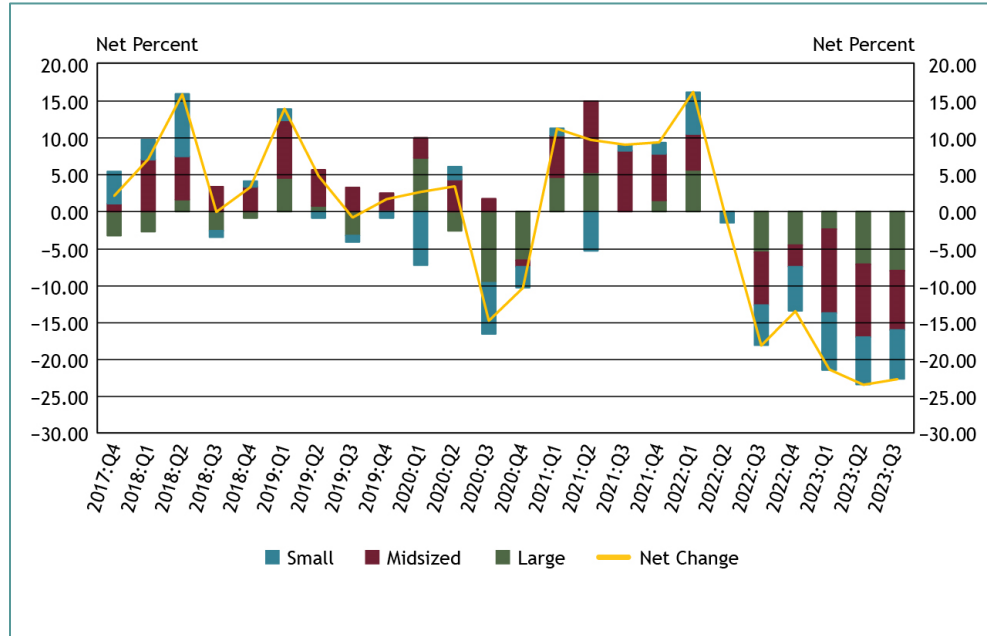
<sup>4</sup> Source: FRED, Consumer Loans: Credit Cards and Other Revolving Plans.

<sup>5</sup> Source: FRBNY Consumer Credit Panel/Equifax



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**Chart 8: Respondents Report Declines in Loan Demand for the Sixth Consecutive Quarter**



*Note: Chart 8 shows diffusion indexes for loan demand. The diffusion indexes show the difference between the percent of banks reporting weakened loan demand and those reporting stronger loan demand. Net percent refers to the percent of banks that reported having weakened (“moderately weaker” or “substantially weaker”) minus the percent of banks that reported having stronger loan demand (“moderately stronger” or “substantially stronger”).*

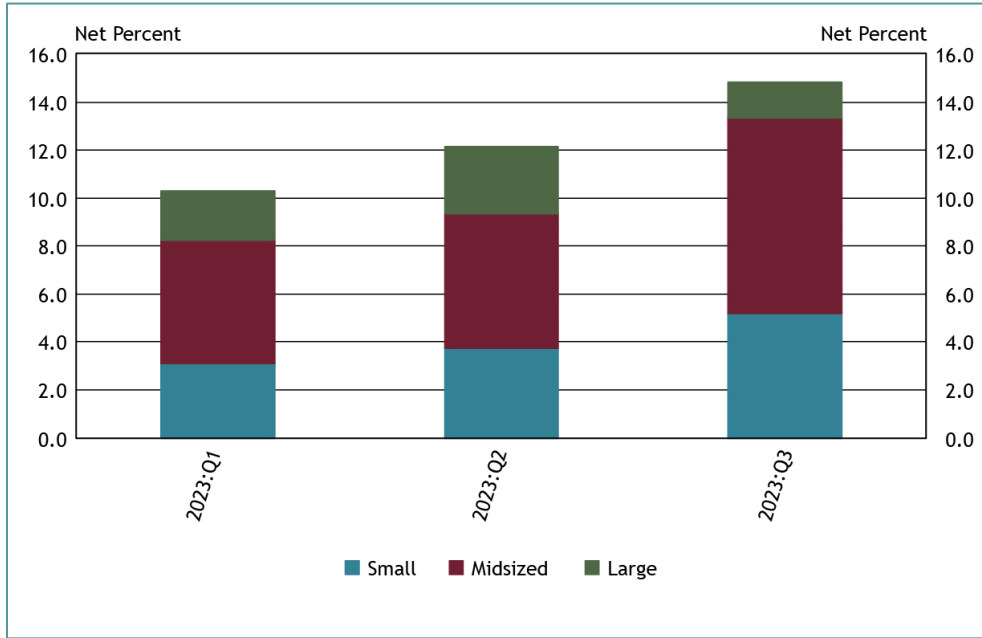
Source: FR 2028D, item 13.

About 42 percent of respondents reported a change in small business loan demand in the third quarter of 2023, a decrease of 7 percent from the second quarter. On net, about 23 percent of respondents indicated weaker loan demand across all bank sizes. This marks the sixth consecutive quarter of respondents reporting a net decline in loan demand.

The timing of softer loan demand aligns with the Federal Reserve’s monetary policy tightening since mid-2022. It is also consistent with the [October 2023 Federal Reserve Senior Loan Officer Opinion Survey \(SLOOS\)](#), where about 53 percent of respondents reported weaker C&I loan demand from small firms (annual sales of less than \$50 million) over the prior three months.

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**Chart 9: Small and Midsized Banks Indicate More Constrained Lending Than Larger Banks**

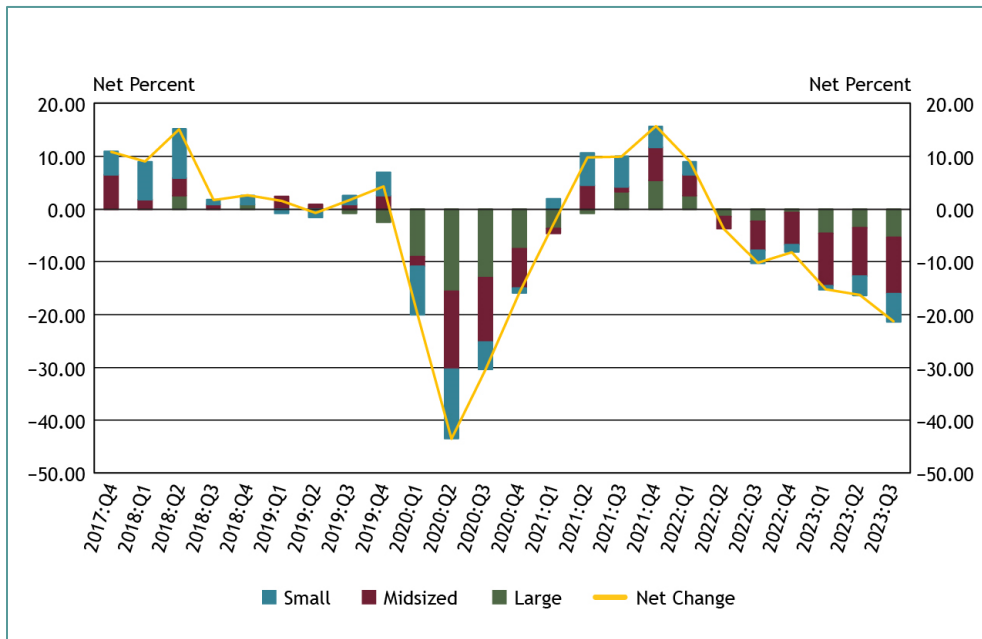


Source: FR 2028D, Special Question.

About 15 percent of all respondents indicated their lending to small businesses was constrained by the availability of liquidity in the market. This is an increase of about 5 percent from the first quarter of 2023 and 3 percent from the second quarter of 2023. Most respondents reporting a constraint were small and midsized banks. For the respondents who indicated lending was constrained, the most cited reason was greater competitive pressures for deposits (100 percent).

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**Chart 10: Overall Credit Quality Continues to Decline**



Note: Chart 10 shows diffusion indexes for credit quality of applicants. The diffusion indexes show the difference between the percent of banks reporting a decline in credit quality and those reporting improvement in credit quality. Net percent refers to the percent of banks that reported declining credit quality (“declined somewhat” or “declined substantially”) minus the percent of banks that reported improving credit quality (“improved somewhat” or “improved substantially”).

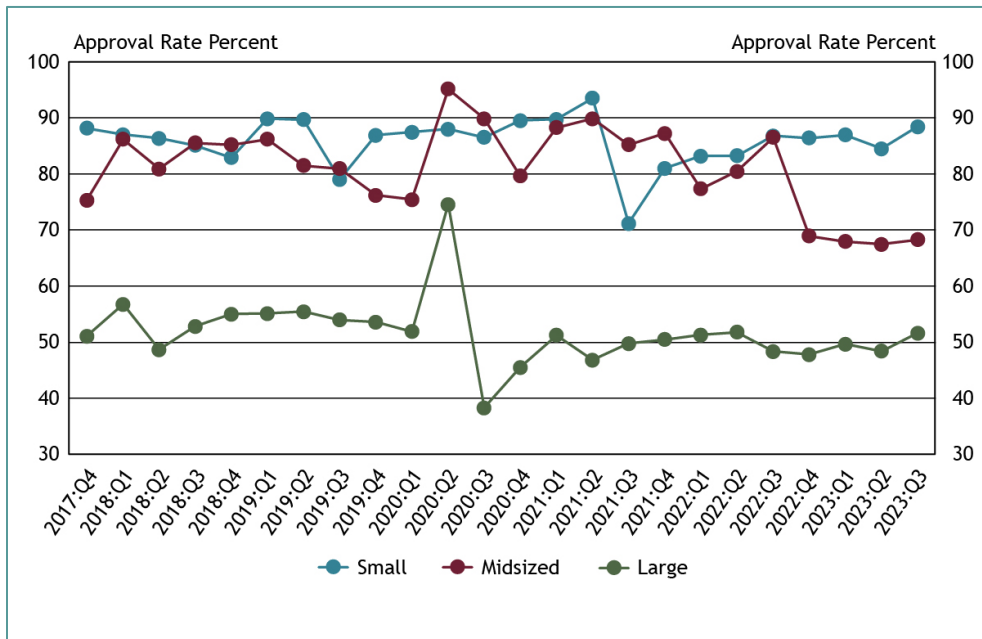
Source: FR 2028D, items 20 and 21.

About 21 percent of survey respondents, on net, reported a decrease in applicant credit quality. This is the sixth consecutive period in which respondents of all bank sizes, on net, reported a decrease. Of the respondents reporting a change in credit quality, whether an increase or decrease, 50 percent cited the debt-to-income level of business owners as a very important reason for a change.

Other commonly cited reasons for a change include the liquidity position of business owners, recent business growth income, and credit scores. The decrease in applicant credit quality reported by firms is consistent with the negative outlook of loan availability reported by small businesses in the [October 2023 NFIB Survey of Loan Availability](https://www.kansascityfed.org/surveys/small-business-lending-survey/).

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**Chart 11: Loan Approval Rates Increase for all Bank Sizes**

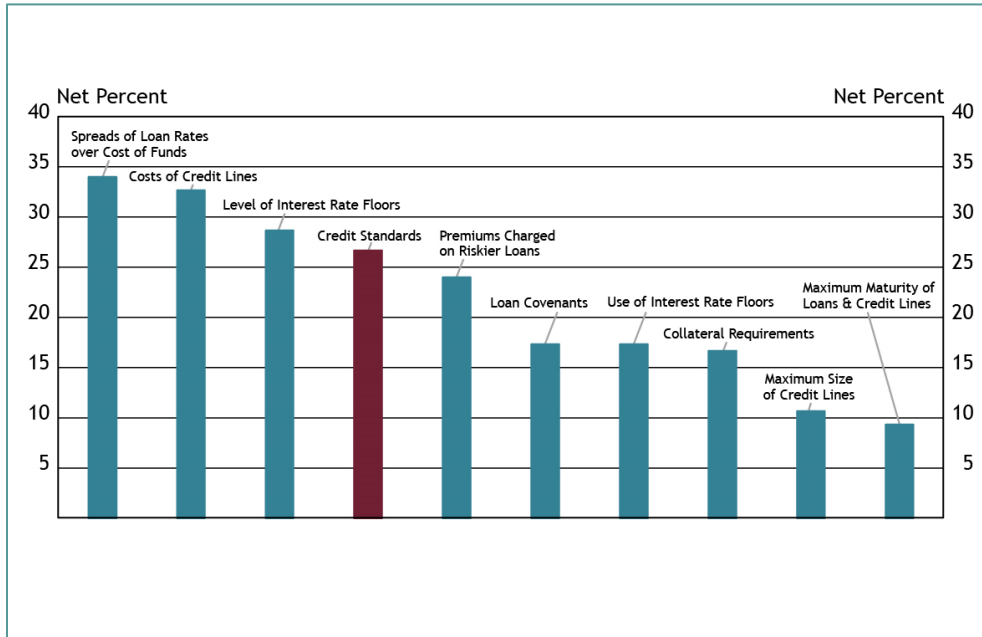


Source: FR 2028D, items 14.a and 15.

Despite diminishing credit quality (Chart 10) and weakening loan demand (Chart 8), application approval rates increased for all respondents in the third quarter. Small bank approval rates increased from 84 percent in the second quarter to 88 percent in the third quarter, while approval rates for large bank respondents increased from 48 percent to 52 percent. Midsized banks increased slightly from 67 percent to 68 percent over the quarter. About 70 percent of respondents indicated borrower financials were the most common reason for denying a loan. Other commonly cited reasons were borrower collateral and credit history.

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**Chart 12: Respondents Report Tightening Credit Standards for the Eighth Consecutive Quarter**



Note: Chart 12 shows diffusion indexes for credit standards (red bar) and various loan terms. The diffusion indexes show the difference between the percent of banks reporting tightening terms and those reporting easing terms. Net percent refers to the percent of banks that reported having tightened (“tightened somewhat” or “tightened considerably”) minus the percent of banks that reported having eased (“eased somewhat” or “eased considerably”). Source: FR 2028D, items 16, 17, 18 and 19.

About 27 percent of respondents reported tightening credit standards (red bar) in the third quarter. This is the eighth consecutive quarter that respondents have reported tightening credit standards and is consistent with the tightening credit standards reported in the [October 2023 Senior Loan Officer Opinion Survey on Bank Lending Practices](#).

On net, respondents indicated that all loan terms tightened. The spreads of loan rates over cost of funds were the most commonly tightened loan term with about 34 percent of respondents, on net, reporting tightening. About 90 percent of respondents cited less favorable or more uncertain economic outlook as a somewhat important or very important reason for the tightening. Other commonly cited reasons were worsening of industry-specific problems and reduced tolerance for risk.

*Other contributors to the release include Alli Baranski, Nicholas Bloom, Thomas Hobson, Stefan Jacewitz, Emily Robinson, and Karen Thompson.*