BTMU LATIN AMERICA TOPICS

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BRAZIL: SUBDUED CREDIT GROWTH AS GOVERNMENT BANKS' LENDING SLOWED IN SEPTEMBER

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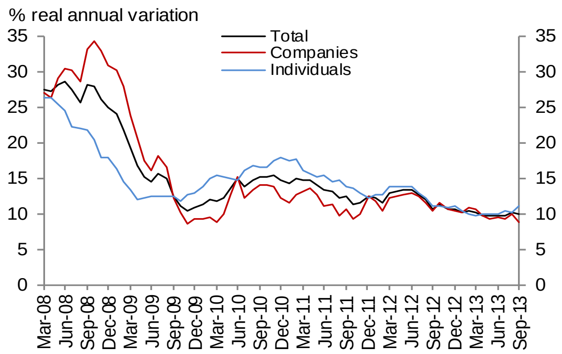
Total credit growth remains moderated, with key disparities in origin of capital and type of lending

Credit growth to the private sector rose 1.0% month-on-month in September—slowing from 1.2% mom in August—to take the stock of outstanding credit to R$2.6trn, or 52.6% of GDP. In annual terms, nominal credit growth to the private sector decelerated to 15.1% from 15.3% in August. Real (inflation-adjusted) credit growth is at 9.9% yoy, displaying the deceleration trend since June 2012. Loan growth to companies slowed 110bp mom to 8.8% yoy in real terms upon the subdued expansion of government banks' directed lending. For individuals, loan growth rose 90bp mom to 11.1% yoy as non-directed loans rose. (Figure 1.)

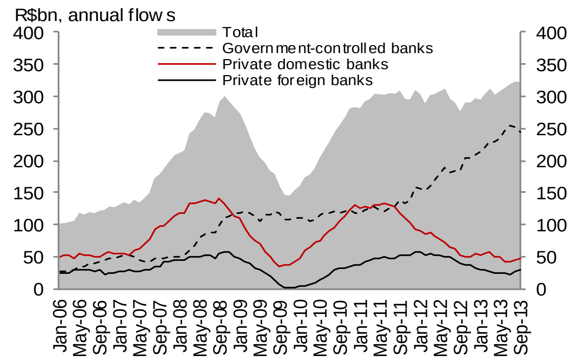
Sizeable growth pace disparities persist between government-controlled vs. private banks and between directed vs. non-directed loans, though the expansion of government banks' lending and directed credit allocations slowed in September. The slowdown of directed loan growth and uptick of non-directed loan growth in real terms does not yet establish a new trend in the Brazilian credit market since it represents only one month of data, but it does interrupt a clear pattern and may mark the beginning of a gradual pullback from government banks.

Figure 1: Bank credit growth to private sector



Source: Central Bank; BTMU Economic Research.

Figure 2: Bank credit flows to private sector by lender



Source: Central Bank; BTMU Economic Research.

Government-controlled banks are still driving credit flows, though at a slowed pace in September

Total credit flows to the private sector remain led by government banks, which have been under pressure to aggressively increase lending to spur credit growth and reduce spreads. Government-controlled banks supplied a dominant 76% of credit flows to the private sector in the 12-months through September. This is, nevertheless, down from 78% the previous month owed to their slower real loan growth of 20.6% yoy compared to 22% yoy in August. (Figure 2.) It will be interesting to see if the deceleration observed in September is owed to: 1) bank teller strikes, which negatively affected directed lending to households, or 2) the government's intent to curb its lending in order to maintain its sovereign credit rating and to assist the BCB's monetary policy actions to contain inflation. The latter would mark an important policy improvement, but it remains to be seen if this indeed marks a deliberate shift in policy.

Real loan growth by BNDES slowed to 11.9% yoy in September (from 13.4% in August), while growth by other government banks decelerated to 27.9% yoy (from 28.8%). Private foreign banks' lending accelerated to 2.1% yoy (from 1.1%) and private domestic banks picked up to -0.1% yoy (from -0.7%). (Figure 3.)

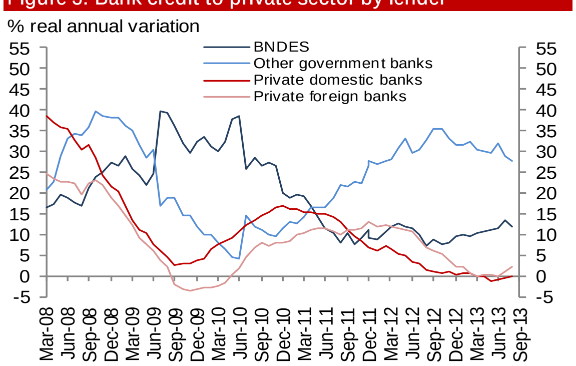
Government banks' market share of outstanding credit to the private sector remained steady at 48% in September compared to August. Private domestic banks' participation continued its downward decline to 35.5% from 35.7%. Private foreign banks' participation rose—for the first time since July 2012—to 16.5%.

Decline of directed loans and pick-up of non-directed loans interrupts trend

In September, there was an interruption in the credit trend which since 2009 has seen directed loan growth exceed non-directed loan growth in the midst of government-controlled banks' acceleration of lending and private banks' conservative lending stance. Directed loans are earmarked funds issued at subsidized rates for specific economic activities, and their allocation is mostly controlled by government banks. These types of loans have expanded to account for 44% of outstanding credit upon the remarkable rise of lending from BNDES—the development bank which has tripled its outstanding credit stock since 2007—as well as mortgage and other lending from government-controlled banks Banco do Brasil and Caixa Econômica Federal.

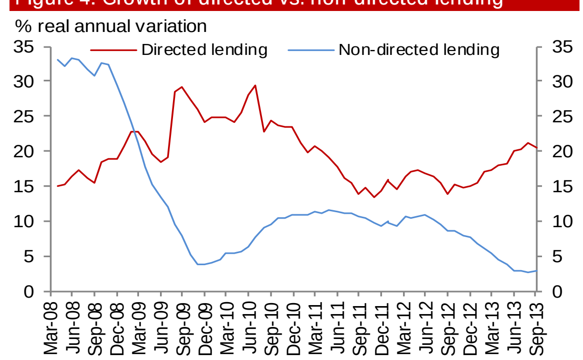
Real annual directed loan growth slowed in September for the first time since November 2012, while non-directed loan growth accelerated for the first time since June 2012. Directed loan growth decelerated 80bp mom to 20.4% yoy in real terms on account of slowed BNDES and mortgage lending. At the same time, non-directed loan growth increased 20bp mom to 2.9% upon a pick-up in non-directed credit card lending and consumer overdrafts. (Figure 4.) Since private banks remain conservative due to consumers' indebtedness, the growth of directed loans should continue to outpace non-directed loans.

Figure 3: Bank credit to private sector by lender



Source: Central Bank; BTMU Economic Research.

Figure 4: Growth of directed vs. non-directed lending



Source: Central Bank; BTMU Economic Research.

Stable overall loan quality, but varied by segment

Loan quality remains controlled on account of the still-favorable labor market dynamics, with the 90-day total non-performing loan ratio remaining stable at 3.25% in September compared to August. Having been on a downward trend, the NPL ratio has lowered from 3.82% last September.

Yet, credit quality improvement is uneven and varied by segment. The 90-day NPL ratio is higher for individual (4.83%) vs. corporate (2.01%) loans; non-directed (5.07%) vs. directed (1.06%) loans; and loans issued by private (4.6%) vs. government banks (1.98%). The poorest credit quality is in the non-directed loan segment to individuals, which was unchanged at 7.0% in September compared to the previous month, but has fallen from its peak of 8.2% last September.

Asset quality has been gradually improving for private banks since October 2012, when the NPL ratio reached 5.6%. In September, the 90-day NPL ratio of domestic banks was unchanged at 4.6% from August, while among foreign banks it fell 40bp mom to 4.6%.

However, credit quality deteriorated for government banks and the directed loan segment in September. At government banks, the 90-day NPL ratio rose 12bp from August to 1.98%. Among directed loans, it rose to 1.6% from 1.0% in August.

High household debt burden is weighing on consumption and loan growth

Brazilian consumers remain indebted. Households' payments on principal and interest obligations as a share of disposable income stood at 21.4% in August compared to 21.46% in July. While it has lowered from the peak of 22.9% in June 2012, it is declining at a very gradual pace. Indeed, the debt service ratio has been hovering at a nearly unchanged rate for most of this year. At this present level, over one-fifth of households' disposable income is still directed to pay debt obligations. (Figure 5.)

While the principal component of the debt service ratio has been in slight decline, the interest component has been rising since April and remains elevated owed to the BCB's monetary tightening cycle and the growth of mortgage loans. (Figures 5 and 6.)

Mortgage loans have grown by an average of 28% yoy in real terms during the first nine months of the year. This strong lending growth—from a low base of less than 8% of GDP and led by government banks—is contributing to the elevation of the household debt service. (Figure 6.) Mortgages have longer maturities and lower rates than other loans issued to individuals, implying that the extended maturities of rising outstanding debt will keep households' debt service ratio high with no direct relief to consumers in the near term.

Moderation of credit growth is testing resilience of consumption

Following a robust credit deepening cycle from 2006-12, Brazilian credit growth is constrained on both the supply and demand sides. Overall, September's lending activity was impacted by bank tellers' labor strike, slowed public bank lending, indebted consumers, and lackluster GDP growth. While interest rates are rising, loan quality is well controlled.

The decelerated pace of aggregate loan growth will restrain inflation pressures but also challenge the resilience of private consumption, the main growth driver of the economy. The cooled credit market and elevated household debt burden will work in the opposite direction of the favorable, but weakening, labor market dynamics in supporting consumption. (Figure 7.)

With gradually improving asset quality, private banks are positioned to regain market share from government banks. In this context, the gap between private bank and government-controlled lending growth should begin to narrow. However, government banks are likely to continue leading credit flows since private banks remain selective in new loan issuances.

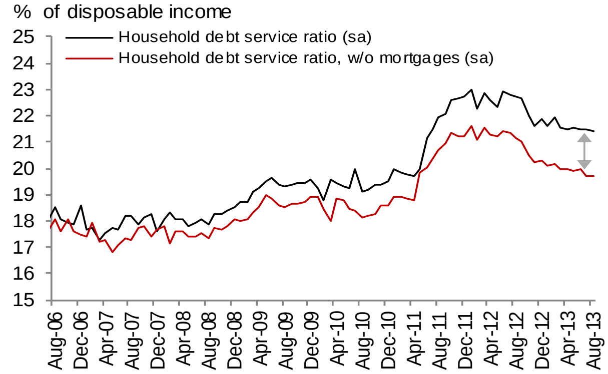
For government banks, it will be important to monitor the ability to sustain such strong lending growth without further fiscal deterioration and the buildup of risks in asset quality and inflation. Moreover, we will be watching to see if the observed lending slowdown of government banks in September was a one-off interruption of the growth trend, or the beginning of an intentional pullback which would mark an improvement to the current policy mix of expansionary fiscal and quasi-fiscal spending.

Figure 5: Household debt service ratio
(% of disposable income, seasonally-adjusted)

	Principal	Interest	Total	Total, without Mortgages
Jan-12	13.86	9.11	22.97	21.61
Feb-12	13.42	8.81	22.24	21.09
Mar-12	13.73	9.14	22.87	21.55
Apr-12	13.48	9.15	22.63	21.31
May-12	13.30	9.05	22.36	21.21
Jun-12	13.72	9.18	22.90	21.41
Jul-12	13.68	9.10	22.79	21.32
Aug-12	13.64	9.06	22.70	21.18
Sep-12	13.64	9.00	22.64	21.02
Oct-12	13.23	8.79	22.02	20.51
Nov-12	13.11	8.51	21.61	20.26
Dec-12	13.21	8.68	21.89	20.32
Jan-13	13.07	8.55	21.62	20.09
Feb-13	13.17	8.74	21.91	20.19
Mar-13	13.06	8.51	21.57	19.96
Apr-13	12.99	8.50	21.49	19.96
May-13	12.93	8.59	21.52	19.92
Jun-13	12.86	8.64	21.50	19.95
Jul-13	12.74	8.72	21.46	19.73
Aug-13	12.74	8.66	21.40	19.73

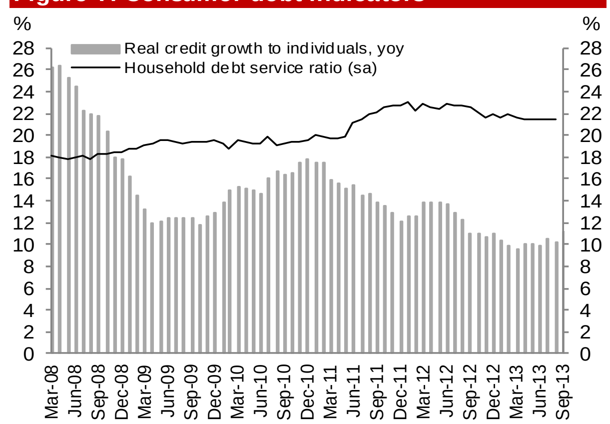
Source: Central Bank; BTMU Economic Research.

Figure 6: Household debt service ratio



Source: Central Bank; BTMU Economic Research.

Figure 7: Consumer debt indicators



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For historical data and commentary following BTMU's Economic News Releases, see our website at: https://reports.us.bk.mufg.jp/portal/site.