US bank lending falls at fastest rate in history

Bank lending in the US has contracted so far this year at the fastest rate in recorded history, raising concerns that the Federal Reserve may have jumped the gun by withdrawing emergency stimulus.

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Published: 8:43PM GMT 17 Feb 2010

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David Rosenberg from Gluskin Sheff said lending has fallen by over $100bn (£63.8bn) since January, plummeting at an annual rate of 16pc. "Since the credit crisis began, $740bn of bank credit has evaporated. This is a record 10pc decline," he said.

Mr Rosenberg said it is tempting fate for the Fed to turn off the monetary spigot in such circumstances. "The shrinking in banking sector balance sheets renders any talk of an exit strategy premature," he said.

The **M3 broad money supply** – watched by monetarists as a leading indicator of trouble a year ahead – has been contracting at a rate of 5.6pc over the last three months. This signals future deflation. The Fed's "Monetary Multplier" has dropped to a record low of 0.81, evidence that the banking system is still broken.

Tim Congdon from International Monetary Research said demands for higher capital ratios and continued losses from the credit crisis are both causing banks to cut lending. The risk of a double-dip recession – or worse – is growing by the day.

"It is absurdly premature to think of withdrawing stimulus while bank credit is still sliding. To have allowed this monetary collapse to occur a full 18 months after the financial cataclysm is extreme incompetence. They seem to have forgotten that the lesson of the 1930s was the falling quantity of money," he said.

Paul Ashworth, US economist for Capital Economics, said that certain Fed officials are clearly worried about lending since they slipped in a warning that bank credit "continues to contract" in their latest statement.

However, regional Fed "hawks" appear to have gained the upper hand. This has echoes of mid-2008 when the Fed talked of tightening, arguably setting off the chain of events that led to the collapse of Lehman Brothers later that year. China has also been calling for a halt to QE, accusing Washington of "monetizing" its deficit in a stealth default on Treasury bonds.

The bank has already wound up its main liquidity operations. Concerns that the Fed may soon reverse quantitative easing altogether have caused a sharp rise in credit spreads in recent weeks.

Fed chair Ben Bernanke first made his name as an expert on the "credit channel" causes of slumps. It is unclear why he has been so relaxed about declining bank loans this time.

"The reason the Great Depression became 'great' was the contraction of credit. You would have thought that a student of the Depression like Bernanke would be alarmed by this," said Mr Ashworth.

http://www.telegraph.co.uk/finance/economics/7259323/US-bank-lending-falls-at-fastest-rate-in-history.html