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# Looser lending standards: So far, so good... - by Daniel Calano

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Money is flowing, and easier to get than ever. Equity is coming from overseas, from institutional investors and now from more “non-bank” financial institutions. Partially as a result, U.S. household debt has risen steadily for 18 consecutive quarters, and is 21% higher than during the Great Recession. U.S. banks are loosening lending policies, and foreign banks are following suit, according to a recent survey from the Federal Reserve Board. It’s been happening for a while, as a growing reaction to the stricter lending policies that followed the 2008 housing market crash. Is it a good thing, or another puff of air into an ominous potential bubble?

The Federal Reserve has eased some lending rules in order to provide opportunities to smaller community banks. The changes proposed were complicated, but the Federal Reserve vice-chair argued that they “expect that their proposal would meaningfully reduce the compliance burden for community banking organizations…”

According to the Federal Reserve survey, the most significant reason that banks are allowed to loosen is competition from non-bank lenders. Essentially “regular banks” have to compete with an ever-expanding lending market that does not have to adhere to stringent rules. The new non-bank lenders have less regulation, can take greater risks, and as a result can charge more interest in pursuing a segment that may not have as good credit. Subprime lending? Sound familiar?

Read the positive rationalization that comes along with this: Loose lending allows for more consumer spending. It helps entrepreneurs and small business owners to expand their enterprise, creating more wealth in the local economy. Loose lending can help reduce the gap between wealth and wages. With more access to capital, people can start businesses and presumably improve their lives. Once again, all sound familiar?

Of course there is a downside that we have witnessed in several recessions. First, loose lending can obviously create more delinquencies. The news is recently full of stories of increasing auto loan delinquencies, student loan delinquencies, some mortgage delinquencies. Loose lending can also foster predatory lending. Back in one real estate recession, we used to call it “loan to own”, where loose lenders made borrowing easy, but at higher rates, and when properties went into technical default, usually missing loan to value targets, predatory lenders could foreclose.

It is hard to argue that loose lending is creating any major problems yet. In reviewing the top issues affecting real estate for this calendar year, reports have sited the top few as interest rates, political uncertainty, housing affordability. Looser lending clearly addresses the first related to interest rates and lending. Not increasing rates, and making capital more available has put yet another boost into the economy. Political uncertainty is in the news, but the administration is clearly making inroads in improving this situation. While our President may take most of the credit, much of it is actually foreign leaders and foreign money wanting to be on the “good side” of the United States. The dollar continues to be strong and increasing in value, and countries around the world want to own it.

We could go on about the other beneficial fallout for increasing capital flow, but the arguments for doing so, while just as true as in the past, can also cause problems. It is a modest manipulation of the economy. While it may not be significant to the world’s economy, the issue that there are growing delinquencies in smaller loans like cars, student debt, small mortgages, is certainly worth watching. Let’s hope it’s as manageable as the Federal Reserve Board says.

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