

# Phoenix Management Services “Lending Climate in America” Survey



**4<sup>th</sup> Quarter 2019  
Summary, Trends and Implications**

PHOENIX  
"LENDING CLIMATE IN AMERICA"

4<sup>th</sup> Quarter 2019

SUMMARY, TRENDS AND IMPLICATIONS

- 1. The housing rebound that began in the spring continues, supported by low mortgage rates, solid job growth, and a reduction in new home inventory. Builders are being encouraged by one of the most attractive periods for house-hunters in many years. How much longer do you believe this growth period will continue?**

Garnering the highest percentage of responses (63%), were lenders that believe despite the housing rebound that began in spring 2019, growth will halt in 2020 and home builders will begin to see a decline. Thirty-seven percent of the lenders surveyed believe growth will continue through 2021.

- 2. U.S. retail sales fell for the first time in seven months in September. The sudden pullback in spending suggests the economy is softer than initially believed, amid concerns the U.S.-China trade war -- and the hundreds of billions of dollars of tariffs -- are beginning to weigh on recession-weary American consumers. As the holiday season picks-up, what do you expect to happen to retail sales?**

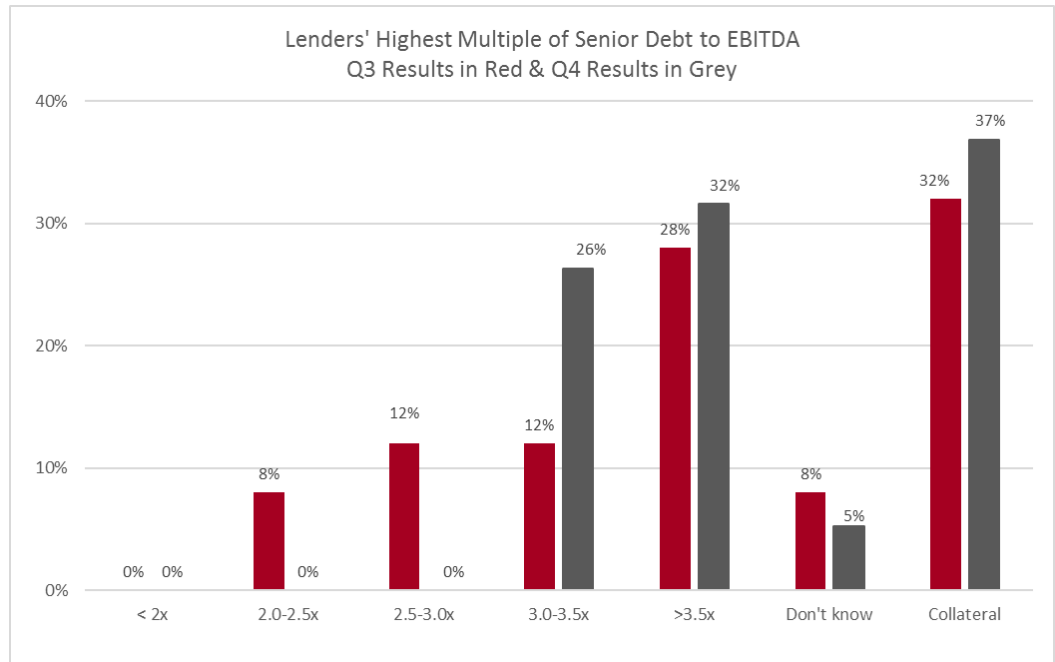
The answer that received the highest percentage response, 47%, were the lenders that expect consumer sales will stay consistent with recent spending trends as the holiday season picks-up. Of the lenders surveyed, 32% expect retail sales will bounce back and be greater than the 2018 holiday season, while 21% expect consumers, concerned with near-term recessionary pressures, will spend less than the 2018 holiday season.

- 3. Which of the below do you expect to be the largest headwind to lending in Q4 2019?**

Lenders garnering 37% of responses expect the effects of the trade-war will be the largest headwind to lending in Q4 2019, while 31% believe overall economic uncertainty will be that largest headwind to lending in Q4 2019. Of the lenders surveyed, 16% believe tightening borrow requirements/standards will be the largest headwind to lending in Q4 2019. In addition, 16% of lenders don't expect any of the above to have significant impact on lending in Q4.

- 4. Lenders increased their highwater leverage multiples this quarter.**

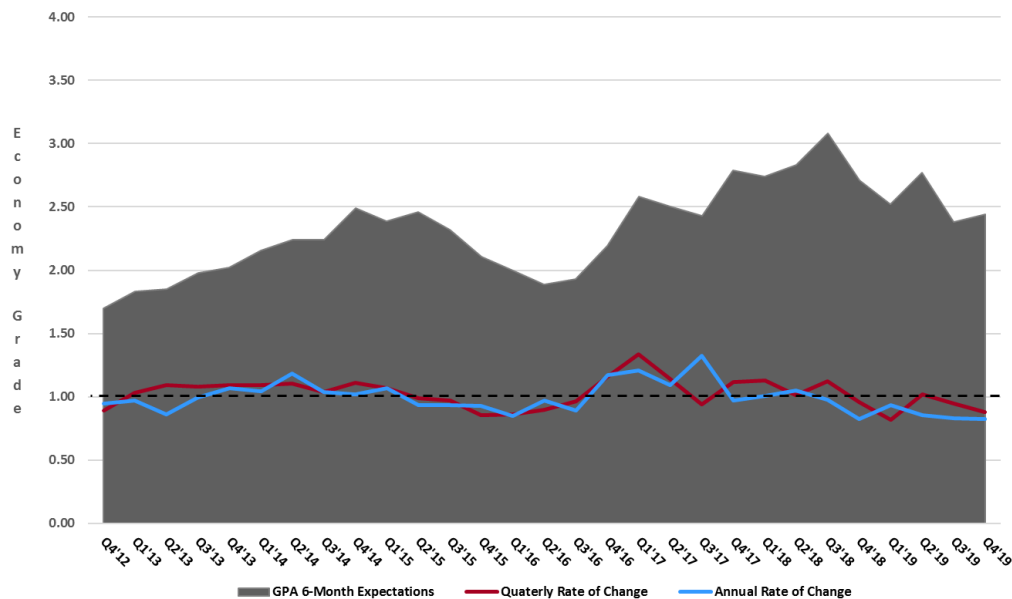
Leverage multiples shifted in Q4 2019 with 32% of lenders indicating that the >3.5x range would be the highest EBITDA ratio they would consider versus 28% in Q3 2019. The percentage of respondents who would consider a debt to EBITDA ratio of 3.0-3.5x increased to 26% from the previous quarter's results of 12%. Thirty-seven percent of lenders responded that they were collateral lenders and therefore do not make decisions based on cash flow/leverage multiples.



## 5. Long-term economic performance expectations decreased in this quarter's survey.

Lenders optimism in the U.S. economy for the near-term increased this quarter to a GPA of 2.44 from the Q3 2019 results of 2.38. 44% of the lenders believe the economy will perform at a “B” level over the next six months, compared to 46% in the previous survey. Of the lenders surveyed, 56% expect the U.S. economy to perform at a “C” grade, compared to 46% in the previous survey, and none of the lenders surveyed believe that the economy will perform at a “D” level, compared to 8% in Q3 2019.

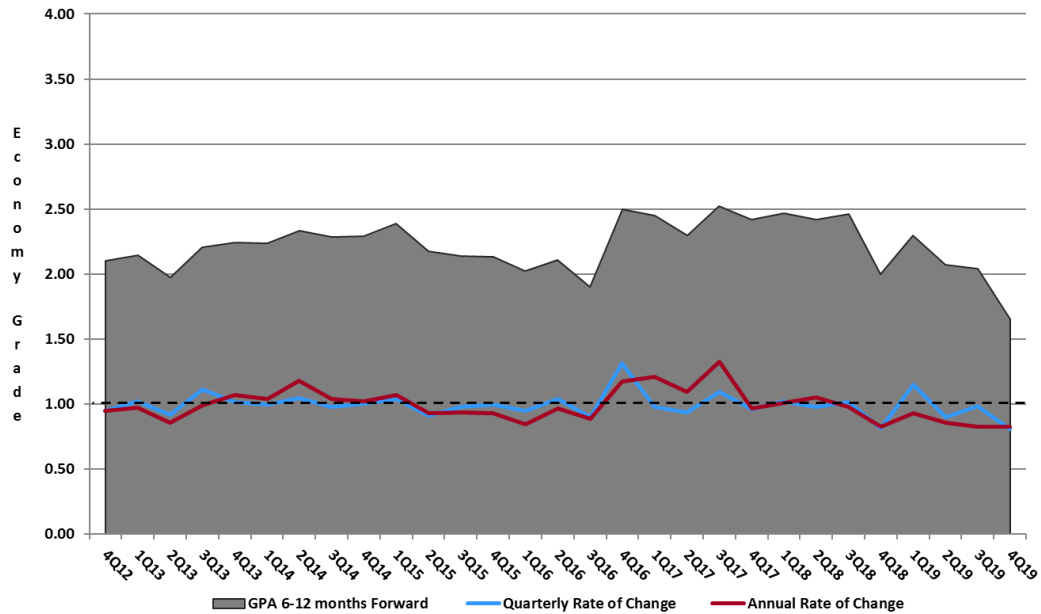
### Lender Expectations for Economy (Forward Six Months) 4.0=A, 2.0=C. 0.0=F



\* Rate of Change of 1.0 is at equilibrium and signifies “no change” from the corresponding prior period of comparison.

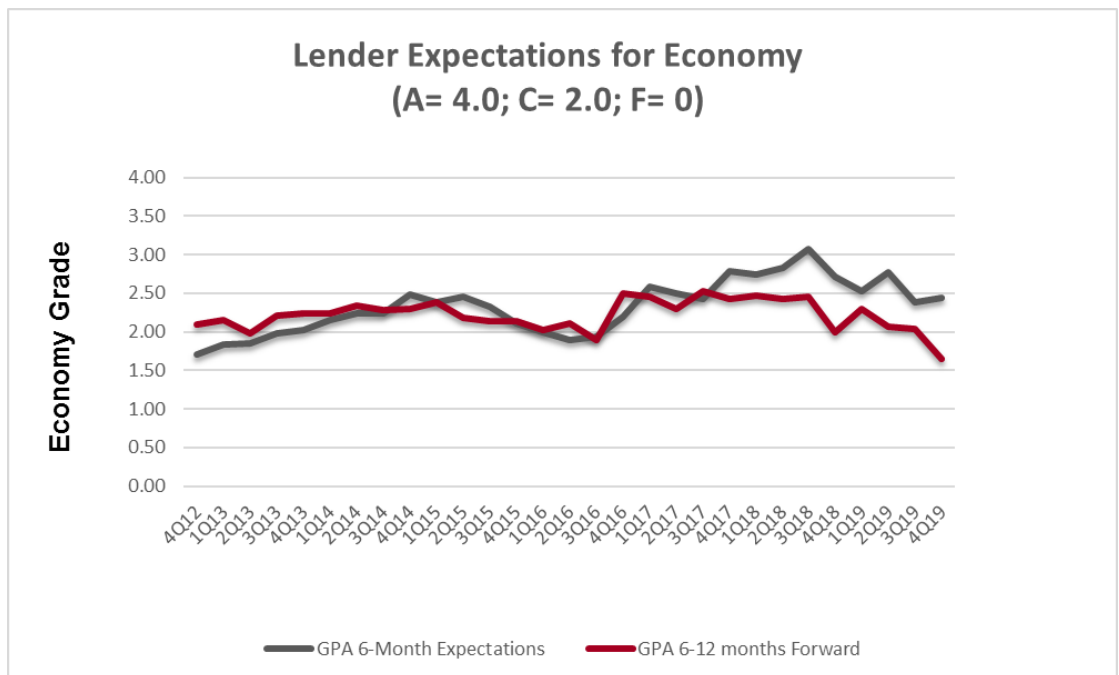
Lenders growth expectations for the U.S. economy beyond six months significantly decreased this quarter. The weighted average decreased to a 1.65 GPA from 2.04 in the previous quarter. 6% of lenders believe the economy will perform at a “B” level in the next six to twelve months which represents a decrease of 27-percentage points from the Q3 2019 results of 33%. The percent of lenders (59%) that believe the economy will perform at a “C” level increased 21-percentage points from Q3 2019. The lenders who believe the economy will perform at a “D” over the next twelve months remained unchanged, while 6% believe the economy will perform at a “F”.

**Lender Expectations for Economy ( Forward Six-Twelve Months)**  
4.0=A, 2.0=C, 0.0=F



\* Rate of Change of 1.0 is at equilibrium and signifies “no change” from the corresponding prior period of comparison.

The Q4 2019 survey continues the trend of a higher near-term GPA than long-term GPA. Lenders are becoming increasingly pessimistic about the U.S. economy in long-term.



**Phoenix Management Services**  
**“Lending Climate in America”**  
**4<sup>th</sup> Quarter 2019**

**Survey Results**

**1. The majority of lenders believe the housing rebound that began in spring will halt in 2020 and home builders will begin to see a decline in growth.**

Lenders were asked: The housing rebound that began in the spring continues, supported by low mortgage rates, solid job growth and a reduction in new home inventory. Builders are being encouraged by one of the most attractive periods for house-hunters in many years. How much longer do you believe this growth period will continue?

Growth will halt in 2020 and home builders will begin to see a decline	63%
It will continue to grow through 2021	37%

**2. The majority of lenders expect that despite the current trade war consumers will stay consistent with recent spending trends as the holiday season picks-up.**

Lenders were asked: U.S. retail sales fell for the first time in seven months in September. The sudden pullback in spending suggests the economy is softer than initially believed, amid concerns the U.S.-China trade war -- and the hundreds of billions of dollars of tariffs -- are beginning to weigh on recession-weary American consumers. As the holiday season picks-up, what do you expect to happen to retail sales?

Consumer sales will stay consistent with recent spending trends	47%
Retail sales will bounce back and be greater than the 2018 holiday season	32%
Consumers, concerned with near-term recessionary pressures, will spend less than the 2018 holiday season	21%

**3. The majority of lenders believe the effects of the trade-war will be the largest headwind to lending in Q4 2019.**

Lenders were asked: Which of the below do you expect to be the largest headwind to lending in Q4 2019?

Effects of the trade-war	37%
Overall economic uncertainty	31%
Tightening borrowing requirements / standards	16%
I do not expect any of the above to have a significant impact lending in Q4 2019	16%

#### 4. Highest Senior Debt to EBITDA Leverage Institutions Would Consider

Respondents were asked the highest multiple of Senior Debt to EBITDA their financial institution would consider with regard to a loan request.

<u>EBITDA Level</u>	<u>3Q 2019</u>	<u>4Q 2019</u>
Greater than 3.5x	28%	32%
Between 3.01x and 3.50x	12%	26%
Between 2.51x and 3.00x	12%	0%
Between 2.01x and 2.50x	8%	0%
Less than 2.0x	0%	0%
Collateral lenders	32%	37%
N/A	8%	5%

#### 5. Anticipated Change in Senior Debt to EBITDA Multiple

Respondents were asked, over the next six months, how the Senior Debt to EBITDA multiple would change at their financial institution.

<u>Change in Senior Debt to EBITDA Level</u>	<u>3Q 2019</u>	<u>4Q 2019</u>
Increase greater than 0.5x	0%	0%
Increase less than 0.5x	12%	0%
Decrease less than 0.5x	12%	6%
Decrease greater than 0.5x	0%	5%
No change	36%	42%
Collateral lenders	24%	37%
N/A	16%	10%

#### 6. Factors with Strongest Potential to Affect Near-Term Economy

Respondents were asked, over the next six months, which two factors had the strongest potential to affect the economy.

<u>Factors Affecting Near-Term Economy</u>	<u>3Q 2019</u>	<u>4Q 2019</u>
Stability of Stock Market	56%	50%
Constrained Liquidity in Capital Markets	32%	44%
Sluggish Housing Market	8%	39%
Other	40%	33%
U.S. Budget Deficit	20%	22%
Unstable Energy Prices	28%	5%

#### 7. Industries Expected to Experience Greatest Volatility

Respondents were asked, over the next six months, which industries will experience the most volatility (i.e. Chapter 11 filings, mergers and acquisitions, declining profits, etc.). Respondents were asked to select the top three industries.

<u>Industries Experiencing Most Volatility</u>	<u>3Q 2019</u>	<u>4Q 2019</u>
Retail Trade	67%	83%
Healthcare and Social Assistance	33%	39%
Construction	29%	28%
Agriculture, Forestry, Fishing, and Hunting	17%	28%
Manufacturing	58%	22%
Mining	17%	22%
Real Estate and Rental/Leasing	17%	17%

## 8. Customers' Plans in the Next Six to Twelve Months

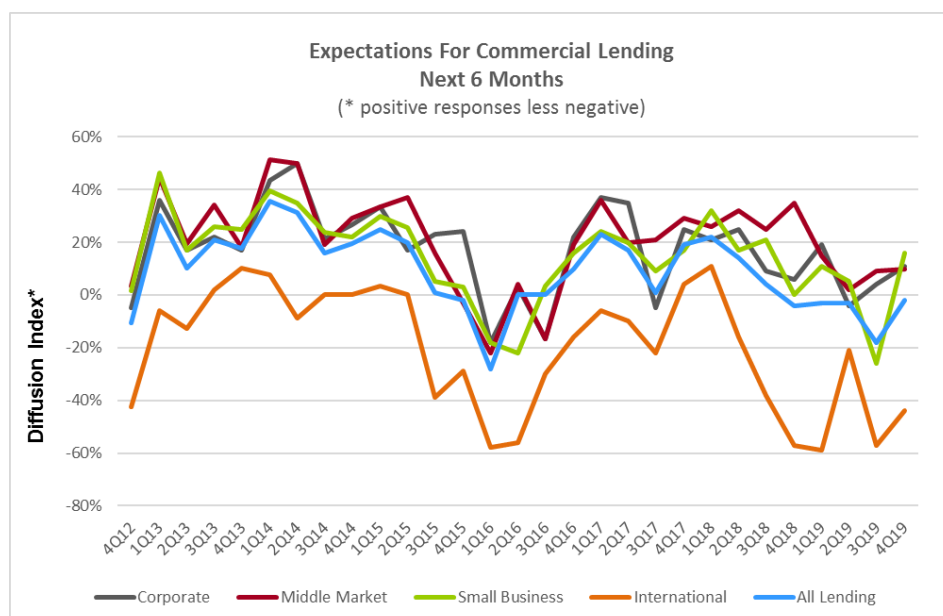
Respondents were asked which of the following actions their customers planned in the next six to twelve months. Lenders were asked to designate all potential customer actions that applied.

<u>Customers' Plans</u>	<u>3Q 2019</u>	<u>4Q 2019</u>
Making an Acquisition	35%	50%
Raising Additional Capital	35%	50%
Capital Improvements	52%	39%
Introducing New Products or Services	52%	33%
Entering New Markets	39%	33%
Hiring New Employees	30%	33%
"Other" Initiatives	9%	0%

## 9. Economic Indicators

Respondents were asked whether they expected the following economic indicators to be up, down, or remain the same over the next six months.

- In Q4 2019, lenders optimism increased in large corporate (11%) and middle market (10%), and small business saw a significant increase (16%). Expectations for international lending also slightly increased in Q4 2019 with a diffusion index of -44%, a 13-percentage point difference from the previous quarter of -57%. The diffusion index for the average for all lending increased to -2% from -18% in Q3 2019.



	<u>3Q/2019</u>					<u>4Q/2019</u>			
	<u>Up</u>	<u>Down</u>	<u>Same</u>	<u>Diffusion Index</u>		<u>Up</u>	<u>Down</u>	<u>Same</u>	<u>Diffusion Index</u>
Corporate Lending	13%	9%	78%	4%	Corporate Lending	11%	0%	89%	11%
Middle Market Lending	26%	17%	57%	9%	Middle Market Lending	16%	6%	78%	10%
Small Business Lending	22%	48%	30%	-26%	Small Business Lending	22%	6%	72%	16%
International Lending	0%	57%	43%	-57%	International Lending	0%	44%	56%	-44%

- The unemployment diffusion index decreased to 3% in Q4 2019 compared to 18% in Q3 2019. In addition, the loan losses diffusion index decreased 56% compared to 66% in Q3 2019, and the interest rate diffusion index decreased from a -26% in Q3 2019 to -11%.

	<u>3Q/2019</u>					<u>4Q/2019</u>			
	<u>Up</u>	<u>Down</u>	<u>Same</u>	<u>Diffusion Index</u>		<u>Up</u>	<u>Down</u>	<u>Same</u>	<u>Diffusion Index</u>
Loan Losses	70%	4%	26%	66%	Loan Losses	56%	0%	44%	56%
Bankruptcies	61%	0%	39%	61%	Bankruptcies	61%	0%	39%	61%
Interest Rates	22%	48%	30%	-26%	Interest Rates	11%	22%	67%	-11%
Unemployment	22%	8%	70%	18%	Unemployment	17%	0%	83%	3%
Bank Failures	9%	9%	82%	0%	Bank Failures	6%	0%	94%	6%

## 10. U.S. Economy Grade – Next Six Months

Respondents were asked how they expected the U.S. economy to perform during the next six months on a grading scale of A through F.

- Lenders optimism on the U.S. economy slightly increased 6 points this quarter from 2.38 in Q3 2019 to 2.44 in Q4 2019. In the current quarter, 44% of respondents believe the economy will perform at a “B” level, which represents a decrease of 2 points from the previous quarter. Of the lenders surveyed, 56% believe the economy will perform at a “C” level which represents an increase of 10 points from the previous quarter. There was a decrease of lenders (0%) that believe the economy will perform at a “D” level from the 8% in Q3 2019.

<u>Grade</u>	<u>3Q/2019</u>	<u>4Q/2019</u>
A	0%	0%
B	46%	44%
C	46%	56%
D	8%	0%
F	0%	0%
Weighted Average Grade	2.38	2.44



## 11. U.S. Economy Grade – Beyond the Next Six Months

Respondents were asked how they expected the U.S. economy to perform beyond the next six months on a grading scale of A through F.

- Lenders expectations for the U.S. economy's performance in the longer term significantly decreased from the prior quarter. The weighted average GPA decreased 39 points from a 2.04 in the Q3 2019 to 1.65 in Q4 2019. Of the lenders surveyed, 59% feel as though the U.S. economy will perform at a "C" level beyond the next six months, while 6% expect the economy to perform at a "B" level, a decrease of 27 percentage points from Q3 2019. The lenders who believe the economy will perform at a "D" over the next twelve months remained unchanged, while 6% believe the economy will perform at a "F".

<u>Grade</u>	<u>3Q/2019</u>	<u>4Q/2019</u>
A	0%	0%
B	33%	6%
C	38%	59%
D	29%	29%
F	0%	6%
Weighted Average Grade	2.04	1.65

## 12. Customers' Future Growth Expectations

Lenders assessed their customers' growth expectations for the next six months to a year.

- The percentage of respondents indicating their customers have "moderate" growth expectations for the next six months to one year decreased 5 percentage points to 65%. In Q4 2019, 12% of lenders ascribe "strong" growth for their borrower's in the next six months, a 5-percentage point decrease from Q3 2019, and 17% of lenders ascribe to "no growth", a 4-percentage point increase from the previous quarter.

<u>Indication</u>	<u>3Q/2019</u>	<u>4Q/2019</u>
Very Strong	0%	6%
Strong	17%	12%
Moderate	70%	65%
No Growth	13%	17%

## 13. Loan Structure

Respondents were asked whether their financial institutions planned to tighten, relax, or maintain their loan structures (collateral requirements, guarantees, advance rates, loan covenants, etc.) in each of four different-sized loan categories.

Many lenders are content right now and plan to maintain their current loan structure. However, in Q4 2019 we did see a slight decrease (12%) of lenders that plan to tighten their loan structure.

	<u>3Q/2019</u>			<u>4Q/2019</u>		
	<u>Tighten</u>	<u>Maintain</u>	<u>Relax</u>	<u>Tighten</u>	<u>Maintain</u>	<u>Relax</u>
Loans > \$25 million	25%	70%	5%	6%	94%	0%
\$15 – 25 million	30%	65%	5%	6%	94%	0%
\$5-15 million	25%	70%	5%	18%	82%	0%
Under \$5 million	26%	63%	11%	17%	77%	6%
Overall Average	27%	67%	6%	12%	87%	1%

#### 14. Interest Rate Spread

Lenders were asked whether their financial institutions planned to reduce, maintain or increase their interest rate spreads and fee structures on similar credit quality loans.

A majority of lenders (74%) continue to maintain their interest rate spreads and fee structures. In Q4 2019, the percentage of lenders that plan to reduce their interest rate spreads increased to 11%, and there was a 4-percentage point decrease (15%) that plan to increase their interest rate spreads.

	<u>3Q/2019</u>			<u>4Q/2019</u>		
	<u>Reduce</u>	<u>Maintain</u>	<u>Increase</u>	<u>Reduce</u>	<u>Maintain</u>	<u>Increase</u>
Loans > \$25 million	10%	80%	10%	13%	81%	6%
\$15 – 25 million	15%	70%	15%	13%	75%	12%
\$5-15 million	5%	74%	21%	12%	69%	19%
Under \$5 million	5%	63%	32%	6%	72%	22%
Overall Average	9%	72%	19%	11%	74%	15%

#### 15. The Fed and Interest Rates

Respondents were asked in what direction they thought the Fed would move interest rates and by how much in the coming six months.

55% of respondents in Q4 2019 believe the Fed will lower interest rates in the next six months. Of the lenders surveyed, 44% of respondents favor a decrease of -1/4 point, and 11% of respondents surveyed believe interest rates believe the Fed will decrease interest rates by -1/2 point or more.

<u>Bps Change</u>	<u>3Q/2019</u>	<u>4Q/2019</u>
+ 1/2 point or more	0%	0%
+ 1/4 point	15%	0%
Unchanged	10%	45%
- 1/4 point	20%	44%
- 1/2 point or more	55%	11%
Weighted Average	-0.30 bps	-0.17 bps

## 16. Current Competition

Respondents were asked to identify the segment of the industry from which they were experiencing the most competition.

- Regional Banks and Commercial Finance Co. placed at the top of the survey, garnering 33% of responses. Local Community/Commercial Banks, at 17% of respondents, saw an decrease of 7 percentage points, and Money Center Banks saw a increase with 6% of respondents.

	<u>3Q/2019</u>	<u>4Q/2019</u>
Regional Bank	48%	33%
Commercial Finance Co.	14%	33%
Local Community/Commercial Bank	24%	17%
Other	14%	11%
Money Center Banks	0%	6%
Factors	0%	0%