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The Two Faces of Cross-Border Banking Flows

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Question, Method, Findings

- How do global and host-country conditions affect cross-border flows **within vs. between** banks ?
- BIS Locational Banking Statistics for 1998-2011
 - liabilities of 25 reporting banking systems towards foreign banks
 - intra-group vs. between group
 - resident vs. national banks
- Intra-group banking flows
 - react less to global and local macro conditions than interbank flows
 - react more to profitability of host country banking sector
 - provide ‘liquidity insurance’ during the financial crisis

Policy relevance

EBCI | Vienna Initiative



**Supervisory guidance on the
strengthening of the sustainability of the business models
of large internationally active Austrian banks**

14 March 2012

What would we expect ?

- Foreign portfolio investment vs. FDI
 - Information asymmetries imply larger volatility of external vs. internal financing (Goldstein & Razin, JIE 2006)
- Interbank market freezes and creditor runs
 - Information asymmetries and coordination failures in the interbank market (Liu, RFS 2016)
- Internal capital markets and resource allocation
 - Authority & information (Stein, JF 1997)
 - Managerial incentives & rent-seeking (Sharfstein & Stein, JF 2000)

Internal capital markets in international banks ?

- What flows should we study in banking groups ?
 - allocation of loanable funds
 - allocation of economic / regulatory capital
- Group members generate own funds / capital
 - local deposits provide loanable funds
 - retained earnings provide economic capital
- Are banks' internal capital market flows proactive ?
 - or are they just a residual which close the gap between local funding and investment opportunities ?

Internal capital markets in banking groups: Evidence

- Domestic banking groups
 - deposit smoothing (Cremers et al., RFS 2011)
 - liquidity shocks are ‘exported’ (Gilje et al., 2015)
- International banking groups
 - lending goals and funding allocation (De Haas & Kirschenmann 2014)
 - local funding and investment opportunities matter for reaction to liquidity shocks (Cetorelli and Goldberg, JIE 2012)

Data to study banks' internal capital markets ?

- Bank-level rather than country-level
 - different banks have different ICM strategies
 - role of host countries varies across banks
- Information type of exposure
 - Debt vs. equity
 - Contract type (on-balance / off-balance, maturity, currency)
- Exogenous shocks
 - Bank funding (Gilje et al. 2015)
 - Investment opportunities (Giroud, QJE 2013)

Data availability

Banks located in Austria

Positions reported by banking offices located in the specified country regardless of the nationality of the controlling parent, in millions of US dollars

Table A5

	Claims			Liabilities		
	Adjusted changes		Outstanding	Adjusted changes		Outstanding
	Q3 15	Q4 15	Q4 15	Q3 15	Q4 15	Q4 15
Cross-border positions	1,467	-9,051	261,780	-4,578	-4,625	171,794
By sector of counterparty						
Banks	2,084	-9,129	114,796	-2,633	-2,731	58,292
Of which: intragroup	3,295	-3,713	6,895	550	227	8,252
Non-banks	-617	78	146,984	-351	-1,155	50,318

Austrian banks

Positions reported by banking offices located in LBS-reporting countries and controlled by parents of the specified nationality, in millions of US dollars

Table A7

	Claims			Liabilities		
	Adjusted changes		Outstanding	Adjusted changes		Outstanding
	Q3 15	Q4 15	Q4 15	Q3 15	Q4 15	Q4 15
Cross-border positions	-924	-7,109	163,810	-3,552	-5,029	133,775
By sector of counterparty						
Banks	400	-4,772	71,679	-2,045	-3,114	41,003
Of which: intragroup	3,516	-3,556	17,334	279	-8	6,602
Non-banks	-1,325	-2,336	92,131	-519	-1,024	36,363

Conclusion

- Intra-group banking flow data helps us further understand aggregate international financial flows:
 - type / proximity of lender / investor and counterparty / investee
 - compare with non-bank exposures
 - look at a broader set of host countries (liabilities to reporting countries)
 - look at currency breakdown ?
 - exploit (now available?) data on bilateral exposures
- The data seems less suited to study international banks' use of internal capital markets
 - resort to annual report data (Allen et al. 2013)