Gregory D Sutton

+41 61 280 8421
greg.sutton@bis.org

3. The international debt securities market

The slowdown in the international debt securities market that had begun in June continued into the third quarter of 2002. Net issuance was only $183 billion (Table 3.1), 47% below the previous quarter's amount. It was the

Main features of net issuance in international debt securities markets

In billions of US dollars

	2000	2001	2001		2002			Stocks at end-Sep 2002
	Year	Year	Q3	Q4	Q1	Q2	Q3	
Total net issues	1,237.3	1,348.8	224.8	339.4	309.4	344.5	182.7	8,777.4
Money market instruments[1]	152.1	–78.9	–45.6	–9.3	–7.8	8.3	10.4	433.1
Commercial paper	*55.2*	*26.9*	*–12.0*	*6.5*	*5.5*	*1.8*	*19.2*	*285.2*
Bonds and notes[1]	1,085.2	1,427.6	270.4	348.8	317.3	336.2	172.3	8,344.3
Floating rate issues	*354.6*	*391.6*	*93.8*	*95.9*	*60.4*	*74.5*	*30.9*	*2,097.4*
Straight fixed rate issues	*713.9*	*996.4*	*170.5*	*237.5*	*253.5*	*247.8*	*144.7*	*5,942.0*
Equity-related issues	*16.7*	*39.7*	*6.2*	*15.3*	*3.3*	*13.8*	*–3.3*	*304.9*
Advanced economies	1,156.7	1,260.7	210.3	324.2	285.3	326.5	166.5	7,712.2
United States	*464.5*	*597.6*	*114.3*	*137.3*	*138.1*	*116.7*	*36.9*	*2,670.2*
Euro area	*558.0*	*551.2*	*87.4*	*149.0*	*128.4*	*152.7*	*91.4*	*3,326.7*
Japan	*–25.8*	*–10.1*	*–6.5*	*–1.8*	*–10.1*	*3.2*	*–6.5*	*261.6*
Offshore centres	15.7	26.4	5.4	5.8	4.4	–0.2	1.6	104.3
Emerging economies	42.1	45.4	–2.0	8.2	11.7	11.4	5.1	532.2
International organisations	22.9	16.3	11.1	1.3	8.0	6.8	9.6	428.7
Private sector	968.9	1,009.0	156.0	256.2	192.6	286.9	121.4	6,564.2
Financial institutions[2]	*796.4*	*799.5*	*133.2*	*196.4*	*178.2*	*243.8*	*120.5*	*5,338.3*
Corporate issuers	*172.5*	*209.5*	*22.8*	*59.8*	*14.3*	*43.0*	*0.9*	*1,225.8*
Public sector[3]	245.5	323.5	57.7	82.0	108.9	50.9	51.7	1,784.5
Central government	*52.6*	*60.5*	*–2.3*	*11.6*	*45.1*	*7.6*	*7.5*	*632.4*
State agencies and other	*192.9*	*263.0*	*60.0*	*70.4*	*63.8*	*43.3*	*44.2*	*1,152.1*
Memo: Domestic CP[4]	*256.8*	*–140.0*	*–49.8*	*30.5*	*–71.1*	*–65.1*	*–10.4*	*1,803.0*
of which: US	*208.3*	*–161.2*	*–58.5*	*28.3*	*–63.3*	*–57.0*	*0.2*	*1,320.8*

[1] Excluding notes issued by non-residents in the domestic market. [2] Commercial banks and other financial institutions. [3] Excluding international organisations. [4] Data for the third quarter of 2002 are partly estimated.

Sources: Bank of England; Dealogic; Euroclear; ISMA; Thomson Financial Securities Data; national authorities; BIS.

Table 3.1

Gross issuance in the international bond and note markets

In billions of US dollars

	2000	2001	2001		2002		
	Year	Year	Q3	Q4	Q1	Q2	Q3
Total announced issues	1,703.4	2,306.5	465.8	554.1	606.4	571.2	453.1
Floating rate issues	518.2	643.6	157.1	168.7	141.9	159.7	151.9
Straight fixed rate issues	1,128.7	1,590.7	297.6	359.1	454.8	390.3	296.4
Equity-related issues[1]	56.5	72.2	11.1	26.3	9.6	21.2	4.8
US dollar	791.8	1,131.9	247.0	243.6	310.8	258.4	207.5
Euro	581.7	841.9	145.7	221.3	228.4	229.5	169.1
Yen	128.7	125.3	32.5	26.2	16.4	25.7	23.5
Other currencies	201.2	207.5	40.6	62.9	50.9	57.6	53.0
Private sector	1,319.4	1,683.1	327.0	425.2	416.8	428.6	324.3
Financial institutions[2]	*1,087.2*	*1,335.4*	*276.0*	*325.8*	*353.3*	*353.9*	*289.7*
Corporate issuers	*232.2*	*347.7*	*51.0*	*99.4*	*63.6*	*74.7*	*34.6*
Public sector	314.8	548.6	118.7	114.1	163.6	122.2	107.6
Central government	*92.9*	*130.8*	*13.4*	*17.9*	*59.3*	*29.8*	*13.0*
State agencies and other	*221.9*	*417.9*	*105.3*	*96.3*	*104.3*	*92.4*	*94.7*
International organisations	69.2	74.8	20.1	14.8	26.0	20.5	21.2
Completed issues	1,705.1	2,306.3	478.1	568.4	587.9	579.2	441.6
Memo: Repayments	*620.0*	*878.7*	*207.7*	*219.6*	*270.6*	*243.0*	*269.2*

[1] Convertible bonds and bonds with equity warrants. [2] Commercial banks and other financial institutions.

Sources: Bank of England; Dealogic; Euroclear; ISMA; Thomson Financial Securities Data; BIS. Table 3.2

lowest level since the fourth quarter of 1998, when the Russian financial crisis and the near collapse of LTCM led to a severe reduction of issuance. The decline affected advanced as well as emerging economies, with a particularly sharp fall in net issuance by entities based in the United States. Both a decline in gross issuance and a rise in repayments (Table 3.2) contributed to the reduction in net borrowing.

The decline in net issuance was accompanied by a widening of credit spreads, which suggests that fund-raising fell in part because investors were less willing to supply funds, a situation that was already becoming apparent towards the end of the second quarter. There is evidence that financial institutions in particular had difficulty raising funds. Financial institutions across the globe reduced their presence in the international debt securities market during the third quarter. This raises the question of whether reduced access to debt markets during the third quarter prevented borrowers from obtaining adequate funding, especially following previous difficulties in the commercial paper and bank loan markets.

Private sector issuance falls sharply

Net issuance by borrowers in advanced economies in the international debt securities market fell sharply between the second and third quarters of 2002. In

Largest quarterly declines in private sector net issuance

Since 1994, in billions of US dollars and percentages

Date	In absolute terms	Date	In percentage terms
1998 Q3	–63.6	1994 Q2	–49.57
1999 Q4	–109.0	1997 Q4	–39.06
2001 Q3	–113.3	1998 Q4	–49.76
2002 Q1	–63.6	2001 Q3	–42.06
2002 Q3	–165.4	2002 Q3	–57.67

Sources: Bank of England; Dealogic; Euroclear; ISMA; Thomson Financial Securities Data; national authorities; BIS. Table 3.3

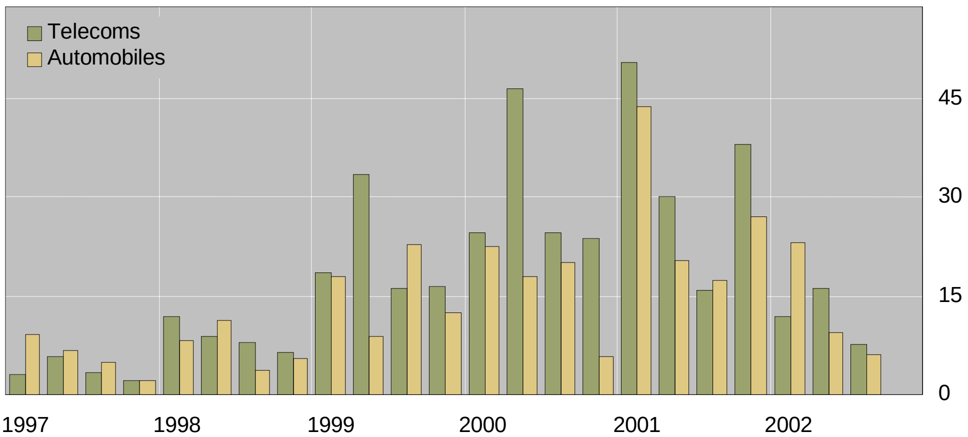
absolute terms, the decline, from $327 billion to $167 billion, was the largest ever recorded. Net issuance by US borrowers fell to $37 billion, 32% of the amount in the second quarter and 27% of that in the first. Net issuance by euro area borrowers also fell sharply between the second and third quarters, down 40% to $91 billion. Repayments by Japanese borrowers actually exceeded issuance over the same period, with net issuance declining from $3.2 billion to –$6.5 billion.

A sharp fall in private sector borrowing ...

The decline in net issuance across the advanced economies can be traced to reduced private sector borrowing in the international debt securities market. For the third quarter, total private sector borrowing amounted to $121 billion, $165 billion less than in the second quarter (Table 3.3). In absolute terms, the decline well exceeded previous contractions in private sector net issuance and stands in sharp contrast to the upsurge in private sector borrowing that occurred between the first and second quarters of this year. Of the most recent decline, 95% is due to reduced private sector borrowing in the advanced economies. Net issuance in the international debt

Announced bond issuance[1] by selected industry sectors

International issuance, in billions of US dollars



[1] Includes bonds issued under EMTN documentation.

Sources: Dealogic; BIS. Graph 3.1

Net issuance of international debt securities by region and currency[1]								
In billions of US dollars								
Region/currency		2000	2001	2001		2002		
		Year	Year	Q3	Q4	Q1	Q2	Q3
North America	US dollar	377.5	526.4	105.9	121.0	126.3	93.3	37.7
	Euro	44.4	64.7	7.1	21.3	17.7	15.1	7.2
	Yen	17.2	17.5	6.7	1.8	–3.5	1.7	–1.8
	Other currencies	17.3	8.3	–1.0	0.7	3.5	6.2	–1.1
Europe	US dollar	169.8	56.1	–0.5	15.4	6.6	43.7	5.6
	Euro	411.0	520.0	79.2	142.1	138.0	133.9	101.7
	Yen	40.4	–1.4	3.9	–2.6	–13.3	–4.7	–6.9
	Other currencies	88.1	71.2	11.9	28.3	17.0	31.2	23.5
Others	US dollar	62.0	70.3	10.9	7.8	23.0	13.4	4.2
	Euro	15.2	12.7	0.3	2.6	2.9	7.2	5.4
	Yen	–20.3	0.6	–1.9	0.9	–12.1	5.9	1.8
	Other currencies	14.9	2.2	2.4	0.1	3.2	–2.3	5.4
Total	US dollar	609.2	652.8	116.2	144.2	155.9	150.4	47.5
	Euro	470.6	597.5	86.5	166.0	158.7	156.2	114.3
	Yen	37.2	16.7	8.7	0.1	–28.9	2.8	–6.8
	Other currencies	120.2	81.8	13.3	29.1	23.7	35.1	27.8

[1] Based on the nationality of the borrower.

Sources: Bank of England; Dealogic; Euroclear; ISMA; Thomson Financial Securities Data; BIS. Table 3.4

securities market by non-financial corporates came almost to a standstill, falling from $43 billion to $1 billion. Reduced issuance by the automobile and telecoms sectors played a role. Total gross announced issuance by firms in these sectors fell in the third quarter of 2002 to the lowest level since the fourth quarter of 1998 (Graph 3.1).

… due mainly to absence of financial institutions

A sharp fall in net issuance by financial institutions made the largest contribution to the decline in private sector borrowing; such borrowing was halved from $244 billion to $121 billion between the second and third quarters. Net borrowing by US financial institutions fell particularly sharply, from $60 billion to $9 billion, after having also declined in the previous quarter. Net issuance by French and Spanish financial institutions in the international debt securities market also fell between the second and third quarters, from $19 billion and $12 billion, respectively, to $2 billion each.

Unsurprisingly, given the large decline in net issuance by US borrowers, net US dollar issuance fell dramatically between the second and third quarters, down 68% to $48 billion (Table 3.4). Net US dollar issuance by European borrowers also fell over the period, from $44 billion to $6 billion. Nevertheless, the period witnessed a number of large US dollar offerings. In addition to several large issues by the US housing agencies, there was a $3 billion issue by the Italian Republic and a $2.75 billion issue by GE Capital.

Credit conditions remain stringent during the third quarter

The continuing slowdown and worsening of credit conditions ...

The fact that declining net issuance in the international debt securities market was accompanied by an increase in credit spreads suggests that a worsening of credit conditions that had begun in June continued into the third quarter. Consistent with this view, gross issuance of non-investment grade securities, which had begun to wane in May, was also quite low during the third quarter (Graph 3.2), and would have been lower still had it not been for two relatively large issues that accounted for 61% of total announcements during the third quarter, a $750 million offering by the Lebanese Republic and a $300 million offering by the Republic of El Salvador. Gross issuance in the investment grade categories fell from $242 billion in the second quarter to $156 billion in the third. The total dollar value of rated bonds issued, $157 billion, was the lowest since the fourth quarter of 1998.

... lead to a sharp fall in straight fixed rate issuance ...

The decline in private sector borrowing was associated with a sharp downturn in straight fixed rate securities issuance. Net issuance of these securities fell by 42% to $145 billion between the second and third quarters; 78% of the decline can be attributed to reduced issuance by financial institutions. Gross announcements of straight fixed rate issues fell from $390 billion to $296 billion over the same period. Nevertheless, the third quarter witnessed the flotation of several large fixed rate issues, including a €5 billion flotation by the European Investment Bank and a $3 billion issue by the Italian Republic.

... and reduced activity of US finance companies

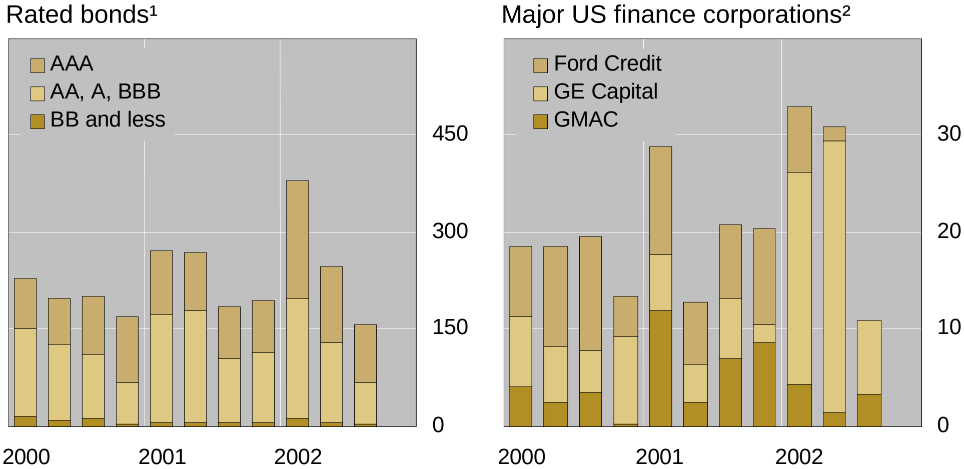
Another potential sign of a worsening of credit conditions, noted in the previous *BIS Quarterly Review*, was the reduced activity of the major US finance companies in the international bond market starting in July 2002. Comprehensive data for the third quarter indicate that this trend continued throughout the period. Gross issuance of bonds and notes by the three major US finance corporations fell to $10.8 billion (Graph 3.2), two thirds of the previous quarter's amount. While this could reflect a reduced desire by these companies to tap the international debt securities market, it is also consistent with the finance companies having greater difficulty raising funds. In some cases, the growing recognition of underfunded pension liabilities may have played a role. Heavy losses on corporate pension plans that had allocated large portions of their portfolios to equity investments led eventually to rating downgrades of some finance companies (see the Overview).

The domestic CP market remains tight

Credit conditions in the domestic commercial paper (CP) market also appear to have remained tight. Between the second and the third quarters of 2002, the stock of domestic CP contracted by $10 billion. This is a much smaller contraction than in previous quarters, but stands in sharp contrast to the generally large positive net issuance of domestic CP in the years preceding the recent market turbulence. For instance, between 1995 and the fourth quarter of 2000, the quarter immediately preceding the beginning of the contraction in the domestic CP market, net quarterly issuance of domestic CP had averaged $55 billion. Negative net issuance by Japanese non-financial corporations accounts for the majority of the most recent contraction in the

Announced issuance by credit rating and issuer

International issuance, in billions of US dollars



[1] Includes bonds issued under EMTN documentation. [2] Bonds and notes.

Sources: Dealogic; Euroclear; Thomson Financial Securities Data; BIS. Graph 3.2

domestic CP market. However, the stock of international CP increased by $19 billion between the second and third quarters.

Emerging market borrowing declines

Reduced borrowing by emerging market countries ...

Net issuance by emerging market borrowers in the international debt securities market fell in the third quarter of 2002. After two quarters above $10 billion, net issuance declined by more than 50% to $5.1 billion, about half the average quarterly net issuance by emerging market borrowers since the onset of the Asian financial crisis. Gross announced issuance fell from $33 billion to $20 billion between the second and third quarters of 2002. The largest emerging market borrower during the third quarter was the United Mexican States, which floated $1.75 billion in new announcements.

... as Taiwanese borrowers withdraw

Emerging Asia was the region with the largest decline in net borrowing. Net issuance by Asia-Pacific borrowers fell from $9.4 billion in the second quarter of 2002 to $5.3 billion in the third, still well in excess of the essentially zero average quarterly net issuance over the period from the fourth quarter of 1997 to the fourth quarter of 2001. More than half of the decline was due to reduced demand from Taiwanese borrowers, whose net issuance fell from a record $3.2 billion to a still relatively strong $0.6 billion.

Even amid political uncertainty ...

Political and economic uncertainty continued to affect some emerging market borrowers (see the Overview). Turkish and Argentine borrowers, for instance, were absent from the international debt securities market during the third quarter of 2002, in spite of the fact that both countries had posted some gross issuance in the second quarter. In the case of Turkey, this may have reflected the desire of borrowers to postpone issuance until political uncertainty had been largely resolved. After the most recent election, the Republic of Turkey floated $750 million in two bond issues. Brazilian borrowers, however,

... Turkey and Brazil float new issues

did tap the international debt securities market for $2.9 billion during the third quarter, although most of the funds were used to repay previously issued obligations. Almost all Brazilian gross issuance during the third quarter can be attributed to a single borrower, a financial company, which floated seven euronotes totalling €2.4 billion.

The fourth quarter sees domestic currency issues

The fourth quarter of 2002 also witnessed international issues in domestic currency by emerging market borrowers. A relatively large issue of this type was that of the Cayman branch of Banco Nacional de Comercio Exterior, a Mexican public bank, which floated a billion peso three-year security. The State Railway of Thailand also floated a local currency international issue, a 1 billion baht six-year security with a coupon of 4.05%.

Argentina's rescheduling has repercussions

The recent failure of Argentina to meet all payment deadlines on a World Bank-guaranteed bond, and the failure of the World Bank to impose expected sanctions, had repercussions in the international debt securities market. Yields rose on other World Bank-backed securities, such as those of Colombia, and Peru reportedly postponed a similarly backed new issue. In addition, the National Power Corporation of Japan reportedly restructured its partially guaranteed bond deal as a larger yen and smaller US dollar bond in response to the greater uncertainty associated with multilateral guarantees.