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The syndicated loan market: structure, development and implications[1]

The syndicated loan market allows a more efficient geographical and institutional sharing of risk. Large US and European banks originate loans for emerging market borrowers and allocate them to local banks. Euro area banks have expanded pan-European lending and have found funding outside the euro area.

JEL classification: G100, G200.

Syndicated loans are credits granted by a group of banks to a borrower. They are hybrid instruments combining features of relationship lending and publicly traded debt. They allow the sharing of credit risk between various financial institutions without the disclosure and marketing burden that bond issuers face. Syndicated credits are a very significant source of international financing, with signings of international syndicated loan facilities accounting for no less than a third of all international financing, including bond, commercial paper and equity issues (Graph 1).

This special feature presents a historical review of the development of this increasingly global market and describes its functioning, focusing on participants, pricing mechanisms, primary origination and secondary trading. It also gauges its degree of geographical integration. We find that large US and European banks tend to originate loans for emerging market borrowers and allocate them to local banks. Euro area banks seem to have expanded pan-European lending and have found funding outside the euro area.

Development of the market

The evolution of syndicated lending can be divided into three phases. Credit syndications first developed in the 1970s as a sovereign business. On the eve of the sovereign default by Mexico in 1982, most of developing countries' debt consisted of syndicated loans. The payment difficulties experienced by many emerging market borrowers in the 1980s resulted in the restructuring of

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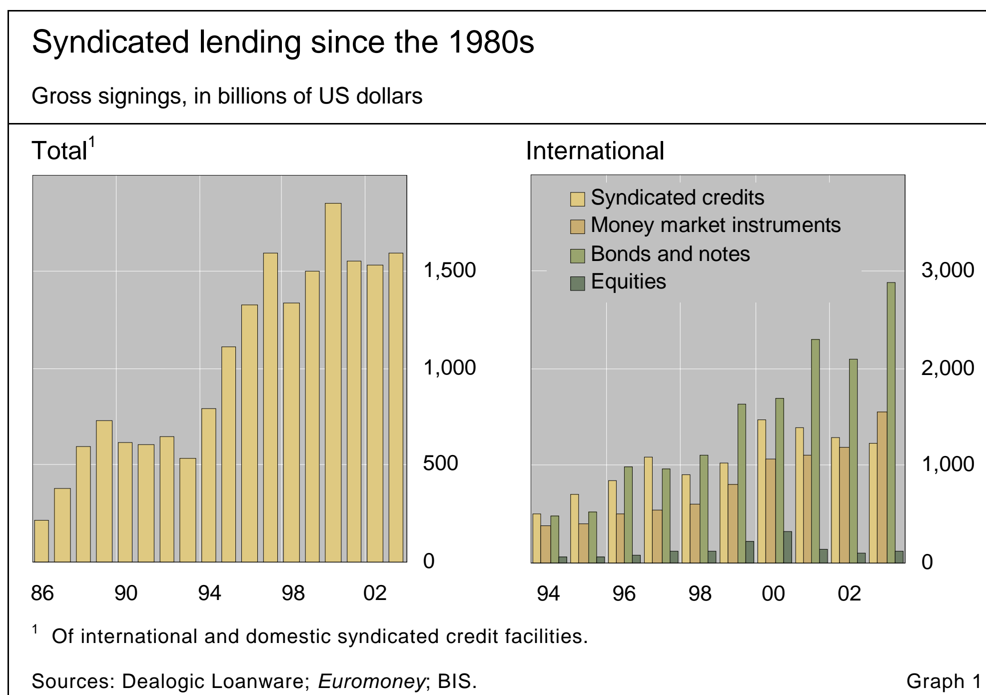
[1] The views expressed in this article are those of the author and do not necessarily reflect those of the BIS. I would like to thank Claudio Borio, Már Gudmundsson, Eli Remolona and Kostas Tsatsaronis for their comments, Denis Pêtre for help with database programming, and Angelika Donaubauer for excellent research assistance.



Syndicated lending since the 1980s

Gross signings, in billions of US dollars

[1] Of international and domestic syndicated credit facilities.

Sources: Dealogic Loanware; *Euromoney*; BIS. Graph 1

Mexican debt into Brady bonds in 1989. That conversion process catalysed a shift in patterns for emerging market borrowers towards bond financing, resulting in a contraction in syndicated lending business. Since the early 1990s, however, the market for syndicated credits has experienced a revival and has progressively become the biggest corporate finance market in the United States. It was also the largest source of underwriting revenue for lenders in the late 1990s (Madan et al (1999)).

Born as a sovereign business …

The first phase of expansion began in the 1970s. Between 1971 and 1982, medium-term syndicated loans were widely used to channel foreign capital to the developing countries of Africa, Asia and especially Latin America. Syndication allowed smaller financial institutions to acquire emerging market exposure without having to establish a local presence. Syndicated lending to emerging market borrowers grew from small amounts in the early 1970s to $46 billion in 1982, steadily displacing bilateral lending.

Lending came to an abrupt halt in August 1982, after Mexico suspended interest payments on its sovereign debt, soon followed by other countries including Brazil, Argentina, Venezuela and the Philippines. Lending volumes reached their lowest point at $9 billion in 1985. In 1987, Citibank wrote down a large proportion of its emerging market loans and several large US banks followed suit. That move catalysed the negotiation of a plan, initiated by US Treasury Secretary Nicholas Brady, which resulted in creditors exchanging their emerging market syndicated loans for Brady bonds, eponymous debt securities whose interest payments and principal benefited from varying degrees of collateralisation on US Treasuries.

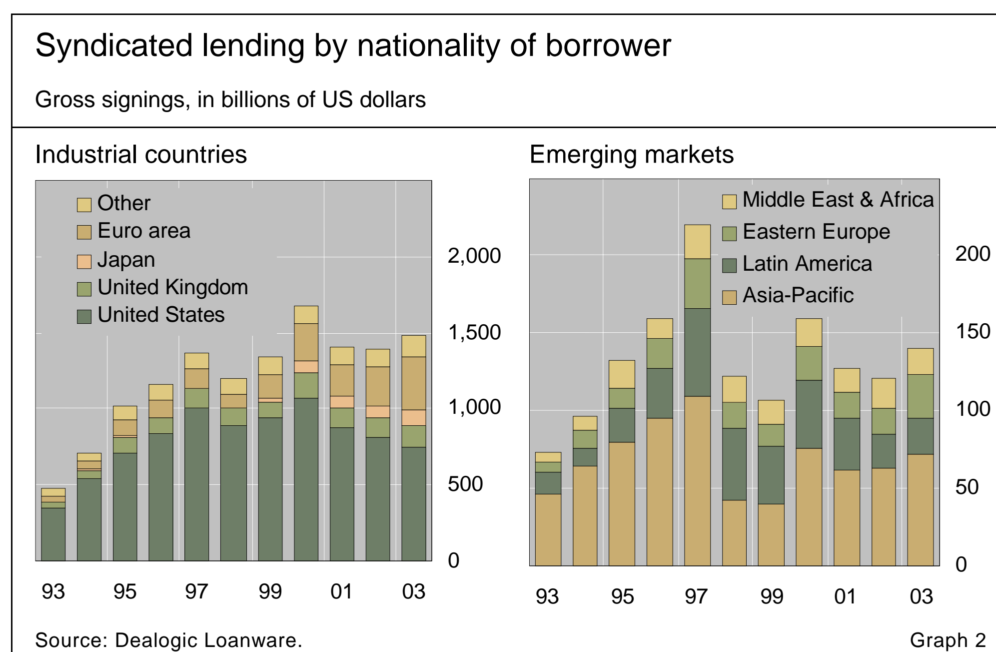
The Brady plan provided a new impetus to the syndicated loan market. By the beginning of the 1990s, banks, which had suffered severe losses in the debt crisis, started applying more sophisticated risk pricing to syndicated lending (relying in part on techniques initially developed in the corporate bond

market). They also started to make wider use of covenants, triggers which linked pricing explicitly to corporate events such as changes in ratings and debt servicing. While banks became more sophisticated, more data became available on the performance of loans, contributing to the development of a secondary market which gradually attracted non-bank financial firms, such as pension funds and insurance firms. Eventually, guarantees and unfunded[2] risk transfer techniques such as synthetic securitisation enabled banks to buy protection against credit risk while keeping the loans on the balance sheet. The advent of these new risk management techniques enabled a wider circle of financial institutions to lend on the market, including those whose credit limits and lending strategies would not have allowed them to participate beforehand. Partly, lenders saw syndicated loans as a loss-leader for selling more lucrative investment banking and other services. More importantly, in addition to borrowers from emerging markets, corporations in industrialised countries developed an appetite for syndicated loans. They saw them as a useful, flexible source of funds that could be arranged quickly and relied upon to complement other sources of external financing such as equities or bonds.

… the syndicated loan market has been booming in recent years

As a result of these developments, syndicated lending has grown strongly from the beginning of the 1990s to date. Signings of new loans – including domestic facilities – totalled $1.6 trillion in 2003, more than three times the 1993 amount. Borrowers from emerging markets and industrialised countries alike have been tapping the market, with the former accounting for 16% of business and, for the latter, an equal split between the United States and western Europe (Graph 2). Syndicated lending in Japan reportedly makes up just a small – albeit growing – fraction of total domestic bank lending, not least because of the traditional importance of "main banks" for corporations.

Global activity is driven by US and western European borrowers



Source: Dealogic Loanware. Graph 2

[2] In an unfunded risk transfer, such as a credit default swap, the risk-taker does not provide upfront funding in the transaction but is faced with obligations depending on the evolution of the borrower's creditworthiness.

Syndicated credits have thus become a very significant source of financing. The international market[3] accounts for about a third of all international financing, including bond, commercial paper and equity issues. The proportion of merger-, acquisition- and buyout-related loans represented 13% of the total volume in 2003, against 7% in 1993. Following a spate of privatisations in emerging markets, banks, utilities, and transportation and mining companies[4] have started to displace sovereigns as the major borrowers from these regions (Robinson (1996)).[5]

A hybrid between relationship lending and disintermediated debt

In a syndicated loan, two or more banks agree jointly to make a loan to a borrower. Every syndicate member has a separate claim on the debtor, although there is a single loan agreement contract. The creditors can be divided into two groups. The first group consists of senior syndicate members and is led by one or several lenders, typically acting as mandated arrangers, arrangers, lead managers or agents.[6] These senior banks are appointed by the borrower to bring together the syndicate of banks prepared to lend money at the terms specified by the loan. The syndicate is formed around the arrangers – often the borrower's relationship banks – who retain a portion of the loan and look for junior participants. The junior banks, typically bearing manager or participant titles, form the second group of creditors. Their number and identity may vary according to the size, complexity and pricing of the loan as well as the willingness of the borrower to increase the range of its banking relationships.

A hybrid instrument ...

Thus, syndicated credits lie somewhere between relationship loans and disintermediated debt (Dennis and Mullineaux (2000)). Box 1 below shows, in decreasing order of seniority, the banks that participated in a simple syndicate structure to grant a loan to Starwood Hotels & Resorts Worldwide, Inc in 2001.

Senior banks may have several reasons for arranging a syndication. It can be a means of avoiding excessive single-name exposure, in compliance with regulatory limits on risk concentration, while maintaining a relationship with the borrower. Or it can be a means to earn fees, which helps diversify their income. In essence, arranging a syndicated loan allows them to meet borrowers' demand for loan commitments without having to bear the market and credit risk alone.

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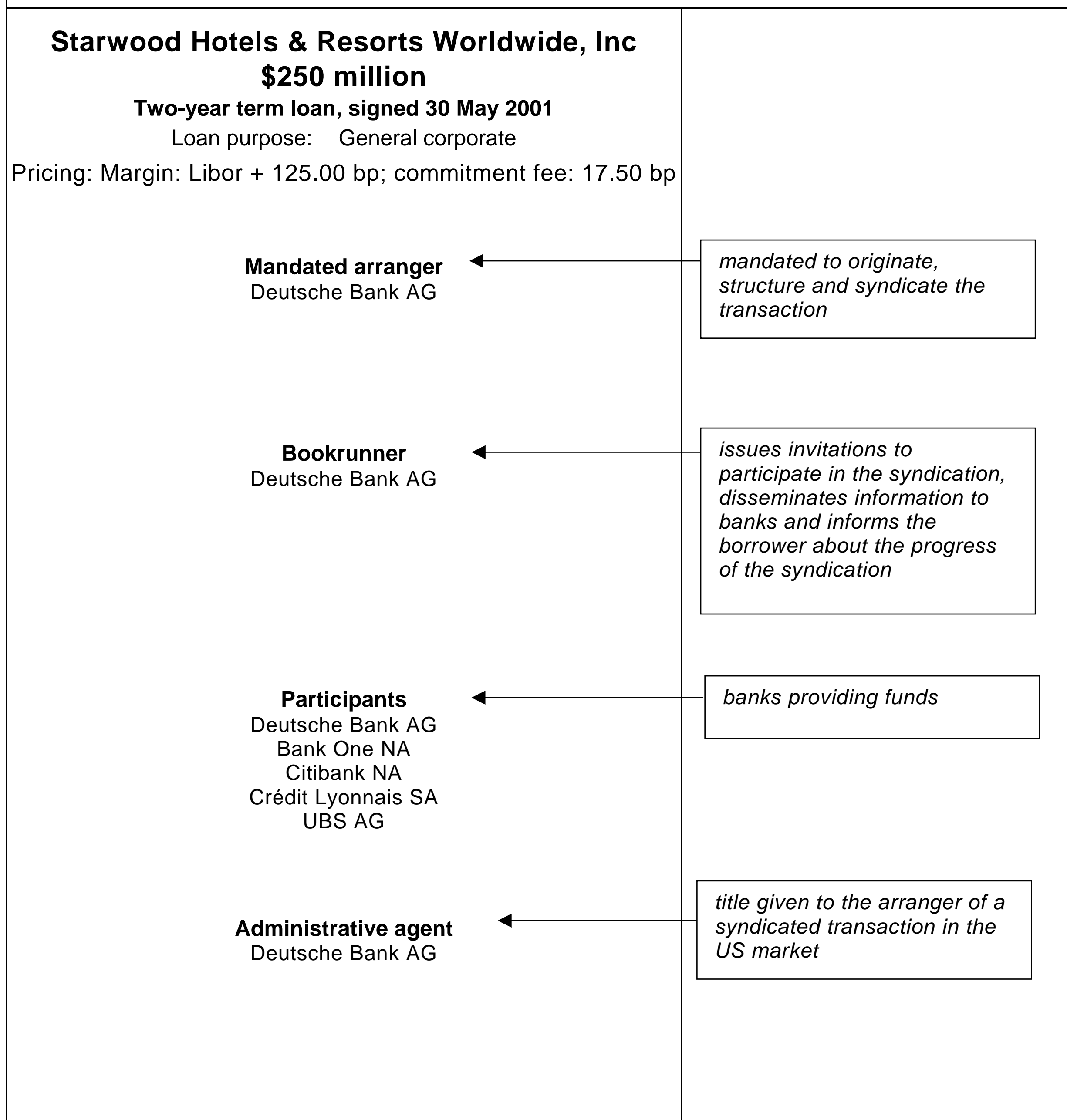
3 An international syndicated loan is defined in the statistics compiled by the BIS as a facility for which there is at least one lender present in the syndicate whose nationality is different from that of the borrower.

4 Syndicated loans are widely used to fund projects in these sectors, in industrial and emerging market countries alike. A feature article on page 91 of this *BIS Quarterly Review* explores the nature of credit risk in project finance.

5 Interestingly, for most of the 1990s, emerging market borrowers were granted longer-maturity loans, five years on average, than industrialised country ones (three–four years).

6 These bank roles, enumerated here in decreasing order of seniority, involve an active role in determining the syndicate composition, negotiating the pricing and administering the facility.

Example of a simple syndicate structure: Starwood



Source: Dealogic. Box 1

… with senior arrangers and junior participants

For junior banks, participating in a syndicated loan may be advantageous for several reasons. These banks may be motivated by a lack of origination capability in certain types of transactions, geographical areas or industrial sectors, or indeed a desire to cut down on origination costs. While junior participating banks typically earn just a margin and no fees, they may also hope that in return for their involvement, the client will reward them later with

more profitable business, such as treasury management, corporate finance or advisory work (Allen (1990)).[7]

Pricing structure: spreads and fees

As well as earning a spread over a floating rate benchmark (typically Libor) on the portion of the loan that is drawn, banks in the syndicate receive various fees (Allen (1990), Table 1). The arranger[8] and other members of the lead management team generally earn some form of upfront fee in exchange for putting the deal together. This is often called a *praecipium* or *arrangement fee*. The underwriters similarly earn an *underwriting fee* for guaranteeing the

Lenders earn fees according to seniority ...

Structure of fees in a syndicated loan

Fee	Type	Remarks
Arrangement fee	Front-end	Also called *praecipium.* Received and retained by the lead arrangers in return for putting the deal together
Legal fee	Front-end	Remuneration of the legal adviser
Underwriting fee	Front-end	Price of the commitment to obtain financing during the first level of syndication
Participation fee	Front-end	Received by the senior participants
Facility fee	Per annum	Payable to banks in return for providing the facility, whether it is used or not
Commitment fee	Per annum, charged on undrawn part	Paid as long as the facility is not used, to compensate the lender for tying up the capital corresponding to the commitment
Utilisation fee	Per annum, charged on drawn part	Boosts the lender's yield; enables the borrower to announce a lower spread to the market than what is actually being paid, as the utilisation fee does not always need to be publicised
Agency fee	Per annum	Remuneration of the agent bank's services
Conduit fee	Front-end	Remuneration of the *conduit bank*[1]
Prepayment fee	One-off if prepayment	Penalty for prepayment

[1] The institution through which payments are channelled with a view to avoiding payment of withholding tax. One important consideration for borrowers consenting to their loans being traded on the secondary market is avoiding withholding tax in the country where the acquirer of the loan is domiciled.

Source: Compiled by author. Table 1

[7] In practice, though, these rewards fail to materialise in a systematic manner. Indeed, anecdotal evidence for the United States suggests that, for this reason, smaller players have withdrawn from the market lately and have stopped extending syndicated loans as a loss-leader.

[8] For this discussion, it has to be recalled that the same bank can act in various capacities in a syndicate. For instance, the arranger bank can also act as an underwriter and/or allocate a small portion of the loan to itself and therefore also be a junior participant.

... as remuneration for their services ...

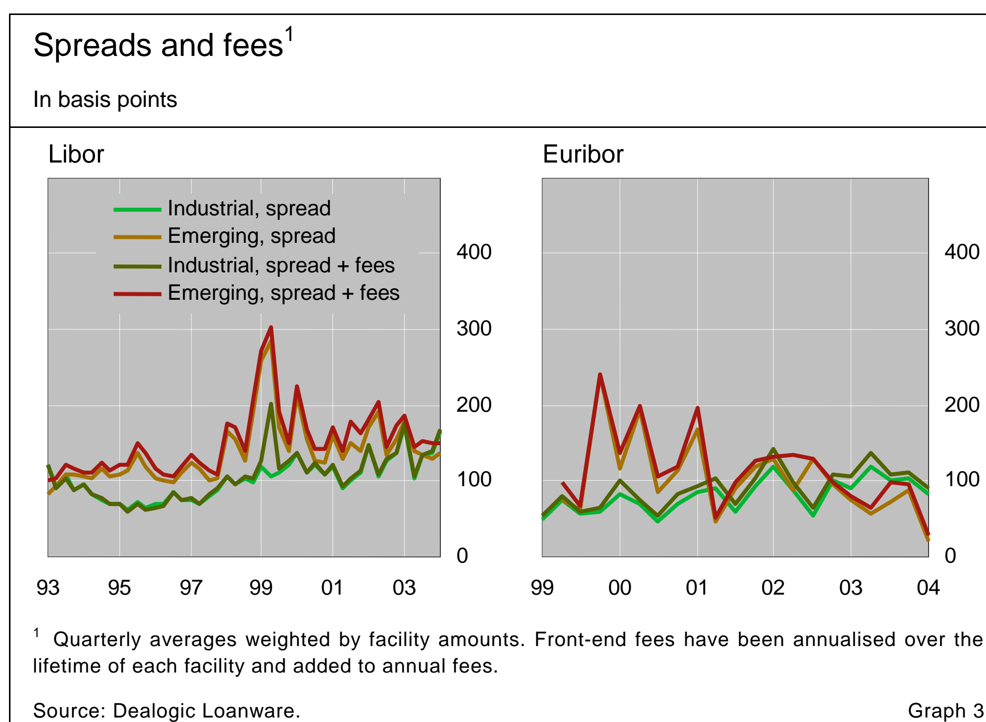
availability of funds. Other participants (those at least on the "manager" and "co-manager" level) may expect to receive a *participation fee* for agreeing to join the facility, with the actual size of the fee generally varying with the size of the commitment. The most junior syndicate members typically only earn the spread over the reference yield. Once the credit is established and as long as it is not drawn, the syndicate members often receive an annual *commitment* or *facility fee* proportional to their commitment (largely to compensate for the cost of regulatory capital that needs to be set aside against the commitment). As soon as the facility is drawn, the borrower may have to pay a per annum *utilisation fee* on the drawn portion. The agent bank typically earns an *agency fee*, usually payable annually, to cover the costs of administering the loan. Loans sometimes incorporate a penalty clause, whereby the borrower agrees to pay a *prepayment fee* or otherwise compensate the lenders in the event that it reimburses any drawn amounts prior to the specified term. Box 1 above provides an example of a simple fee structure under which Starwood Hotels & Resorts Worldwide, Inc has had to pay a commitment fee in addition to the margin.

... or in connection with specific loan events

At an aggregate level, the relative size of spreads and fees differs systematically in conjunction with a number of factors. Fees are more significant for Euribor-based than for Libor-based loans. Moreover, for industrialised market borrowers, the share of fees in the total loan cost is higher than for emerging market ones. Arguably this could be related to the sectoral composition of borrowers in these segments. Non-sovereign entities, more prevalent in industrialised countries, may have a keener interest, for tax or market disclosure reasons, in incurring a larger part of the total loan cost in the form of fees rather than spreads. However, the total cost (spreads, front-

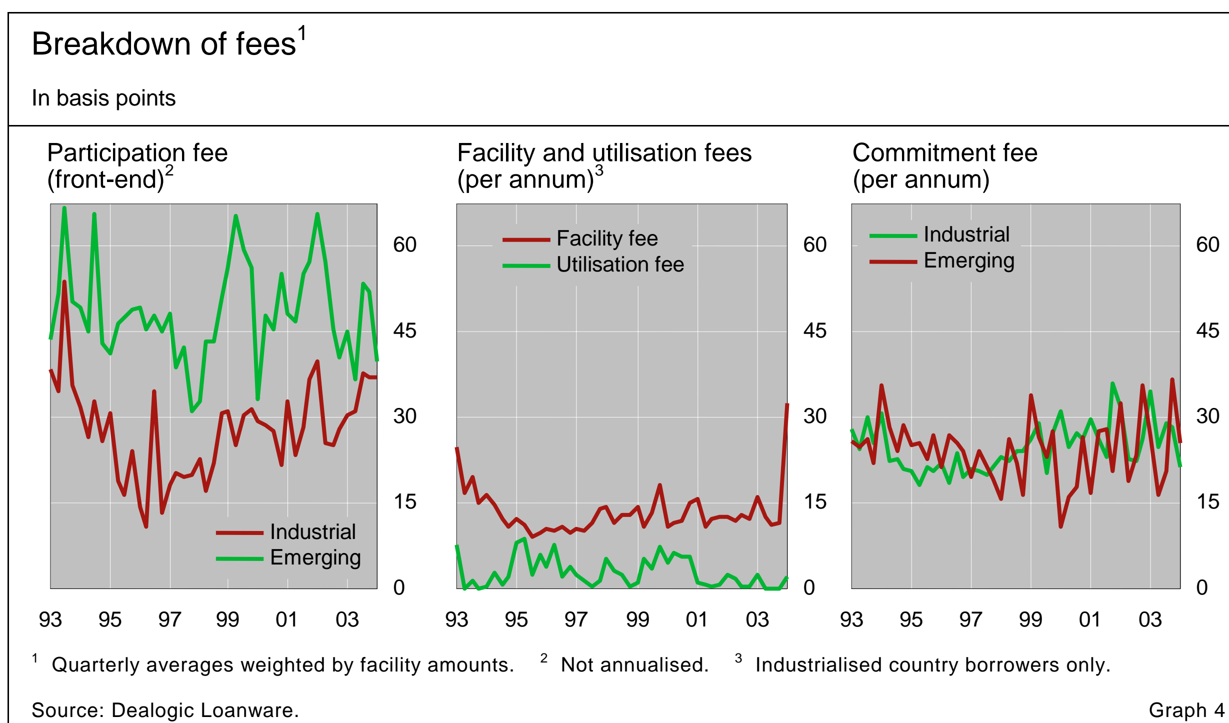
Spreads and fees[1]

In basis points



[1] Quarterly averages weighted by facility amounts. Front-end fees have been annualised over the lifetime of each facility and added to annual fees.

Source: Dealogic Loanware. Graph 3



Breakdown of fees[1]

In basis points

[1] Quarterly averages weighted by facility amounts. [2] Not annualised. [3] Industrialised country borrowers only.

Source: Dealogic Loanware. Graph 4

end and annual fees)[9] of loans granted to emerging market borrowers is higher than that of facilities extended to industrialised countries (Graphs 3 and 4). There is also more variance in commitment fees on emerging market facilities. In sum, lenders seem to demand additional compensation for the higher and more variable credit risk in emerging markets, in the form of both spreads and fees.

Spreads and fees are not the only compensation that lenders can demand in return for assuming risk. Guarantees, collateral and loan covenants offer the possibility of explicitly linking pricing to corporate events (rating changes, debt servicing). Collateralisation and guarantees are more often used for emerging market borrowers (Table 2), while covenants are much more widely used for

Non-price components in the remuneration of risk

Share of syndicated loans with covenants, collateral and guarantees, in per cent, by nationality of borrower

	Covenants		Collateral		Guarantees	
	Emerging	Industrialised	Emerging	Industrialised	Emerging	Industrialised
1993–96	0	16	40	15	31	7
1997–2000	2	24	49	16	22	4
2001–04[1]	3	19	37	13	21	4

[1] First quarter only for 2004.

Source: Dealogic Loanware. Table 2

[9] One should note that the fees shown in Graphs 3 and 4 are not directly comparable. In Graph 3, for the purposes of comparability with spreads, annual and front-end fees are added together by annualising the latter over the whole maturity of the facility, assuming full and immediate drawdown. Graph 4, on the other hand, shows annual and front-end fees separately without annualising the latter.

borrowers in industrialised countries (possibly because such terms are easier to enforce there).

Primary and secondary markets: sharing versus transferring risk

Commercial banks still dominate the primary market

While commercial banks dominate the primary market, both at the senior arranger and at the junior funds provider levels, other institutions have made inroads over time. Globally, there are virtually no non-commercial banks or non-banks among the top 200 institutions that have around 90% market share. However, investment banks have benefited from the revival of syndicated lending in the 1990s. They have taken advantage of their expertise as bond underwriters and of the increasing integration of bank lending and disintermediated debt markets[10] to arrange loan syndications. Besides the greater involvement of investment banks, there is also growing participation by multilateral agencies such as the International Finance Corporation or the Inter-American Development Bank.[11]

Increased role of the secondary market

Syndicated credits are increasingly traded on secondary markets. The standardisation of documentation for loan trading, initiated by professional bodies such as the Loan Market Association (in Europe) and the Asia Pacific Loan Market Association, has contributed to improved liquidity on these markets. A measure of the tradability of loans on the secondary market is the prevalence of transferability clauses, which allow the transfer of the claim to another creditor.[12] The US market has generated the highest share of transferable loans (25% of total loans between 1993 and 2003), followed by the European marketplace (10%). The secondary market is commonly perceived to consist of three segments: par/near par, leveraged (or high-yield) and distressed. Most of the liquidity can be found in the distressed segment. Loans to large corporate borrowers also tend to be actively traded.

Secondary market participants and strategies: market-makers ...

Participants in the secondary market can be divided into three categories: market-makers, active traders and occasional sellers/investors. The market-makers (or two-way traders) are typically larger commercial and investment banks, committing capital to create liquidity and taking outright positions. Institutions actively engaged in primary loan origination have an advantage in trading on the secondary market, not least because of their acquired skill in accessing and understanding loan documentation. Active traders are mainly investment and commercial banks, specialist distressed debt traders and so-called "vulture funds" (institutional investors actively focused on distressed

... active traders ...

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[10] For instance, it is very common nowadays for a medium-term loan provided by a syndicate to be refinanced by a bond at, or before, the loan's stated maturity. Similarly, US commercial paper programmes are frequently backed by a syndicated letter of credit.

[11] This provides an opportunity for risk-sharing between public and private sector investors. It usually takes the form of syndicated loans granted by multilateral agencies with tranches reserved for private sector bank lenders.

[12] Transferability is determined by consent of the borrower as stated in the original loan agreement. Some borrowers do not allow loans to be traded on the secondary market as they want to preserve their banking relationships.

debt). Non-financial corporations and other institutional investors such as insurance companies also trade, but to a lesser extent. As a growing number of financial institutions establish loan portfolio management departments, there appears to be increasing attention paid to relative value trades. Discrepancies in yield/return between loans and other instruments such as credit derivatives, equities and bonds are arbitraged away (Coffey (2000), Pennacchi (2003)). Lastly, occasional participants are present on the market either as sellers of loans to manage capacity on their balance sheet or as investors which take and hold positions. Sellers of risk can remove loans from their balance sheets in order to meet regulatory constraints, hedge risk, or manage their exposure and liquidity.[13] US banks, whose outstanding syndicated loan commitments are regularly monitored by the Federal Reserve Board, appear to have been relatively successful in transferring some of their syndicated credits, including up to one quarter of their problem loans, to non-bank investors (Table 3). Buyers of loans on the secondary market can acquire exposure to sectors or countries, especially when they do not have the critical size to do so on the primary market.[14]

... and occasional participants

While growing, secondary trading volumes remain relatively modest compared to the total volume of syndicated credits arranged on the primary market. The biggest secondary market for loan trading is the United States, where the volume of such trading amounted to $145 billion in 2003. This is equivalent to 19% of new originations on the primary market that year and to 9% of outstanding syndicated loan commitments. In Europe, trading amounted to $46 billion in 2003 (or 11% of primary market volume), soaring by more than 50% compared to the previous year (Graph 5).

Secondary trading is still relatively thin ...

Distressed loans continued to represent a sizeable fraction of total secondary trading in the United States, and gained in importance in Europe.

US syndicated credits[1]

	Share of total credits[2]			*Memo:*	Percentage classified[3]			
	US banks	Foreign banking organisations	Non-banks	*Total credits ($ bn)*	US banks	Foreign banking organisations	Non-banks	Total credits
2000	48	45	7	*1,951*	2.8	2.6	10.2	3.2
2001	46	46	8	*2,050*	5.1	4.7	14.6	5.7
2002	45	45	10	*1,871*	6.4	7.3	23.0	8.4
2003	45	44	11	*1,644*	5.8	9.0	24.4	9.3

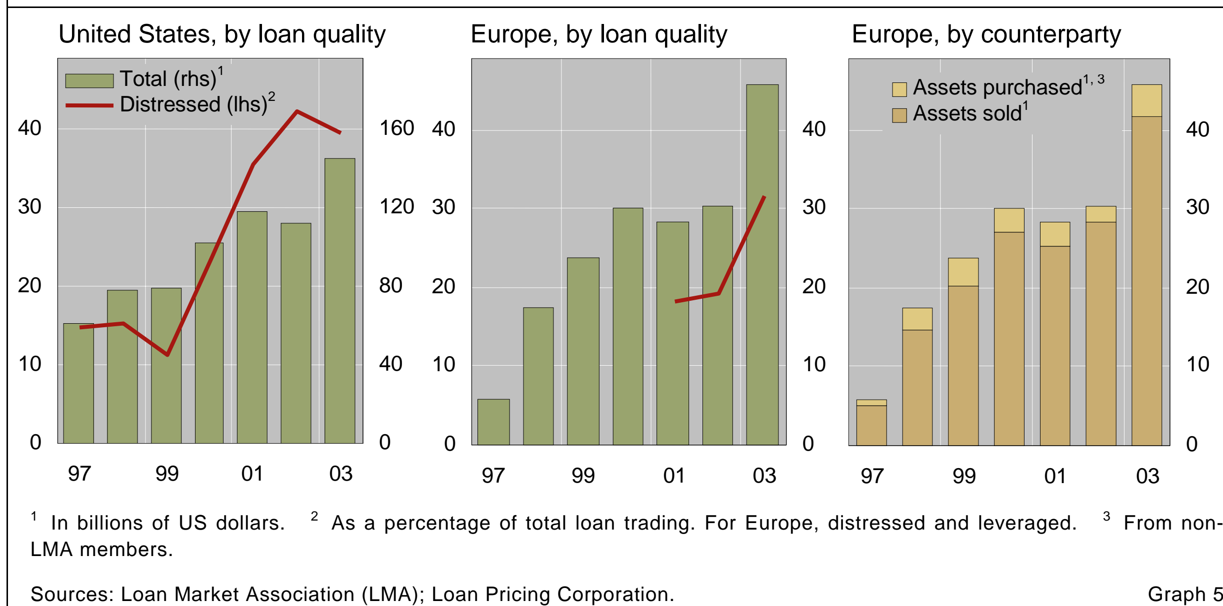
[1] Includes both outstanding loans and undrawn commitments. [2] Dollar volume of credits held by each group of institutions as a percentage of the total dollar volume of credits. [3] Dollar volume of credits classified "substandard", "doubtful" or "loss" by examiners as a percentage of the total dollar volume of credits.

Source: Board of Governors of the Federal Reserve System. Table 3

[13] The seller banks often enhance their fee income by arranging new loans to roll over facilities they had previously granted to borrowers. They may sell old facilities on the secondary market to manage capacity on their balance sheet, which is required to hold some of the new loans.

[14] For example, minimum participation amounts on the primary market may exceed the bank's credit limits.

US and European secondary markets for syndicated credits



[1] In billions of US dollars. [2] As a percentage of total loan trading. For Europe, distressed and leveraged. [3] From non-LMA members.

Sources: Loan Market Association (LMA); Loan Pricing Corporation. Graph 5

Admittedly, this to some extent reflects higher levels of corporate distress in Europe. But as the investment grade segment matures, it is also indicative of sustained investor appetite and of the market's improved ability to absorb a larger share of below par loans (BIS (2004)).

... especially in Asia

In the Asia-Pacific region, secondary volumes are still a tiny fraction of those in the United States and Europe, with only six or seven banks running dedicated desks in Hong Kong SAR, and no non-bank participants. In 1998, the Asian secondary market was exceptionally active. That year, large blocks of loan portfolios changed hands as Japanese banks restructured their distressed loan portfolios.[15] Trading was more subdued in subsequent years,[16] although banks' interest appears to have recently been rekindled by the secondary prices of loans, which have decreased less than those of collateralised debt obligations and bonds.[17]

Geographical integration of the market

As financial markets are becoming more integrated geographically, a question is how this process manifests itself in syndicated lending in the form of cross-border deals. To answer this question, we examine the nationality composition of syndicates on the primary market, where information is readily available

[15] Banks tend to trade blocks of loans when they restructure whole portfolios. In normal times, loan by loan trading is more common.

[16] Nonetheless, Japanese banks have recently been very active in transferring loans on the Japanese secondary market. According to a quarterly survey conducted by the Bank of Japan, for the financial year April 2003–March 2004, such transfers totalled ¥11 trillion, 38% of which were non-performing loans. This was followed in the second quarter of 2004 by unusually weak secondary market activity by historical standards.

[17] According to practitioners, major international banks with an Asian presence are among the main sellers of loans, while demand comes from Taiwanese and Chinese banks.

about individual participants. We first perform this exercise at a global level and then within the euro area, in order to assess any impact from the introduction of the single currency.

Table 4 shows the degree of international integration of syndicated loan markets, measured by the share of loans arranged or provided by banks of the same country or region as the borrower. At the senior arranger level, the nationality composition is calculated based on the number of deals, and at a junior participant level based on the dollar amounts provided by individual financial institutions. A number of findings stand out.

First, unsurprisingly, there appears to be relatively little penetration by foreign lenders in the market for loans to Japanese, euro area and US borrowers. The senior arranger and junior funds provider banks in loan facilities

International integration of the market

By borrower nationality	% of deals[1] where the arranger is of the same nationality[2] as the borrower (based on number of deals)		% of funds[1] provided by banks of the same nationality[2] as the borrower (based on USD amounts)	
	1993–98	1999–2004[3]	1993–98	1999–2004[3]
Main countries and regions				
United States	74	70	61	62
Euro area[4]	59	72	71	67
United Kingdom	58	43	35	42
Other western Europe	37	26	36	25
Japan	62	84	63	87
Other industrialised economies	67	65	61	57
Asia-Pacific	29	37	34	51
Eastern Europe	9	12	10	13
Latin America/Caribbean	5	7	6	8
Middle East & Africa	15	20	22	28
Offshore	54	36	44	31
Euro area countries				
Austria	5	42	33	42
Belgium	17	22	31	16
Finland	26	13	16	9
France	48	50	45	46
Germany	43	46	57	44
Greece	7	29	8	24
Ireland	20	18	16	14
Italy	34	53	39	48
Luxembourg	10	8	30	7
Netherlands	24	29	28	25
Portugal	31	27	30	23
Spain	64	51	64	49
Euro area[5]	39	42	43	38

[1] Calculated also including purely domestic deals. [2] From the same region, where regions are shown. [3] For 2004, first quarter only. [4] Borrower from any euro area country, arranger/provider from any euro area country. [5] Borrower from same euro area country as arranger/provider, euro area average.

Sources: Dealogic Loanware; author's calculations. Table 4

Integration in industrial countries …

set up for these borrowers are often from the borrowers' own country, with the share of deals arranged or of funds provided by foreign institutions rarely exceeding 30%.[18]

Second, foreign banks appear more present (with shares often in excess of 60%) in syndicates set up for European borrowers from outside the euro area and, in particular, the United Kingdom. It is interesting to note that Japanese borrowers tend to pay higher fees on average than UK borrowers, whose market is characterised by more foreign bank penetration. This may suggest that the market is more contestable in the United Kingdom.

… and emerging markets

Third, with the possible exception of Asia, syndicates put together for emerging market borrowers tend to be dominated by foreign lenders. Interestingly, for all emerging market borrowers, but especially in the Middle East and Africa and Asia-Pacific regions, "domestic" banks (ie from the same geographical area as the borrower) are more present as junior funds providers than as senior arrangers. It would appear typical for a major international bank to arrange the syndication and then allocate the credit to regional lenders.[19] Given that the presence of a reputable major foreign arranger has a "certification effect" for banks which are ranked lower in the syndicate, this makes cross-border investment in a junior funds provider capacity easier than the provision of screening and monitoring services as a senior arranger.

Some pan-European integration

Finally, the advent of the euro appears to have led to some integration in the pan-European syndicated loan market, especially at the arranger level. The first two columns of Table 4 show that within the euro area, the percentage of loans arranged by banks from the same country as the borrower is about the same before and after 1999 (39% versus 42%).[20] Meanwhile, the overall share of euro area arrangers rose from 59% to 72%, suggesting that euro area banks have been arranging a higher share of loans for borrowers from euro area countries other than their own.[21] At the same time, the additional credits arranged at a pan-European level seem to have been funded largely by banks from outside the euro area, since the share of euro area banks among junior funds providers has remained relatively stable (last two columns of Table 4). This could reflect a greater balance sheet capacity outside the euro area.

[18] For US borrowers, the statement about low foreign penetration should be balanced by the relatively high share – approximately 45% since 2000 – of total syndicated credits held by foreign banking organisations, after allowing for transfers on the secondary market (Table 3).

[19] For more background and an extension of the analysis to bond markets, see McCauley et al (2002).

[20] While the euro is widely used as a currency of denomination for European (including eastern European) borrowers, the US dollar is still the currency of choice for syndicated lending worldwide (US dollar facilities represented 62% of total syndicated lending in 2003, while the euro accounted for 21%, and the pound sterling and the Japanese yen for 6% each).

[21] In a study of the bond underwriting market, Santos and Tsatsaronis (2003) show that the elimination of market segmentation associated with the single European currency failed to result in an intensification of the business links between borrowers and bond underwriters from the euro area. It must be stressed, though, that bond underwriting and syndicated loan markets are quite different, as bonds are sold to institutional investors and loans mainly to other banks.

Conclusion

This special feature has presented a historical review of the development of the market for syndicated loans, and has shown how this type of lending, which started essentially as a sovereign business in the 1970s, evolved over the 1990s to become one of the main sources of funding for corporate borrowers.

The syndicated loan market has advantages for junior and senior lenders. It provides an opportunity to senior banks to earn fees from their expertise in risk origination and manage their balance sheet exposures. It allows junior lenders to acquire new exposures without incurring screening costs in countries or sectors where they may not have the required expertise or established presence. Primary loan syndications and the associated secondary market therefore allow a more efficient geographical and institutional sharing of risk origination and risk-taking. For instance, loan syndications for emerging market borrowers tend to be originated by large US and European banks, which subsequently allocate the risk to local banks. Euro area banks have strengthened their pan-European loan origination activities since the advent of the single currency and have found funding for the resulting risk outside the euro area.

However, we find that the geographical integration of the market appears to vary among regions, as reflected in varying degrees of international penetration. While these differences could also be related to disparities in the sizes of national markets, further research is needed to improve our understanding of market contestability by assessing whether they are systematically related to differences in loan pricing, especially fees.

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