Highlights of international banking and financial market activity

The BIS, in cooperation with central banks and monetary authorities worldwide, compiles and disseminates several datasets on activity in international banking and financial markets. The latest available data on the international banking market refer to the first quarter of 2008. The discussion on international debt securities and exchange-traded derivatives draws on data for the second quarter of 2008.

The international banking market

Growth in international bank claims continued to slow in the first quarter of 2008. BIS reporting banks’ gross international claims on non-bank borrowers expanded by $365 billion, the smallest first quarter increase since 2003. This helped to push down the year-on-year growth rate of total international claims from 21% in the previous quarter to 16%. The $1.4 trillion expansion in total international claims (to $40 trillion) mainly reflected greater interbank activity, as banks transferred funds from their offices in the United States to those in the United Kingdom and the euro area.

In the first quarter of 2008, reporting banks continued their net transfer of funds out of the United States, a trend evident since the onset of the financial turmoil in mid-2007. Gross cross-border claims on all sectors in the United States had grown to $5.3 trillion by the second quarter of 2007, outpacing the

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1 Queries concerning the banking statistics should be addressed to Patrick McGuire and Goetz von Peter and queries concerning international debt securities and derivatives statistics to Naohiko Baba.

2 International claims are comprised of cross-border claims in all currencies plus claims on residents in foreign currencies.

3 In the BIS locational banking statistics, there is a strong seasonal component in claims on both banks and non-banks, with relatively large expansions in the first quarter of each calendar year.

4 The BIS consolidated banking statistics on an immediate borrower basis (IB basis) also indicate an increase in international claims in the first quarter of 2008. Total international claims expanded by $1.9 trillion during the quarter, although some of this was the result of the depreciation of the US dollar over the quarter, which tends to boost end-of-period stocks in other currencies when expressed in US dollars.
growth in cross-border liabilities to counterparties there. This increase in claims had been behind a cumulative *net* transfer of US dollar-denominated funds into the United States via the international banking system of more than $1 trillion since 2000 (Graph 1, left-hand panel).\(^5\) These net flows reversed in mid-2007; since then, an estimated $321 billion in net US dollar-denominated funds have been transferred out of the United States, much of this the result of interbank activity.\(^6\) Admittedly, in the first quarter of 2008, claims (in all currencies) on all sectors in the United States booked by banks abroad expanded (by $134 billion). However, an even larger increase in these banks’ international liabilities to the banking sector in the United States resulted in a $259 billion net outflow from the country during the quarter.

The expansion in international claims on non-bank borrowers worldwide was relatively weak in the first quarter of 2008. Total claims grew by $365 billion, the smallest first quarter expansion since 2003. Banks’ outstanding *loans* to non-banks actually increased by more ($530 billion), with greater credit in all major currency segments. Euro-denominated loans to non-banks grew by $247 billion, chiefly the result of lending by banks in the United Kingdom to residents of the United Kingdom ($109 billion) and the euro area ($49 billion), as well as intra-euro area cross-border lending ($31 billion). US dollar-denominated loans to non-banks also increased, by $230 billion, mainly to non-banks in emerging economies ($53 billion), the United States ($51 billion) and the euro area ($43 billion).

### Cumulative net claims in US dollars (all sectors)\(^1\)

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\(^1\) Panels indicate the total net capital flows via banks from residents of the country/region in the panel heading to residents of the countries/regions in the legend. These flows are calculated by consolidating (across the asset and liability side of the balance sheet, and across sectors) the positions booked by banks inside and outside the country/region in the panel heading. A positive value indicates a flow out of the country/region in the panel heading.

Source: BIS locational banking statistics by residence.  

### Graph 1

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\(^5\) The calculation of the total net transfer of funds via the international banking system takes into account claims and liabilities booked by banks outside the United States, as well as changes in net positions vis-à-vis non-residents booked by banks in the United States. See “Tracking international bank flows”, *BIS Quarterly Review*, December 2006, for more discussion on the construction of these net capital flow figures.

\(^6\) See “International banking activity amidst the turmoil” in the *BIS Quarterly Review*, June 2008.
Even as loans to non-banks expanded, however, banks’ outstanding debt securities claims on non-banks dropped significantly (by $98 billion), the first quarterly decline since the first quarter of 2001 (Graph 2, left-hand panel).\(^7\)\(^8\) While this is suggestive of an unwinding of positions, the decrease also includes writedowns of structured finance products and other securities during the period. Euro-denominated claims dropped the most, with decreases reported by banks in the euro area and the United Kingdom. That said, reporting banks’ US dollar-denominated debt securities claims on non-banks also fell markedly (by $23 billion). Banks in the United Kingdom reduced their claims by $39 billion, mostly vis-à-vis borrowers in the United States and offshore centres. Across all reporting countries, reduced holdings of US government debt securities did not seem to be the driving factor (see below), suggesting that much of the decrease reflected sales and writedowns of bonds issued by corporate and non-bank financial entities.\(^9\)

This fall in debt securities claims seemed to coincide with a broader shift in bank balance sheets away from the US non-bank private sector, at least for some banking systems. The BIS consolidated banking statistics on an ultimate risk basis (UR basis) indicate that, in absolute terms, gross claims on the non-bank private sector in the United States have remained flat since mid-2007,

\(^7\) Reporting banks’ international claim and liability positions are broken down into “loans and deposits”, “debt securities” and “other positions”. The last category includes equity assets and liabilities, working capital provided by head offices and on-balance sheet derivatives positions, making it impossible to obtain a precise measure of equity positions alone. Moreover, not all reporting countries provide a complete instrument breakdown. In particular, banks in the United States do not separate debt securities positions from equity and other positions.

\(^8\) Reporting banks’ equity and other securities claims on non-banks fell by a further $90 billion.

\(^9\) The BIS consolidated statistics (IB basis) indicate that international claims on the US public sector actually increased, by $24 billion.
after a steady period of growth since at least 2005 (Graph 3, left-hand panel). In the most recent quarter, the share of claims on the US non-bank private sector dropped below 70% of reporting banks’ total foreign claims on the United States, with several major banking systems reporting noticeable shifts (Graph 3, right-hand panel). In absolute terms, total claims on the US non-bank private sector booked by banks headquartered in the euro area (excluding Ireland) and Switzerland fell by a combined $94 billion, with German, Dutch, Spanish and Swiss banks accounting for the bulk of this. In contrast, UK, Belgian and Irish banks’ outstanding claims on this sector grew by a combined $88 billion.

At the same time, the BIS data indicate that reporting banks increased their holdings of public sector debt. Across all reporting banking systems, the outstanding stock of claims on the public sector rose by nearly $400 billion (+10% to $4.35 trillion), although this partially reflected exchange rate valuation effects. Assuming that all claims on the euro area public sector are euro-denominated claims, the increase in banks’ holdings of euro area public debt (reported at $143 billion) amounted to $21 billion (+1%) at constant exchange rates. Similarly, reporting banks also stocked up on Japanese ($35 billion, +9%) and US ($68 billion, +11%) public sector debt. The general movement towards public debt was particularly evident for French, Swiss, Japanese and German banks, whose stocks grew more than $40 billion in each case (at constant exchange rates).

Banks’ cross-border equity and other liabilities surged in the first quarter of 2008, as banks tapped international sources of funds.10 Total equity and

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10 See footnote 7.
other liabilities rose by $122 billion overall, the largest quarterly increase on
record by a considerable margin (Graph 2, right-hand panel). Some $41 billion
of this increase was booked by banks in the euro area, and an additional
$54 billion by bank offices in offshore financial centres. Banks’ debt securities
liabilities also grew, by $201 billion, roughly half of which was denominated in
US dollars.

At the same time, reporting banks’ total deposit liabilities vis-à-vis official
monetary authorities dropped noticeably in the first quarter (by $38 billion to
$1.44 trillion), in part reflecting movements in foreign exchange reserves
placed in commercial banks abroad (Graph 4, left-hand panel). US dollar-
denominated liabilities dropped the most, lowering the US dollar share of total
liabilities vis-à-vis official monetary authorities to 52%, from 54% in the
previous quarter. On a residence basis, bank offices in the United Kingdom and
the United States and across the euro area reported the largest decreases. By
bank nationality, however, the decreases seemed to be concentrated in Swiss,
US and German banks (Graph 4, right-hand panel). Identifying with any degree
of precision which central banks accounted for these moves is difficult because
of incomplete data on the residence of the central bank counterparty. However,
data on reserve holdings reported by 63 monetary authorities to the IMF reveal
an aggregate decrease of $56 billion in deposits placed in commercial banks in
the first quarter of 2008, with relatively large decreases reported by the
monetary authorities in Russia ($39 billion), India ($10 billion), Indonesia
($10 billion), Malaysia ($4 billion) and Romania ($5 billion).

Banks’ positions vis-à-vis official monetary authorities are reported as a memo item in the BIS
statistics, and thus are not broken down by the country of residence. Reported liabilities will
include deposits placed in reporting banks as part of central bank reserve management,
reverse repo positions vis-à-vis reporting banks, and any loans which have arisen in the
context of central banks’ liquidity enhancement operations. There are some differences in the
definition of official monetary authorities across reporting countries. For example, positions
vis-à-vis central governments and other international organisations are included in this sector
in the data reported by the United States.
More broadly, the BIS data also indicate large reductions in liabilities to the banking sector of various emerging economies, particularly in the Asia-Pacific region. In some cases, these moves seemed to reflect to some extent the activity of central banks discussed above, since, on a disaggregated basis, these are generally classified as part of the banking sector in the BIS statistics. For example, BIS reporting banks’ liabilities to banks in Russia and Romania, countries whose monetary authorities reported significant decreases in deposits in commercial banks, fell by $14 billion and $5 billion, respectively. Elsewhere, reporting banks’ liabilities to banks in Asia-Pacific dropped by $50 billion in the first quarter of 2008, the first decrease in more than 10 quarters and the largest on record for this region. Liabilities to banks in China decreased the most (by $28 billion), although the reduction in positions vis-à-vis banks in Korea (–$9 billion), Malaysia (–$6 billion), Thailand (–$6 billion) and the Philippines (–$4 billion) was also noticeable. In addition, liabilities to banks in Hong Kong SAR (classified as an offshore centre in the BIS data) fell by $24 billion.

The international debt securities market

Borrowing in the international debt securities market recovered sharply in the second quarter of 2008 despite the continued turmoil in financial markets. Net issuance of bonds and notes increased to $1,071 billion, up substantially from $371 billion in the first quarter and recovering almost to the level recorded just before the recent turmoil began (the second quarter of 2007). Borrowing through money market instruments remained active, although net issuance declined from the record level of the previous quarter.

The increase in bond and note issuance stemmed chiefly from the euro-denominated segment (Graph 5, left-hand panel). Net issuance of euro-denominated bonds and notes rose to $464 billion, more than four times the level of the previous quarter. The gain was mostly accounted for by the issuance of private financial institutions. By nationality of issuer, the most substantial growth came from Spanish borrowers, followed by French, Belgian and Irish borrowers.

A sharp recovery was also evident across other currency denominations. Net issuance of dollar-denominated bonds and notes increased from $185 billion to $392 billion in the second quarter of 2008, while sterling-denominated bonds and notes rose substantially, from $31 billion to $142 billion, the highest level on record. Yen issuance also rose, from $7 billion to $15 billion. In particular, net issuance of yen-denominated bonds in Japan by non-Japanese issuers in the Japanese local market (samurai bonds) continued to be active at $7 billion in the second quarter of 2008, up from $4 billion the previous quarter.

By sector, private financial institutions showed a remarkable recovery, with net issuance of bonds and notes almost quadrupling in the second quarter of 2008 to $827 billion. Corporate issuance also rebounded, albeit to a lesser degree: net issuance increased to $131 billion, more than double the level of the previous quarter.
The breakdown by nationality of issuer indicates that the largest growth in net issuance was from UK borrowers, up from $12 billion to $186 billion, largely driven by an unprecedented level of activity by UK private financial institutions. A large increase also came from US, Spanish and French borrowers. By contrast, a decline in net issuance was recorded for Australian, Greek, Austrian and German borrowers.

The quarter saw a recovery in mortgage-backed bonds (for which only gross figures are available). Gross issuance of mortgage-backed bonds increased from the previous quarter’s $52 billion to $188 billion. By nationality, the largest increase was again from UK borrowers, from $8 billion to $90 billion (Graph 5, right-hand panel). Most of the UK issuance followed the Bank of England’s announcement in April 2008 of a Special Liquidity Scheme that enables UK banks to swap illiquid assets such as mortgage-backed securities against UK Treasury bills. Belgian and Irish borrowers showed a large increase as well. In particular, Bass Master Issuer in Belgium issued a series of euro-denominated mortgage-backed bonds that totalled more than $23 billion in June 2008. Meanwhile, the US government-sponsored agencies, Fannie Mae in particular, continued to play a large role in the international debt market. Fannie Mae issued $62 billion worth of bonds and notes, its highest quarterly level of issuance ever.

There was a rise in issuance across a wide range of credit classes. In particular, gross issuance of investment grade bonds with ratings less than AAA surged to $691 billion from $368 billion in the previous quarter. This level corresponds to more than double the five-year quarterly average throughout 2007. As for other credit classes, gross issuance of AAA-bonds showed a modest increase to $484 billion from $434 billion, while that of non-investment grade bonds went up to $11 billion from $2 billion.

In the emerging economies, net issuance of bonds and notes grew strongly, rebounding from the previous quarter’s decline. This coincided with a significant narrowing of emerging market bond spreads. The increase was most
marked in emerging Europe, followed by Latin America and Africa and the Middle East. By currency of denomination, most of the increase came from US dollar- and euro-denominated bonds and notes, but local currency denominated issuance also showed a recovery.

Borrowing through money market instruments continued to be fairly active, although net issuance of money market instruments decreased to $68 billion in the second quarter of 2008, from the record level of $154 billion in the previous one. The largest decline took place in euro-denominated instruments (Graph 5, centre panel). However, at $993 billion, gross issuance was virtually flat.

Derivatives markets

The second quarter of 2008 saw a retreat in activity on the international derivatives exchanges. Total turnover based on notional amounts decreased from the high of $692 trillion recorded in the first quarter to $600 trillion. Most of the contraction was due to derivatives on short-term interest rates, which had contributed most to the record turnover in the first quarter. Turnover also declined in derivatives on long-term interest rates and stock indices. By contrast, turnover in derivatives on foreign exchange gained modestly. Turnover in derivatives on commodities, measured only in terms of the numbers of contracts, dropped, although year-on-year growth remained quite high.

Turnover in derivatives on short-term interest rates contracted to $473 trillion in the second quarter of 2008 from the previous quarter’s $548 trillion. The most significant fall was in the US dollar segment, which had surged in the previous quarter, but turnover in the euro, sterling and Australian dollar segments also declined. In particular, turnover in futures and options on three-month eurodollar rates retreated markedly. This coincided with a further deterioration in liquidity conditions in term money markets over the quarter, as evidenced by widening spreads of US dollar Libor over the overnight index swap rate. However, turnover in futures and options on federal funds rates rose, almost reaching the record high of the fourth quarter of 2007.

Activity in equity derivatives fell to $67 trillion in the second quarter of 2008 from $73 trillion in the previous one, representing a year-on-year decrease of 3%. By currency of denomination, euro- and US dollar-denominated equity derivatives contracts declined the most. By contrast, the largest increase came from Korean won-denominated contracts.

Trading continued to be robust in the foreign exchange segment of the derivatives exchanges. Turnover grew from $6.7 trillion to $7.5 trillion in the second quarter of 2008, resulting in a year-on-year growth rate of 44%. The increase was attributable mostly to the euro, and offset a decline in currencies such as the yen and Australian dollar.

Trading in commodity derivatives declined from the record level of the previous quarter, but continued to be quite active. Global turnover in commodity derivatives measured in numbers of contracts (notional amounts are not available) decreased from 470 million to 434 million, although the year-on-year growth rate remained high at 37%. The largest fall was observed in...
agricultural derivatives, followed by precious metals, non-precious metals and energy products. The decline in turnover in agricultural derivatives came chiefly from Asian exchanges, in particular Chinese ones. This coincided with an easing of price increases in agricultural products over the quarter. Since the beginning of 2007 at least, the rise in commodity derivatives turnover has been largely in line with a significant increase in non-commercial traders’ net long positions, amid the relative decline in commercial traders’ positions (Graph 6).