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Highlights of international banking and financial market activity[1]

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 2009. The discussion on international debt securities and exchange-traded derivatives draws on data for the *second* quarter of 2009.

The international banking market

As tensions in financial markets began to subside in the first quarter of 2009, the contraction of banks' international balance sheets slowed. Banks still registered an $812 billion fall in their *interbank* positions comparable to that experienced in the fourth quarter of 2008, reflecting protracted funding pressures. However, the decrease in international credit to *non-banks*, at $258 billion, was only one fourth that seen in the previous quarter (Graph 1). Banks also trimmed their international credit to emerging markets, but their local lending from offices in emerging market host countries remained stable.

Contraction in credit to non-banks slows

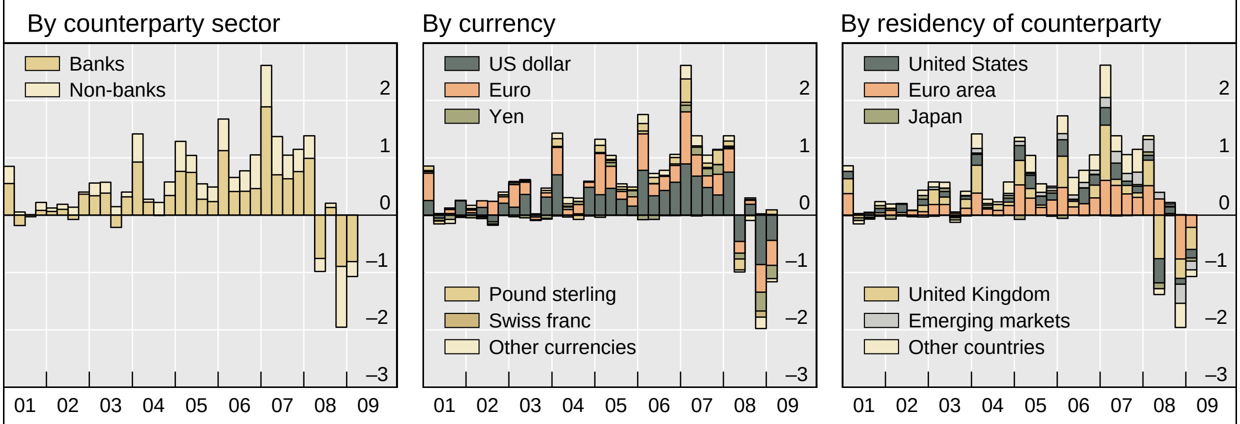
International bank credit to non-bank entities continued to decline in the first quarter of 2009. BIS reporting banks' international claims on these borrowers fell by $258 billion (to $12 trillion), much less than the $1 trillion decrease in the previous quarter (Graph 1). The drop occurred vis-à-vis non-bank residents of the United Kingdom (–$128 billion) and, to a lesser extent, Japan (–$40 billion) and emerging markets (–$29 billion).[2] By contrast, claims on non-bank entities in the United States changed little (Graph 2, left-hand panel).

[1] Queries concerning the banking statistics should be addressed to Patrick McGuire and Blaise Gadanecz, and queries concerning international debt securities and exchange-traded derivatives statistics to Naohiko Baba.

[2] Banks resident in the United Kingdom, Germany, Belgium, Hong Kong SAR, Ireland and Switzerland reported the largest declines in claims on non-banks.

Changes in gross international claims[1]

In trillions of US dollars



[1] BIS reporting banks' cross-border claims (including inter-office claims) in all currencies plus locally booked foreign currency claims on residents of BIS reporting countries.

Source: BIS locational banking statistics by residence. Graph 1

Further writedowns and disposals of debt securities contributed to the reduction in claims on non-bank borrowers in the first quarter (Graph 2, centre panel).[3] Banks, particularly those in major euro area countries and Asian financial centres, reported reduced holdings of securities issued by residents of offshore centres (by $16 billion) and emerging markets (by $14 billion). Conversely, banks increased their debt securities claims on non-bank entities in the United States by $20 billion, in part the result of greater claims on the US public sector (see below).

Higher claims on the public sector

A closer look using the BIS consolidated banking statistics, which contain a finer sectoral breakdown, shows that banks trimmed their exposures to the non-bank *private* sector, whereas claims on the public sector actually grew (Graph 2, right-hand panel).[4] In particular, several banking systems registered lower consolidated claims on the US non-bank private sector. Euro area banks' claims dropped by $120 billion, or 8%, while Swiss banks' claims fell by $57 billion, or 13%. Intra-euro area claims on the non-bank private sector, as well as claims on the UK non-bank private sector, registered modest declines after taking currency effects into account.[5] At the same time, banks increased

[3] Overall, the BIS locational banking statistics actually show a modest increase in holdings of debt securities ($5 billion), following a large decrease in the fourth quarter of 2008 (–$202 billion). The increase in the first quarter seems to reflect larger holdings of US and euro area government securities, as evidenced by the BIS international consolidated banking statistics. According to loss data reported to Bloomberg by 85 large internationally active banks, writedowns and disposals amounted to $80 billion in the first quarter of 2009 and $218 billion in the fourth quarter of 2008.

[4] In the first quarter of 2009, investment banks were included for the first time in the population of reporting institutions in the US consolidated banking statistics. This creates a break in series of approximately $800 billion in US banks' total international claims ($1 trillion in their foreign claims, if local positions in local currencies are included). All quarter-on-quarter changes discussed in this section are corrected for this and other breaks.

[5] No currency breakdown is available in the BIS consolidated banking statistics. However, assuming that banks' foreign claims on the euro area non-bank private sector are denominated in euros, claims decreased by $62 billion (2%). A similar calculation for claims

their holdings of US Treasuries; their exposure to the US public sector rose by $116 billion or 16%, with the largest increase reported by Japanese, UK and euro area banks. Banks' claims on the euro area public sector also grew, by $32 billion (2%), once exchange rate movements are taken into account. In contrast, claims on the Japanese public sector declined by $39 billion (10%).[6]

Derivatives positions fall in value as market conditions stabilise

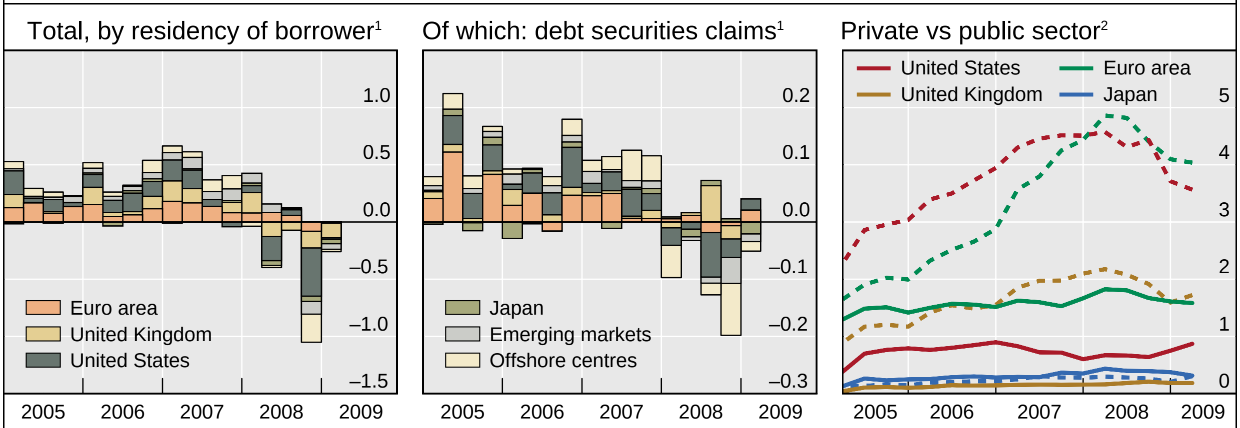
Banks also reported lower off-balance sheet positions, in part as a result of exchange rate movements. Reflecting a combination of cutbacks in new commitments and existing facilities not being rolled over, the value of undisbursed credit commitments, especially those granted by German, UK and Swiss banks, fell by $221 billion (5%) in the first quarter. Guarantees extended worldwide, including for trade credit, project loans and structured products, fell by $574 billion (9%). More than half of the decline was reported by US banks. Lastly, the value of derivatives contracts plunged by over $1 trillion (15%),[7] with UK banks responsible for half of this total.

Weak syndicated lending to non-banks in the second quarter

Data on syndicated loans suggest that lending to non-banks continued to be weak in the *second* quarter of 2009. Signings of international syndicated loan facilities granted to non-bank borrowers (in both advanced economies and emerging markets) in the first and second quarters of 2009 ($182 billion and $241 billion, respectively) were still only at approximately half their level of one year earlier. Average spreads over Libor on syndicated loan facilities continued to rise into the first quarter of 2009, but came down slightly in the second. In

Claims on the non-bank sector

In trillions of US dollars



[1] Quarter-on-quarter currency valuation adjusted changes. [2] BIS reporting banks' total consolidated claims on the public sector (solid lines) and the non-bank private sector (dashed lines). Stocks outstanding; not adjusted for movements in exchange rates.

Sources: BIS locational banking statistics; BIS consolidated banking statistics on an ultimate risk basis. Graph 2

on the UK non-bank private sector shows a $46 billion (3%) decline. The euro and sterling depreciated against the US dollar in the first quarter of 2009 by 4.6% and 2%, respectively.

[6] These calculations assume that claims on the euro area (Japanese) public sector are denominated in euros (yen).

[7] Banks' derivatives positions had risen during the crisis, particularly in the *fourth* quarter of 2008, reflecting the extent to which these positions moved "into the money" following central banks' coordinated interest rate cuts, as well as exchange rate movements and the general rise in volatility in all asset markets.

February and March, the ratio of the dollar volume of announced but not completed signings to total loan signings (for non-bank borrowers)[8] came down to levels closer to its historical trend, after spiking in November and then again in January.

Funding pressures persist

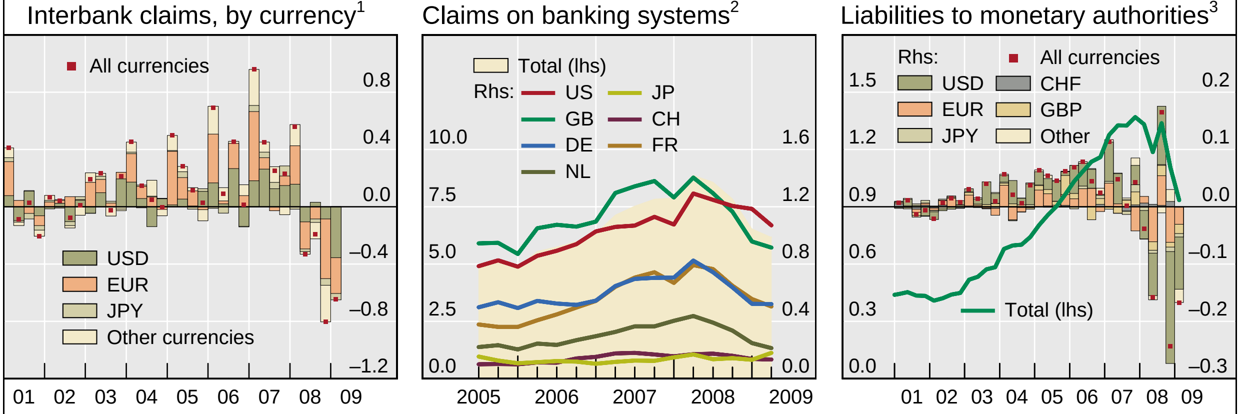
Interbank contraction continues

Throughout the crisis, but particularly after the Lehman failure, major central banks adopted unprecedented policy actions to supply banks with liquidity. Nevertheless, funding pressures remained evident in the first quarter, despite the reduction in Libor-OIS spreads and an easing of tensions in financial markets. Banks continued to trim their claims on other (unaffiliated) banks (Graph 3, left-hand and centre panels). The decline in these international positions, by a total of $646 billion, or 6%, occurred in both the euro and US dollar segments (it had affected mainly the euro segment in the fourth quarter of 2008). The contractions in interbank credit to euro area (–$348 billion), US (–$116 billion) and UK (–$67 billion) banks were the largest.

Contributing to banks' funding pressures, liabilities to central banks, which typically reflect deposits of foreign exchange reserves, continued to fall in the first quarter, albeit at a slower pace than in the previous one (Graph 3, right-hand panel). The $146 billion reduction (after adjusting for currency valuation effects) brought the outstanding stock of liabilities to monetary authorities to $932 billion, roughly two thirds of the peak level reached in the fourth quarter of 2007. The decline was registered by banks resident in the United Kingdom, the

Funding sources under pressure

In trillions of US dollars



[1] Exchange rate adjusted changes in international interbank credit to other (unaffiliated) banks. [2] Consolidated foreign claims (ultimate risk basis) of all reporting banks on banks headquartered in the country indicated in the legend; not adjusted for movements in exchange rates. [3] Exchange rate adjusted changes (stacked bars) in and stocks outstanding, expressed at constant Q1 2009 exchange rates (green line), of international liabilities to official monetary authorities.

Sources: BIS consolidated statistics (ultimate risk basis); BIS locational statistics by residence and nationality. Graph 3

[8] This ratio gauges the ease (or difficulty) with which lead arranger banks can place announced loan facilities on the market (syndicating them to second-tier banks and other participants). High values of the ratio signal a high syndication failure rate, suggesting insufficient market appetite to absorb the supply of new loans at the set of terms on offer.

United States and a number of other European countries, and mostly represented a withdrawal of US dollars.[9]

Banks' local lending in emerging markets holds up

Several banking systems continued to trim their exposures to emerging markets. While most registered reductions in the outstanding stock of international consolidated claims, their local positions in local currencies (corrected for currency valuation effects) remained relatively stable (Graph 4).[10]

Lower international claims on emerging markets, induced by valuation effects

Banks' consolidated international claims on emerging market borrowers fell by a combined $89 billion (4%) in the first quarter of 2009, although this was in part driven by the 4.6% depreciation of the euro against the US dollar.[11] Among those banking systems with the largest exposures to emerging markets, Austrian, German, Dutch, Swedish and UK banks reported the bulk of the decline (Graph 4, green lines). A large part of these banking systems' emerging market exposure is vis-à-vis counterparties in emerging Europe, where international claims dropped by $53 billion during the quarter. If one assumes that all international claims vis-à-vis these borrowers are denominated in euros, the adjusted decline is more modest, at $14 billion.

Looking only at international claims provides an incomplete picture of internationally active banks' total exposures to emerging markets. Indeed, most major banking systems' local claims in local currency are at least as large as their international claims (Graph 4). At one extreme are Spanish and UK banks. Spanish banks' local claims extended in local currencies to emerging market borrowers (mostly in Latin America) are three times the size of their international claims on the same borrowers, while those of UK banks are about 50% larger. At the other extreme are German and Swedish banks, whose international claims are about five times the size of their local claims in local currency.

Higher local positions in local currencies

As Graph 4 shows, after adjusting for currency effects and reporting breaks, local claims in local currencies on emerging market borrowers

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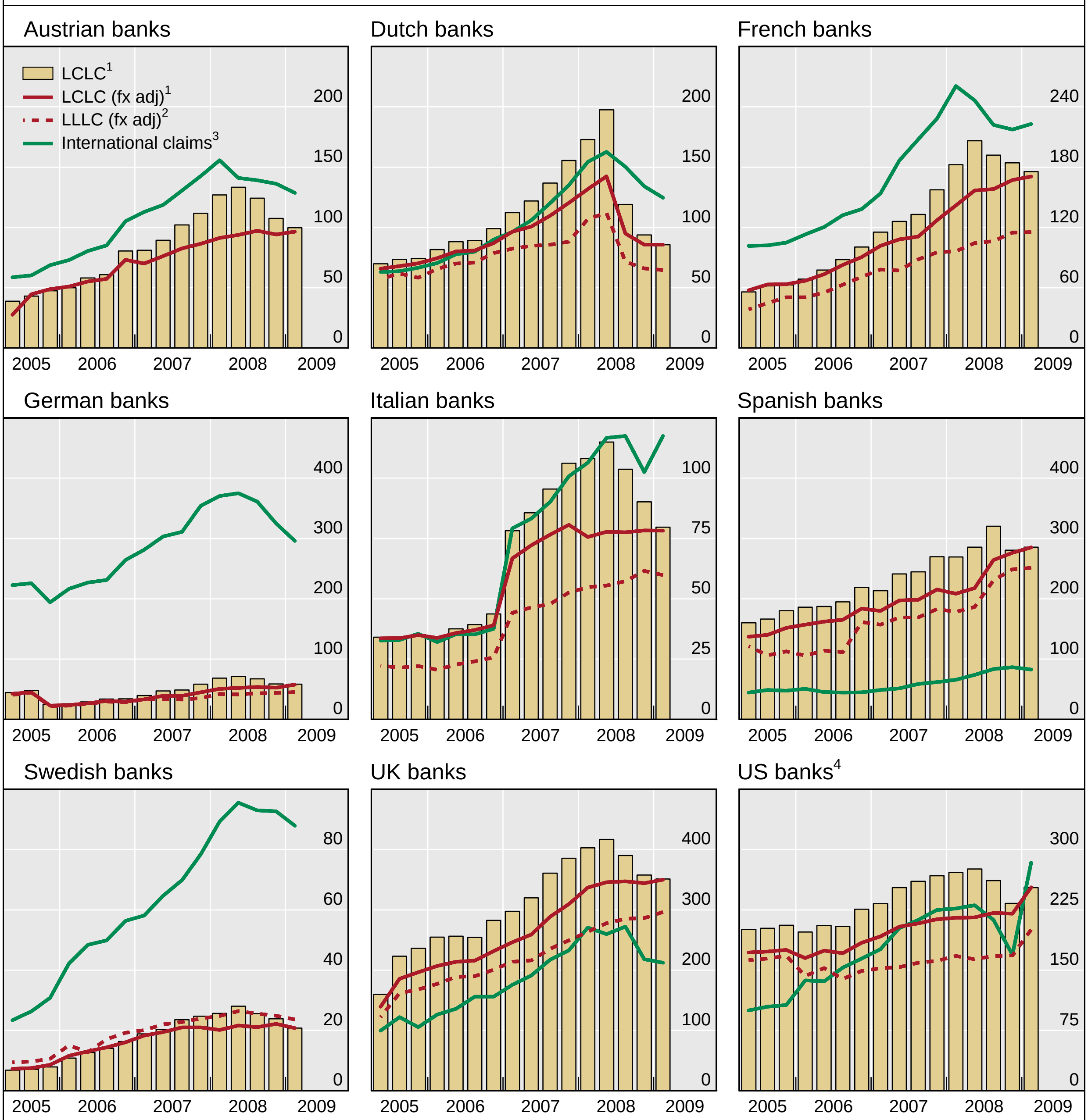
9 It is impossible to identify in the BIS banking statistics which central banks accounted for these moves. However, data on the composition of foreign exchange reserves reported by 63 monetary authorities to the IMF indicate that monetary authorities in Japan, the euro area, Thailand and Ukraine reported decreases in placements of foreign exchange reserves in commercial banks. BIS reporting banks also registered large moves (vis-à-vis all sectors) in liabilities to residents of reserve-accumulating countries. Banks' international liabilities to all oil-exporting countries worldwide decreased by $73 billion, with US dollar positions down the most.

10 The inclusion of US investment banks in the US reporting population (see footnote 4) accounts for the jump in US banks' local and international positions in the first quarter. Likewise, ABN AMRO sold some of its business units in the second half of 2008, which brought about a downward move in Dutch banks' positions during that period.

11 The BIS locational banking statistics, which track reporting banks' exchange rate adjusted *cross-border* claims (including their inter-office positions), also show a decline. Overall, cross-border claims on emerging markets dropped by $134 billion in the first quarter of 2009, a large drop by historical standards but considerably less than the $282 billion reduction in the previous quarter. Claims on Asia-Pacific fell by $59 billion, while claims on borrowers in emerging Europe dropped by $41 billion.

Claims on emerging markets

By banking system, in billions of US dollars



[1] Local claims in local currency, or local currency claims extended by banks' foreign offices to residents of the host country. The bars show reported claims whereas the solid red line tracks claims expressed at constant Q1 2009 exchange rates. [2] Local liabilities in local currency, adjusted for exchange rate movements. [3] International claims comprise cross-border claims in all currencies and local claims in foreign currencies extended by banks' foreign offices to residents of the host country; these claims are not adjusted for exchange rate movements, since no currency breakdown is available. [4] See footnotes 4 and 10 in the main text.

Source: BIS consolidated statistics (immediate borrower basis).

Graph 4

increased by $50 billion. Reporting banks, in particular Belgian, UK, German and French banks, expanded their claims, in particular to borrowers in Korea, Mexico and emerging Europe. Austrian banks' local currency claims extended by their offices in emerging Europe stood at $99 billion, little changed from the previous quarter. By contrast, Swedish banks' local claims in local currencies on Baltic country borrowers declined by 9%, to $14 billion.

The international debt securities market

Higher issuance led by government support …

Continued government support led to an increase in net issuance of international debt securities in the second quarter of 2009. Against a backdrop of robust gross issuance together with significantly lower repayments, net issuance rose to $837 billion, up from $668 billion in the first quarter. The increase was mostly accounted for by bonds and notes issued by financial institutions, particularly in the euro area, as well as public sector borrowers. By contrast, possibly reflecting the shift to longer-term debt instruments, money market borrowing continued to stagnate with net repayments of $68 billion.

… dominated by bonds and notes in euros

Net issuance was dominated by bonds and notes denominated in euros, followed by those in dollars (Graph 5, left-hand panel). Net issuance in euros rose to $429 billion from $276 billion in the first quarter. By contrast, net sterling issuance decreased by almost half to $59 billion. Yen issuance contracted further, with net repayments of $12 billion. The Swiss franc segment saw a retreat from the record level in the previous quarter, but remained strong with net issuance of $9 billion.

The breakdown by nationality largely mirrors the pattern of the currency composition. In particular, French net issuance more than tripled to $131 billion in the second quarter. Conversely, net issuance by Swiss, UK and Japanese borrowers dropped. US net issuance also fell slightly, despite the increase in dollar-denominated issuance.

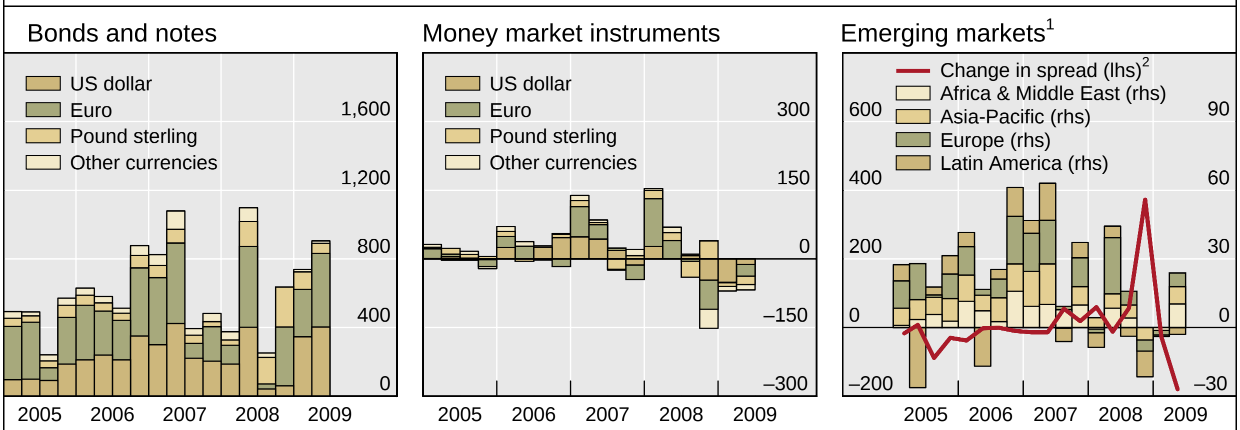
Strong issuance by financial institutions

Supported by government guarantee schemes, particularly in the euro area, financial institutions recorded the largest increase in net issuance of bonds and notes in the second quarter, from $427 billion to $544 billion. By credit quality class (for which only gross figures are available), gross issuance of investment grade bonds by financial institutions continued to be robust, while issuance of non-investment grade bonds remained weak.

Corporate borrowing fell slightly, from $181 billion to $172 billion. Borrowing by US corporations declined the most, from $121 billion to $81 billion. In contrast to the issuance by financial institutions, gross issuance

International debt securities issuance

Net issuance, in billions of US dollars



[1] Bond and note issuance, by nationality. [2] Quarterly change in spread of JPMorgan EMBI Global Composite index, in basis points.

Sources: Dealogic; Euroclear; Thomson Reuters; Xtrakter Ltd; BIS. Graph 5 of non-investment grade bonds by corporate borrowers picked up sharply in the second quarter.

Larger presence of public sector borrowers

Public sector borrowers continued to play a significant role in the international debt securities market in the second quarter. Their net issuance of bonds and notes rose to an all-time high of $348 billion. In particular, international organisations doubled net issuance of bonds and notes to $65 billion; the main issuers were the EIB and the IBRD. Governments increased net issuance from $98 billion to $124 billion. The most active government borrower in the second quarter was Greece, followed by Spain, the United Kingdom and France.[12] Borrowing by public financial institutions was also active at $139 billion, although it fell short of the record level in the previous quarter.

The shift from floating to straight fixed rate borrowing continued, as borrowers sought to lock in low interest rates. Also, equity-related bonds and notes recorded positive net issuance, which was last seen in the second quarter of 2008, against the background of the recovery in equity markets.

Strong recovery in emerging markets

In the emerging economies, net issuance of bonds and notes recovered strongly to $21 billion from net repayments of $4 billion in the previous quarter (Graph 5, right-hand panel). This coincided with a significant narrowing of emerging market bond spreads. The increase was most marked in Africa and the Middle East, followed by emerging Europe and Asia-Pacific. By contrast, Latin American borrowers continued to repay their debt. By nationality, the United Arab Emirates, Korea and Russia showed a particularly strong recovery.

Net repayments in the money market

Borrowing via international money market instruments continued to stagnate. Money market net borrowing was –$68 billion in the second quarter, compared to –$70 billion in the previous one (Graph 5, centre panel). The net repayments of money market debt possibly reflect the shift to issuance of longer-term bonds and notes, given the rollover risks highlighted during the recent financial turmoil. By currency, large decreases were recorded in the euro, sterling and Swiss franc segments, while the US dollar segment decreased net repayments substantially to $13 billion from $51 billion in the previous quarter.

Derivatives markets

Small rebound in derivatives activity

The second quarter of 2009 saw a small rebound in activity on the international derivatives exchanges, although trading volumes were still well below the pre-crisis level two years before. Total turnover based on notional amounts increased to $426 trillion from $366 trillion in the previous quarter, consistent with a return of risk appetite (Graph 6).

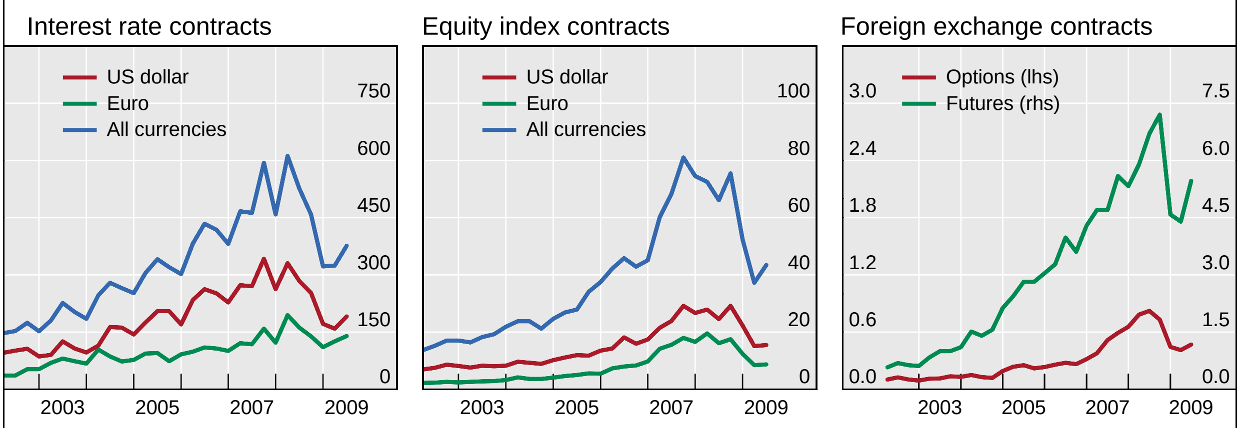
Robust activity in derivatives on US dollar short-term interest rates

The increase was mostly accounted for by derivatives on short-term interest rates. Turnover in this segment rose to $344 trillion in the second quarter, compared to $294 trillion in the previous one (Graph 6, left-hand panel). The increase was most marked in US dollar contracts, followed by euro,

[12] International bonds and notes only, comprising all foreign currency issues plus all domestic currency issues launched in the domestic market by non-residents.

Turnover of exchange-traded derivatives[1]

Quarterly data, in trillions of US dollars



[1] Futures and options.

Sources: FOW TRADEdata; Futures Industry Association; BIS calculations. Graph 6

sterling and yen contracts. In particular, turnover in futures on three-month eurodollar rates picked up sharply to $115 trillion from $96 trillion in the previous quarter, possibly due to stabilising money market conditions amid a gradual retreat of concerns over the financial system.

Turnover in equity index derivatives also increased in the second quarter, from $37 trillion to $43 trillion (Graph 6, centre panel). The increase was attributable in large part to the Korean market, where trading volumes rose significantly from $7.6 trillion to $12.0 trillion in the second quarter chiefly as a result of rising equity valuations. Global turnover measured in the number of contracts traded rose only by less than 100 billion.

Activity in foreign exchange derivatives began to recover as well (Graph 6, right-hand panel), with turnover increasing to $5.9 trillion from $4.8 trillion in the previous quarter. The gain in activity among the main currencies was particularly marked for contracts with one leg in sterling. A significant increase in notional amounts of futures contracts in such currency segments as the Australian and Canadian dollar, Swiss franc and New Zealand dollar possibly reflected renewed interest in FX carry trades as investors' confidence returned.

Trading in commodity futures and options increased slightly in the second quarter. Global turnover in commodity derivatives measured in numbers of contracts (notional amounts are not available) stood at 446 million, compared to 423 million in the previous quarter. Major contributors were contracts on agricultural products and non-precious metals, while trading in energy derivatives fell.