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II. Highlights of international financing

1. The international banking market

The first quarter of 2000 saw extraordinarily intense activity in the international banking market. The activity was driven by interbank transactions, which served to rechannel funds to non-bank borrowers in Europe. As a result, banks more than doubled their cross-border loans to the non-bank sector in developed countries. Banks continued to purchase international securities at a somewhat slower rate than that established during 1999. Also, lending in all European currencies was up by 11%, while there was limited growth in yen positions because Japanese banks continued to unwind lending from overseas branches. Repayments from developing countries appear to have bottomed out, with some resumption of new lending to Asia.

Table II.1.1

Main features of cross-border claims of BIS reporting banks[1]

In billions of US dollars

	1998	1999					2000	Stocks at end-March 2000
	Year	Year	Q1	Q2	Q3	Q4	Q1	
Claims on developed countries	**564.7**	**438.1**	**90.3**	**60.0**	**193.0**	**94.7**	**446.9**	**7,820.7**
of which: intra-euro 11	*296.7*	*250.2*	*131.9*	*35.0*	*84.7*	*– 1.3*	*107.1*	*1,570.7*
Interbank loans	285.9	23.3	– 18.3	– 83.4	126.4	– 1.5	321.4	4,710.7
Loans to non-banks	21.5	100.7	5.9	67.2	2.9	24.8	65.4	1,399.7
Securities[2]	257.4	314.1	102.7	76.2	63.7	71.4	60.1	1,710.3
Claims on offshore centres	**–172.3**	**–105.4**	**– 69.1**	**– 44.7**	**– 26.4**	**34.8**	**– 50.4**	**1,158.1**
Interbank loans	–166.7	–140.3	– 78.1	– 51.7	– 47.2	36.6	– 62.3	804.0
Loans to non-banks	– 26.7	6.7	2.6	1.0	12.7	– 9.6	2.4	227.3
Securities[2]	21.1	28.2	6.4	5.9	8.1	7.8	9.5	126.8
Claims on developing countries[3]	**– 78.9**	**– 60.5**	**– 5.5**	**– 21.1**	**– 31.2**	**– 2.7**	**– 2.2**	**915.6**
Interbank loans	– 63.6	– 57.6	– 10.4	– 20.4	– 22.5	– 4.3	6.8	372.7
Loans to non-banks	– 8.9	– 9.5	4.6	– 3.3	– 8.8	– 2.0	– 15.7	411.3
Securities[2]	– 6.5	6.5	0.2	2.7	0.0	3.6	6.7	131.6
Unallocated	**– 33.9**	**– 31.2**	**– 2.5**	**– 5.5**	**– 13.6**	**– 9.5**	**9.7**	**199.6**
Total	**279.5**	**241.0**	**13.2**	**– 11.4**	**121.8**	**117.4**	**403.9**	**10,094.2**
Interbank loans	31.9	–224.8	–113.4	–156.0	37.7	6.9	269.5	5,958.1
Loans to non-banks	– 26.7	90.1	1.0	62.2	6.1	20.8	53.6	2,069.5
Securities[2]	274.3	375.7	125.6	82.4	78.0	89.7	80.8	2,066.6
Memorandum item: Syndicated credits[4]	*902.0*	*957.1*	*172.5*	*271.1*	*264.3*	*249.2*	*269.2*	

[1] Changes in amounts outstanding excluding exchange rate valuation effects. [2] Partly estimated. The data include other assets, which account for less than 5% of the total claims outstanding. [3] Including eastern European countries. [4] Announced new facilities.

Interbank activity surges as the market rechannels funds to Europe

The most striking development in the international banking market in the first quarter of 2000 was a surge in cross-border interbank lending within the developed countries. The sum of these lending flows rose to $321 billion, the largest such amount since the fourth quarter of 1997. The main impetus for the surge appears to have been a strong demand for financing by borrowers in Europe, particularly by telecommunications firms. To meet this demand, international banks rechannelled funds through various banking centres around the world, in the process causing interbank balance sheets to expand sharply. This surge in activity resembled the multiplier process observed in 1997, when the growth in interbank activity was driven by an effort to recycle large repayment flows from borrowers in Asia during the financial crisis in that region.

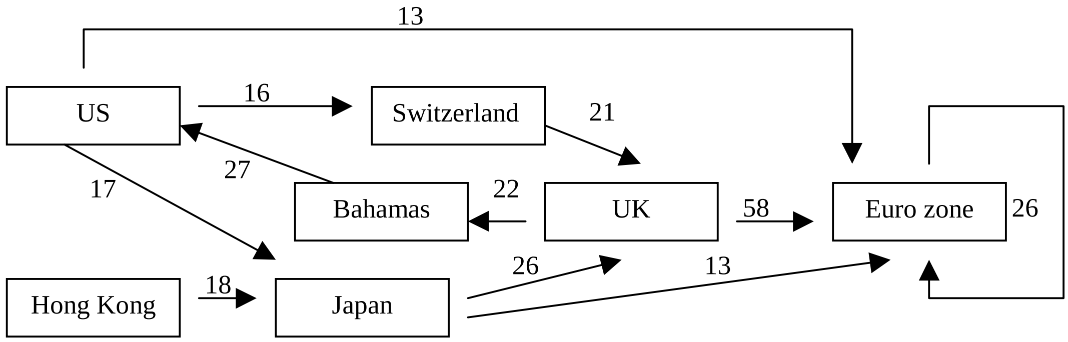
Taking into account both assets and liabilities, the largest net interbank flows during the recent quarter involved banking centres in the United States, Switzerland, Hong Kong, Japan and the United Kingdom. Interbank funds appear to have been raised in New York and Hong Kong, passed on to Zurich and Tokyo and pooled in London, although not necessarily in that sequence. Euro area banking centres were able to draw heavily on these funds. The major net changes in interbank claims are illustrated in Graph II.1.1. With each cross-border transaction adding to outstanding positions, the rechannelling process led to an aggregate increase in interbank assets amounting to about five times the increase in international loans to non-banks in this quarter.[3]

Some of the interbank fund-raising took the form of a winding-down of short-term inter-office claims on offshore centres by banks in the United States and Japan. In particular, US banks received large repayments from their own offices in the Bahamas, which more than accounted for a $20 billion decrease in claims on the offshore centre. At the same time, a $25 billion contraction in claims on Hong Kong and an $11 billion fall in claims on Singapore were largely due to the further unwinding of Japanese banks' "yen impact" loans, ie yen funds lent to companies resident in Japan, but channelled via Japanese banks' overseas branches[4].

Graph II.1.1

Major net interbank flows in 2000 Q1[1]

In billions of US dollars



[1] Only includes the largest net flows into and out of the country or region. For example, a flow of $13 billion from the United States to the euro zone implies that banks in the United States added $13 billion in claims (net of liabilities) to banks in the euro area.

[3] Gross increases in interbank asset stocks can exceed net increases by further substantial amounts, since banks will build up additional liability and asset positions as they parcel up and distribute wholesale funds to banks in other reporting countries until all funds have been placed with non-bank borrowers.

[4] See Bank of Japan, *Quarterly Bulletin* (May 2000), p 176.

New developments in the banking statistics

In this quarter, there are some changes in the content and presentation of the locational banking statistics. Firstly, the reporting population has been expanded: Australia's and Portugal's locational data have been incorporated from the fourth quarter of 1997 onwards, increasing the coverage of BIS banking data by about 1% of reported assets.[①] Furthermore, the locational data reclassified by the nationality of the head office of the reporting banks now include submissions from Australia and Portugal (from end-1997 onwards), the Cayman Islands (from end-1999) and Bahrain (from the first quarter of 2000).

Secondly, the layout of Table 1 in the statistical annex has changed: the regional concept of the "BIS reporting area" is no longer used to classify external assets and liabilities. Due to an expansion in the number of countries reporting to the BIS, data in this classification would be difficult to compare over time. Instead, asset and liability exposures are now broken down by major instrument: loans and deposits, holdings of securities and other assets on the assets side and loans and deposits, own issues of securities and other liabilities on the liabilities side.

Thirdly, the country classification of the banking statistics has been revised slightly in several annex tables. For example, successor republics to the former Soviet Union located in Asia are now classified under developing countries in Asia and no longer under Europe.

[①] The published banking flows have been adjusted to eliminate distortions that would result if flows were computed including the increases in stocks due to additional reporting banks.

More generally, a small part of the rise in interbank flows may have reflected business that had been deferred to guard against possible Y2K disruptions. A similar dip and recovery after the millennium change can be seen in the turnover data on major exchange-traded short-term interest rate futures (Graph II.3.2), which are used actively by banks to hedge borrowing and lending requirements in the interbank market. The same shift was also evident in net international bond issues (Graph II.2.1).

Lending to non-bank borrowers strengthens

International banks employed the funds made available through the interbank market and slowed down their investment in securities somewhat to support renewed lending to non-bank borrowers in developed countries. Cross-border loans to these borrowers reached $65 billion in the first quarter of 2000, much of the money going to borrowers in the United States, the euro area and the United Kingdom. Non-bank residents in the United States received $33 billion, in the euro area $29 billion and in the United Kingdom $8 billion. Cross-border investments in securities totalled $60 billion, the lowest level since the third quarter of 1998.

Banks in the United Kingdom were the largest providers of direct cross-border credit to non-bank borrowers in developed countries. These banks provided $24 billion in loans and $12 billion in securities investments to borrowers in the United States, $6 billion in loans to borrowers in Japan, a further $5 billion to the Netherlands and $4 billion in securities investments to borrowers in Italy.

Syndicated loans for mergers and acquisitions by telecommunications firms appear to account for a significant part of such lending flows. The two largest international lending deals signed in the first quarter were a €30 billion facility to support the takeover of Germany's Mannesmann AG by the United Kingdom's Vodafone Airtouch and a €13 billion facility to finance the acquisition of Germany's E-Plus by the Netherlands' KPN. The lending upswing in Europe also reflected stronger economic growth and booming house prices especially in Ireland, the Netherlands, Finland and Portugal, where banks may have drawn from the international market to finance domestic lending.

Syndicated credits in the second quarter of 2000

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With $297 billion of announced new facilities, the second quarter of 2000 was the most active for international syndicated credits since 1997. While the increase on the previous quarter was 10%, the second quarter has typically been a strong quarter, and adjusting for this seasonality would convert the quarterly change into a 29% drop. After a record amount of deals to finance mergers and acquisitions in the first quarter, the second quarter saw an almost 50% decline in such business. Nonetheless, the telecommunications sector, where many of the mergers took place, continued to account for some of the biggest transactions.

Developed countries made up nearly 90% of total new facilities, with US and British borrowers getting the lion's share. The largest deal was a £16 billion commercial paper backup facility for British Telecom. Seven large US banks and securities firms also borrowed at least $2 billion each. Outside the developed countries, the most notable hub of activity was Hong Kong, where borrowers obtained a total of $14 billion, including $9 billion to finance the acquisition by Pacific Century CyberWorks of a majority stake in Hong Kong Telecom from parent company Cable & Wireless of the UK. Figures from Capital Data Loanware indicate that in the first half of the year there were about $40 billion worth of revolving international syndicated loans[①] geared, at least partially, to support the planned purchases by telecommunications companies of third-generation mobile phone licences auctioned off by various European governments. They included a €30 billion credit arranged for France Telecom, some of which helped it pay for Orange's UMTS (Universal Mobile Telecommunications System) licence as it acquired that company.

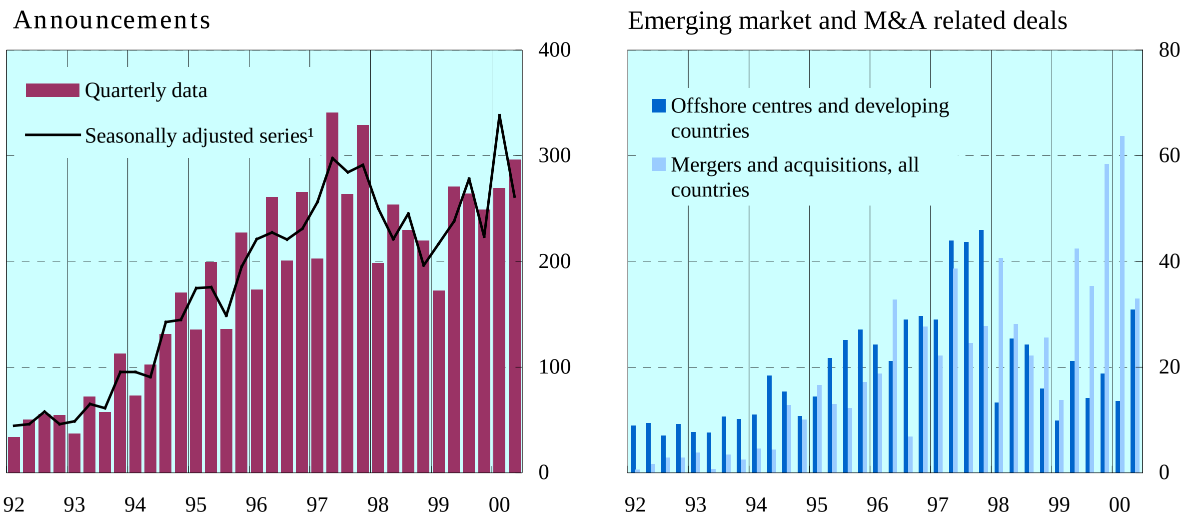
Developing countries accounted for only 5% of total activity. The largest such facilities were a $1.5 billion refinancing package in two tranches for the South African Reserve Bank and a $600 million term loan to finance the expansion of a petrochemical plant for Arabian PetroChemical Co of Saudi Arabia.

Transactions are bigger than ever. The average facility size has risen steadily since 1992, when the BIS began compiling the statistics, and has stepped up in 2000, reaching a record of $426 million in the most recent quarter. The average number of fund providers has remained constant at around 10, suggesting that individual syndicate members are providing larger amounts, at least initially. Meanwhile, the share of "club deals", which are not widely advertised to the market but reserved for a limited number of insiders, has grown from 4% of the total in 1993 to 6% in the first half of 2000.

Box Graph II.1.1

Announced facilities in the international syndicated credit market

In billions of US dollars



[1] US Census Board X11 Arima seasonal adjustment process (multiplicative method).

Sources: Capital DATA; BIS.

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① Note that these facilities are not yet included in Table 10 of the statistical annex, which classifies the facilities based on the signing date. These credits have been confirmed as funded, but not signed, during the first half of 2000.

Table II.1.2

Banks' claims on developing countries[1]

In billions of US dollars

	1998	1999					2000	Stocks at end-March 2000
	Year	Year	Q1	Q2	Q3	Q4	Q1	
Total claims	**–78.9**	**–60.5**	**– 5.5**	**–21.1**	**–31.2**	**– 2.7**	**– 2.2**	**915.6**
Africa & Middle East	21.8	1.9	– 2.0	– 3.7	2.2	5.4	– 6.7	153.9
Saudi Arabia	6.4	2.0	– 0.5	– 0.4	2.0	0.9	– 1.3	25.1
South Africa	– 0.6	– 1.0	1.2	0.0	– 1.5	– 0.6	– 0.3	17.9
Asia & Pacific	–96.6	–54.3	– 4.2	– 8.1	–24.4	–17.6	2.4	317.4
China	–10.3	–16.0	– 2.6	– 0.4	– 7.3	– 5.7	0.1	66.6
Indonesia	–14.1	– 6.2	0.8	– 2.1	– 3.7	– 1.1	– 1.5	44.4
Korea	–32.9	– 5.1	2.1	– 0.2	– 1.3	– 5.8	5.6	75.0
Malaysia	– 6.7	– 4.1	– 0.2	– 0.8	– 1.5	– 1.5	0.3	20.2
Philippines	– 0.8	0.5	0.0	1.0	– 1.8	1.2	– 0.7	16.3
Thailand	–28.9	–17.2	– 5.3	– 2.7	– 5.8	– 3.5	– 0.4	35.4
Europe	3.8	8.0	3.2	– 2.1	2.0	4.8	– 0.1	161.3
Russia	– 6.1	– 8.1	– 3.6	– 1.5	– 1.7	– 1.4	– 1.4	41.4
Turkey	2.8	6.6	2.8	1.1	1.4	1.3	2.5	41.0
Latin America & Caribbean	– 8.0	–16.1	– 2.6	– 7.2	–11.0	4.7	2.2	283.0
Argentina	0.6	0.6	1.5	– 0.1	– 2.0	1.1	– 1.8	46.3
Brazil	–10.2	– 8.7	– 6.2	– 3.2	– 3.3	4.0	2.0	88.6
Chile	– 0.4	– 1.7	0.3	– 0.8	– 1.0	– 0.2	0.7	19.1
Mexico	0.4	– 4.2	0.0	– 1.5	– 1.7	– 1.0	– 1.3	59.6

[1] Including eastern Europe. Changes in amounts outstanding excluding exchange rate valuation effects.

Repayments from developing countries bottom out

Repayments from emerging markets appear to have bottomed out in the first quarter (Table II.1.2). These repayments had averaged $15 billion a quarter in 1999 and were down to $2.2 billion in the more recent quarter. In fact, there was a small resumption of lending to Asia, following 10 consecutive quarters of repayments. The fall in claims on developing countries was more than accounted for by a $6.7 billion reduction on Africa and the Middle East, most of which was due to a reduction in US positions on the Middle East. There was some new bank credit to Latin America, while exposures vis-à-vis developing countries in Europe remained relatively unchanged.

Borrowers in *Asia* in aggregate received net new lending of $2.4 billion. Following a large repayment in the fourth quarter of 1999, South Korea borrowed $5.6 billion from international banks, reflecting trade credit for booming imports. The BIS consolidated banking statistics show that Korean short-term debt to international banks has been rising again (to $39 billion or 58% of claims outstanding) after shrinking to $30 billion at end-1998. This ratio is higher than the average for Asian countries (Table II.I.3), but it is still far below the peak of $71 billion at June 1997 (68% of claims outstanding). Moreover, South Korea's foreign exchange reserves of about $80 billion in the first quarter of 2000 comfortably exceeded these short-term claims.[5] In contrast, the biggest net reductions in banks' claims were reported vis-à-vis Indonesia ($1.5 billion) and India ($1.1 billion).

Bank claims on *Latin America and the Caribbean* increased by $2.2 billion, with borrowers in the region continuing to rely more heavily on securities issuance than on bank loans (Graph I.8). Strong

[5] A comprehensive analysis of external liquidity would need to take developments in other liability and asset positions into account.

GDP growth in Brazil was reflected in about $1.2 billion of external borrowing by the banking sector.[6] Chile, the only other major Latin American borrower in the first quarter, attracted $0.7 billion of fresh credit. Borrowers in Argentina and Mexico repaid funds: $1.8 billion and $1.3 billion respectively.

There was a marginal cutback in lending in aggregate to developing countries in *Europe* during the first quarter. However, within the region, bank credit to Turkey increased by $2.5 billion while that to Russia fell by $1.4 billion. Turkey's borrowing was mostly short-term and reflected a generally improved economic context supported by high privatisation receipts and an IMF-sponsored economic stabilisation package. Meanwhile, international banks continued to reduce their exposure to Russian banks, while a modest amount of Russian non-bank international securities was purchased by UK banks. In February, Russia reached an agreement in principle with its London Club of commercial creditors to restructure its Soviet-era debt.

Lending shifts towards European currencies

The strong expansion of the interbank market was reflected in a 11% increase in lending in the euro, pound sterling and Swiss franc (Table II.1.4).[7] Intra-euro 11 transactions in euros also grew strongly, by 8%. Lending in US dollars and yen increased by only 3%, but relative to a very large base in the case of the dollar. Japanese banks continued to unwind "yen impact" loans, so that lending by banks in London and Frankfurt accounted for most of the increase in yen positions. Noteworthy once again was the small increase in the use of other and unallocated currencies, suggesting that international banks are perhaps limiting their exchange rate and liquidity exposure in more exotic currencies.

Table II.1.3

Maturity breakdown of cross-border claims outstanding by residence of borrower

Percentage shares of amounts outstanding in 2000 Q1

	Developed countries	**Offshore centres**	**Developing countries**			
			Africa & Middle East	**Asia & Pacific**	**Europe**	**Latin America & Caribbean**
Up to and including one year	57.2	51.2	54.3	46.9	40.5	48.3
Over one year and up to two years	2.8	9.1	7.0	7.7	8.0	6.9
Over two years	20.4	27.5	33.9	29.4	42.7	35.9
Unallocated	19.7	12.2	4.8	16.0	8.8	8.8
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: BIS consolidated banking statistics.

6 Excluding a participation investment of a Dutch bank in a Brazilian bank.

7 The data on foreign currency lending cover banks' foreign currency positions with residents as well as cross-border positions that involve a foreign currency for either lender or borrower. Hence, the reported flows exclude cross-border transactions in euros between residents of the euro area.

Table II.1.4

Composition of foreign currency bank lending[1]

In billions of US dollars

	1998	1999					2000	Stocks at end-March 2000
	Year	Year	Q1	Q2	Q3	Q4	Q1	
US dollar	88.4	22.8	–112.1	17.1	26.9	90.9	122.5	4,648.1
Euro[2]	137.1	228.8	153.1	8.8	91.2	– 24.3	180.0	1,759.1
Japanese yen	– 37.2	–217.2	–147.2	– 74.9	– 26.1	31.0	28.1	950.1
Pound sterling	51.6	18.7	22.0	6.1	8.0	– 17.4	52.2	516.5
Swiss franc	23.5	37.5	22.6	– 0.1	15.3	– 0.3	34.7	342.8
Other and unallocated	–153.7	– 98.3	..	– 8.8	– 53.5	2.7	8.2	1,860.5
Total	**109.7**	**– 7.7**	**–100.1**	**– 51.8**	**61.8**	**82.6**	**425.7**	**10,077.1**
Memorandum item: Cross-border domestic currency intra-euro 11 positions	*160.7*	*286.3*	*142.2*	*48.9*	*87.8*	*7.3*	*103.9*	*1,292.7*

[1] Changes in amounts outstanding excluding exchange rate valuation effects. The data on foreign currency lending cover banks' foreign currency positions with residents as well as cross-border positions that involve a foreign currency for either lender or borrower. Hence, the data exclude cross-border transactions in euros between residents of the euro area. [2] For 1998, data relate to five euro legacy currencies (BEF, DEM, FRF, ITL and NLG) and the ECU, which were reported separately. Changes for 1999 Q1 are adjusted on an estimated basis to exclude the data for six euro legacy currencies (ATS, ESP, FIM, IEP, LUF and PTE) that were previously not reported separately but included under "Other and unallocated".