Philip D Wooldridge

(+41 61) 280 8819
philip.wooldridge@bis.org

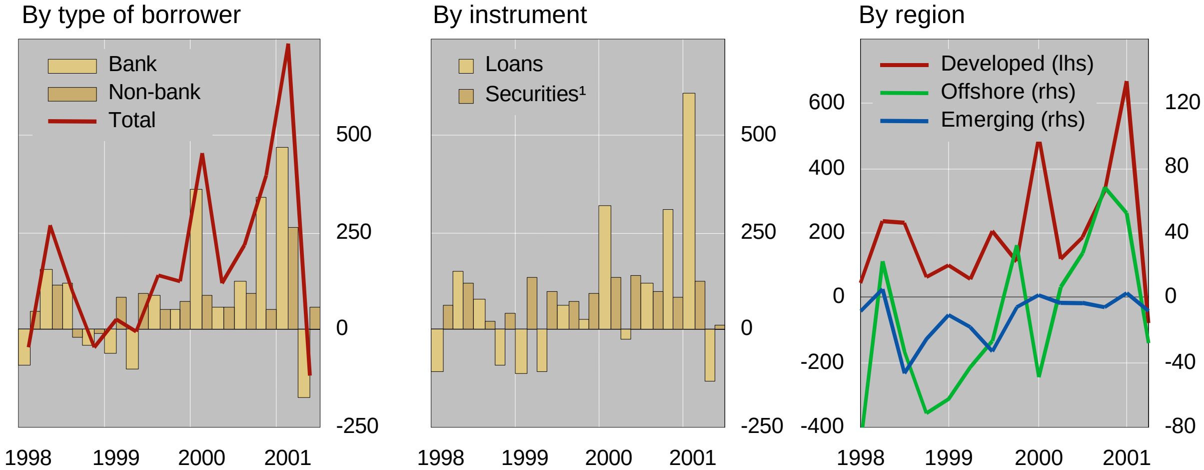
2. The international banking market

Weak demand for bank financing restrained the growth of the international banking market in the second quarter of 2001. The locational banking statistics indicate that cross-border claims of BIS reporting banks fell by $118 billion in the second quarter to $10.9 trillion (Graph 2.1). Cross-border flows to corporations and other non-bank borrowers slowed considerably from the first quarter's remarkably high levels, as the deterioration in global economic conditions dampened demand for new bank financing. With no need to recycle either large repayments from non-bank borrowers or loans to such borrowers, banks unwound some of the large interbank positions they had built up in the previous quarter. Consequently, cross-border claims on banks contracted by a record $175 billion.

The picture in emerging economies was more mixed. Demand in several regions remained weak, with Asia and oil-exporting countries in particular continuing to post current account surpluses. Banks in the reporting area reduced their cross-border claims to countries perceived to be higher risks, such as Turkey. They increased their claims on several other lower-grade

Cross-border claims of BIS reporting banks

Exchange rate adjusted changes in amounts outstanding, in billions of US dollars



[1] Mainly debt securities. Other assets account for less than 5% of total claims outstanding. Data are partly estimated.

Graph 2.1

borrowers, including Argentina, but at the same time limited their ultimate risk exposure through the use of credit risk mitigants such as guarantees. Overall, cross-border claims on emerging economies fell by $8 billion in the second quarter.

Weakening demand for dollar interbank funding

Large decline in dollar-denominated interbank claims

Following several quarters of rapid growth, the international interbank market contracted by $204 billion in the second quarter (Table 2.1). A weakening of demand for US dollar funding appears to have been responsible for much of the contraction. Repayments to banks in the Caribbean and other banking centres resulted in a $100 billion decline in dollar-denominated interbank claims. The turnaround in lending by US banks was especially noteworthy. Banks abroad had tapped banks in the United States for substantial amounts of dollar funding in the final quarter of 2000 and first quarter of 2001. By contrast, in the second quarter they paid down their outstanding dollar loan balances.

In the euro segment of the international interbank market, activity returned to more normal levels in the second quarter, with claims increasing by $10 billion, down from the first quarter's exceptionally high level of $315 billion. Flows between the United Kingdom and the euro area, which had driven the expansion in the first quarter, reversed direction in the second, resulting in a partial unwinding of cross-border euro positions on the United Kingdom. Intra-euro area business, on the other hand, continued to expand. The largest transactions were between banks domiciled in Germany and France and their offices in Luxembourg.

International interbank claims

Exchange rate adjusted changes in amounts outstanding, in billions of US dollars

	1999	2000				2001		Stocks at end-June 2001
	Year	Year	Q2	Q3	Q4	Q1	Q2	
Total claims on banks[1]	12.6	945.4	62.7	145.3	323.8	569.0	– 204.1	7,971.8
of which: cross-border	*– 17.2*	*892.8*	*60.1*	*126.5*	*342.5*	*472.0*	*– 175.0*	*7,206.9*
US dollar	– 108.3	324.9	37.8	77.5	116.4	146.0	– 100.1	3,269.1
Euro	281.8	312.1	31.4	27.5	39.5	314.5	10.3	2,091.5
of which: intra-euro area[2]	*154.3*	*88.4*	*– 13.1*	*10.9*	*15.8*	*63.9*	*25.7*	*774.8*
Japanese yen	– 195.9	81.8	– 5.4	– 2.4	88.0	– 9.2	– 21.6	580.6
Pound sterling	– 0.3	65.4	4.4	9.4	4.0	52.9	– 41.0	354.6
Swiss franc	14.5	– 0.7	– 29.3	7.2	– 11.2	18.8	– 12.9	186.9
Other currencies[3]	20.9	161.8	23.9	26.2	87.2	45.9	– 38.7	1,489.1

[1] Cross-border claims on banks in all currencies and local claims on banks domiciled in reporting countries in foreign currencies. [2] Euro-denominated cross-border claims of reporting banks in the euro area on residents of the euro area. [3] Including unallocated currencies.

Table 2.1

Banks willing to lend but finding few borrowers in the United States

The shift in funding patterns in the interbank market reflected a fall-off in flows to non-bank borrowers in the second quarter. The deterioration in the global economic outlook muted non-bank demand for new bank financing; as a result, cross-border flows to non-banks slowed to $57 billion in the second quarter from $267 billion in the first (Table 2.2).

Fall-off in cross-border flows to US non-banks ...

Just as the expansion in the first quarter had been driven by flows to the United States, so too was the slowdown in the second. Cross-border claims on non-bank borrowers in the United States increased by only $10 billion in the second quarter, the smallest increase in two years. Both lending and securities purchases were weak.

... even as syndicated lending rises

The slowdown in cross-border flows to US non-banks is surprising considering that US borrowers raised a record amount (in gross terms) in the international syndicated credit market in the second quarter. The conflicting movements in the locational and syndicated banking statistics suggest that syndicated loans were either intended primarily as backup facilities and so were not drawn down, or were used to refinance maturing loans, or were sold in the secondary market.[1] Indeed, all three explanations were probably behind the fall-off in cross-border flows to US non-banks in the second quarter. Deteriorating earnings prospects led borrowers active in the commercial paper (CP) market to bolster their credit lines in expectation of a loss of access to that market. General Motors Acceptance Corporation's signing of a $14.7 billion facility in June looks especially prescient given its downgrade in October and consequent reduced access to the CP market. Borrowers also appear to have taken advantage of the decline in yields following the Federal Reserve's interest rate cuts to refinance outstanding loans. Finally, banks found receptive buyers for investment grade loans, with credit spreads narrowing despite the deteriorating economic outlook.

Taken together, the three sets of banking statistics published by the BIS – locational, consolidated and syndicated lending – indicate that international banks remained willing, in the second quarter, to extend credit to US borrowers. Cross-border flows to US non-banks did slow. But even as corporate earnings prospects were deteriorating, banks in the reporting area

---

[1] The international syndicated credit statistics and the locational banking statistics are not directly comparable. The former are gross figures based on signed facilities, whereas the latter are net figures based on reporting banks' balance sheets. Moreover, the former include local lending by domestic banks (when part of an international syndicate), whereas the latter refer to the cross-border positions of international banks. The participation of US banks is substantial in the case of international syndicated lending to US borrowers, and so local lending explains part of the conflicting movements in the two sets of statistics. In addition, international banks participating in the syndicate may have funded the loans through their US-based branches or subsidiaries. However, this is unlikely to have been the case because US flow-of-funds data show a sharp slowdown in domestic bank lending in the second quarter. Furthermore, no acceleration in the pace of local lending by foreign banks in the United States is evident in the consolidated international banking statistics.

Banks' cross-border claims on non-bank borrowers Exchange rate adjusted changes in amounts outstanding, in billions of US dollars								
	1999	2000				2001		Stocks at end-June 2001
	Year	Year	Q2	Q3	Q4	Q1	Q2	
Total claims on non-banks	303.1	296.9	58.2	94.1	53.8	266.5	57.4	3,705.3
Loans	102.7	66.7	– 0.2	22.9	16.8	198.7	36.7	2,204.3
Securities[1]	200.3	230.2	58.4	71.3	37.0	67.8	20.7	1,501.0
Developed countries	275.3	265.8	40.5	81.2	55.7	228.9	45.8	2,766.5
Europe	259.0	205.9	25.5	67.3	39.2	92.1	23.8	1,496.5
of which: intra-euro area[2]	*156.8*	*60.8*	*3.5*	*12.2*	*10.9*	*42.6*	*7.2*	*641.2*
Japan	– 64.5	– 67.5	– 8.5	– 10.3	– 33.5	– 7.0	4.3	113.5
United States	86.0	123.4	26.8	22.3	48.4	141.5	9.8	1,066.6
Offshore centres	24.6	47.0	18.5	7.0	16.2	25.2	7.5	366.6
Emerging economies	– 15.9	– 15.7	2.9	5.2	– 13.6	9.3	4.8	489.8
Unallocated[3]	19.1	– 0.2	– 3.6	0.8	– 4.5	3.0	– 0.7	82.3
US dollar	141.5	125.0	25.2	26.7	58.2	137.5	30.1	1,724.6
Euro	185.1	157.4	16.6	52.6	21.2	128.3	– 0.2	1,139.8
Japanese yen	– 7.0	19.1	37.4	– 8.6	– 26.0	6.2	7.3	256.1
Other currencies[4]	– 16.5	– 4.6	– 20.9	23.4	0.4	– 5.5	20.2	584.8

[1] Mainly debt securities. Other assets account for less than 5% of total claims outstanding. Data are partly estimated. [2] Euro-denominated cross-border claims of reporting banks in the euro area on residents of the euro area. [3] Including claims on international institutions. [4] Including unallocated currencies. Table 2.2

showed no signs of reducing their claims on the non-bank private sector, whose share in outstanding consolidated claims on the United States remained stable at 57% in the second quarter. Instead, they reduced their holdings of US Treasury securities, resulting in a 1 percentage point decline in the public sector's share of outstanding claims, to 13%.

In the third quarter too, bank funding for US borrowers seemed to be available, at least for investment grade borrowers. Syndicated lending to the United States slowed from the second quarter's exceptionally high levels (see "International syndicated credits: shift towards higher-rated borrowers" on page 21). Nevertheless, at $181 billion, it was not far below the levels of a year earlier, when the US economy was growing much more rapidly than it did in the third quarter of 2001.

Flows to European non-banks slow but remain positive

Flows to non-banks in Europe also slowed in the second quarter, but not as sharply as in the United States. Cross-border claims on European non-banks increased by $24 billion, below the levels of recent quarters but still positive (Table 2.2). Italy was the largest recipient of funds, followed by France. The United Kingdom and the Netherlands experienced the largest declines.

Intra-European business again accounted for most of the activity in the second quarter. Flows to non-bank borrowers in Europe from banks domiciled within Europe totalled $20 billion, compared to $4 billion from banks outside

German banks strengthen their position in Europe

Europe.[2] Through HypoVereinsbank's purchase of Bank Austria, German banks strengthened their position as the leading source of international bank credit to governments, corporations and non-bank financial institutions in Europe. According to the consolidated banking statistics, German banks' share of outstanding international claims on European non-banks increased by 2 percentage points in the second quarter, to 25%. Japanese banks maintained their 11% market share, followed by Swiss and French banks at 9% each, and US banks at 8%.

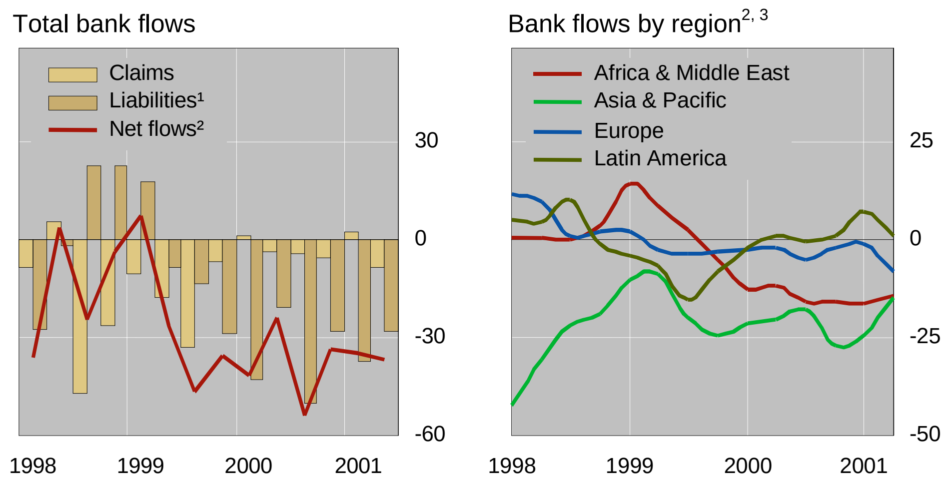
New financing for emerging economies is limited to top-tier credits

Large decline in cross-border claims on emerging economies ...

Whereas demand factors appeared to be driving the slowdown in bank flows to the developed countries in the second quarter, the picture in emerging economies was more mixed. The second quarter saw cross-border claims on emerging economies contract by $9 billion, the largest decline in nearly two years (Graph 2.2 and Table 2.3). Demand for external bank finance remained weak in Asia and other regions with current account surpluses. Banks in the reporting area continued to lend modest amounts to emerging economies in need of external finance, including higher-risk borrowers such as Argentina and Russia. At the same time, however, they took steps to limit their exposure by, for example, lending primarily to top-tier borrowers or only against collateral and guarantees.

Banks' external positions vis-à-vis emerging economies

Exchange rate adjusted changes in amounts outstanding, in billions of US dollars



[1] A negative (positive) value indicates an increase (decrease) in BIS reporting banks' liabilities vis-à-vis emerging economies. [2] Changes in claims minus changes in liabilities. [3] Two-quarter moving average.

Graph 2.2

[2] The locational banking statistics do not include securities purchases by banks in the United States, only loans, and so they underestimate banking flows between Europe and the United States. The consolidated banking statistics include both loans and securities. The Statistical Annex outlines the main differences between the consolidated and locational banking statistics.

Banks' external positions vis-à-vis emerging economies

Exchange rate adjusted changes in amounts outstanding, in billions of US dollars

	1999	2000				2001		Stocks at end-June 2001
	Year	Year	Q2	Q3	Q4	Q1	Q2	
Total claims	– 68.0	– 11.9	– 3.6	– 3.9	– 5.5	2.7	– 8.4	867.3
Africa & Middle East	0.2	– 7.6	– 1.0	– 1.6	1.2	– 5.6	– 1.6	139.5
Saudi Arabia	2.1	0.1	– 0.1	0.0	1.4	– 1.9	0.1	23.8
Asia & Pacific	– 61.3	– 29.0	– 7.2	– 6.6	– 18.2	– 0.8	– 1.5	272.8
Mainland China	– 17.1	– 5.4	– 3.4	– 1.6	– 0.4	– 1.8	1.5	57.7
Taiwan, China	– 3.3	– 4.3	– 0.1	– 1.1	– 4.3	– 0.2	1.3	15.8
Europe	9.1	10.9	2.6	0.3	8.4	0.4	– 7.3	158.5
Russia	– 6.5	– 6.6	– 1.3	– 3.3	– 0.6	– 1.2	0.3	33.7
Turkey	5.9	11.3	2.6	2.5	3.4	– 2.3	– 5.1	40.4
Latin America	– 16.0	13.8	2.1	4.0	3.2	8.7	2.0	296.5
Argentina	0.7	1.2	– 0.1	2.3	0.3	– 1.7	1.5	46.4
Brazil	– 8.9	9.5	0.2	3.2	4.6	4.0	0.0	98.2
Total liabilities[1]	32.6	141.5	20.5	50.2	28.2	37.5	28.3	1,089.5
Africa & Middle East	– 6.9	47.2	8.4	21.0	10.1	17.8	3.3	328.2
Saudi Arabia	– 17.9	10.9	– 0.9	7.3	4.9	4.7	– 1.4	62.1
Asia & Pacific	5.0	65.3	9.5	12.1	16.9	12.5	14.7	378.2
Mainland China	– 4.1	35.7	10.4	5.2	8.1	0.6	3.5	104.5
Taiwan, China	7.5	19.2	0.6	6.1	12.6	3.4	6.8	73.2
Europe	20.8	19.4	4.8	7.7	5.0	6.0	3.0	127.4
Russia	3.8	7.2	3.4	3.2	– 1.8	3.8	2.6	29.4
Turkey	3.3	2.3	– 0.6	0.3	2.6	– 1.3	0.5	19.3
Latin America	13.8	9.6	– 2.1	9.3	– 3.9	1.2	7.3	255.7
Argentina	0.1	3.2	0.1	3.7	– 1.0	– 6.0	2.3	36.6
Brazil	2.2	– 4.6	– 8.9	2.3	0.7	– 2.6	2.2	46.6
Net flows[2]	– 100.7	– 153.4	– 24.1	– 54.1	– 33.7	– 34.8	– 36.7	– 222.2
Memo: OPEC deposits	*– 19.6*	*37.7*	*9.1*	*17.9*	*8.5*	*12.7*	*2.3*	*243.7*

[1] Mainly deposits. Other liabilities account for less than 1% of the total outstanding. [2] Total claims minus total liabilities.

Table 2.3

… especially Turkey

Turkey again experienced the largest contraction in claims. The $5.1 billion fall in the second quarter brought the total decline in the first half of 2001 to 15% of cross-border claims on Turkey outstanding at the end of 2000. Maturing short-term credits extended to Turkish banks and public sector borrowers accounted for most of the fall. The Turkish government repaid a $1 billion syndicated loan arranged in December 2000. Turkish banks, which had borrowed heavily in 2000, were absent from the international syndicated loan market in the second quarter. However, top-tier banks returned to the market in the third, signing $1.4 billion in new credits.

Following six consecutive quarterly increases, cross-border claims on Brazil were unchanged in the second quarter. While banks in the United States and the euro area continued to lend sizeable amounts to Brazilian borrowers, this was offset by a $3 billion decline in holdings of bank-issued securities reported by banking centres in the Caribbean. The consolidated statistics show a $1.5 billion increase in international claims on Brazil in the second quarter, suggesting that inter-office transactions may have been behind the sales of securities.

Cross-border claims on Argentina and Russia rise …

In Argentina, cross-border claims increased by $1.5 billion in the second quarter despite growing concern about the country's economic and fiscal prospects at the time. Banks in Europe and the United States reduced their holdings of Argentine securities, but these sales were offset by $1.7 billion in new lending from banks in the United States and other banking centres. This increase in cross-border claims on Argentina must, however, be distinguished from changes in banks' ultimate risk exposure. Indeed, the consolidated banking statistics show that banks in the reporting area reduced their exposure to Argentina in the second quarter. International on-balance sheet claims fell by $1.6 billion, or 2%, after consolidation of the operations of local subsidiaries with those of the parent bank. Foreign banks' subsidiaries in Argentina appear to have sold dollar bonds issued by the Argentine government, contributing to a 3 percentage point drop in claims on the public sector in the second quarter to 20% of total consolidated claims. Whereas such sales do not necessarily affect cross-border positions, they would result in a decline in consolidated claims.[3] Banks' net risk exposure, which also takes credit risk mitigants into account, fell by an even larger $3.2 billion, suggesting that banks did not renew unsecured credits and sought guarantees and collateral for their claims.

… but banks' net risk exposure continues to fall

In Russia too, cross-border claims rose in the second quarter even while banks' net risk exposure continued to decline. The increase in cross-border claims amounted to only $0.3 billion, but it interrupted the long decline in claims that began when Russia declared a debt moratorium in August 1998. Over the June 1998 to June 2001 period, cross-border claims on Russia fell by $26 billion, or 40%. The international banking market remains closed to all but the top-rated Russian borrowers. What new lending takes place tends to be collateralised, for example by oil and gas revenues, or guaranteed, usually by European or other export credit agencies. Owing to such guarantees, banks' net risk exposure to Russia fell by approximately $1 billion in the second quarter.

Deposit flows from OPEC members slow …

Oil-exporting countries and emerging economies in Asia continued to recycle their current account surpluses through the international banking market. However, there were signs that net outflows from these regions to banks might soon diminish. While OPEC members repaid another $2.8 billion to banks in the reporting area in the second quarter, falling oil prices slowed deposit flows to $2.3 billion, their lowest level since 1999. Changes in banks' claims and liabilities vis-à-vis Asia as a whole stayed in line with recent trends, with claims falling by $1.5 billion and liabilities rising by $14.7 billion. But cross-border claims on several countries are no longer declining, and indeed in some cases are beginning to trend upwards. Cross-border claims on the Philippines and Malaysia increased for the third consecutive quarter, by $0.5 billion and

---

[3] Such sales would affect cross-border positions if the proceeds were remitted to head office.

$0.3 billion respectively. Moreover, the composition of claims is shifting away from the private sector and towards the public sector. Claims on public sector borrowers increased by 2 percentage points in the Philippines and 3 percentage points in Malaysia, to 20% of outstanding consolidated claims. In Taiwan, China (hereafter Taiwan), public sector claims doubled to 12% of consolidated claims.

… while those from Taiwan and mainland China continue

In addition to public sector borrowers, banks in Taiwan received substantial amounts from banks in the reporting area, resulting in a $1.3 billion increase in claims on that economy. However, with dollar funding available domestically, banks in Taiwan channelled surplus dollars back into the international banking market, contributing to a $6.8 billion increase in banks' liabilities vis-à-vis Taiwan. Similarly, in mainland China cross-border claims increased by $1.5 billion. Yet, with little need for dollars, banks in mainland China continued to deposit large amounts with banks abroad, boosting international banks' liabilities vis-à-vis mainland China by $3.5 billion in the second quarter.[4]

[4] Special features in past issues of the *BIS Quarterly Review* examine the growth of foreign currency deposits in Taiwan and mainland China. See Robert N McCauley and Y K Mo, "Foreign currency deposits of firms and individuals with banks in China", August 2000, pp 35-9, and Ben S C Fung and Robert N McCauley, "Analysing the growth of Taiwanese deposits in foreign currency", September 2001, pp 49-56.

International syndicated credits: shift towards higher-rated borrowers

Blaise Gadanecz

Following a record second quarter, new signings of international syndicated credit facilities slowed to $304 billion in the third. On a seasonally adjusted basis, signings fell by 26%. A reduction in lending to lower-rated borrowers was an important factor behind the slowdown in the third quarter. Whereas borrowers rated triple-B or below had accounted for approximately two thirds of syndicated lending to rated borrowers during the past few years, this proportion fell to 50% in the third quarter. Nevertheless, overall activity in the international syndicated credit market remained above average levels for the 1997–99 period, when the growth of the global economy was considerably stronger.

Borrowing by US entities totalled $181 billion in the third quarter, down by 42% from second quarter levels but only 9% below levels one year earlier. Financial institutions, including the finance subsidiaries of corporations, were much less active in the syndicated loan market; their share of facilities arranged for US borrowers fell to 20% in the third quarter from 39% in the second. The largest facilities in the third quarter were signed by Philip Morris USA, for $8 billion, and Kraft, for $6 billion. These deals helped to boost the food, drink and tobacco sector's share of total lending to 12%, compared to an average of 3% over the previous year.

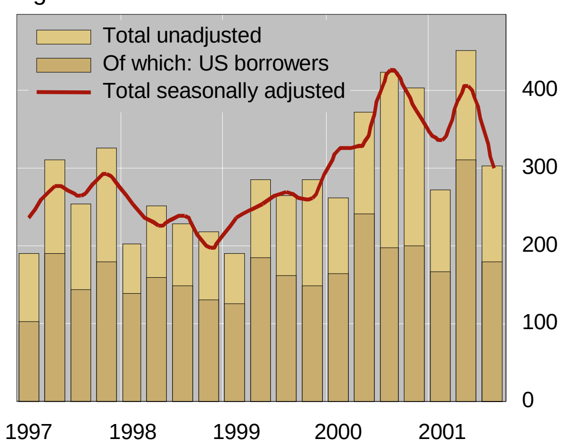
In Europe, signings fell by 21% from second quarter levels, to $75 billion, and by 58% from the levels of a year earlier, when telecoms borrowing had been at a peak. The largest deals were arranged by telecoms to refinance maturing facilities. British Telecom closed a facility for £5.5 billion, and Telecom Italia and Deutsche Telekom facilities for €5 billion each.

Facilities arranged for emerging economies increased to $18 billion in the third quarter, above average levels in the first half of 2001 but still below 2000 levels. South African borrowers secured the largest amount, at $4.6 billion. The South African Reserve Bank borrowed $1.5 billion to refinance bilateral loans, and Old Mutual, an insurance company, £900 million to refinance an earlier facility. Korean borrowers, mainly banks, signed facilities totalling $1.6 billion. After two quarters of negligible borrowing, Turkish entities raised $1.5 billion in the third. Almost all of this was raised by Turkish banks, signalling their re-entry into the international syndicated credit market. They had to pay for the privilege, however. Spreads on Libor-based facilities arranged by Turkish banks widened to more than 200 basis points in the third quarter from approximately 110 basis points in 2000. Signings by Latin American entities fell to their lowest level since 1999, with Mexican borrowers in particular much less active than in recent quarters. Argentina raised $0.4 billion in the third quarter, all of it for oil and gas projects.

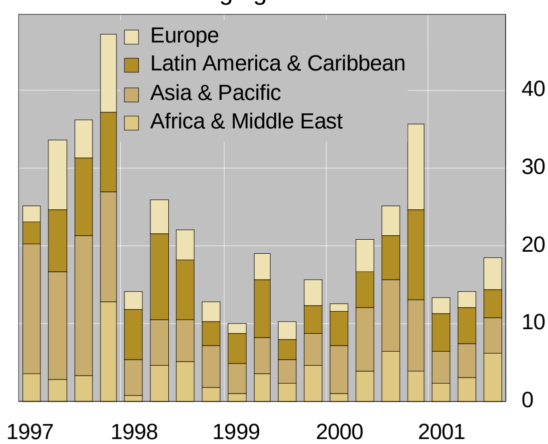
Activity in the international syndicated credit market

In billions of US dollars

Signed facilities



Facilities for emerging economies



Sources: Dealogic Capital Data Loanware; BIS.