Global Liquidity and the Future of Banking

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Two Themes

- European global banks as transmission channel of global liquidity
- US Dollar as currency underpinning global banking system
Mapping Global Liquidity

- Consequences of global liquidity for United States
- Consequences of global liquidity for Europe
- Consequences of global liquidity for emerging/developing economies
Figure 1: Total Liabilities of Barclays (1992 - 2007) (Source: Bankscope)
Figure 2: Barclays, risk-weighted assets and total assets (Source: Bankscope)
Figure 3: Barclays, capital ratios (Source: Bankscope)
Figure 4: BNP Paribas total liabilities (Source: Bankscope)
Figure 5: BNP Paribas risk-weighted assets and total assets (Source: Bankscope)
Figure 6: BNP Paribas capital ratios (Source: Bankscope)
Figure 7: Société Générale liabilities 1999 - 2010 (Source: Bankscope)
Figure 8: Société Générale risk-weighted assets and total assets (1999 - 2010) (Source: Bankscope)
Figure 9: Société Générale capital ratios 1999 - 2010 (Source: Bankscope)
Figure 10: Cross-border foreign currency claims of BIS reporting banks by currency (Source: BIS locational banking statistics, Table 5A)
Figure 11: US dollar cross-border foreign currency claims and US commercial bank total assets (Source: Flow of Funds, Federal Reserve and BIS locational banking statistics, Table 5A)
Figure 12: US Dollar-denominated assets and liabilities of euro area banks
(Source: ECB Financial Stability Review, June 2011, p. 102)
Figure 13: European global banks add intermediation capacity for connecting US savers and borrowers.
Figure 14: International claims of European BIS reporting banks on US counterparties (Source: BIS consolidated banking statistics, Table 9D)
Figure 15: Claims outstanding on Federal Reserve Term Auction Facility (TAF) on US and non-US banks (Source: Federal Reserve disclosures on TAF)
Figure 16: Claims outstanding on Federal Reserve Term Auction Facility (TAF) on non-US banks (Source: Federal Reserve disclosures on TAF)
Figure 17: Top 30 claims outstanding on Federal Reserve Term Auction Facility (TAF) on non-US banks (Source: Federal Reserve disclosures on TAF)
Why did European banks expand so much?

Two candidate explanations:

• Basel II and EU Capital Adequacy Directive (CAD) allowed European banks to expand assets without incurring rising risk-weighted assets

• Advent of Euro opened up cross-border banking market within the eurozone
Figure 18: Cross-border domestic currency assets and liabilities of eurozone banks (Source: BIS locational banking statistics, Table 5A)
Figure 19: Cross-border domestic currency assets and liabilities of eurozone banks (Source: BIS locational banking statistics, Table 5A)
Figure 20: International claims of European BIS-reporting banks on counterparties in Spain (Source: BIS consolidated banking statistics, Table 9D)
Figure 21: International claims of European BIS-reporting banks on counterparties in Ireland (Source: BIS consolidated banking statistics, Table 9D)
Figure 22: Current account of Ireland and Spain (Source: IMF International Financial Statistics)
Implications for Current Conjuncture in Europe

- Europe has a **twin crisis**, combining **banking crisis** with **sovereign debt crisis**
  - Emerging economy crises of 1990s were **twin crises**, combining **banking crisis** with **currency crisis**

- Deleveraging by European banks will impact not only eurozone, but also
  - US shadow banking system
  - Capital flows to emerging economies (see below)
  - Emerging Europe, especially
Consequences for Emerging Economies

Borrowers in A

Borrowers in B

Borrowers in C

Banks in A

Banks in B

Banks in C

Global Banks

Wholesale Funding Market
Figure 23: Interoffice assets of foreign banks in the United States (Source: Federal Reserve, series on “Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks”)

Billion Dollars

-100
0
100
200
300
400
500
600
700
800
900


Interoffice Assets of Foreign Banks in US

Net Interoffice Assets of Foreign Banks in US

30-Jun-08
31-Dec-08
Figure 24: Interoffice assets of foreign banks in Japan (Source: Bank of Japan)
Figure 25: Net interoffice assets of foreign banks in Japan (Source: Bank of Japan)
Figure 26: External claims (loans and deposits) of BIS reporting banks on counterparties listed on right (Source: BIS locational banking statistics Table 7A)
Figure 27: International claims of European BIS-reporting banks on counterparties in Korea (Source: BIS consolidated banking statistics Table 9D)
Missed Opportunity for Europe in 2010?

• Basel III as trade negotiation, instead of policy toward financial stability

• Did European leaders at G20 meetings act in global interest?
  – in their own national interest?
  – in their banking sector’s long-term interest?
  – None of the above?