



Comments on "*Are credit trends in Asia worrying?*" by Krishna Srinivasan

**Presentation to the Reserve Bank of India and European
Commission ASEM conference,
"Investment and its Financing: What causes private
investment to remain relatively low in Asia?"
Mumbai, 16 December 2010**

Robert N McCauley*

**Monetary and Economic and Banking Department
Bank for International Settlements**



General comments

- Question that Srinivasan poses is a very important.
- Generally do not argue with outline of answer.
 - Variety of quantities and prices consulted.
 - Take well the emphasis on risks of capital inflows.
- Need to pay particular attention to the growth of private debt to GDP.
 - Schularick and Taylor show that bank credit growth regularly outpaces money growth.
 - Follows that “excess liquidity” (M2/GDP) not so telling.



Difficult to track private credit/GDP

- Not enough to measure *domestic bank* credit to the private sector.
 - Domestically, credit booms marked by intensification of competition for market share, often featuring non-bank financial intermediaries.
 - Internationally, cross-border bank lending tends to be pro-cyclical.
- With financial development at home, growing access of private firms to foreign bank credit, and rapid internationalisation of domestic currency, it is increasingly difficult to track private credit.



Domestic market share competition in credit booms

- Nordic credit boom in late 1980s saw finance companies gain share at the expense of banks.
- Japan bubble in 1980s
 - preceded by big banks' losing their big firm customer base to internal funds and bond market; and
 - featured strong competition by nonbank financial firms for lending to SMEs based on real estate collateral.
- US credit boom in 2000s, instead of
 - government channel (Fannie & Freddie),
 - private mortgage financing channels (eg originator-brokers-securitiser-SIV-money market mutual funds).
 - Wall Street: "yes we can" but no they couldn't.



Cross-border bank credit

- Private firms can borrow from domestic banks onshore, foreign banks onshore and banks offshore.
- Reserve requirements (CRR) that are remunerated at zero or below-market yield provide a strong incentive to borrow from banks offshore.
 - Indian nonbanks have drawn loans from BIS-reporting banks of \$54 billion in June 2010, up by \$6 billion in the second quarter alone.
 - Chinese nonbanks have relatively much smaller loans from BIS-reporting banks of \$50 billion in June 2010, up by \$3 billion in Q2.
- Internationally, cross-border bank lending tends to be procyclical.

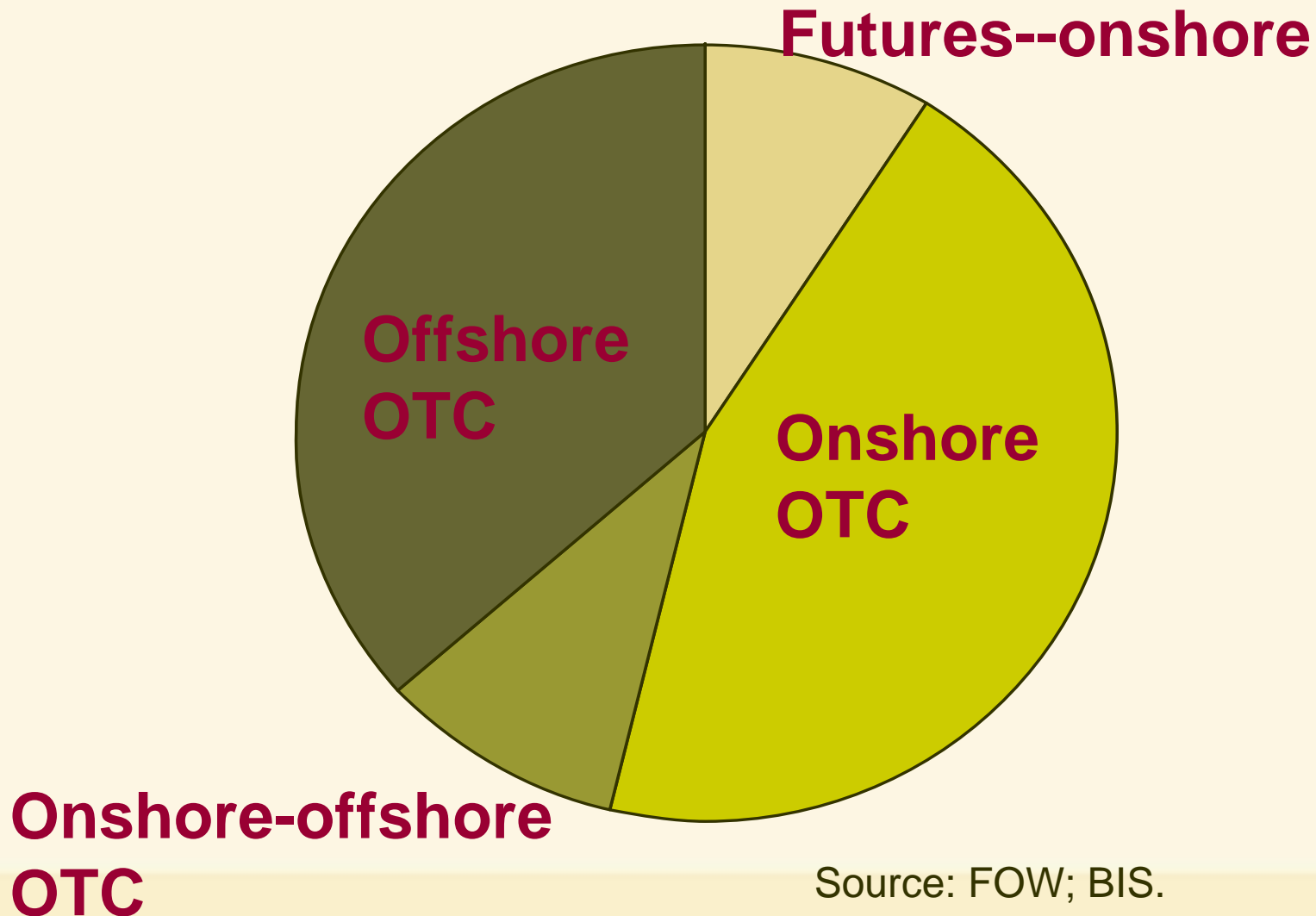


Cross-border bond credit with rapidly internationalising rupee

- “BIS data on overseas dollar-rupee market surprises one and all”
 - Mobis Philipose, In the money, *MINT*, 8 December
- Offshore foreign exchange trading develops over time into offshore bond market.



Geography of all INR trading, 2010





Cross-border bond credit: an example

- Korean EXIM bank sells INR bond to offshore investors at yield below the Indian government onshore.
 - This is evidence of the effectiveness of controls on non-resident holding of Indian domestic bonds.
- Say Korean EXIM Bank lends the INR to Korean companies expanding their operations in India.
- Seen as a replacement for INR borrowing from local banks, the offshore bond issue is in effect contributing to credit to the private sector in India.