

3. The international debt securities market

The fourth quarter completed a banner year for international debt securities. Issuance of bonds and notes in the quarter was \$826 billion on a gross basis, bringing the total for 2004 to \$3.3 trillion (Table 3.1). This represents a 14.5% expansion over 2003 and a historical peak relative to global GDP, indicating that borrowers had relatively easy access to international credit markets last year. The most significant increase in the fourth quarter was debt issued by the largest developed economies, particularly the euro area. Gross high-yield issuance in developed economies remained at an elevated level and gross issuance by entities in emerging market economies reached its highest yearly total ever, as spreads on emerging market debt fell to historical lows. In addition, net issuance of all international debt securities was up by almost \$80 billion and \$19 billion from entities in the euro area and the United States, respectively, in the fourth quarter (Table 3.2). By contrast, net issuance was negative in Japan.

Sharp turnaround in euro area issuance

Euro area issuance surges

Despite ongoing weakness in the euro area economy, both gross and net issuance of international debt securities by euro area entities rose markedly in the fourth quarter. Total gross issuance (bonds and notes plus money market securities) increased to \$614 billion, from \$543 billion in the third quarter, and net issuance to \$218 billion from \$138 billion. All of the largest euro area economies except Germany saw net issuance rise sharply. These increases in borrowing activity, expressed in US dollars as reported in Tables 3.1 and 3.2, mainly reflect a jump in issuance in euros and not valuation effects deriving from the decline in the dollar vis-à-vis the euro. For example, gross issuance in euros by euro area entities was €326 billion in the fourth quarter, up 13.4% over the previous one.

Rapid increase in borrowing by euro area corporates

Financial firms continued to account for the bulk of new international debt issuance from the euro area, but non-financial corporations increased borrowing much more rapidly, with net issuance expanding by a factor of five in the fourth quarter. By contrast, government borrowing continued to be weak, as in the third quarter, but this was largely in line with past seasonal patterns.

Gross issuance in the international bond and note markets							
In billions of US dollars							
	2003	2004	2003	2004			
	Year	Year	Q4	Q1	Q2	Q3	Q4
Total announced issues	2,885.5	3,303.4	711.8	982.8	768.8	725.7	826.1
Bond issues	1,611.1	1,790.4	404.5	570.1	402.5	377.8	440.0
Note issues	1,274.4	1,513.0	307.3	412.7	366.4	347.9	386.0
Floating rate issues	962.7	1,258.8	257.6	337.4	306.4	285.2	329.7
Straight fixed rate issues	1,834.7	1,987.3	427.6	628.0	444.1	430.0	485.2
Equity-related issues ¹	88.1	57.3	26.6	17.4	18.3	10.5	11.2
US dollar	1,171.8	1,154.5	268.1	357.2	257.3	255.5	284.5
Euro	1,288.1	1,598.0	316.9	478.5	379.0	349.7	390.7
Yen	102.8	111.5	29.0	29.3	33.8	22.4	26.1
Other currencies	322.9	439.4	97.7	117.8	98.7	98.0	124.8
Developed countries	2,621.6	3,012.4	656.8	906.8	694.8	655.4	755.5
United States	739.5	772.5	173.6	249.8	167.9	169.6	185.2
Euro area	1,294.4	1,463.1	327.2	438.7	355.2	305.2	364.0
Japan	48.3	61.9	18.5	20.3	19.8	12.0	9.8
Offshore centres	31.7	41.6	11.1	7.2	7.0	14.0	13.4
Emerging markets	139.7	152.1	33.8	45.1	36.7	35.0	35.3
Financial institutions	2,279.2	2,689.5	593.3	788.1	603.3	606.1	691.9
Private	1,913.3	2,276.1	506.0	663.4	515.7	501.2	595.9
Public	366.0	413.3	87.3	124.8	87.6	104.9	96.1
Corporate issuers	271.2	271.4	68.8	61.9	72.3	62.4	74.8
Private	219.1	231.2	56.6	52.8	60.6	57.0	60.7
Public	52.1	40.2	12.2	9.0	11.7	5.4	14.1
Governments	242.6	245.4	39.6	109.1	62.9	35.9	37.5
International organisations	92.5	97.2	10.1	23.7	30.3	21.3	21.9
Completed issues	2,866.6	3,303.2	734.4	934.1	796.5	708.4	864.2
<i>Memo: Repayments</i>	<i>1,478.0</i>	<i>1,740.3</i>	<i>326.3</i>	<i>448.4</i>	<i>453.2</i>	<i>403.0</i>	<i>435.8</i>

¹ Convertible bonds and bonds with equity warrants.

Sources: Dealogic; Euroclear; ISMA; Thomson Financial Securities Data; BIS.

Table 3.1

Net US issuance growing, but still at a low level

Net issuance of international debt securities by US borrowers once again rose in the fourth quarter, totalling \$59.6 billion. About two thirds of the increase in net issuance can be attributed to financial corporations, though borrowing by corporates increased by more on a percentage basis (82% versus 38%). The pickup in issuance may be partly a result of generally good price terms for US corporate borrowers, as spreads tightened in both the US and European markets. The fall in spreads was largest in the high-yield class (see below), yet they also fell on A- and BBB-rated debt, reaching levels not observed since 1998.

Increase in net US issuance in fourth quarter ...

... but yearly total
still low by historical
standards

On an annual basis, however, net issuance was still below the level posted in 2003. Even looking further back in time, US borrowers on the international debt market were relatively subdued in 2004. On an absolute basis, US net issuance of \$230 billion in 2004 fell short of the levels recorded in the years all the way back to 1998; a similar picture emerges when viewing net issuance as a percentage of GDP.

One reason for the weakness in net issuance witnessed earlier in 2004 was the marked decline in borrowing on the international market by Fannie Mae and Freddie Mac. Continuing this trend, combined net borrowing by these two institutions shrank for the second consecutive quarter, although the decline in new issuance of \$548 million in the fourth quarter was much less severe than the sharp fall of \$7,707 million seen in the third quarter. Nonetheless, in terms of gross issuance, Fannie Mae and Freddie Mac continued to be among the largest US borrowers in the fourth quarter, along with General Electric Credit Corporation and the Federal Home Loan Banks. Another possible

Main features of net issuance in international debt securities markets								
In billions of US dollars								
	2003	2004	2003	2004				Stocks at end-Dec 2004
	Year	Year	Q4	Q1	Q2	Q3	Q4	
Total net issues	1,463.9	1,623.9	457.3	520.5	347.7	323.2	432.4	13,928.0
Money market instruments ¹	75.3	61.0	49.2	34.9	4.4	17.8	4.0	663.8
Commercial paper	83.3	40.4	48.7	8.8	-3.4	25.8	9.1	483.3
Bonds and notes ¹	1,388.6	1,562.8	408.1	485.6	343.3	305.4	428.4	13,264.3
Floating rate issues	384.4	644.4	152.3	153.6	163.5	129.8	197.5	3,668.8
Straight fixed rate issues	983.3	924.6	240.0	338.8	172.1	178.3	235.3	9,225.0
Equity-related issues	20.9	-6.2	15.7	-6.8	7.7	-2.7	-4.4	370.5
Developed countries	1,357.3	1,493.6	433.4	484.8	317.8	291.6	399.4	12,474.8
United States	269.2	230.1	97.8	125.5	4.3	40.6	59.6	3,358.8
Euro area	768.1	803.2	223.2	231.8	215.6	138.3	217.6	6,208.7
Japan	-1.0	16.6	7.9	6.4	11.0	0.7	-1.5	298.3
Offshore centres	15.8	25.2	9.0	1.0	4.3	9.7	10.2	159.9
Emerging markets	67.6	82.0	19.0	24.7	18.5	14.7	23.9	737.1
Financial institutions	1,179.7	1,370.7	408.0	417.9	282.3	294.9	375.5	10,373.5
Private	976.0	1,146.4	347.7	343.1	234.9	236.6	331.8	8,747.0
Public	203.6	224.3	60.3	74.8	47.4	58.4	43.7	1,626.5
Corporate issuers	113.2	70.1	40.9	7.1	11.3	10.4	41.2	1,635.4
Private	93.4	52.0	37.3	-0.0	7.8	9.9	34.3	1,360.5
Public	19.8	18.1	3.6	7.1	3.5	0.5	6.9	275.0
Governments	147.9	160.0	12.5	85.5	47.0	10.8	16.8	1,362.8
International organisations	23.2	23.1	-4.2	10.0	7.1	7.1	-1.2	556.3
<i>Memo: Domestic CP²</i>	<i>-41.0</i>	<i>139.3</i>	<i>8.2</i>	<i>57.9</i>	<i>-19.8</i>	<i>-0.7</i>	<i>101.9</i>	<i>2,079.3</i>
<i>Of which: US</i>	<i>-81.3</i>	<i>114.0</i>	<i>-1.5</i>	<i>47.8</i>	<i>-26.8</i>	<i>6.7</i>	<i>86.3</i>	<i>1,402.7</i>

¹ Excluding notes issued by non-residents in the domestic market. ² Data for the fourth quarter of 2004 are partly estimated.

Sources: Dealogic; Euroclear; ISMA; Thomson Financial Securities Data; national authorities; BIS. Table 3.2

Net issuance of international debt securities by region and currency ¹								
In billions of US dollars								
		2003	2004	2003	2004			
		Year	Year	Q4	Q1	Q2	Q3	Q4
United States	US dollar	210.1	128.1	75.3	102.7	-28.5	6.6	47.3
	Euro	47.8	55.3	14.6	13.7	21.2	16.6	3.8
	Pound sterling	11.8	25.4	7.2	3.5	5.4	10.7	5.8
	Yen	-1.5	4.3	0.8	1.3	1.5	1.0	0.5
	Other	1.0	17.0	-0.1	4.4	4.7	5.7	2.1
Euro area	US dollar	87.1	76.8	24.2	17.9	34.7	10.0	14.1
	Euro	646.5	660.2	181.6	192.0	158.8	115.0	194.4
	Pound sterling	17.4	35.9	5.1	6.7	15.2	6.0	7.9
	Yen	-12.3	2.9	0.3	1.5	3.6	0.5	-2.7
	Other	29.4	27.5	12.1	13.7	3.3	6.6	3.8
Others	US dollar	164.4	202.5	48.8	53.8	47.1	46.8	54.8
	Euro	138.6	231.1	35.8	71.0	40.8	66.4	53.0
	Pound sterling	70.5	89.6	26.5	21.5	22.3	12.1	33.7
	Yen	9.4	16.5	10.6	2.5	10.7	3.2	0.2
	Other	43.6	50.8	14.6	14.5	6.9	15.9	13.5
Total	US dollar	461.6	407.4	148.3	174.4	53.3	63.4	116.2
	Euro	832.9	946.6	231.9	276.7	220.7	198.0	251.2
	Pound sterling	99.7	150.9	38.8	31.7	42.8	28.9	47.5
	Yen	-4.4	23.8	11.7	5.2	15.8	4.7	-1.9
	Other	74.0	95.3	26.6	32.6	15.0	28.3	19.5

¹ Based on the nationality of the borrower.

Sources: Dealogic; Euroclear; ISMA; Thomson Financial Securities Data; BIS.

Table 3.3

explanation for the weaker activity by US firms last year was a partial substitution out of longer-dated instruments by financial institutions as the commercial paper market rebounded in the United States.

Along with the rise in net issuance by US entities, the share of net borrowing by all nationalities in US dollars increased strongly, from 19.6% to 26.9%, in the fourth quarter (Table 3.3). At the same time, the shares of gross and net issuance in the euro declined slightly. In the light of the fact that the effective exchange rate of the dollar remained low relative to its historical average, and the US dollar depreciated by 5% in the quarter, these changes seem to run contrary to the positive relationship observed in the past between a currency's strength and its share of international debt issuance.

Share of net
issuance in US
dollars rises

Japanese issuance falters as economy slows

The most noticeable weak spot in the international debt securities market over the past two quarters has been the lack of new borrowing by Japanese entities. Net issuance declined during the fourth quarter, coming in at a negative -\$1.5 billion, following the modest increase of \$721 million in the third quarter. Gross issuance was also weak, totalling only \$20.4 billion. This reduction in borrowing came against a mixed economic background. On the one hand, the

Net issuance in
Japan is negative in
the fourth quarter ...

soft patch in the economy persisted and the expectation that goods price deflation was nearing its end subsided. On the other hand, rating upgrades outpaced downgrades on Japanese issuers and financing conditions remained favourable, as credit spreads continued to be tight. This suggests that the decline in issuance may have been mainly due to a reduced demand for funds on the international market by borrowers.

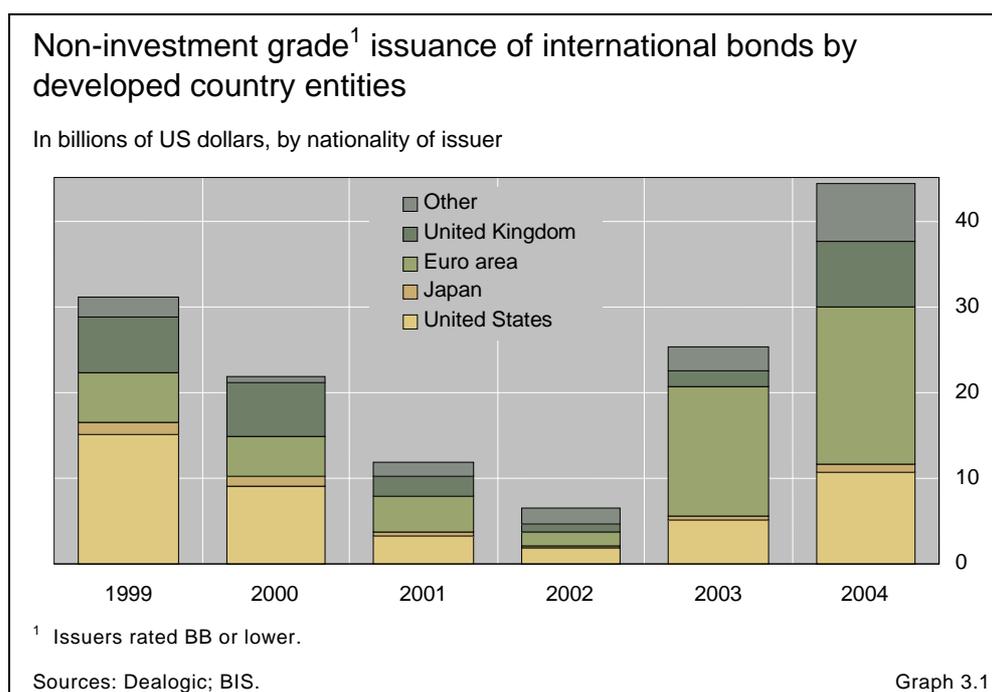
... but higher overall in 2004 than in 2003

From a longer-term perspective, however, net borrowing on the international market by Japanese entities showed marked improvement last year, which might be a sign that the general process of deleveraging by Japanese firms that has taken place over recent years has come to its end. Net issuance had been negative in 2000–03. By coming in at a positive \$16.6 billion in 2004, it reached its highest level since 1996. To be sure, part of this improvement was due to revaluation effects, as the yen appreciated by 4.3% vis-à-vis the dollar last year. But most of the increase was not simply due to valuation effects, as Japanese entities issued, on net, ¥1,585 billion worth of debt in yen on the international market in 2004, up from ¥615 billion in 2003.

High-yield issuance still buoyant

Market conditions remain attractive for high-yield borrowers ...

As global investors continued their search for yield during the fourth quarter, and in the process narrowed spreads on high-yield debt even further (see the Overview), lower-rated entities in developed economies continued their brisk rate of borrowing in the international market. Although gross high-yield issuance by nationals of developed economies fell slightly in the quarter to \$12.6 billion from \$13 billion in the previous one, the level of borrowing remained elevated. Indeed, for the year as a whole, gross issuance was \$44.3 billion, far eclipsing the total reached in every year since 1999 (Graph 3.1).



The modest overall drop in gross high-yield issuance masks some quite marked differences across economies. For instance, gross issuance by US-based entities grew by 1.5% in the quarter, whereas it declined significantly for entities in the euro area (-49%) and Japan (-59%). The fact that spreads on high-yield debt continued to narrow in the euro area from October to December suggests that the precipitous drop in issuance was driven by a lack of demand for funding by speculative grade firms given the persistent sluggishness displayed by the euro area economy. Similarly, the drop in total debt issuance for Japanese firms also appears to reflect weak demand on the part of borrowers.

... though borrowing differs sharply across countries

Technology and financial firms were the largest issuers of speculative grade debt in industrial countries in the fourth quarter. The largest private completion was by Elan Finance Corp Ltd of Ireland, a firm with a rating of B- and US residency, which issued a dollar-denominated bond in the amount of \$850 million at a spread of 387 basis points over seven-year US Treasuries. Rogers Wireless Inc, a Canadian firm rated BB, completed a \$550 million fixed rate issue with a spread of 330 basis points. HCA Inc (Hospital Corporation of America) completed an issue in the international market on 19 November 2004 in the amount of \$750 billion and at a spread of 220 basis points over 10-year US Treasuries.

Emerging market borrowing sets a new record in 2004

Borrowing in the international debt market by entities in emerging market countries set a record in 2004, totalling \$167 billion, surpassing the previous record level of \$163 billion reached in 1996. Net issuance of \$82 billion was also strong compared to the average level of \$46 billion recorded over the five-year period 1999–2003, but was still somewhat lower than the previous high of \$94 billion set in 1997. Emerging market borrowers clearly took advantage of the very favourable pricing environment, as spreads on JPMorgan Chase's EMBI+ fell below 350 basis points, a historical low, in December 2004 (see the Overview).

Gross issuance by emerging market economies sets a yearly record

Gross issuance by emerging market economies in the fourth quarter was \$39.8 billion, up from \$38.5 billion in the third quarter, but still below the levels reached in the first half of the year. Net issuance rose by a wider margin, going from \$14.7 billion to \$23.9 billion quarter to quarter. In fact, net borrowing reached its second highest quarterly level since early 2001, coming in slightly below the figure posted in the first quarter of 2004.

Most of the growth in net issuance during the latest quarter was due to Asian entities, though entities from Latin America and the Middle East and Africa posted gains as well (Graph 3.2). By contrast, net issuance was relatively flat in emerging Europe. Financial institutions once again topped governments in net borrowing, and there was only a slight increase in net issuance by non-financial corporations.

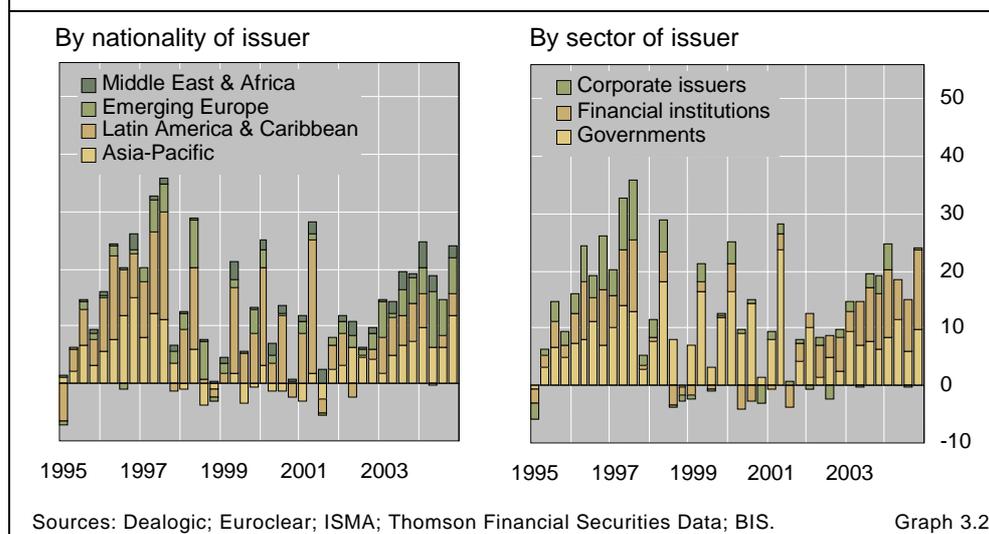
Borrowing is strongest by Asian entities ...

Among Asian borrowers, Chinese entities were the most active during the fourth quarter, with net issuance of \$4 billion accounting for one third of total net issuance from the region. The People's Republic of China came to the

... particularly the Chinese government ...

International debt securities issues by emerging market entities

Net issuance, in billions of US dollars



market on 21 October with two large issues. The larger of these was a 10-year bond denominated in euros and totalling \$1,248 million, while the other was a \$500 million bond denominated in US dollars, with a maturity of five years. The combined face value of these two issues represented the largest completion ever by the Chinese government in the international bond market. Amongst the objectives for the euro-denominated bond issue were the creation of a new euro benchmark and broader distribution of Chinese government debt across European investors. With nil repayments, this brought net issuance by the Chinese government to \$1.7 billion during the quarter, reversing a decline of \$300 million recorded in the previous one, in which the government did not issue any securities but only repaid a part of its existing debt.

... and Asian
financial institutions

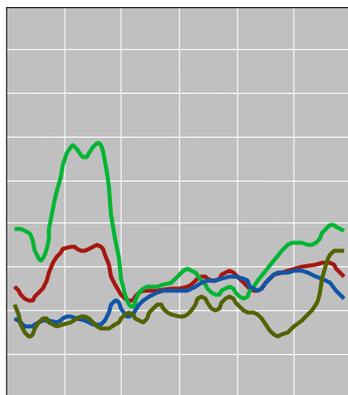
Nonetheless, despite the two large issues from the Chinese government, financial institutions continued to be the largest issuers of Asian debt in the international market. For instance, 63% of the net issuance out of China was due to Chinese financial institutions. Net issuance by financial institutions in Korea, Malaysia and India was also robust during the fourth quarter. For example, the Korea First Mortgage No 3 plc issued a euro-denominated bond with a long maturity of 31½ years that completed in early December in the amount of \$729 billion.

The Republic of the Philippines, normally a very active borrower, did not issue any debt during the fourth quarter in the face of adverse market conditions. Progress on fiscal consolidation, including the passage of legislation intended to boost tax revenues, helped to turn market sentiment around early in 2005. This paved the way for the announcement of a new bond on 26 January in the amount of \$1.5 billion and with a maturity of 25 years, the largest issue ever by the government and its first long-dated bond since 2000. Nevertheless, a one-notch downgrade by Standard & Poor's in mid-January, followed by a two-notch downgrade by Moody's in February, reminded investors of the Philippines' weak fiscal position.

Average maturity of emerging markets issues¹

Fixed rated international bonds and notes, in number of years

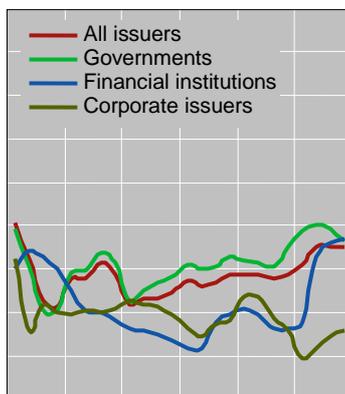
Asia-Pacific



1999 2000 2001 2002 2003 2004

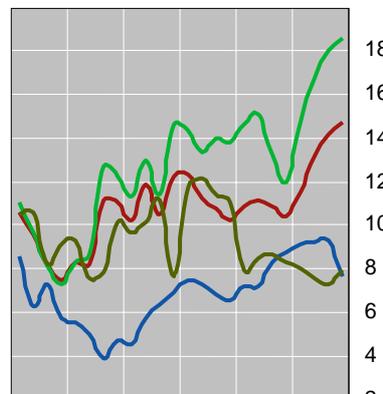
¹ Four-quarter moving average.

Emerging Europe



1999 2000 2001 2002 2003 2004

Latin America & Caribbean



1999 2000 2001 2002 2003 2004

Graph 3.3

The largest issues in Latin America were completed by sovereigns, in both large and small economies. The government of Brazil issued a 15-year bond denominated in US dollars in the total amount of \$1 billion in October, and followed this up in December with a \$500 million 9.6-year bond. The Mexican government issued a 15¼-year medium-term note in euros for \$971 million and the Republic of Peru a 10-year bond in euros totalling \$806 million. The announcement of such large issues denominated in euros suggests that demand by European investors in search of higher-yielding debt securities was strong during the quarter. The Republic of Venezuela increased net issuance the most among Latin American governments, with its total rising from nil in the third quarter to \$2 billion in the fourth quarter. By contrast, net issuance by non-financial corporations in the region declined for the third consecutive quarter, and net issuance by financial institutions was negative (–\$1 billion).

The fourth quarter was also notable for the fact that gross issuance in local currency by Latin American entities reached its highest level by far (\$516.4 million) since the full onset of the Argentina crisis. This brought the total for 2004 to \$855.7 million, not far off the face value of \$939.1 million reached in 2001. This surge of borrowing in bonds and notes in local currency coincided with a significant increase in local currency bank loans to the region (see the section on the international banking market). Three debt securities were brought to the market during the quarter. The Republic of Colombia announced a bond issue in November totalling 954.5 billion Colombian pesos (\$373.8 million), while in December two medium-term notes were announced by Brazilian banks Banco Bradesco SA and Banco do Brasil SA, for 271 million and 125.7 million reais (\$97.4 million and \$45.2 million), respectively.

In emerging Europe, the largest single issue was by the Republic of Hungary, which launched a seven-year fixed rate bond in euros with a face value of \$1.263 billion and a coupon of 3.625%. The Republic of Turkey

Governments are the most active borrowers from Latin America ...

... and the value of local currency issues rises

Hungary and Turkey complete large issues

completed an issue in late November, in the amount of \$500 million. This was a dollar-denominated bond with a maturity of 10 $\frac{1}{3}$ years and issued at a spread of 286 basis points over 10-year US Treasuries. Borrowing by Russian financial firms, which had been fuelling issuance from emerging European economies in the recent past, slowed down in the fourth quarter, with net issuance falling from \$2.9 billion to \$1.9 billion.

Finally, borrowers from emerging market economies extended the average maturity of their bond and note issues in 2004. Along with record gross issuance and the tightening in spreads, this is a further indication that financing conditions as a whole were very favourable last year. Four-quarter moving averages of the maturity of newly issued bonds and notes across the main regions were 7.6 years (Asia-Pacific), 9.0 years (emerging Europe) and 14.7 years (Latin America) by end-2004 (Graph 3.3). For governments, the corresponding numbers were 9.7 years (Asia-Pacific), 9.3 years (emerging Europe) and 18.6 years (Latin America). However, in the fourth quarter specifically, average maturity declined across each of these regions and in most sectors.

