



A few observations on Central Banks and the Financial Crisis

**48th ACI World Congress
13 March 2009
Cape Town, South Africa**

Louis de Montpelliér*
Deputy Head of Banking Department
Bank for International Settlements

*The views expressed are those of the author and not necessarily those of the BIS



Two forces at work on central bank balance sheets since August 2007...

- Bold policy moves
 - Funding banks in domestic currency
 - Funding banks in foreign currencies
 - Funding non-banks in domestic currency
 - US: financing ABCP, CP, MBS, AB corporate bonds
 - Japan: financing CP, corporate bonds, bank equities
 - UK: government and corporate bonds
 - ... even funding non-banks in foreign currencies

- Risk-aversion in managing reserves



...with divergent results on central bank assets

- Risk-taking in monetary and credit operations:
 - Credit risk of banks, but collateralised
 - Credit risks of non-banks, some collateralised, some not
 - Duration risk
 - Equity risk
- Risk-avoidance in managing reserves:
 - Less credit risk, even where government support has been made explicit in the case of US agencies
 - Less duration risk



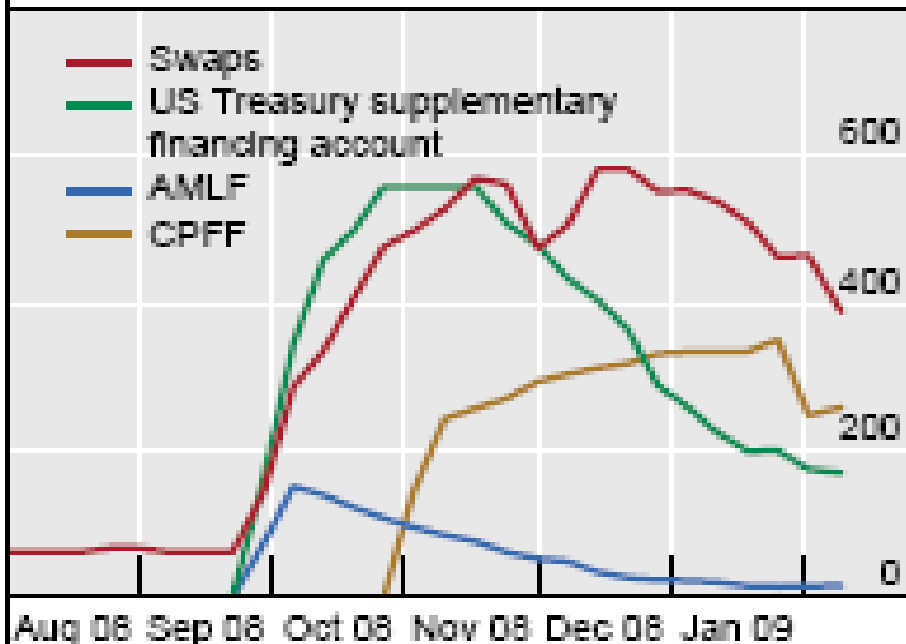
For instance, the Fed's balance sheet ...

- Has grown from \$800 billion to \$1.9 trillion since August 2007
- Facilities also helped other market participants than US banks to secure US dollar funding:
 - AMLF: Asset-backed CP Money Market Fund Liquidity Facility
 - CPFF: Commercial Paper Financing Facility
 - 15 Swap lines providing US dollar funding to foreign central banks

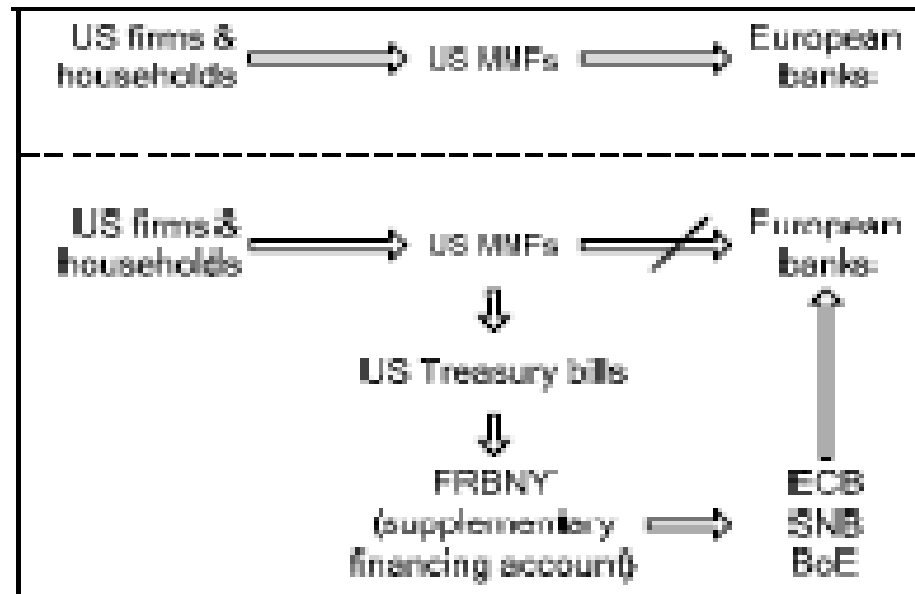


Federal Reserve liquidity and official reintermediation

Federal Reserve liquidity operations¹



Official reintermediation of US dollar credit to non-US banks



¹ Outstanding amounts, in billions of US dollars; Wednesday observations.

Sources: Federal Reserve; Datastream.

Graph 6

Note: AMLF is Asset-Backed Commercial Paper Money Market Fund Liquidity Facility; CPFF is Commercial Paper Financing Facility

Source: Baba, McCauley and Ramaswamy, "US dollar money market funds and non-US banks", *BIS Quarterly Review*, March 2009.



Official holdings of US dollars securities: between June 2007 and June 2008, growth still favours US Treasuries & agencies (\$ billions) ...

	Treas bills	Agency paper	Corp short-term*	Bank depos & repos	Treas bonds	Agency bonds	Corp bonds	Equities
June 2007	159	80	17	704	1,452	750	99	266
June 2008	225	130	18	613	1,684	966	106	363

*Mostly commercial paper

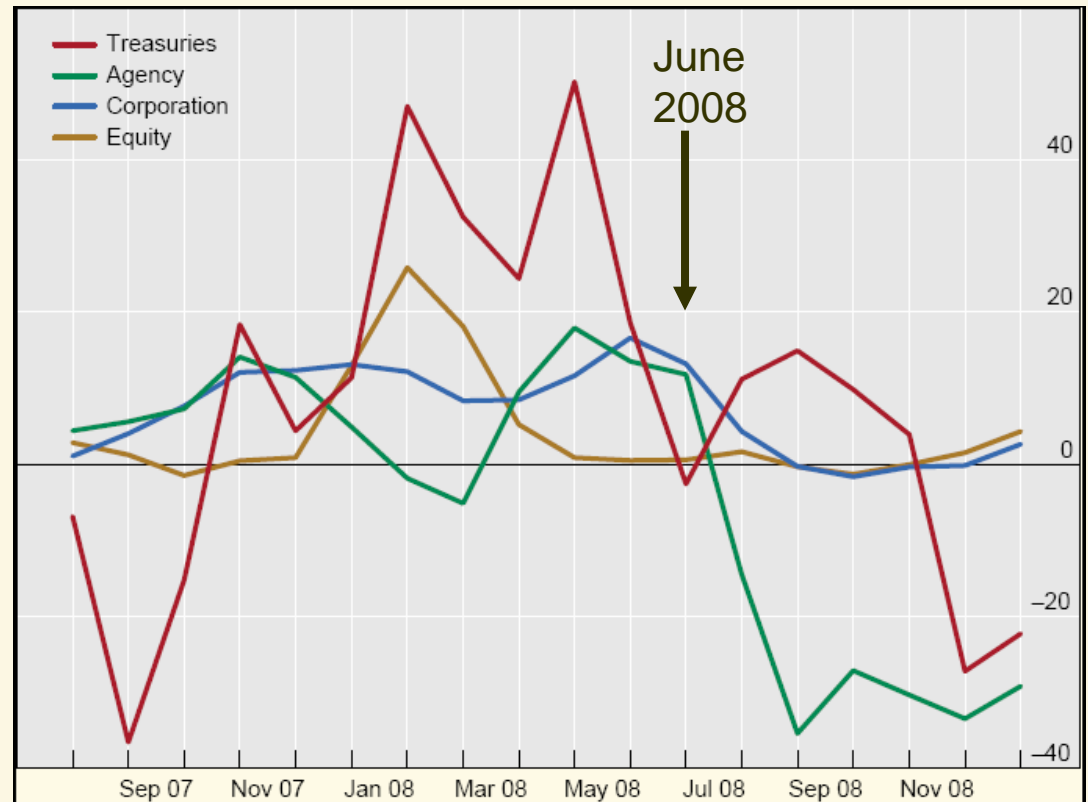
Sources: Treasury International Capital; BIS



...but from June 2008, official institutions are selling long-term US securities...

(Cumulative purchases since June 2007, \$ billions)

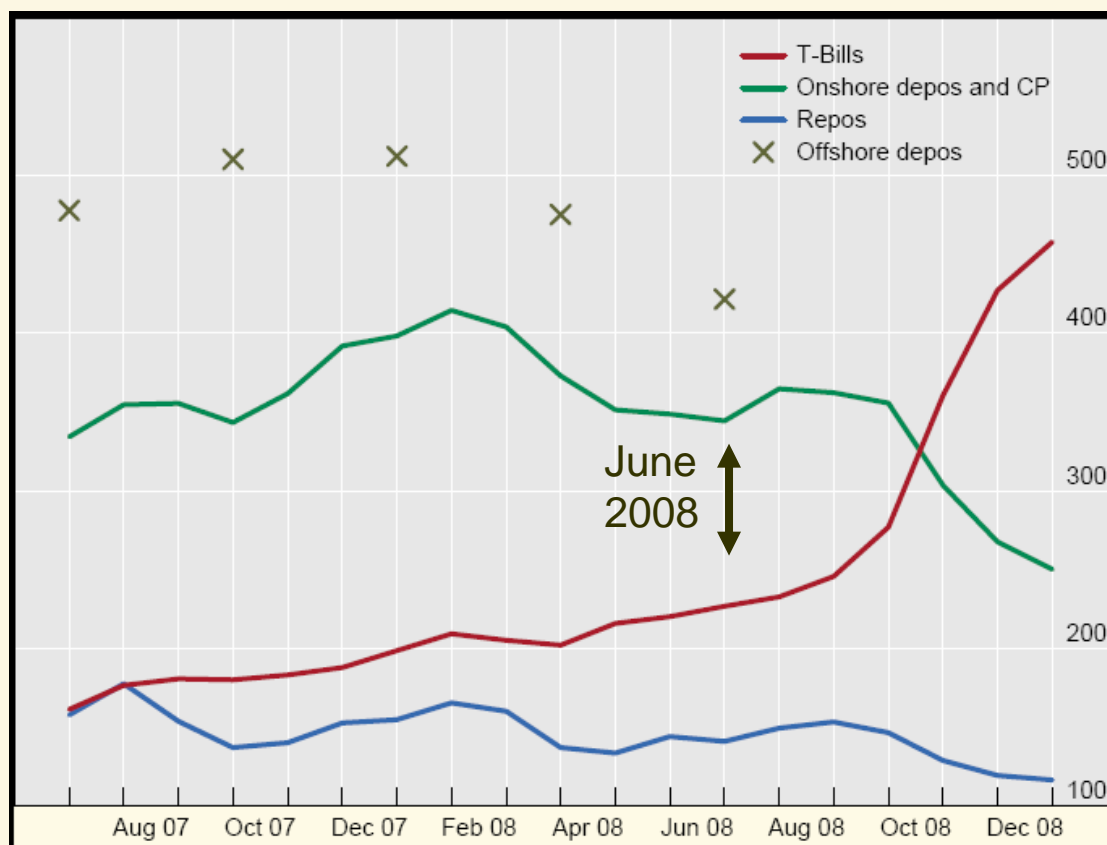
- Starting from 6/08, officials sell agencies and corporate bonds
- Selling of Treasury coupon securities after the Lehman failure





...and flee to quality at the short end. (according to US Treasury & BIS statistics, \$ billions)

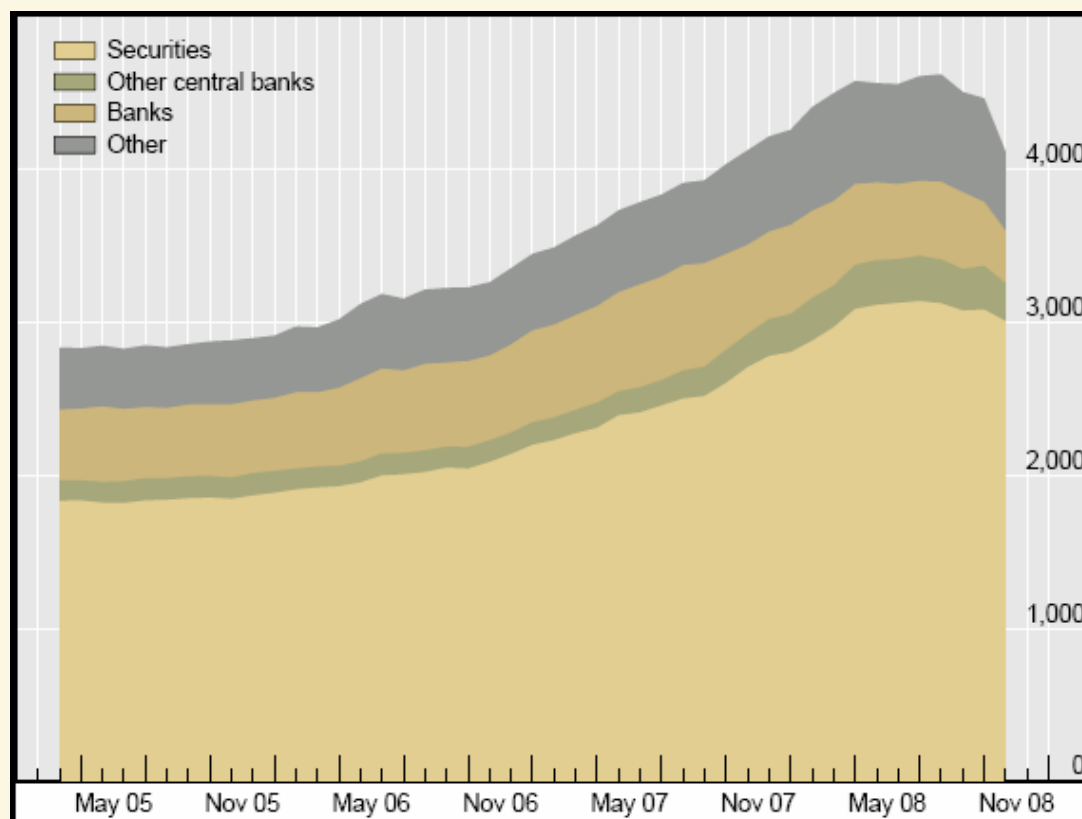
- In last quarter of 2008, foreign officials bought \$200 billion in T-bills and sold \$100 billion in bank deposits and CPs
- Much larger shifts than 8/82, 5/84, 10/87 or 9/98





National data (SDDS) also show flight to quality (billions of US dollars)

- The 63 authorities that report on their reserve holdings to the IMF under the SDDS have seen overall holdings decline and a stable allocation between securities and other
- But big shift from bank deposits to claims on central banks





Active international cooperation amongst central banks strengthened in crisis time ...

- Individual policy actions beneficial to global markets
- Swap lines between central banks
- Coordinated liquidity provisions and interest rate policy actions
- Cooperation on global monetary and financial stability through BIS based Committees



The Basel Process

- Bi-monthly meetings of Central Bank Governors at the BIS
- The Financial Stability Forum (FSF)
- The Basel Committee on Banking Supervision (BCBS)
- Other Committees based at the BIS:
 - The Committee on the Global Financial System (CGFS)
 - The Committee on Payment and Settlement Systems (CPSS)
 - The Markets Committee (MC)
 - The Irving Fisher Committee on Central Banks Statistics (IFC)
- The Financial Stability Institute (FSI)
- The Joint Forum
 - between the International Associations of Insurance Supervisors and of Deposit Insurers (IAIS and IADI) and the International Organisation of Securities Commissions* (IOSCO)

* based in Madrid