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Rapid Expansion of Overseas Banking

by Eckard Paul Imhof, Los Angeles *

Since the mid-sixties the expansion of the overseas banking system of American banks accelerated. New impulses will be generated by the "petrodollars" of the oil producing countries which will most likely be handled by the overseas branches.

The worldwide net-work of American branch banks is preparing to meet a new challenge. Oil producing countries may generate as much as \$ 50 bn annually over and above their import needs. While President Nixon's international economic report of February 1974 has urged that Euro-dollar market operations of U.S. banks be brought home, it appears more likely that overseas branches will handle a major share of the "petrodollar"-business.

Last January 29, the U.S. Government has ended certain capital controls, which had contributed substantially to the spectacular growth of branch banking abroad in recent years. However, many restrictions remain in force on the U.S. market. There are reserve requirements and ceilings on deposit yields, for instance. If subjected to all domestic regulations, U.S. banks would become less competitive than their international counterparts. For practical considerations the Federal Reserve Board could hardly grant exemptions for repatriated Euro-dollars. There is no way of isolating less regulated funds effectively and preventing loans contrary to national monetary policy, if administered by the same domestic banking office using two separate sets of books.

Spectacular Expansion

Assets of foreign branches of U.S. banks have for the first time exceeded the \$ 100 bn mark in July 1973. The \$ 50 bn mark had been reached in May 1971. The most recent statistics published by the Federal Reserve Board reports total assets of \$ 110.6 bn as of September 30, 1973, of which nearly two thirds or \$ 70.3 bn were payable in U.S. dollars¹. The bulk of the ever-growing Euro-dollar pool is held at foreign branches of American

banks. Total assets of foreign branches have increased by 48 p.c. in the first three quarters of 1973, Euro-dollar assets by 40 p.c.

A number of factors have stimulated the spectacular expansion of American banks overseas. Financing needs of world trade and U.S. direct investments in foreign countries have rapidly increased. Major banks have ventured abroad to serve their corporate clientèle wherever there was a need. Strong incentives to shift credit operations to overseas branches had resulted from various restrictions on the transfer of capital. An interest equalization tax was among the measures implemented in the sixties in order to bolster the U.S. balance of payments. Because anti-trust- and banking laws impose stringent limitations on major banks' domestic growth, branching out abroad became even more attractive. The Chase Manhattan Bank for instance was able to open hundred branches and subsidiaries overseas before obtaining the first foothold in up-state New York. First National City Bank of New York may engage in retail banking in England (moneyshops) but is restricted to the financing of foreign trade in California (Edge-Act corporation).

From 1960 through 1972 overseas branches of U.S. banks have grown considerably faster than either world trade or U.S. direct investment abroad. U.S. exports have expanded 2.5 fold, U.S. imports even 3.6 fold. The bookvalue of direct foreign investment has almost tripled. During the same period the number of American banks with foreign subsidiaries has increased from 8 to 108. The number of overseas branches has increased from 131 to

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¹ Fred B. Ruckdeschel, Assets and Liabilities of Foreign Branches of U.S. Banks. In: Federal Reserve Bulletin, February 1972. He explains the monthly reporting system.

627. The assets of overseas branches of members of the Federal Reserve System have expanded 22 fold. That is a remarkable increase of 2,100 p.c.

The Overseas Banking Empire

The expansion of the overseas banking empire accelerated in the mid-sixties. Not until 1967 the full impact of American capital controls became evident. Table 1 compares the growth of assets at American banks abroad with foreign trade statistics and the bookvalue of U.S. direct investment abroad.

Table 1

Expansion of Branch Banking Overseas Compared with Foreign Trade and US Direct Investment Abroad, 1967–1972

(in bn \$)

Global	1967	1968	1969	1970	1971	1972
Assets of Overseas						
Branches of Member Banks Federal Reserve System	15.7	23.0	41.1	52.6	67.1	77.4
US Exports	31.5	34.6	38.0	43.2	44.1	49.8
US Imports	26.8	33.2	36.0	40.0	45.6	55.6
Bookvalue, US Direct Investments Abroad	59.5	65.0	71.0	78.1	86.0	94.0
Western Europe						
Assets of Overseas Branches of Member Banks Federal Reserve System	10.9	17.3	31.2	39.2	48.1	53.9
US Exports	10.3	11.3	12.4	14.5	14.2	15.3
US Imports	8.2	10.3	10.1	11.2	12.6	15.4
Bookvalue, US Direct Investments Abroad	17.9	19.4	21.7	24.5	27.6	30.7

In the 1960–1972 period assets of all Federally insured commercial banks in the U.S. have increased by 190 p.c. Assets at overseas branches have represented only 1.4 p.c. of total assets of American banks in 1960, in 1972 already 10.5 p.c. Banks with foreign branches have grown considerably faster than competitors limited to the domestic banking business. Because only few

major banks had the capability to venture abroad, the concentration of the U.S. banking industry was greatly enhanced.

During the credit crunch of 1969/70 multinational banks have enjoyed considerable competitive advantages, because they were able to draw on Euro-dollar liquidity for domestic loans. Nearly \$ 15 bn or approximately one third of total assets at foreign branches was loaned to parent banks in the U.S. The multinational banks thwarting of U.S. monetary policy was sharply criticized by Andrew F. Brimmer, Member of the Board of Governors of the Federal Reserve System². In the face of shrinking deposits regional banks had to sell treasury bills to maintain their loan volume. Subsequent to 1970 more U. S. banks established branches overseas. Direct participation in the Euro-market was perceived as safeguard against possible repetitions of the credit crunch.

Overseas offices of 22 major American banks have reported deposits aggregating \$ 100.2 bn as of December 31, 1973 (Table 2). A year earlier the 22 banks had reported total overseas deposits of \$ 66.5 bn. Total deposits at Federal Reserve member banks' offices abroad reached \$ 67.8 bn in 1972. The three largest banks alone accounted for 46 p.c. Their share has, however, slightly decreased in 1973. While the three largest U. S. banks have added \$ 10 bn to deposits at overseas branches last year, the highest rates of increase were achieved by banks, which are now trying to make up for a belated entry into branch banking abroad.

Growth rates of 66 p.c. to 70 p.c. were achieved last year at foreign branches of Bankers Trust,

² Andrew F. Brimmer, Multi-National Banks and the Management of Monetary Policy in the United States; presented before a Joint Session of the American Economic Association and the American Finance Association, Toronto, Canada, December 28, 1972.



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Table 2
Deposits at Overseas Offices of Leading Commercial Banks

Banks	in mn \$		p.c. of total deposits		
	1973	1972	1973	1972	1964
First National City Bank, New York	16,989	12,425	49	45	16
Bank of America, San Francisco	13,015	10,566	35	33	10
Chase Manhattan Bank, New York	12,700	8,172	43	37	12
Morgan Guaranty Trust, New York	6,492	4,889	42	38	8
Manufacturers-Hanover Bank, New York	5,499	3,857	32	28	5
Bankers Trust, New York	5,484	3,216	39	30	4
Marine Midland Bank, Buffalo, N. Y.	4,154	2,394	40	28	2
Continental Illinois Bank, Chicago	4,021	2,753	32	28	1
Chemical Bank, New York	3,908	2,831	27	22	3
First National Bank of Chicago	3,436	2,342	29	27	—
Mellon National Bank, Pittsburgh, Pa.	2,826	1,703	39	31	—
First National Bank of Boston	2,508	1,555	40	34	6
Security Pacific Nat. Bank, Los Angeles	2,216	1,921	20	19	—
Wells Fargo Bank, San Francisco	1,974	1,163	22	16	—
United California Bank, Los Angeles	1,646	623	25	12	—
Crocker National Bank, San Francisco	1,275	1,091	16	18	—
Franklin National Bank, New York	1,136	772	31	19	—
National Bank of Detroit	873	684	16	13	—
Cleveland Trust	657	320	23	12	—
Harris Bank, Chicago	630	380	22	16	—
Bank of New York	540	240	28	14	—
Seattle First National Bank	352	261	12	10	—

New York; Wells Fargo Bank, San Francisco; Mellon National Bank, Pittsburgh, Pa.; First National Bank of Boston; Marine Midland Bank, Buffalo, N.Y.; and Harris Bank, Chicago. Overseas deposits with United California Bank's foreign branches increased by 150 p.c., domestic deposits by only 3.7 p.c. The Bank of New York's domestic deposits were down by 4 p.c. while deposits at offices abroad increased by 120 p.c.

Five major American banks carry at least 40 p.c. of their deposits at overseas branches. Most dependant on Euro-dollar business is First National City Bank of New York (FNCB) with 49 p.c. of total deposits overseas. FNCB's foreign deposits alone exceed total deposits of all, but the four largest, American banks. In 1973 a single major bank has grown faster at home than abroad. Crocker National Bank, San Francisco has acquired almost \$ 1 bn in deposits from FDIC, the liquidator of U.S. National Bank of San Diego. Major foreign banks face substantial losses in the

aftermath of the San Diego bankruptcy, and are currently engaged in litigation against FDIC and Crocker. It is conceivable that resulting illwill may have slowed the growth of Crocker National Bank's international business in the final quarter of 1973.

Average increase of deposits of America's 1,000 largest banks was 15 p.c. in 1973. The 100 largest, which include most of the multinational banks, increased deposits by 18.5 p.c., the other 900, predominantly domestic banks by an average 8 p.c. Close to one third of the 100 leading banks' deposits are held at overseas branches.

Foreign branches are heavily engaged in the inter-bank business. As of December 31, 1972 approxi-

Table 3
Assets and Liabilities of Foreign Branches of US Banks

(in mn \$, December)

Item	Assets		Liabilities	
	1971	1972	1971	1972
Total Assets (Liabilities)	61,334	80,034	61,336	80,053
Claims on (to) US	4,798	4,735	3,114	3,559
Claims on (to) parent bank	2,311	2,124	669	1,000
Claims on (to) foreigners	54,752	73,031	56,124	73,842
Claims on (to) foreign branches of parent bank	11,211	11,717	10,773	11,344
Other foreign banks	24,550	36,738	31,081	42,531
Official institutions	1,167	1,665	5,513	8,486
Nonbank Foreigners	17,823	22,910	8,756	11,483
Other Assets (liabilities)	1,785	2,268	2,098	2,634

The rounding of monthly figures may explain slight differences between assets and liabilities.

Table 4
Assets and Liabilities of Overseas Branches of Member Banks Federal Reserve System 1971 and 1972

(in mn \$)

Item	1972	1971
Assets		
Cash	30,199	20,425
Loans	36,300	27,671
Due From Head Office & US Branches	2,004	3,717
Due From Other Overseas Branches Of Own Bank	5,308	not separately reported
Other Assets	3,536	15,241
Total Assets	77,437	67,054
Liabilities		
Demand Deposits	6,249	6,058
Time Deposits	61,567	44,765
Due to Head Office & US Branches	992	1,798
Due to Other Overseas Branches Of Own Bank	5,072	not separately reported
Other Liabilities	3,548	14,442
Total Liabilities	77,437	67,054

mately two thirds of assets and liabilities represented claims on or due to banks. Tables 3 and 4 give a breakdown of balance sheet items of foreign branches of U.S. Banks and overseas branches of member banks of the Federal Reserve System for 1971 and 1972.

Changing Regional Structure

More than half of the U.S. banks' overseas assets are concentrated in London. Approximately one sixth of foreign assets are held by 89 U.S. branch banks in Continental Europe. By far the fastest growth rate is reported for American branches on the Bahamas, where assets have reached \$ 18.7 bn as of September 30, 1973. Because the costs of establishing and operating a London office are prohibitive, medium-sized American banks prefer to base their Euro-dollar operations on the Bahamas. There are also tax advantages. Since the political climate has deteriorated, the Grand Cayman Islands have become popular. Only the largest banks operate branches in Latin America, Africa and Asia. The Third World represents a small share of the U.S. banking empire overseas. Table 5 illustrates changes in regional structure from 1967 through 1972.

Andrew F. Brimmer, probably the most prominent student of American International Banking has

Table 5
Regional Structure — Expansion of Branch-Banking Overseas 1967–1972
(Assets in mn \$)

Location	1972	1971	1970	1969	1968	1967
U.K. and Ireland	40,915	35,143	29,668	24,753	13,177	8,178
Continental Europe	13,033	12,913	9,496	6,464	4,121	2,721
Bahamas	11,576	7,849	4,421	2,993	*	*
Latin America	2,602	2,519	2,055	1,584	1,736	1,270
Far East	7,119	6,221	4,423	3,257	2,663	2,267
Middle East and Africa	386	384	315	265	284	257
US Overseas Areas and Trust Territories	1,807	2,025	2,233	1,804	1,037	965
Total Assets	77,437	67,054	52,611	41,120	23,018	15,658
Number of Branches						
U.K. and Ireland	53	48	44	40	35	25
Continental Europe	89	80	72	64	46	34
Bahamas	94	73	61	31	*	*
Latin America	227	229	223	203	178	133
Far East	97	83	79	76	72	63
Near East and Africa	17	17	14	7	9	9
US Overseas Areas and Trust Territories	50	47	43	38	35	31
Total Branches	627	577	530	459	375	295

* Bahamas not separately reported, included in Latin America.

remarked³, that the rate of profit which the banks can earn on the resources of their foreign branches appears to be ominously thin. For example, in 1972, the rate of return on the assets of the London branches of U.S. banks seems to have been in the neighbourhood of 0.12 p.c. This contrasted sharply with the rate of 0.54 p.c. earned on the total assets of these same U.S. banks. For all insured commercial banks in the U.S., the rate of return on total assets was roughly 0.79 p.c. in 1971.

Commercial banks in the U.S. were, according to Brimmer, "significant participants in the outflows which occurred last year during the intense speculation against exchange rates. These institutions contributed on balance some \$ 2.5 bn to the volume of funds which moved abroad in connection with the exchange rate speculation early in 1973". The pattern was quite reminiscent of the outflows which occurred during May and August of 1971. A study published by the U.S. Treasury last August also identifies multinational banks as one of the more important causes in the worsening of the U.S. balance of payments deficit in the first quarter of 1973.

At year end 1973 major U.S. banks have revealed significant increases in foreign earnings. For example J. P. Morgan, parent of New York's Morgan Guaranty Trust Co., reported that operating net rose almost by 22 p.c. to \$ 145.6 mn. A major factor was a dramatic rise in income from foreign exchange trading. Such income, before expenses and taxes, rocketed to \$ 42.4 mn in 1973 from \$ 19.7 mn a year earlier. Also aiding earnings was the devaluation of the dollar during the first quarter of 1973. A \$ 4.2 mn after-tax gain in the dollar value of Morgan's net investment in foreign branch and subsidiary operations resulted. However, a \$ 547,000 reserve against possible future losses in currency translation has been established.

Concern has been voiced about high-risk loans and slim profit margins in the Euro-dollar market. On the basis of available data it remains difficult to assess the vulnerability of major U.S. banks to fluctuations of foreign exchange markets and economic reversals abroad. Meanwhile "the banking scramble for Arab dollars" is well underway⁴. Nearly a dozen American banks have recently bought or are presently negotiating for interest in financial institutions in Beirut, Lebanon and all over the Middle East.

³ Andrew F. Brimmer, American International Banking, Trends and Prospects; presented before the 51st Annual Meeting of the Bankers' Association for Foreign Trade, Boca Raton, Florida, April 2, 1973.

⁴ Business Week, March 16, 1974.