

LES EUROMARCHES

Evolution, structure, volume & instruments

- Origines et développements
- Eurocrédits et Euro-émissions obligataires
- Clauses juridiques des Syndications bancaires

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The Euromarkets: evolution, structure, instruments

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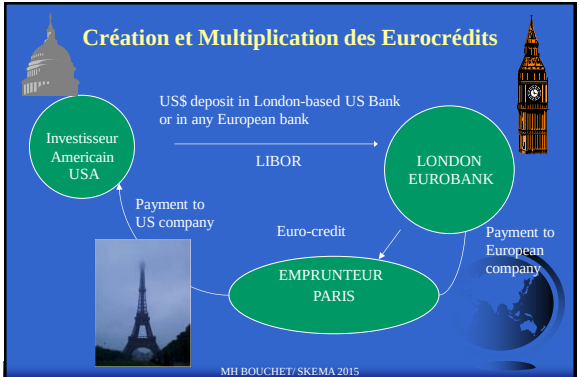
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Qu'est-ce qu'une EURODEVISE?

- C'est une devise convertible qui circule librement en-dehors du pays d'émission, sous forme de prêt ou de dépôt.
- C'est la résidence de la banque et non sa nationalité qui fait d'elle une "euro-banque".
- Les dépôts en eurodevises sont généralement à court terme < 1 an alors que les crédits sont à moyen et long-terme, d'où une activité bancaire d'intermédiation financière et de transformation de maturité dans les bilans.

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Création et Multiplication des Eurocrédits



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The Euromarkets

ORIGINS of the EURO-DOLLAR MARKETS

In the late 1950s, expansion of a free flowing and unregulated international money market in parallel with rapid trade growth and rising international capital flows

- 1945-1971: Growing role of the US\$ as international means of payment and reserve asset “\$ as good as gold...”
- 1958: free convertibility of most Western world currencies = expansion of international capital flows
- 1960: Paris-based soviet Narodny Bank used \$ instead of rubles for foreign trade and payments. The Bank lent \$ to European banks to earn interest on \$-deposits.

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The roots of the Euro-dollar market expansion in the US banking regulations

- Refusal of the US Fed to abandon the Regulation Q interest rate ceilings on time deposits in the US.
- Regulation M set non-interest bearing reserve requirements as a proportion of banks’ deposits.
- 1963: Interest Equalization Tax imposed by the US Fed to discourage US investors from investing in foreign securities. Thus, non-US borrowers had to sell securities outside the US market.
- American banks have been able to make higher profits lending in the Eurocurrency markets than they could lending at home.

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➤ 1960s: Expansion of US multinational corporations in Western Europe. Many US banks set up overseas branches in Europe

➤ 1960s: Rising US balance of payments deficit (hence increasing net US \$ balances outside the United States)

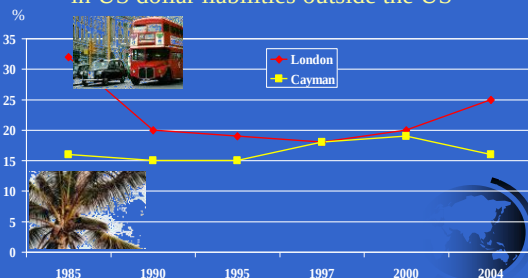
➤ Desire of Russia and Eastern European countries to keep their \$ balances outside the US (Paris-based Eurobank telex code)

➤ Britain’s policy of £ replacement by \$ in trade financing operations

➤ Investment of \$-denominated official reserves outside the United States (hence, in the Eurodollar Market)

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Respective shares of London & the Caribbean in US dollar liabilities outside the US



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The Euro-Dollar Money

Multiplier

US\$ Deposit in a United States-based bank → transfer to a Eurobank outside the US → creation of a Eurodollar time deposit

→ The Eurobank must employ this increase in assets in an interest earning investment

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- Investment in US T bill or interest earning CD = no credit creation (leakages outside the Euro-dollar system)
- Investment in Government obligations outside the US = no credit creation
- **Euro-dollar loan to non-bank borrowers: multiplier effect and on-going eurodollar credit expansion**

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Multiple credit creation (unless the funds lent to the borrower are used in the US, such as the purchase and import of US products, and constitute “leakages”)

or

Interbank deposit of the Eurodollar funds in another Eurobank

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I- Eurocrédits syndiqués

- Instruments bancaires
- Intermédiation financière
- Volume et Evolution

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Les Eurocrédits

- Juxtaposition de crédits accordés, du fait de leur montant important, par un ensemble de banques réunies dans un syndicat bancaire international qui mutualisent le risque de défaut, sous l'autorité et la coordination d'un **chef de file**.
- C'est un crédit à moyen terme, de l'ordre de 3 à 8 ans.
- On distingue les *term loans* et les crédits *revolving*.

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Qui emprunte?

- Inter-bancaire= 63%
- Non-bancaire = 37%
- Pays émergents= 9%
- Zone Euro= 34%
- USA = 26%
- Japon= 4%
- Offshore centers= 13%

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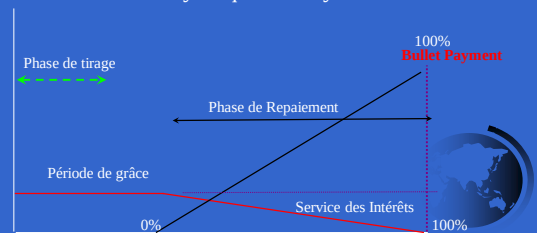
Les Eurocrédits

- Les « term loans » se distinguent par trois phases: tirage, période de grâce, et remboursement
- Les crédits revolving permettent une grande souplesse pour tirage et remboursement au gré du débiteur sur toute la durée de vie de l'emprunt, avec un plafond défini.
- Les eurocrédits syndiqués: syndicat bancaire permet la mutualisation des risques, sous la forme d'un Club « deal » (nombre limité de grandes banques) ou d'un syndicat international plus large. (underwriting)

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Les Eurocrédits

Crédits syndiqués à moyen-terme



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Phases de syndication bancaire

- Lead manager ou chef de file (commission de direction ou upfront management fee or *praecipium* fee 1/2%)
- Placing memorandum (underwriting commitment fee pour prise ferme de sous-participations avec commission de garantie)
- Commission d'engagement sur les montants non tirés
- Publication d'un tombstone et distribution d'un prospectus
- Club deal (une dizaine de grandes banques internationales)
- Détermination des marges et commissions (management fee and upfront fee, participation fee 3/8%, commitment fee 3/16%, agent fee)
- Distribution of commissions de participations aux souscripteurs (underwriters)
- Banque AGENT (distribution semi-annuelle des paiements d'intérêt sur une base pro rata)

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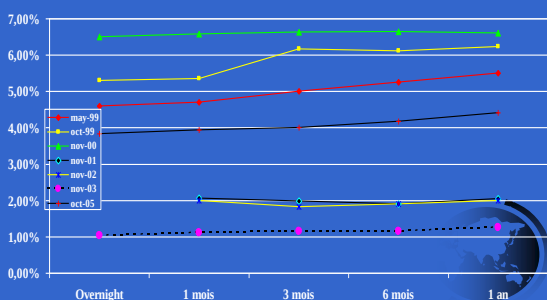
Taux de base sur les Euromarchés: taux flottant: LIBOR

- Base Rate: 3 or 6-month LIBOR + Spread en pdb
- Oct. 2007 = 4,85%
- Février 2015: 0,25%

Spread, Interest Rate: Usually expressed in percentage points over and above a reference rate such as LIBOR or the prime rate in the country of the creditor. The spread added to the reference rate constitutes the interest rate applicable to the loan.

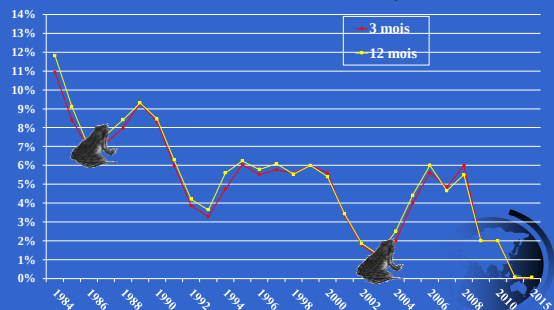
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Euro-Dollar LIBOR 1999-2006 term structure



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Evolution du taux Euro-\$ LIBOR



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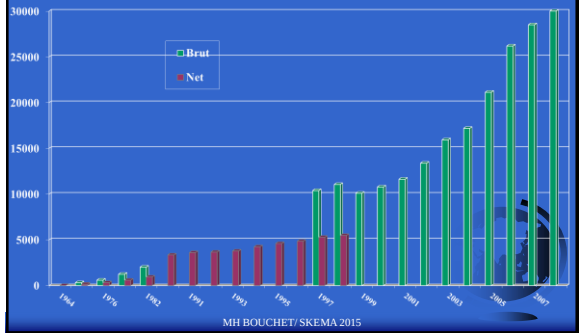
Volume "brut" et "net" du marché

- The Gross size of the market comprises the overall international bank claims, i.e, cross-border claims in all currencies + local claims in foreign currencies.
- The Net size of the market is equal to the Gross size - interbank redepositing
 - Fin-1998: taille brute= US\$11,048 milliards
 - taille nette 1998= US\$5,485 milliards
 - Fin-2001= US\$12,000 milliards
 - Fin 2005= 21,125 milliards
 - Fin-2009= US\$30,500 milliards



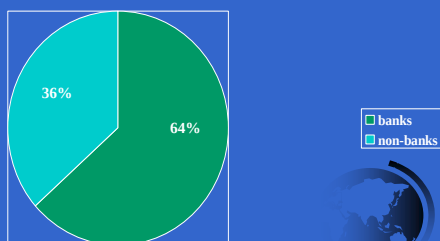
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Evolution du marché international des crédits bancaires vis à vis des non-résidents 1964-2009 en milliards de US\$



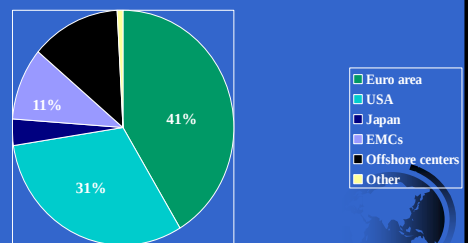
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Composition of international banks' cross-border claims 2009

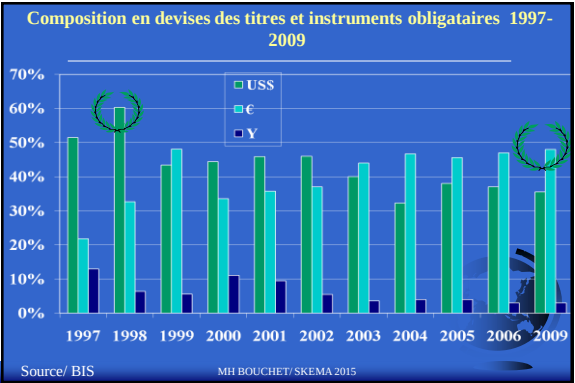
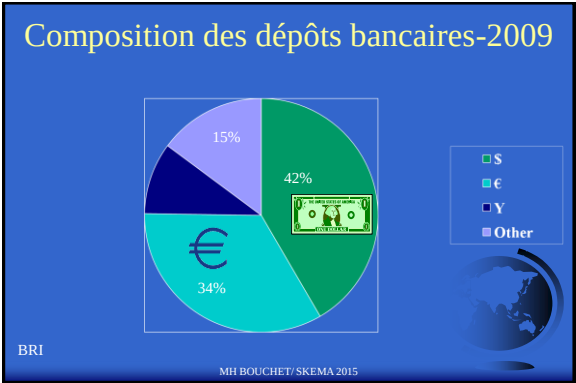
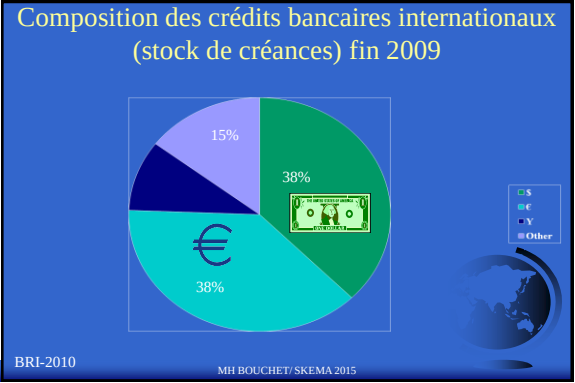
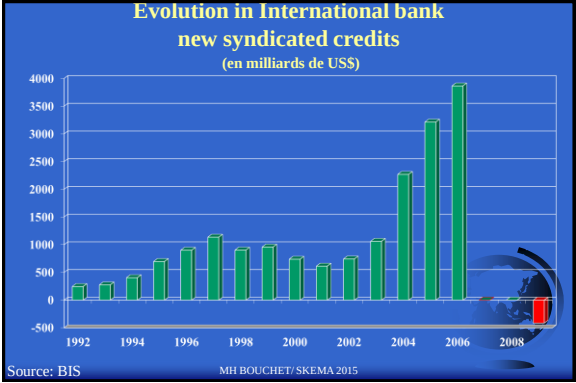


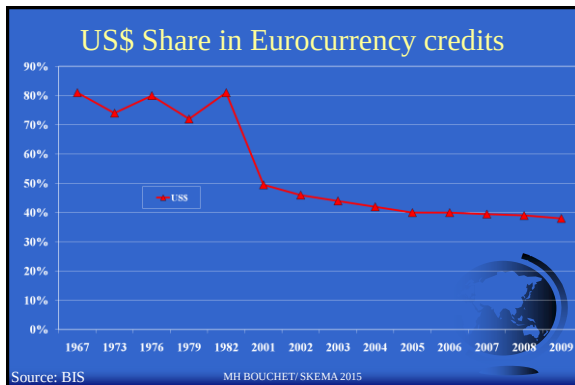
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Composition of international banks' cross-border claims on non-bank borrowers



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Marché des Eurodevises instruments de captation d'épargne (dépôts)

- **Term deposits and CDs:** negotiable instruments that can be traded on the secondary market. Because of higher liquidity, CDs pay lower interest rate (<about 10 basis point: a basis point is 0,01%). Very popular with company treasurers, because of low risk and high flexibility.

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Marché des Eurodevises instruments de crédits bancaires

- **Eurocredits:** medium to long-term loans denominated in euro-currencies (> 1 year)
- **Stand-by Credit:** A commitment to lend up to a specified amount for a specific period, to be used only in a certain contingency. (commitment fee paid on the unused portion of a facility)
- **Euro-commercial paper:** short-term euronotes issued by companies < 365 days. Nominal value of notes > \$500,000, with corporate and sovereign issuers. Investment grade rating not required. Euronotes are unsecured debt securities <1 year

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Clauses Financières des Eurocrédits syndiqués

- Bullet Maturity:** One-time payment of principal at maturity.
- Currency Redenomination:** Switching of loans denominated in one currency or currencies into the currency of the creditor country or into ECUs. (The mechanism is intended to bring about a better match between the currency mix of debt service payments and the currency composition of external receipts.)
- Interest Rate Switching:** Selection of a new basis for interest calculations on an existing loan. The options may include LIBOR, a domestic rate, the prime rate or a fixed rate, to which a margin is added.

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II- Le Marché des Titres en Euro-devises

- Eurobonds: appel direct à l'épargne institutionnelle et/ou privée
- Emission hors du pays de la monnaie d'émission (ex. Londres ou global bonds)

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Marché des Euro-obligations

- Déf.: Titres à moyen et long-terme (5/10 ans) libellés en devises émis par l'intermédiaire d'un syndicat bancaire international et offerts à des investisseurs sur les marchés globaux
- Le cours du marché de l'obligation est la valeur actualisée des flux futurs que le titre assure ($I + P$)

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Marché des Euro-obligations

- Obligations classiques à **taux fixes**
- Obligations à **taux variables** (FRNs)
- Obligations à **coupon zéro** (intérêts capitalisés)
- **Global bonds** (ex. IBRD)
- Emissions **garanties** (« collateralized » bonds): Bradys
- Obligations avec **option** monétaire ou à double devise (paiement d'intérêt ou remboursement dans une devise différente de celle de l'émission)
- Obligations **convertibles** en actions (remboursements en actions de la société émettrice à prix déterminé au cours d'une période spécifiée)

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EUROBONDS

- Eurobonds: long-term financial instruments issued by MNCs or country governments, and denominated in a currency other than that of the country of placement.
- Eurobonds are underwritten by a multinational syndicate of investment banks and simultaneously placed in many countries. They are issued in **bearer form**, and coupon payments are made yearly. No taxation (pas de « retenue à la source » pour les titres au porteur)
- The US\$ accounts for about 70% of eurobonds. Liquidity in the secondary market is monitored by Euro-clear. Highly tradeable securities. Mainly in London and Luxembourg.

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Clearing procedures in the international bond markets

- International Securities Market Association (ISMA)
- Euroclear (created by Morgan in 1968)
- CEDEL (Centrale de livraison des valeurs mobilières) created in Luxembourg in 1970
- Eurobonds are engraved certificates. Euroclear and Cedel have a network of custodian banks where the certificates are deposited in bearer form for safekeeping. They manage the clearing of transactions on settlement date.

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Montage et Procédures d'émissions

- Chef de file (lead manager) et agent
- Syndicat: management group avec co-chef de file
- Syndicat de prise ferme (underwriting group)
- Syndicat de placement (selling group): placement du papier auprès des investisseurs finaux sans garantie
- Trustee: banque extérieure au syndicat de direction dont le rôle est de protéger les investisseurs en suivant les paiements et l'amortissement
- Tombstones et roadshow

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Eurocurrency market Instruments

- **FRNs**: medium-term notes where the interest is fixed as a percentage above six-month LIBOR (amounted to \$283 billion in 1997 and \$259 billion in 1998). Negotiable and transferable securities with flexible interest rate, fixed interest periods, and issued in pre-determined and uniform amounts. **FRNs are directed at institutional investors**
- **Note-issuance facility (NIF)**: A medium-term legally-binding commitment under which a borrower can issue a short-term paper in its own name, underwritten by banks which are committed either to purchase any notes the borrower is unable to sell, or to provide credit.

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Eurocurrency market Instruments

- **Equity-linked bonds**: convertible bonds or bonds with equity warrants (amounted to \$64 billion in 1997, and \$32 billion in 1998). Right to acquire equity stock in the issuing company (sometimes with detachable warrants containing the acquisition rights). The market value of an ELB is composed of the naked value and the conversion value.



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Eurocurrency market Instruments

- **Note-issuance facility (NIF):** A medium-term legally-binding commitment under which a borrower can issue a short-term paper in its own name, underwritten by banks which are committed either to purchase any notes the borrower is unable to sell, or to provide credit. Issuing procedures with arranger or placing agent and tender panel.
- **Stand-by credit:** A commitment to lend up to a specified amount for a specific period, to be used only in a certain contingency. (commitment fee paid on the unused portion of a facility)



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Euromarket financial instruments

Revolving Underwriting Facility (RUF): Medium-term facility provided by banks on which the borrower can draw at any time of its life, usually certificates of deposits (CDs) or short-term promissory notes. Banking agents attempt to place these securities in the market. Maturities range from 1 to 9 months and carry a Libor-related coupon.



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Marché des Euro-obligations: parts de marché

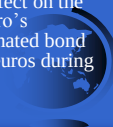
- Deutsche Bank
- Morgan Stanley
- Warburg Dillon Reed
- ABN Amro
- Merrill Lynch
- JP Morgan
- Salomon/Citibank
- RBC
- Paribas
- Barclays
- Commerzbank
- Credit Suisse First Boston

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Eurobond Market

- By spreading the risk among thousands of investors, both private and institutional, as opposed to a handful of banks in the loan market, the bond markets lower the cost of risk and thus reduce the cost of funding for companies and other borrowers. This in turn enables companies to raise larger amounts of debt.
- Many companies took benefit of the depreciating euro in the first half of 1999 to borrow in Euros and swap the proceeds into US\$, which had an immediate downward effect on the value of the €, hence the link between the euro's weakness and the popularity of the euro-denominated bond market (US\$300 b worth of securities issued in euros during the first half of 1999)



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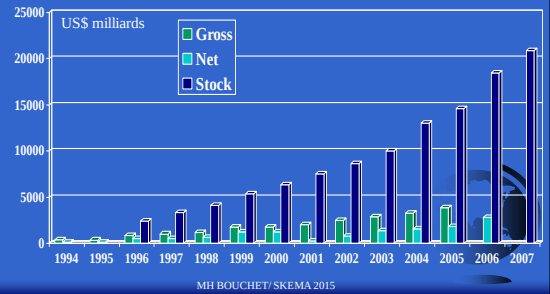
Emerging Markets Eurobonds

- High risk/high yield with low default track record (premium of 20 basis points compared with US corporate borrowers for identical ratings)
- historically, defaults only in the 1930s and late 1980s but recovery rate is better for sovereign debtors than corporate debtors (75% vs 40%)
- problem of comparability of treatment with Paris Club and London Club debts (Pakistan, Ukraine)
- Market risk remains high due to lower amounts (US\$250 b for sovereign bonds vs US\$600b for US corporate bonds) and concentration on 5 countries (Argentina, Mexico, Korea, Brazil and Russia)

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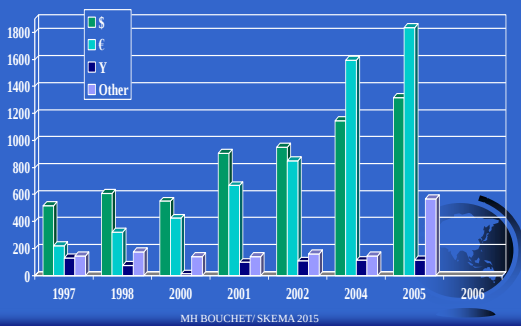
Le Marché des Eurobonds

Gross= completed new bond and note issues in US\$ billion
Net= Gross - redemptions and repurchases



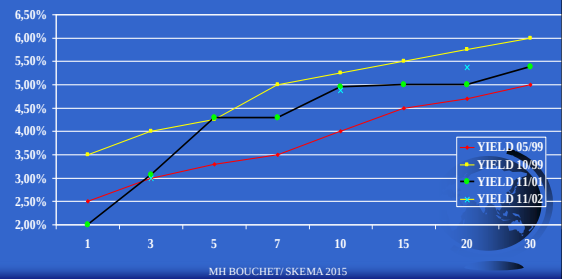
Le Marché des Eurobonds et sa composition en devises

Euro-bond and Euro-note issues in US\$ billion

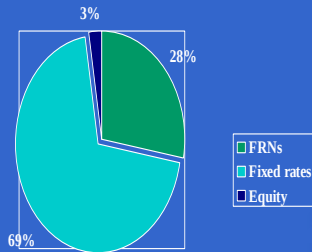


US Treasury bond Yield Curve in Per cent

as of May 15, October 24, 1999, Nov. 22, 2001 & Nov.02



Composition des Bonds & Notes 2006



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Principaux Emetteurs de « Euro denominated convertible debt »

- ☛ France Telecom € 6.2 billion
- ☛ Vivendi Univ. € 2.8 billion
- ☛ Olivetti € 2.5 billion
- ☛ PPR € 1.4 billion
- ☛ Lafarge € 1.3 billion
- ☛ Artemis € 1.2 billion
- ☛ Danone € 1 billion

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Emetteurs d'Obligations libellées en € en 2004-05

- ☛ Peugeot PSA: €500 million (A2/A-)
- ☛ Italie: € 4 milliards en Octobre 2004 (inflation-indexed bonds)

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Emetteurs d'Obligations libellées en Roubles

- ☛ La BERD a lancé une émission de \$150 million libellée en roubles avec une maturité de cinq ans. (on-lending)

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Clauses Juridiques des eurocrédits syndiqués



- Problem of “comparability of treatment” between various categories of creditors:
- Axiom: *an emerging market is a market from which you cannot emerge in an emergency!*
- Ex.: Paris Club insists on involving **Eurobond investors** in refinancing and restructuring workouts. Test cases: Pakistan, Russia, Ukraine, Romania, Ecuador and Venezuela (US\$60 billion question!); Rumania alone owes US\$863 million eurobonds (i.e., tradeable instruments)



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Clauses Juridiques des eurocrédits syndiqués

- **Prepayment clause**: The prepayment clause is a standard clause in loan agreements between a debtor and a creditor bank. In its various forms, it can provide the debtor with the opportunity to accelerate repayment of the loan on a voluntary basis and/or provide for acceleration of repayment due to changes in laws affecting the creditor. In rescheduling agreements, the clause is intended to prevent the obligor to grant a preferential repayment schedule to other banks which have not signed the convention and which would be paid ahead of normal maturity terms.



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Clauses Juridiques des eurocrédits syndiqués

- **pro rata sharing** : A legal covenant in commercial bank agreements which specifies that debt service payments are to be made through the agent bank for allocation on a pro rata basis to all creditor banks. Further, payments received or recovered by any one lender must be shared on a pro rata basis with all co-creditors under the loan agreement. Thus, no one lender may be placed in a more favorable position than its co-lenders with respect to payments received and/or recovered.
- **cross-default**: A legal wrinkle which allows one creditor to declare default and exercise its remedies against the borrower in cases where **other loans** of the borrower have been suspended, terminated, accelerated or declared in default by other creditors.



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Clauses Juridiques des eurocrédits syndiqués

- **Mandatory repayment clause**: standard clause in loan agreements that stipulates certain circumstances under which repayment is accelerated. The debtor, by being obligated to prepay any one creditor, must repay all lenders on a pro rata basis. In the context of rescheduling agreements, the provision is intended to neutralize “free rider” banks which do not participate in debt restructuring and new money agreements. The provision applies across the universe of public sector borrowers so that a voluntary prepayment of one or more credits by one borrower would trigger mandatory prepayment not only by that borrower but also by the other public sector borrowers.



Ex. Ecuador’s default on Brady bonds in October of 1999!

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Clauses Juridiques des eurocrédits syndiqués

Negative Pledge : cette clause protège les prêteurs d'un risque de subordination en interdisant à l'emprunteur de gager des actifs qui donneraient un rang supérieur à d'autres créanciers, par des garanties de remboursement privilégié.



Subordination: ranking of current debt compared to future debt obligations in case of default

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Clauses Juridiques des eurocrédits syndiqués

Optional prepayment provision: The optional prepayment provision permits the borrower to prepay all or part of the loan provided it prepays all lenders under the agreement on a pro rata basis.

Pari-passu clause: la dette contractée vis à vis du syndicat des eurobanques a le même rang que celui des dettes contractées ultérieurement, et elle n'est donc pas subordonnée à d'autres créances de rang supérieur.

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Clauses et conditions de qualité de signature

- Elles indiquent les conditions que doit respecter l'emprunteur, public ou privé:
- ratios d'endettement
- cash flow
- rentabilité
- liquidité et solvabilité
- notification en cas de défaillance
- actions requérant l'approbation du prêteur

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