Box D: Banks' Funding

Australian banks currently source just over a quarter of their funding from offshore capital markets. Another quarter is sourced from domestic capital markets, with the balance coming from domestic deposits.[1] The turbulence in global capital markets in August and September significantly affected debt markets, including the short-term debt markets in which banks raise some of their offshore funds.

However, the market volatility does not appear to have had a significant impact on the operations of banks in Australia. Banks continued to lend normally through this period, with their domestic loan book increasing by $40 billion over August and September, slightly faster than the average rate of growth seen over the year to date (Table D1, Graph D1). Banks' holdings of domestic debt securities and other financial assets rose by $69 billion, largely reflecting increased holdings of other banks' certificates of deposit.

Table D1: Banks' Sources and Uses of Funds[(a)]

	Level in July 2007	Change over August and September 2007	
	$ billion	$ billion	Per cent
Sources of funds	**1 804**	**143**	**7.9**
Domestic deposits	759	29	3.8
Domestic capital markets	401	73	18.3
– Certificates of deposit	216	66	30.6
– Other	185	8	4.1
Offshore capital markets	486	13	2.7
Other liabilities	158	27	17.0
Uses of funds	**1 918**	**145**	**7.6**
Domestic loans	1 221	40	3.3
Domestic debt securities and other financial assets	354	69	19.5
– Certificates of deposit	71	49	69.8
– Other	283	20	7.0
Offshore assets	149	17	11.1
Other assets	194	19	9.8

(a) Excludes securitisation

Sources: APRA; RBA

Banks were still able to source some of their funding from offshore capital markets during this period, though increased investor risk aversion meant that much of the borrowing was at higher spreads and for shorter terms than usual. Despite the difficulties, banks' foreign liabilities increased by $13 billion over August and September, a similar pace to which they had been

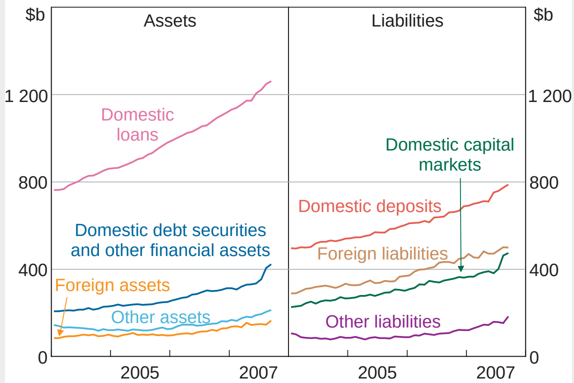
1 *Certificates of deposit have been included in domestic capital market funding, whereas financial corporations' deposits have been included in deposits.*

growing over the past few years. The growth in foreign liabilities was broad-based across deposits, long-term debt securities and short-term debt securities.

Funds raised in domestic capital markets increased by $73 billion. Much of the growth was due to banks issuing certificates of deposit to each other in August. A significant part of this was a precautionary move to boost assets that could be used as collateral for repos with the Reserve Bank should capital markets deteriorate further, and did not provide any net funding to the banking system. But even excluding these transactions, domestic capital market funding rose by $24 billion, suggesting that banks relied a little more than usual on domestic capital markets during this period.

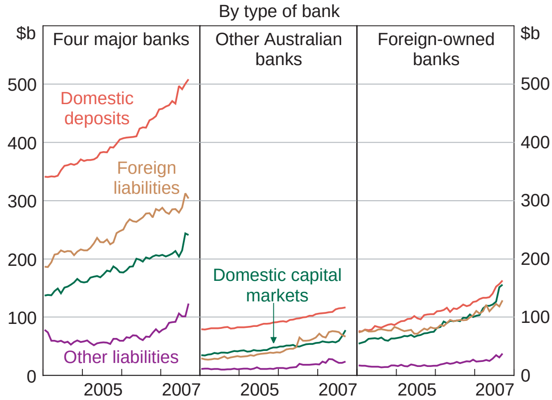
Domestic deposits increased by $29 billion over August and September, with strong growth in deposits from both households and non-financial corporates. The increases in banks' other assets and other liabilities were largely offsetting, and mainly reflected changes in the fair values of the banks' derivative positions.

Graph D1
Balance Sheets of Banks in Australia



Sources: APRA; RBA

Graph D2
Liabilities of Banks in Australia
By type of bank



Sources: APRA; RBA

There was relatively little variation across the different types of banks (Graph D2). Major banks' and foreign banks' lending both increased by about 4 per cent over the two months, with particularly strong growth in business lending in August. Other Australian banks' lending also rose steadily over the period. Foreign liabilities increased by similar amounts across the different types of banks. Increases in domestic liabilities ranged from 8 per cent for the four major banks, through to 14 per cent for foreign-owned banks. The issuance of certificates of deposit increased markedly in August for all banks, though the four majors and the smaller Australian banks recorded the strongest growth. The smaller Australian banks and foreign banks also increased their sales of securities under repo to boost their liquidity. Deposits grew steadily across all banks.

The fact that banks continued to have good access to offshore capital markets during the market turbulence is related to their robust financial positions and their solid reputations with investors. Australian banks' profits and assets have been growing strongly, their impaired assets are low by historical and international standards, and they have very little exposure to US sub-prime mortgages and leveraged loans (the two asset classes that triggered the recent capital market turbulence). This strong position is reflected in listed banks' share prices, which have risen by 8 per cent since the end of June, compared with a 6 per cent fall for overseas banks.