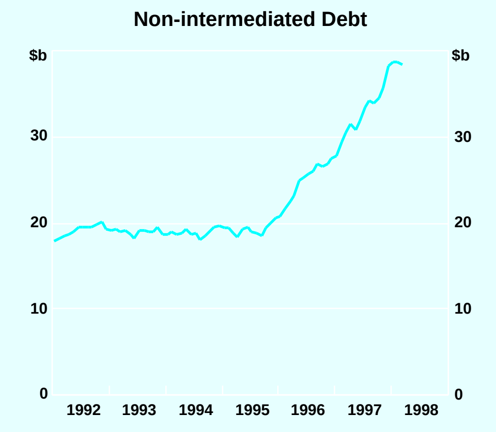
Box F: Growth in Non-intermediated Debt

Over the past two years, non-intermediated debt – that is, debt raised by companies issuing securities directly to the market – has picked up sharply, with annual growth rates rising from less than 2 per cent in 1995 to around 30 per cent over the year to March 1998. Since late 1995, the level of non-intermediated debt on issue has almost doubled, having remained broadly unchanged during the first half of the 1990s (Graph F1).

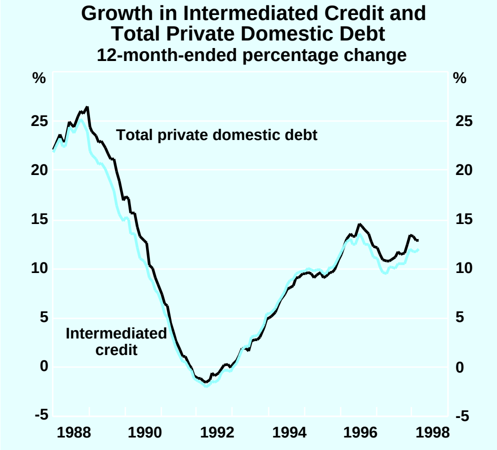
Graph F1



The rate of increase of non-intermediated debt over the past two years has outpaced that of *lending by intermediaries*. Non-intermediated debt, however, remains a relatively minor source of funds; currently, it amounts to about $38 billion, compared to intermediated credit of about $530 billion. That said, the solid growth in non-intermediated debt has led to the total borrowings (or debt) of households and businesses growing by a bit over 1 percentage point faster than credit from intermediaries over the past year or so, with a growth rate of 13 per cent, or twice the rate of growth of nominal GDP.

Around 60 per cent of the non-intermediated funding represents direct approaches to capital markets by corporations (down from around 70 per cent in early 1995), while the remaining

Graph F2

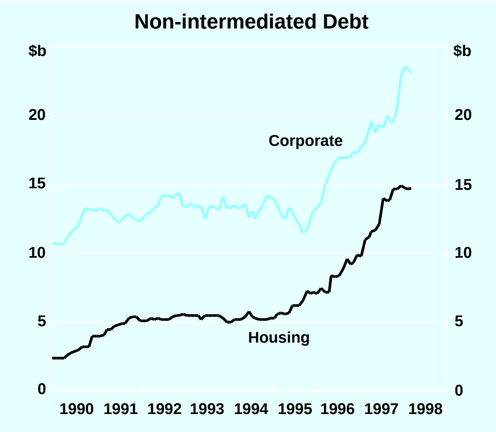


40 per cent reflects issues of debt to finance housing loans by mortgage managers and banks (up from around 30 per cent in early 1995). Some banks have also recently issued debt against corporate loans, although this development has not yet had a significant impact on the figures. The statistics shown here avoid the problem of 'double counting' since securitisation of loans by banks has the effect of reducing their balance sheets (and credit) while boosting the level of non-intermediated debt.

Non-intermediated corporate debt – such as bond issues and promissory notes – began to rise rapidly in early 1996, following a prolonged period of weakness in the early 1990s when companies had focused on reducing gearing ratios from the unsustainable levels of the late 1980s (Graph F3). This type of debt has grown at about twice the pace of intermediated credit (at an annual rate of around 20 per cent) over the past year. Since early 1990, non-intermediated debt of the corporate sector has doubled as a ratio to intermediated credit, to almost 9 per cent.

The growth of the corporate debt market has been helped by the reduction in governments' demands on capital markets and by the growing appetite for securities by superannuation funds. It has also been

Graph F3



helped by the fall in inflation, which has led to a sharp fall in capital market interest rates, thereby reducing the relative attractiveness of funding through the banking system. Any long-term tendency for companies to approach capital markets directly should, over time, continue to exert downward pressure on margins on business lending of intermediaries, including banks.

The emergence of the mortgage-backed securities market has also owed importantly to these factors. Over the past year, there has been a sharp rise in issues of debt to finance loans by mortgage managers and by banks which have restructured parts of their housing loan portfolios. New lending for housing originated by mortgage managers has grown in the past year at around $1^1/_2$ times the rate of lending by other financial institutions. ✠