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EIR Economics

Bankers report hyperbolic growth rate of derivatives

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The total amount of derivatives outstanding as of March 31, 1995, was $57.3 trillion, according to a survey released Dec. 18 by the Bank for International Settlements (BIS). The survey, conducted by the central banks and monetary authorities of 26 countries, is estimated to have covered about 90% of intermediaries active in the derivatives markets.

Of the derivatives outstanding, $40.7 trillion, or 71% of the total, were in the over-the-counter market (OTC), about which the BIS admits "only limited data are available." Interest rate derivatives accounted for $26.6 trillion, 65%, of the OTC total, with foreign exchange derivatives accounting for another $13.2 trillion, or 32%. Equity and stock indices derivatives stood at $599 billion, and commodities derivatives accounted for the remaining $317 billion. These figures were adjusted by the BIS to eliminate double-counting.

There were $16.6 trillion in exchange-traded derivatives outstanding on March 31, of which $15.7 trillion, 95%, were interest rate derivatives, while equity and stock indices derivatives totalled $645 billion, commodities derivatives $142 billion, and foreign exchange derivatives $120 billion. The exchange-traded figures were not adjusted for double-counting.

The BIS survey also looked at daily turnovers of derivatives in April 1995. For OTC derivatives, it reported global turnover of $1.2 trillion a day gross, or $839 billion a day after adjusting for double-counting. Turnover was $1.1 trillion a day for exchange-traded derivatives. The survey also found that traditional foreign exchange transactions were $1.2 trillion a day.

While these figures are not directly comparable due to the presence of some double-counting in the exchange-traded derivatives totals, they nevertheless provide an indicator of the hyperbolic growth of financial aggregates, and the speed at which the financial system is racing toward disintegration. One can quibble with the numbers, but the process which the numbers reflect—hyperbolic growth of the financial aggregates compared to monetary aggregates, coupled with the decline of the physical economy—is what defines the crisis; the numbers are merely imperfect reflections of that reality.

Multiplying the adjusted OTC daily turnover of $839 billion by 244, the number of trading days in a year, yields an annual OTC turnover of $205 trillion; doing the same for the unadjusted exchange-traded daily turnover of $1.136 trillion, yields an annual exchange turnover of $277 trillion, for a total annual derivatives turnover of $482 trillion. By the same method, the $1.2 trillion in daily traditional foreign exchange transactions yields an annual turnover of $293 trillion. All together, that comes to $775 trillion a year in combined derivatives and foreign exchange turnover, worldwide.

If one compares the $45 trillion figure in derivatives outstanding on Dec. 31, 1994, by Securities Data, with the $57.3 trillion figure on March 31, 1995, provided by the BIS, one gets a growth of $12.3 trillion, 27%, for the first quarter, which is slightly larger than the $12 trillion in derivatives outstanding at the end of 1992. Again, these numbers may not be directly comparable, but given the spotty reporting, they are the best we have.

That $12.3 trillion growth in the first quarter, projected linearly, would be a $49 trillion growth for the full year, for a total outstanding of $94 trillion at the end of 1995, and an annual turnover approaching $2 quadrillion. *EIR* doubts the derivatives market doubled in 1995, but even if the growth in the last three quarters as a whole merely equalled the apparent first quarter growth, that would be a $25 trillion growth, almost 60%, for the year, to $70 trillion, or about $1.4 quadrillion in annual turnover.

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London dominates

The leader in the global derivatives markets, as one might suspect, is the City of London. Britain had a daily average turnover of $351 billion in OTC derivatives and $247 billion in exchange-traded derivatives, for a daily derivatives total of $598 billion. When one adds in the empire, including the places where the British queen is sovereign (Australia, Canada, and New Zealand, among the countries in the study), and the other Commonwealth countries in the study (Hongkong, Singapore and South Africa), the British Empire total rises to $879 billion in daily derivatives turnover, or 38% of the world total. The empire dominated the OTC market, with 47% of the world total, and had 29% of the exchange-traded market.

By comparison, the United States had $164 billion in OTC turnover and $196 billion in exchange turnover, for a total derivatives turnover of $360 billion a day, or 16% of the global total. Japan had $138 billion in OTC turnover and $451 billion in exchange turnover, for a daily total of $589 billion, or 26% of the world total. The United States had 14% of the OTC market and 17% of the exchange market, while Japan had 12% and 40%, respectively.

The case of France is interesting. The BIS study put the French daily turnover at $146 billion, which appears to conflict with a derivatives survey released in November by the BIS's Basel Committee and the International Organization of Securities Commissions. The Basel Committee survey of 67 commercial banks and 12 securities firms in the Group of 10 countries, found France second only to the United States in derivatives exposure.

The Basel survey showed 20 selected U.S. banks and securities firms to have had $20.3 trillion in derivatives outstanding at the end of 1994, followed by eight French banks with $11.7 trillion; nine Japanese banks and securities firms with $9.9 trillion; eight British banks with $6.7 trillion; and three Swiss banks with $5.3 trillion.

France's Société Générale led the list among individual institutions, with $3.3 trillion in exposure; followed by Chemical Banking with $3.2 trillion; Citicorp with $2.7 trillion; J.P. Morgan with $2.5 trillion; France's Paribas with $2.1 trillion; and Swiss Bank Corp. with $2.0 trillion. By comparison, the seven German banks surveyed had a total exposure of $3.1 trillion, and the five Canadian banks $2.5 trillion.

U.S. exposure rises

The Basel survey put the exposure of 10 U.S. banks at $14.5 trillion at the end of 1994, and put the exposure of 10 securities firms at $5.8 trillion. The leader among the securities firms was Salomon, with $1.5 trillion; followed by Merrill Lynch at $1.2 trillion; Lehman Brothers at $1.1 trillion; Goldman Sachs at $995 billion; and Morgan Stanley at $835 billion. At the end of 1994, according to the Federal Deposit Insurance Corp., the U.S. banking system as a whole had a total of $15.8 trillion in derivatives; by Sept. 30, 1995, that figure had risen $2.5 trillion, or 16%, to $18.2 trillion (the numbers appear not to add up, due to rounding).

The derivatives holdings of the big U.S. banks have all risen during 1995, with one exception. Chemical Banking continued to lead the pack as of Sept. 30, having increased its derivatives portfolio $525 billion, 16%, to $3.7 trillion during 1995. J.P. Morgan was second, with an increase of $919 billion, 37%, to $3.4 trillion. Citicorp was third, increasing just $32 billion to $2.7 trillion; BankAmerica rose 26%, to $1.7 trillion; and Chase Manhattan rose 24%, to $1.5 trillion.

The glaring exception was Bankers Trust, which has been effectively taken over by federal regulators, much as Citicorp was in November 1990. Bankers Trust's derivatives holdings have fallen $117 billion, 6%, since the end of 1994, and $247 billion, 12%, since they peaked at $2.1 trillion on March 31, 1995. At the end of the third quarter, the bank had $1.9 trillion in derivatives.

The takedown of Bankers Trust began in the fall of 1994, with a rash of lawsuits against the bank by customers who had lost money in derivatives deals. Federal regulators began an investigation, and in December 1994, fined the bank $10 million. As part of the settlement with regulators, the bank agreed to implement a series of reforms to be dictated by federally approved outside consultants. The result has been a systematic purge of its top executives, and the winding down of some of the more egregious derivatives deals. The bank still faces a civil racketeering charge, filed in federal court in Cincinnati by Procter & Gamble, one of its derivatives victims.

Bankers Trust is likely being groomed as a merger target, as part of the biggest wave of big-bank mergers since July-August 1991, when 6 of the 12 largest banks in the country were merged. Chemical Banking, which acquired Manufacturers Hanover ($68 billion in assets) in 1991, is now acquiring Chase Manhattan ($120 billion); the resulting bank, which will retain the Chase Manhattan name, will have $308 billion in assets and some $5.2 trillion in derivatives. Detroit's NBD has acquired First Chicago, creating the $124 billion First Chicago NBD Corp., and North Carolina's First Union will swell to $122 billion with the acquisition of New Jersey's First Fidelity. Rhode Island's Fleet Financial is joining the top 10 with the acquisitions of Shawmut and NatWest USA, the U.S. arm of Britain's National Westminster. Other regional mergers include the acquisition by Pittsburgh's PNC of Midlantic; Philadelphia's CoreStates buying Meridian; the Bank of Boston buying Baybanks; and Cleveland's National City buying Integra.

Vultures are also circling Los Angeles-based First Interstate (it had $59 billion in assets in 1989, compared to $55 billion today). San Francisco's Wells Fargo has launched a hostile takeover attempt against First Interstate, which is trying to escape by selling itself to First Bank System of Minneapolis.