ANALYSIS OF RECENT CHANGES IN BANK DEPOSITS IN SPAIN

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Introduction

Bank deposits are the traditional source of funding for commercial banks, whose business is to raise funds from the public and channel them to other sectors (intermediation). Deposits therefore make up a significant part of bank liabilities, particularly in Spain where commercial banking predominates over investment banking.

This traditional business of raising deposits from the public is a retail banking activity (characterised by a large number of relatively small customers) as distinct from wholesale banking where each customer provides a large amount of funds, usually through financial market transactions (securities issuance, interbank funding, etc.). This different customer profile means that the funds raised behave differently and have different characteristics. Thus retail deposits, even if they are short-term or even sight deposits, tend to show highly stable behaviour. This derives, on the one hand, from the aggregation of numerous agents with different liquidity needs and, on the other, from the guarantees provided by third parties (deposit guarantee fund) which do not exist for wholesale deposits.

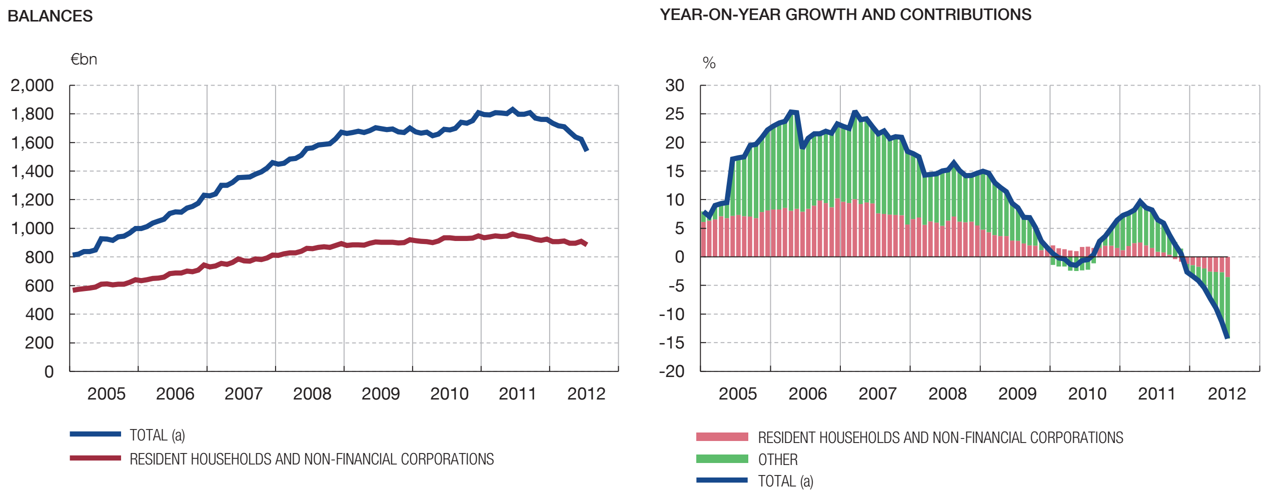
In practice, however, not all bank deposits fit the classical definition of retail liabilities. Interbank deposits are the most obvious example: they are clearly wholesale funding and in crisis situations such as the present one they are significantly more volatile than traditional retail deposits. General government deposits, whose relative weight is comparatively small (1.8 % of total liabilities in July 2012), also have their own specific behaviour, which is generally determined by other factors than those affecting households and non-financial corporations. And even in other deposits, i.e. those classified under the “Other sectors” heading (that is, other than monetary financial institutions and general government), it is necessary to distinguish between the various groups of agents in order to assess their behaviour properly. This is because the “Other sectors” group as defined for statistical analysis purposes is highly heterogeneous, since it includes, apart from households and non-financial corporations, central counterparties, insurance corporations and pension funds, investment funds, financial vehicle corporations (securitisation SPVs), preference share issuers, securities brokers and dealers and other financial intermediaries or auxiliaries.

In Spain there are basically two statistical sources of data on bank deposits: financial statements harmonised at euro area level (EMU returns) which institutions submit regularly to the Banco de España (BE) and supervisory returns. This article analyses the former.[1]

1 The EMU returns data are published in Chapter 8 of the Banco de España’s *Boletín Estadístico* and the supervisory returns data in Chapter 4. The differences between these two chapters are explained in the methodological notes accompanying them. Three differences, however, are particularly noteworthy. First, the sector analysed is slightly different: Chapter 4 focuses on credit institutions, whereas Chapter 8 includes other monetary financial institutions (OMFIs) which include credit institutions and money market funds (MMFs), although the latter represent only 0.2 % of the total balance sheet. Second, the definition of “rest of the world” differs: in Chapter 8 it refers to the world other than the euro area and in Chapter 4 to the world other than Spain. Third, since December 2008 securitisation transactions in which the originator acquires all the securities issued (known as “retained securitisations”) are recorded in Chapter 8 as an addition to deposits and a simultaneous addition to securities on the assets side, whereas in Chapter 4 the two items offset each other and neither deposits nor securities holdings are recorded.

DEPOSITS OF OTHER RESIDENT AND NON-RESIDENT SECTORS WITH SPANISH MONETARY FINANCIAL INSTITUTIONS

CHART 1



SOURCE: Banco de España.

a The series is affected by a statistical change. In June 2005, as the result of a change in the accounting regulations, derecognition of loans transferred to securitisation funds after 31 December 2003 was not allowed if the institutions maintained substantial exposure to risk; instead, these loans had to be recognised on the balance sheet, adding higher deposits with securitisation vehicles as a balancing item on the liabilities side.

The EMU returns show that the total deposits of other resident and non-resident sectors with Spanish monetary financial institutions (MFIs)[2] amounted to €1,540 billion in July 2012, representing 42 % of the total liabilities of these institutions. Chart 1 shows that these deposits grew continuously during the expansionary phase of the Spanish economy and in the early stages of the crisis that erupted in 2007. Only from June 2011 did a decline begin, which seems to have quickened somewhat in recent months. Between June 2011 and July 2012 the decrease was €291 billion (16 %). However, the fall in deposits of households and non-financial corporations resident in Spain (which constitute what are traditionally known as resident retail deposits) was substantially smaller (€76 billion in the same period, or 8 % with respect to the mid-2011 level). The remainder relates to a variety of deposits, most of which are essentially wholesale deposits, on occasions rather unique, and which, accordingly, should be analysed separately.

It is worth mentioning here that the European Central Bank (ECB), within the framework of its “monetary analysis” (the former “Pillar 1” of its monetary strategy), also disseminates on its website an indicator of deposits in Spain and in the other euro area countries. This indicator, which has drawn some attention from analysts and is very similar to that considered here, recorded a balance as at July 2012 of €1,509 billion, with a fall from June 2011 of €233 billion. The differences between the two are basically that the ECB indicator includes only those deposits in which the counterparty is an agent resident in the euro area (instead of those of residents all over the world), and that these deposits also include non-central government deposits, the justification here being that this is the money-holding sector defined in Eurosystem statistics.

The rest of the article is structured as follows: Section 2 analyses the deposits of other resident and non-resident sectors other than Spanish households and non-financial corporations, which are examined in Section 3, and Section 4 summarises the main conclusions drawn.

2 Spanish MFIs also include the Banco de España (BE). However, in this chapter, unless indicated otherwise, the term MFI refers to monetary financial institutions excluding the BE.

DEPOSITS OF OTHER RESIDENT AND NON-RESIDENT SECTORS WITH SPANISH MONETARY FINANCIAL INSTITUTIONS

TABLE 1

€bn

	Balances		Change in balances						
	June 2011	July 2012 (a)	2011 Q3	2011 Q4	2012 Q1	2012 Q2	July 2012	Cumulative June 2011-July 2012 (a)	Cumulative % change on June 2011 balance
TOTAL	**1,831.5**	**1,540.4**	**-23.3**	**-47.8**	**-49.4**	**-87.8**	**-82.7**	**-291.1**	**-15.9**
Households and non-financial corporations resident in Spain	959.8	884.0	-23.2	-12.5	-13.2	-0.8	-26.0	-75.8	-7.9
Households and NPIs	741.1	709.3	-10.0	-4.4	-7.0	-0.2	-10.2	-31.7	-4.3
Non-financial corporations	218.7	174.7	-13.2	-8.1	-6.3	-0.7	-15.8	-44.0	-20.1
Other euro area residents	754.3	598.8	0.4	-23.4	-11.4	-75.9	-45.2	-155.5	-20.6
Households and non-financial corporations resident in other euro area Member States	20.9	11.9	-2.3	-0.7	-1.2	-4.8	0.0	-9.0	-43.3
Non-MFI investment funds, insurance and pension funds	83.2	79.7	-1.6	1.7	5.8	-7.8	-1.6	-3.5	-4.2
Other non-MFI financial institutions resident in Spain	599.9	485.9	-15.2	-9.4	-8.3	-42.1	-39.1	-114.0	-19.0
Asset securitisation vehicles	430.3	355.3	-8.5	-3.8	-15.1	-21.7	-26.0	-75.0	-17.4
Companies issuing preference shares and other financial instruments	107.8	83.6	-1.7	-8.8	-1.6	-12.1	…	-24.2	-22.4
Central counterparties	31.6	27.0	-5.2	1.8	5.3	0.2	-6.8	-4.6	-14.6
Other	30.2	26.3	0.2	1.3	3.1	-8.5	…	-3.9	-12.9
Other non-MFI financial institutions resident in other euro area Member States	50.3	21.3	19.6	-15.1	-7.7	-21.2	-4.5	-28.9	-57.5
Securitisation vehicles	6.1	2.4	1.5	-5.7	0.6	-0.8	0.6	-3.7	-60.8
Central counterparties	28.3	8.5	18.7	-7.0	-9.6	-17.8	-4.0	-19.8	-70.0
Other	15.8	10.4	-0.6	-2.4	1.4	-2.6	-1.2	-5.4	-34.0
Rest of world residents	117.5	57.6	-0.6	-12.0	-24.8	-11.1	-11.5	-59.9	-51.0
Central counterparties	58.8	12.7	2.3	-11.9	-18.4	-8.5	-9.6	-46.1	-78.4
Other	58.7	44.9	-2.9	-0.1	-6.4	-2.5	-1.9	-13.8	-23.5

SOURCE: Banco de España.

a In the case of the resident sectors in Spain (Companies issuing preference shares and other financial instruments and Other), both the cumulative figure and the July balance are as at June, as this information is only available quarterly.

Deposits of the other sectors other than Spanish households and non-financial corporations

Table 1 offers an overview of all other resident and non-resident sector deposits. As can be seen, a large part (43 %) of these deposits does not correspond to Spanish households and non-financial corporations and is shared between a heterogeneous group of agents, headed by financial institutions which accounted for more than 90 % of the outstanding balance as at July 2012. Accordingly, this is essentially wholesale funding. Moreover, a substantial part does not, in effect, reflect a genuine raising of funds by banks. Thus, of the above-mentioned 43 %, deposits of securitisation vehicles, of companies issuing preference shares and other marketable securities and of central counterparties accounted for three quarters of the outstanding balance and for slightly more than 80 % of the decline since June 2011. Both the breakdown and the development of these headings should be analysed in detail.

Deposits of securitisation vehicles are the largest item by far, totalling, in July 2012, €355 billion from entities resident in Spain and a further €2 billion from other euro area countries.

That is, 55 % of all deposits excluding those of Spanish households and non-financial corporations. The importance of this heading is due to the characteristics and legislation applicable to securitisations in Spain. Over time, Spanish institutions have basically performed two kinds of securitisations: of loans and of single-certificate privately-placed covered bonds (“*cédulas hipotecarias singulares*”). In the first case, loans held by the originator are transferred to an external vehicle, which issues notes to investors to obtain funds with which to finance the acquisition. In principle, the institution should not record any change in its liabilities, since the loans sold are simply replaced by the cash received in exchange on the assets side of the balance sheet. However, since June 2005 and where the originator retains a large part of the total risk of the loans transferred (which was the case in a very high percentage of transactions, in order to make the notes issued more attractive to investors), the BE requires, for risk control reasons, that these loans remain on the balance sheet of the originator, even though legally they no longer belong to it, recording as a necessary balancing item on the liabilities side a (fictitious) deposit from the securitisation fund. In the second case, and in order to facilitate the sale of covered bonds issued by small MFIs on the financial markets, these covered bonds, together with those of other institutions, are transferred to an external vehicle which issues new securities to investors. These single-certificate privately-placed covered bonds are recorded as a liability on the balance sheets of the institutions receiving the funds but, despite being marketable securities, are actually classed as deposits, as their sole purpose is to back the notes issued. The strong increase in the deposits of other sectors other than Spanish households and non-financial corporations seen in Chart 1 during the economic boom years is largely due to these two types of transactions and is connected, therefore, with funding obtained on the financial markets rather than through retail deposits. Moreover, it does not necessarily reflect actual deposits.

Furthermore, since mid-2007 the vast majority of new securitisations made by Spanish MFIs were acquired by the originators themselves (in what are known as “retained securitisations”), with a view to increasing the assets available for use in monetary policy transactions with the Eurosystem. In consequence, in this case there was no actual flow of funds and, since the securitised loans remained on the assets side of the balance sheet there was, until December 2008, no account entry as a result of the securitisation. However, in December 2008 a change was made to the euro area statistics, requiring that these transactions be recorded as an increase in deposits (on the liabilities side) and in holdings of securities with securitisation vehicles (on the assets side).

Accordingly, the deposits of securitisation vehicles heading is determined essentially by the outstanding balance of securitisations in Spain.[3] The balance peaked in 2009 and a clear decline set in as from 2011, a process that has quickened considerably since May 2012. This steeper rate of decline is not only due to the low volume of new issues, but primarily to the increase in redemptions, as a result of the early termination of some transactions for reasons of collateral management. As the majority of these redemptions relate to retained securitisations, just as there was no effective flow of funds to the originators when they were issued, nor is there any outflow when they are redeemed. It is estimated that of the fall in deposits of securitisation vehicles of €75 billion between June 2011 and July 2012, retained securitisations account for approximately €60 billion. Regular maturities of securitised assets must also be taken into account, but as they entail a decrease

3 A small percentage (9 % in July 2012) corresponds to pure cash deposits of securitisation vehicles with MFIs, but this component, far from declining, rose by €7 billion between June 2011 and July 2012.

both in liabilities and assets the effect is also offset, generating no additional funding needs for the credit institutions. This figure is rather more difficult to gauge, but bearing in mind that in 2011 total redemptions of securitised assets issued before August 2007 (and, therefore, in the main probably not retained) amounted to €15 billion, it seems it could explain a substantial part of the rest of the decline in these deposits.

The deposits of companies issuing preference shares and other marketable securities are a result of the way in which Spanish institutions use non-banking subsidiaries resident in Spain to issue securities on the financial markets. This is a result of the historical context since, until 2003, for regulatory reasons, transactions of this kind were primarily performed outside Spain. Clearly these transactions are securities-based funding, even though the funds obtained on the markets reach the MFIs' balance sheets in the form of deposits from these specialist subsidiaries. As at June 2012 (the latest data available) these deposits amounted to €84 billion, that is, 12 % of all deposits of the other sectors excluding Spanish households and non-financial corporations. This is a drop of €24 billion with respect to 12 months earlier, essentially as a result of the early redemptions made by Spanish credit institutions, especially of preference shares.

Lastly, the deposits of central counterparties (CCPs), resident in Spain and abroad, amounted to €48 billion (7 % of the total) as at July 2012, having more than halved (falling by 59 %) since June 2011. These deposits are repurchase agreements, generally involving two banking counterparties operating through the CCPs, to facilitate the transaction due to the reduced counterparty risk. Changes in deposits from Spanish CCPs are normally offset by similar movements on the assets side, as in the main it is the Spanish MFIs that operate through these counterparties, meaning that there are no net funding needs for the system as a whole. Positions with non-residents began to grow notably in mid-2010, in light of the difficulties Spanish MFIs had in obtaining funding through bilateral repos due to the double default risk.[4] Liabilities with these non-resident CCPs rose from virtually zero to a peak of some €100 billion in autumn 2011. Subsequently, ongoing transactions have gradually been redeemed or not renewed as greater recourse has been had to Eurosystem funding. In the period analysed here (June 2011 to July 2012), these positions with non-residents fell by €66 billion, of which €25 billion are due to the reclassification of some deposits as MFI deposits in May 2012, as they corresponded to CCPs that are also MFIs. This entailed a simultaneous increase in deposits with MFIs and, in consequence, generated no additional funding needs.

Overall, these three types of deposits, which are very different from "genuine" retail banking deposits, account for at least €173 billion[5] of the total decline of €215 billion excluding Spanish households and non-financial corporations. As is explained above, much of this decrease does not correspond to an effective decline in the resources available to Spanish MFIs.

Deposits of Spanish households and non-financial corporations

Deposits of Spanish households and non-financial corporations held with Spanish MFIs amounted, as at July 2012, to €884 billion (57 % of the "other sectors" total), the majority corresponding to households. Recently, these deposits have shown increasingly

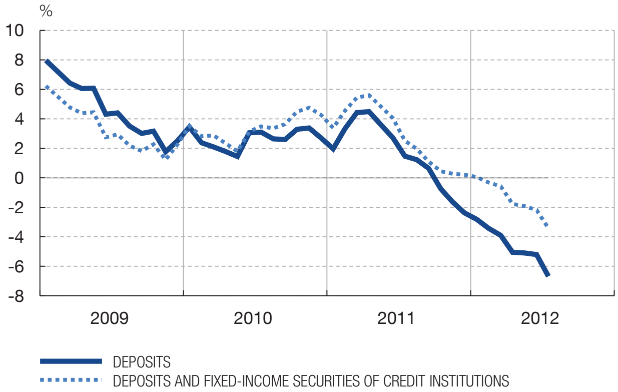
4 The risk that the issuer of the collateral (generally the Spanish State) and the institution (MFI) supplying it to obtain the funding will both default on their payments simultaneously, rendering the collateral unenforceable.

5 The July data for deposits of companies issuing preference shares and other marketable securities are not yet available, as the information is only quarterly. Nevertheless, there are data showing that the outstanding balance of the securities issued by these companies fell again in July, so the figure will most likely be somewhat higher.

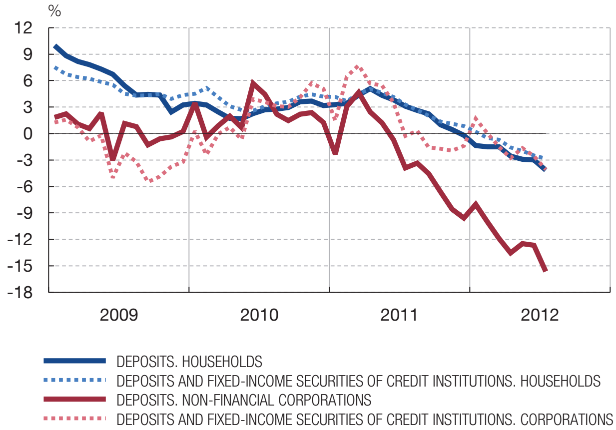
DEPOSITS AND FIXED-INCOME SECURITIES OF CREDIT INSTITUTIONS HELD BY RESIDENT HOUSEHOLDS AND NON-FINANCIAL CORPORATIONS

CHART 2

HOUSEHOLDS AND CORPORATIONS (TOTAL)
Year-on-year growth



HOUSEHOLDS AND CORPORATIONS (SECTORAL BREAKDOWN)
Year-on-year growth



SOURCE: Banco de España.

pronounced rates of decline (see Chart 2), although less so for households (-4.2 % year-on-year as at July 2012) than for corporations (-15.6 %). There are several factors behind these developments.

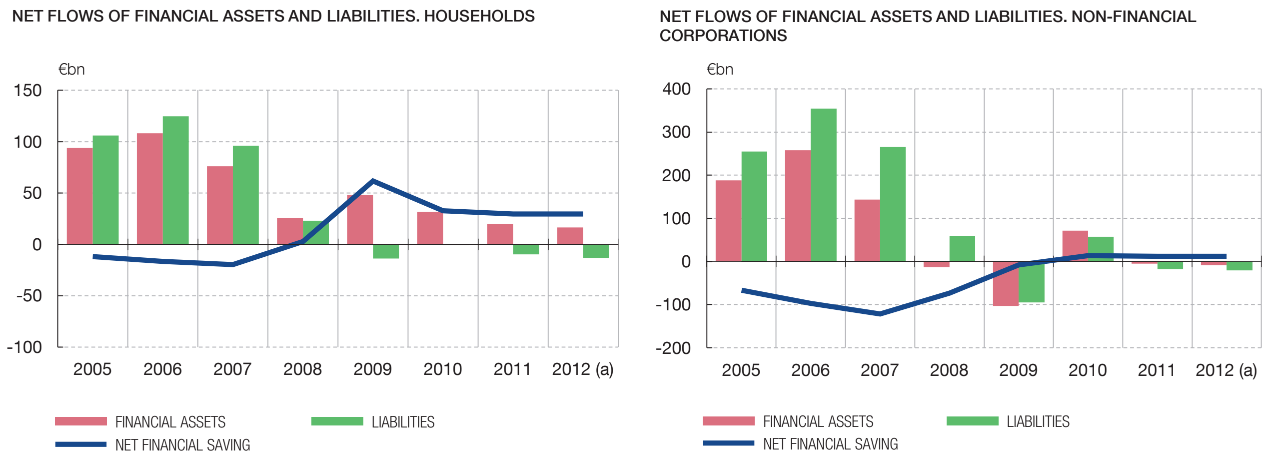
First, sluggish income growth, high unemployment and the need to reduce high debt levels make it particularly difficult for these agents to grow their financial assets. As both panels of Chart 3 show, during the economic boom years corporations and households increased their holdings of financial instruments significantly, in a setting in which easy borrowing conditions triggered strong credit growth. The funds obtained allowed them not only to spend beyond their income (reflected in negative net financial saving), but also to significantly grow their financial assets, including deposits. With the onset of the crisis, the supply of funds declined and lending conditions tightened, prompting progressively lower and eventually negative growth rates in loans. As a result of this credit squeeze, the rate of growth of financial assets has declined, although net financial saving of Spanish households and non-financial corporations has moved into positive territory. In turn, the deleveraging process in which these agents are currently immersed signifies not only that they are less able to accumulate assets, but also, in some cases, that they will need to use part of those assets to pay off their debts, which is another factor that is taking its toll on bank deposits.

Nevertheless, the change in households' financial assets in the last four quarters up to 2012 Q1 (the last quarter for which there are Financial Accounts data available) remained positive, and in the case of corporations it was only marginally negative. The decline in bank deposits cannot, therefore, be attributed only to the factors described above.

There is a second phenomenon that has emerged in recent months and that also helps explain the performance of deposits of Spanish households and corporations, namely portfolio adjustments out of bank deposits into other instruments (see the left-hand panel of Chart 4), most notably fixed-income securities issued by the MFIs themselves. This shift, which is particularly pronounced in the case of corporations, was encouraged by the regulatory changes introduced in 2011. Thus, in July of that year, contributions to the Deposit Guarantee Fund (DGF) were increased for institutions arranging new deposits with

FINANCIAL ASSETS AND LIABILITIES OF RESIDENT HOUSEHOLDS AND NON-FINANCIAL CORPORATIONS

CHART 3



SOURCE: Banco de España.

a Cumulative four-quarter data up to 2012 Q1.

interest rates higher (by a certain amount) than the reference rates set. A few months later, in December, overall contributions to the DGF were raised. This effect will foreseeably tend to reverse in coming months, since Royal Decree-Law 24/2012 of 31 August 2012 removed the penalisation on high interest rate deposits.

The left-hand panel of Chart 4 also shows that, on Balance of Payments data, there has likewise been a certain shift towards deposits abroad, although in moderate amounts, as well as a (considerably less pronounced) shift towards public debt securities.

Given that part of the shift out of deposits has been into fixed-income securities issued by banks, the sum of both these headings would be a better gauge of how the funds raised by MFIs from households and corporations have evolved. As Chart 2 shows, this exercise results, as at July 2012, in a significantly slower year-on-year rate of decline in liabilities obtained from households and corporations, from 4.2 % to 2.9 % in the case of households, from 15.6 % to 4.1 % in the case of corporations, and from 6.7 % to 3.4 % overall. All the same, there is still a decline in the funds held with MFIs. However, taking into account all the flows of funds, that is, both financial assets and liabilities, it is clear, as the right-hand panel of Chart 4 shows, that in net terms Spanish households and corporations have continued to place funds with MFIs since 2009, in contrast to the pattern seen during the economic upturn.

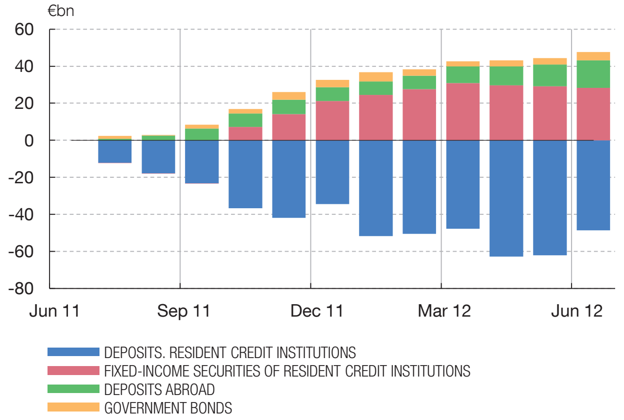
Conclusions

Bank deposits in Spain include a highly heterogeneous range of deposits and counterparties. In particular, financial intermediaries account for a very large part of the total balance, and in recent years their behaviour essentially determines that of deposits overall. Accordingly, a study of retail funds raised by Spanish MFIs cannot be based on the analysis of headings such as the deposits of the "Other sectors" (i.e. other than MFIs and general government) or on the indicator published by the ECB in the framework of its monetary analysis. Moreover, the analysis must also include information on the holdings of securities other than shares issued by the banks. This is particularly necessary at the present time, due to the recent change in the way in which credit institutions market these instruments with respect to their widespread placement with retail customers. Adjusted for that effect, deposits of corporations and households have recently declined at a moderate but

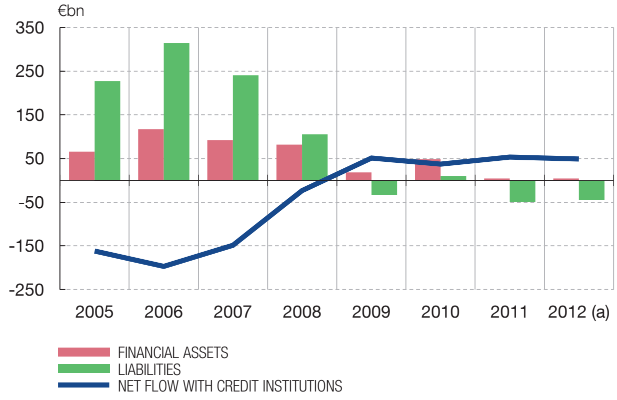
FINANCIAL ASSETS OF RESIDENT HOUSEHOLDS AND NON-FINANCIAL CORPORATIONS

CHART 4

ASSETS. HOUSEHOLDS AND NON-FINANCIAL CORPORATIONS
Cumulative change since June 2011



NET FLOWS OF FINANCIAL ASSETS AND LIABILITIES WITH CREDIT INSTITUTIONS. HOUSEHOLDS AND NON-FINANCIAL CORPORATIONS



SOURCE: Banco de España.

a Cumulative four-quarter data up to 2012 Q1.

increasingly pronounced rate, essentially as a result of the deleveraging process, falling income levels and the credit squeeze facing these agents in Spain.

The other deposits included in the “Other sectors” heading are essentially wholesale deposits, linked in the main to interbank and securities market transactions, and recently they have fallen more sharply. However, a very significant part of this decline is due to adjustments primarily of an accounting nature that have no real net effect on the funding needs of MFIs.

14.9.2012.