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Talking point

European banks retreating from the US

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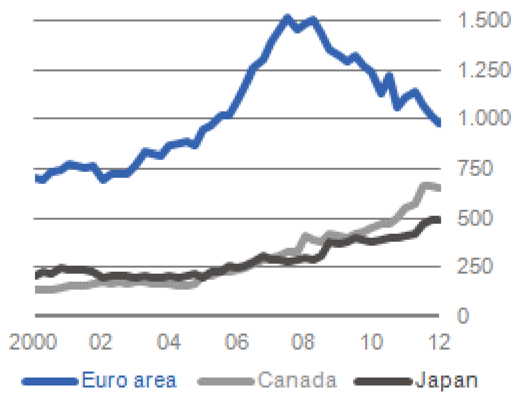
Since the outbreak of the financial crisis in 2007, euro-area banks have been gradually cutting back their exposure to the US market, thereby making room for others to step in. Especially financial institutions from Canada, Japan and certain emerging countries have expanded their US business significantly.

Prior to the financial crisis, Europe's banks steadily expanded their presence in the US. Assets held by euro-area banks peaked in September 2007 at more than USD 1.5 tr – equivalent to 50% of all foreign bank assets in the US. Since then, this share has plummeted to 30% (USD 973 bn). German banks cut their US assets to USD 267 bn – the lowest level since December 2004. With a reduction of almost 70% compared to pre-crisis levels, Dutch banks similarly slashed their US activity. Banks from Belgium and Ireland left the US market almost entirely. Contrary to the general downward trend in Europe, Spain and France managed to expand their US business until the end of 2008, with France replacing Germany as the largest euro-area holder of US assets. However, after considerable volatility in 2009 and 2010, US assets of French banks have also declined lately.

Euro-area banks in reverse gear

Foreign bank assets in the US in USD bn



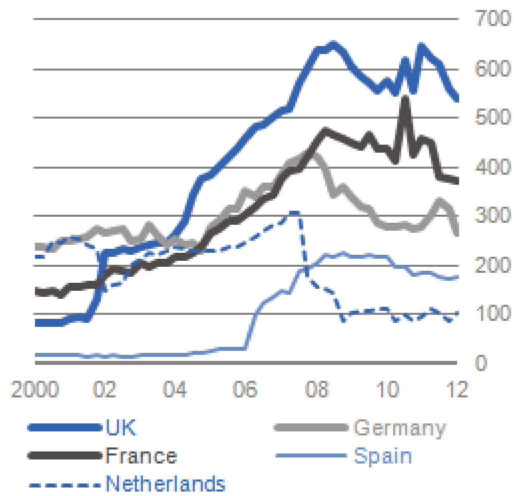
Sources: Fed, DB Research

The reduced presence of euro-area banks is hardly surprising as the entire European banking market is under substantial pressure to deleverage and refocus on domestic markets. Among German financial institutions, Landesbanks were particularly eager to shrink their US activity following government bailouts during the crisis. As a result, German bank assets in the US are now concentrated at very few institutions. Similarly, banks from Belgium, Ireland and the Netherlands were hit hard by the financial crisis, which may explain their drastic retreat from the US market. With USD funding conditions remaining tight for most European financial institutions, a further pull-back seems highly likely in the near future (EU banks are also reducing their Asian exposure for the same reasons).

While euro-area banks turned their focus back to their national markets, Canadian and Japanese banks seized the opportunity and significantly increased their US presence. With assets now totalling USD 655 bn, Canadian banks have more than doubled their pre-crisis US business volume. Japanese banks have similarly increased their total US assets to USD 487 bn. Taken together, banks from both countries now own more US assets than all euro-area institutions combined. This surge in Canadian and Japanese activity can be attributed to their historically close links with the US and the relatively modest impact of the financial crisis on both countries' financial systems. In addition to Canadian and Japanese banks, institutions from Brazil, India and China have made successful inroads into the US market, too. Even though their market shares are still very limited, the pace at which they have been catching up is remarkable (the three countries' combined US bank assets rose not less than nine-fold over the past five years). Indeed, in light of the US recovery and large emerging market banks' growing efforts to diversify internationally, it is hard to see this trend changing anytime soon.

German banks losing ground

Top 5 EU countries, total US assets in USD bn



Sources: Fed, DB Research

In spite of all these changes, foreign banks' total share in the US market has been surprisingly stable. Since 2007, it has been hovering around 23% and today stands at 23.5%. This relatively high proportion, in an international comparison, may be attributable mainly to the attractiveness as well as openness of the US market, and is particularly impressive considering its large absolute size. In Germany, on a contrasting note, foreign banks' combined market share adds up to only 11% – in spite of the single European market for financial services and the common currency.

Overall, however, the robustness of foreign banks' significant share in the US is likely to be tested now as domestic institutions are also preparing to fill the gap left by euro-area banks. In contrast to their European peers, most US banks have returned to strong profitability levels and started to expand lending volumes again. Organically or via US portfolio acquisitions, domestic US banks may thus also gain business at the expense of troubled European competitors in the next few years.

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