Financial Crises and the Presence of Foreign Banks

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Chapter 7
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Introduction
Foreign banks have entered many transition and emerging economies in recent years, sometimes before economic and banking crises have developed, and often after. Today, in a number of countries foreign banks own as much as 90 per cent or more of the banking systems’ assets. The question then naturally arises as to what the effect of the foreign presence is on crises, especially on preventing or ameliorating them, in addition to their possible role in the restructuring phase already flagged in Chapter 2 of this volume.

This chapter first discusses the motives, modes and regulation of foreign banks. In analyzing foreign entry, it is important to distinguish between classic or traditional foreign banks and the innovators, which in turn one can classify either as “bettors”, “prospectors” or “restructurers”. Innovators enter in response to the opportunities that crises create, but this chapter argues that their entry and the reforms that accompany it erode the very conditions that drew the banks. In the long-run then, it may well be that the relative and possibly even absolute importance of foreign-owned banks in host-country banking systems may shrink. A further distinction is in the mode of entry, as between affiliate, branch and subsidiary, a choice that is largely based on the foreigners’ motive for entry.

Section 2 observes that foreign banks have in most cases not played an important role in the emergence of crises, primarily because they did not have a significant presence
before the crisis began. Lastly, however, Section 3 argues that foreign banks can help in the aftermath of a crisis by acting as microeconomic rehabilitators of failed banks and as instruments of system wide reform.

1. Foreign Direct Investment in Banking in Developing Economies

To provide some background to the discussion of the role of foreign banks in financial crises, this section deals with motives, modes and regulation. Motives are the strategies of the foreign banks that bring them to the host countries. Modes deals with the legal form of the banks’ presence. Lastly, regulation is critical to understanding the scope of activities in which foreign banks may engage.

1.1 Motives

One can broadly classify foreign banks into two categories based on their strategies in the host countries: the traditionals and the innovators. The traditionals consist of those many foreign banks, especially those operating via a branch or a small, wholly-owned subsidiary in a national financial center, that are mainly engaging in classic international banking. These banks process trade payments, finance trade, trade foreign exchange, and lend to corporations, both to their home country clients operating in the host country and to host country firms that require an alternative to the services that local banks can offer. The traditionals do not seek to engage in retail banking, with the limited exception of ethnic banks, that is, banks that have come to serve the needs of recent or perhaps even long-established emigrants from the home country resident in the host country.

Deregulation, transition and crisis have created opportunities for the second group, the innovators. The innovators are innovative in two non-exclusive ways:
frequently their responses to the new opportunities represent behaviors that are new to the banks themselves, and their responses are to bring governance, methods, and products that are new (or at least scarce) in the markets that they enter. They also bring capital, but this is in many ways their least important function. The innovators come in three varieties: the bettors, the prospectors, and the restructurers.

The bettors include everything from various quangos (quasi-autonomous, non-governmental organizations) and development banks to banks, investment or private equity firms and individuals betting on the post-deregulation environment or on the success of transition. Some examples would include the International Finance Corporation, the Deutsche Entwicklungsgesellschaft, and the European Bank for Reconstruction and Development. The bettors’ involvement is heavily financial. Through their activities they acquire a portfolio of investments. They hope to create the bulk of the value to themselves through having made good bets on the capabilities of the institutions and the management teams in which they invest. In time, one can expect them to exit due either to the success or to the failure of their investments. In the meantime, they may perform a screening and signaling function. Their involvement as major investors (10-40 per cent share positions) gives the banks in which they invest some legitimacy in an environment where there may be numerous new and reorganizing local banks.

What distinguishes the bettors from the prospectors and the restructurers is that the bettors do not actually manage the banks in which they invest. The bettors’ governance role is frequently a negative one – they impede malfeasance. Their presence therefore is a signal of probity but because they do not manage their investment, less so
one of competence. The bettors invest together with a strategic investor that has the
largest and often a majority stake. A strategic investor is a firm, usually operating in the
same or a similar field, which takes a controlling equity stake. The strategic investors
acquire their targets and manage them. These strategic investors do expect to earn a
return on risk capital, but more importantly they also expect to earn a return on the
management skills, systems and experience that they bring to bear.

The structure of strategic investor supported by bettors is similar in practice if not
in legal form to the Commandite of the pre-Great Depression world. The strategic
investor is analogous to the general partner in a Commanditte and the bettors are
analogous to the limited partners. Strategic investors may be domestic or foreign, and the
foreigners in turn may be prospectors or restructurers.

The prospectors are foreign banks that perceive the existence of a possible
opportunity in the unsettled situation following opening, crisis or deregulation. The
prospectors typically have no particular experience with the host country or clients there.
The prospectors simply are willing, often for idiosyncratic reasons, to engage in
exploratory forays. What distinguishes prospectors from restructurers (see below) is that
the prospectors’ engagement is exploratory rather than part of a broader strategy.

The prospectors establish small subsidiaries or joint ventures, or take large equity
positions in local banks that are small relative to the foreign bank. If the foray shows
promise they are willing to expand further. If it does not, they cut their losses, generally
by selling out to local or other foreign banks. The metaphor here is the gold mine model
of Moffett et al. (1989). The prospector sinks an exploratory shaft in a promising
location. If he does not strike gold-bearing ore, the prospector moves on. If he does
strike gold the mine then follows the ore vein, wherever it leads. One illustrative example is Allied Irish Banks (AIB) and its investments in Poland and Singapore (Table 1a). A more complex example involving several prospectors is Prager Handelsbank (Table 1b).

Many prospectors establish de novo ventures because they have very focused strategies. Examples would include Porsche Bank and Opel Bank in Hungary, both of which specialize in consumer finance, especially the purchase of their owners’ cars. The evidence in Majnoni et al. (2003) for Hungary suggests that greenfield operations achieve higher profitability than restructured ones due to the introduction of new financial products.

The last category is that of the restructurers. These acquire a large bank in a privatization or a rescue and proceed to attempt to fix it. The investment is not a trial foray but rather a large-scale commitment. Frequently, it is part of a program of similar investments. Banks such as Unicredito (Italy), Erste Bank (Austria), KBC (Belgium), Société Générale (France), and others have acquired banks throughout the transition economies. As one can see from Table 2, these restructurers have acquired banks in four or more countries. From the names of the local banks alone one can infer that these are recent acquisitions. (The names differ from country to country and the parent has not yet rebranded the subsidiaries with a common identity.) Also, in the Czech Republic and Slovakia all four compete with each other; in other countries, though only one to three of these banks is present, other foreign banks are also present. The presence of several foreign banks from different countries brings a rivalry to the market for bank services.
Although the identities of the restructurers may change, one can find similar patterns in other regions of the world. Nordic banks have been active in the Baltic. Greek banks such as National Bank of Greece, Commercial Bank of Greece and Alpha Bank have been equally acquisitive in the Balkans-Black Sea region. Somewhat similarly, banks such as Santander and BBVA (Spain) and HSBC (UK) have acquired banks throughout Latin America (Guillén and Tschoegl 2000).

Although some prospectors and restructurers may hope to sell out within the medium term (say 3-7 years), most view their engagement as open-ended. At entry they have no exit plan but instead anticipate retaining ownership into the indefinite future, subject of course to profitability. However, in time one can expect that most will sell their operations to local banks as the evolution of the host markets erodes their comparative advantage vis-à-vis their local competitors.

The basis for the argument for the long-run return of the financial systems to predominantly domestic control is the metaphor of ecological succession (Koford and Tschoegl 2002). Ecological succession is a dynamic model that posits that the first plants to arrive in disturbed or clear soil stabilize the soil and change light conditions, creating opportunities for successor species. This in turn provides opportunities for yet other species. The mix of plant and animal species continues to evolve until the system reaches the final steady state of a climax forest. Of course, when fire, flood or landslide clears a patch in the forest, the process starts again in that patch. During the process one must be careful not to assume that the current situation is in equilibrium. One should not mistake a current phase, especially not an early one, for the ultimate steady state.
The foreign banks are the fast growing plants that are the first responders to the new opportunity given by the disturbed, hospitable soil that crises or transition have created. This does not mean that all foreign banks are innovators; some international banks will remain with traditional international banking. It just means that among the foreign banks there are those that will respond quickly and in ways that take them beyond traditional international banking. They can respond quickly because they are well-capitalized, efficient, and have surplus managerial resources (Kindleberger 1969 and Tschoegl 2004).

In all this, it is important to remember that the ecological succession metaphor concerns itself with the evolution of a system after a disturbance. It is not designed to deal with steady states. It is not a model for the role of foreign banks in mature, stable markets, though as Norway shows (Engwall et al. 2001 and Tschoegl 2002a), even in mature markets it has applicability in crises. For a discussion of the role of foreign banks in a large, competitive market such as the U.S., see Tschoegl (2001).

We can think of the share of banking system assets in foreign banks relative to total banking system assets as the proportion of the system’s biomass accounted for by the fast responding plants. One feature of the ecological succession process is that there is both a numerator and a denominator effect. The behavior of the foreign banks themselves has a large effect on the numerator. Over the long term the response of the domestically owned banks will have a large effect on the denominator.

As the foreign banks enter, especially when they acquire host country banks in privatizations, rescues and repairs, the numerator grows more rapidly than the denominator. What draws the foreign banks is the opportunities the situations present,
now that the banks are able or even encouraged to enter. Weill (2003) found that in the Czech Republic and Poland, foreign-owned banks were more efficient than domestic-owned banks but that this was not due to scale differences or the structure of activities. Demirgüç-Kunt and Huizinga (1999) and Claessens et al. (2001) found that foreign banks tended to have higher margins and profits than domestic banks in developing countries, but that the opposite held in industrial countries. Similarly, Dopico and Wilcox (2002) found that foreign banks were more pervasive in countries where banking was more profitable and where the banking sector was smaller relative to GDP. Conversely, foreign banks had a smaller presence in mature, competitive markets.

Although markets that are growing, underbanked or uncompetitive draw foreign banks, by their entry the foreign banks change the environment. The literature on the effect of foreign banks on host country banking systems, especially margins, suggests that the effect is precisely to undermine the conditions associated with the presence of foreign banks. For instance, Lensink and Hermes (2003) found that foreign entry is associated with shrinking margins in developing countries, but not necessarily in developed countries. For the Philippines, Unite and Sullivan (2003) found that foreign competition compelled domestic banks to be more efficient, to focus operations, and to become less dependent on relationship-based banking practices.

This means that over time, measured in decades, the foreign banks will find that the conditions that drew them have eroded, and some will withdraw, selling their subsidiaries to locally-owned banks. When one examines histories of particular banks or of banking systems in particular countries, one can rapidly identify a number of mechanisms that operate to reduce the foreign presence. Some foreign banks sell out
because they find they are not competitive. Others sell because their parent is in
difficulty at home and sells the foreign operation in order to raise funds. Yet others sell
out to local investors and banks when host country markets are depressed and the foreign
owners see little benefit from staying. Lastly, some simply sell out to local banks
growing by acquisition.

For instance, in 1999 Sumitomo Bank sold the subsidiary it had established in
California in 1952 to Zions Bancorp, which was expanding into California. Of course,
sometimes the exiting bank will sell to another foreign bank. Thus UFJ Holdings (the
company created in Japan to merge Sanwa Bank, Tokai Bank and Toyo Trust) announced
the sale of United California Bank to BancWest, a subsidiary of Banque Nationale de
Paris Paribas, which had entered in 1970. Sanwa had established its subsidiary in 1972
and Tokai in 1974. In both the Sumitomo and Sanwa-Tokai cases the parents sold not
because of difficulties with their California operations but rather because of difficulties at
home. Of the eight subsidiaries that Japanese banks established in California between
1952 and 1978, three remain, the rest having disappeared through merger into the
survivors or sale; assets in California subsidiaries of Japanese banks peaked in the early
1990s and has fallen since though the largest subsidiary, Bank of Tokyo-Mitsubishi’s
Union Bank of California continues to grow (Tschoegl 2003).

Similarly, in 2003 Banco Bilbao Vizcaya Argentaria sold its Brazilian operations
to Bradesco. BBVA had bought Banco Excel-Economico in 1998 for 1 real. BBVA sold
because it realized that it would be too expensive to achieve a profitable scale. As part of
the sale price BBVA took a small equity stake in Bradesco, thus converting its strategy
for Brazil from that of a restructurer to that of a bettor. In 2003, Lloyds TSB sold its
Brazilian operations to HSBC (Hongkong and Shanghai Bank Corporation). HSBC had entered in 1997 and the purchase of Lloyds is its third in Brazil. Lloyds’ association with Brazil dated back to ancestors of the Bank of London and South America (BOLSA), which in 1863 and 1864 were the first banks in Brazil. However, Lloyds management has decided to focus on its operations in the UK; for example it agreed in October 2003 to sell National Bank of New Zealand, with which it has been associated since the 1870s, to ANZ Bank.

To this point the discussion has focused on the numerator of the ratio of assets in foreign-owned banks to total assets in the banking system. There is, however, a denominator effect as well. The argument here comes from Huang and Di (2003). They point out that the conditions that constrain foreign firms may also constrain host country firms. If, as we have argued above, the conditions constrain host country firms more than they do foreign firms, the foreign firms may increase their ownership of assets in the host country. However, the liberalization and regulatory reform that accompanied the entry of the foreign firms benefits the domestic firms as well. It will take time for them to overcome their administrative heritage from the previous conditions but once they do, one can expect them to grow rapidly. The result will be an increase in the numerator, and a decline in the ratio, even without denominator effects.

Foreign banks have not displayed any long-term comparative advantage in retail banking vis-à-vis host country banks, especially in reaching rural areas and the unbanked. This means that local banks will have more scope to continue to dominate retail banking, as long as they can retain or achieve absolute cost and efficiency advantage as well as comparative advantage. As the local banks improve their efficiency, foreign banks will
increasingly specialize once more in international activities, even if they do not immediately exit retail banking. Still, it is not unusual to see a foreign bank sell its retail activities to a local bank while it retains a branch in the national financial capital to enable it to continue to offer corporate and wholesale banking services.

Saying that over time one should expect to see foreign banks exiting retail banking abroad does not mean that all foreign banks will do so. Currently, HSBC is striving to become, in the words of its slogan, “the world’s local bank” (Tschoegl 2003). Some particularly capable foreign banks may retain a presence for a long time. However, one must keep in mind too that over time management changes and HSBC’s push in North America is only about 20 years old, while that in Latin America is about five.

It can be argued that increasing globalization makes the metaphor of ecological succession suspect. However, Goldsmith (1969, 360-367), referring to the 19\textsuperscript{th} and early 20\textsuperscript{th} Centuries, the first era of globalization, noted that outside of Europe and North America the development of financial systems was widely based on foreign banks but that over time the foreign banks had lost their predominance as local banks arose and waxed. Goldsmith does not go into detail; his focus was on macroeconomics. Triner’s (1996 and 2002) description of the development of banking in Brazil, especially after the reforms of 1905, shows a pattern consistent with the ecological succession metaphor. Koford and Tschoegl (2002) apply the metaphor to the history of foreign banks in Bulgaria since the late 19\textsuperscript{th} Century. Tschoegl’s earlier papers on the foreign bank presence in Japan (Tschoegl 1988) and Saudi Arabia (Tschoegl 2002c) and Phylatkis’ (1988) paper on the eclipsing of British banks in Cyprus before independence, also offer evidence for the applicability of the metaphor in that era.
1.2 Modes

The three most common forms of legal presence are branches, affiliates, and subsidiaries, though their availability to foreign banks varies by country. That is, some countries permit foreign banks to operate via a branch but not a subsidiary, or vice-versa. Legal form is not an arbitrary formality but can be intimately tied to both the banks’ strategies and to the regulatory environment. The distinction between the three is not a matter of arcane legal minutiae but rather can be of substantive importance, especially in crises.

A branch is an integral part of the parent. A branch may make loans or take deposits; generally it may provide a full range of banking services. Banks prefer to use foreign branches for wholesale and corporate banking activities in host countries, including foreign exchange and money market trading. The reason is that a branch generally lends, borrows and trades on the basis of its parent’s full capital base. Thus the branch can lend more to any one borrower than could a similar sized subsidiary (see below) and, in borrowing and trading, the branch shares the parent’s credit rating. Because it is part of the parent bank, a branch requires careful supervision as mistakes at a branch could bankrupt the parent. However, what facilitates supervision is that branches’ activities such as trading and lending to local subsidiaries of home country firms are ones that the bank must necessarily manage centrally.

An affiliate or associate is an independent legal entity (i.e., locally incorporated) in which the foreign bank has less than majority ownership. Generally, foreign banks prefer not to put their name on affiliates as that would suggest full responsibility for an entity over which they do not exercise full control. Furthermore, if through a combination of share ownership and management contract the foreign bank does exercise
control, then it will wish eventually to assume full control to capture more of the return from its management without having to dispute transfer pricing decisions with minority shareholders.

A subsidiary, like an affiliate, is a separate legal entity incorporated in the host country, but one in which the foreign parent has majority ownership. A subsidiary may fail even though the parent is solvent. Conversely, a subsidiary may be solvent even though the parent has failed. The subsidiary lends based on its own capitalization rather than that of the parent, something that can prove to be a major constraint. Certainly, a subsidiary can refer to its parent a loan that exceeds its allowable lending limits but, in that case, the bank could lend from its branch in the first place. Thus, many banks conclude that a subsidiary provides a relatively poor platform from which to conduct corporate lending or trading activities (Heinkel and Levi 1992).

Generally, a branch costs less to establish than a subsidiary. There are no costs of incorporation, no need to report annually or quarterly to local registrars of companies, no need for a board of directors, and so forth. However, when a bank has sufficient assets at risk where the risk is location-specific there may come a time when it becomes sensible to incorporate locally.

Du (2003) has pointed out that multinational companies may borrow from local banks to enlist the services of those banks as monitors of the local operation. The local bank, as local creditor with often first rights to any assets in bankruptcy, has an incentive to intervene quickly if it senses problems. Similarly, a foreign bank with a number of branches in a country thousands of miles from home, branches whose profitability depends on a local economy about which the parent knows little, may decide to
incorporate locally to enlist the governance services of the local central bank, and local depositors when there is no deposit insurance. These parties are more likely to sense and react to some problems of which headquarters, dependent on reports from its managers, might be unaware. Thus, when the assets at stake are large enough and the local regulatory authorities are capable, the foreign parent may decide that the costs of incorporation are an acceptable cost for assistance with governance.

As the US deregulated banking, many multi-bank holding companies merged their subsidiaries, converting their offices into direct branches of the parent (Wheelock and Wilson 2002). The argument above suggests one reason they could do so was because all were already subject to oversight by the Federal Reserve and Federal Deposit Insurance Corporation; amalgamating did not imply any loss of a local regulator. By contrast, the little cross-border acquisition activity within the EU has led to little or no amalgamation (and has been limited primarily to the Nordic countries).

Interestingly, looking at the U.S. as a host-country, the ten banks that control the 12 largest subsidiaries of foreign banks (accounting for about 90 per cent of the assets in U.S. subsidiaries of foreign banks) continue to choose the subsidiary form rather than branches of the parent (Tschoegl 2002b). The parent banks involved do have branches, but these are in financial centers and engage in wholesale and corporate banking. They are not retail banking operations (Tschoegl 2001). HSBC Canada, the largest foreign bank and the seventh largest bank in Canada, continues to operate via a subsidiary even though it now has the option to adopt the branch form, and even though several foreign banks with only one office in Toronto switched when the option became available in 1999.
It is important to emphasize that this argument for incorporation has nothing to do with taxes. While tax conditions can be relevant, a subsidiary, especially one that the parent does not own outright, tends to have much less flexibility in its tax management than a branch. When one observes a parent maintaining, say in the US, both a branch for corporate and wholesale banking and a subsidiary for retail banking, this argues that taxes are not the issue and that the branch’s lack of local limited liability is important for trading.

The choice between operating via a branch or via a subsidiary also may have little to do with the value of the option to abandon implicit in limited liability (see below). Incorporation as a device for enlisting the governance assistance of host country regulators is a much more promising explanation.

Regulators in the home and host country frequently try to retain the advantage to them of one form or the other. Thus regulators in the home country may attempt to “ring fence” the parent’s assets to insulate them from developments in bank’s branches abroad. At the same time regulators in the host country may require a branch to allocate a certain amount of capital to the branch to protect local depositors in the event the parent fails. Local regulators may also require a parent bank to issue a “comfort letter” pledging support to a subsidiary. Still, as we discuss in the next section, regulators monitor and regulate branches differently from subsidiaries.

The issue of the choice between branch and subsidiary can have implications for the role of foreign banks in a crisis. In a crisis, local depositors frequently engage in a “flight to quality”. That is, they withdraw their funds from domestic banks in which they have lost confidence and redeposit the funds in less risky banks. Often these are
government-owned banks, but also often these are foreign banks. Depositors will find
the branches of a foreign bank, especially one from a country with good regulatory
supervision, particularly attractive. Branches cannot fail unless the parent fails, and the
probability of the parent failing generally does not depend highly on conditions in the
host economy. Also, most parents of foreign branches are large relative to the size of the
branch. Still, although shifting deposits to branches of foreign banks may be a sensible
strategy, it is usually of limited use to most citizens because of the paucity of accessible
offices. Most foreign banks maintain only one location, which they have placed in the
host country’s financial center. Obviously the option is of some use to corporations.
Subsidiaries and affiliates may also benefit from a flight to quality, but if so, this will
depend more on the quality of the management of the bank than on the bank’s legal
status. Both subsidiaries and affiliates are host country legal persons and their
performance is heavily bound up with domestic politics and economics. A subsidiary
may benefit from the perception that the parent will stand behind it to protect the parent’s
name and reputation. Obviously, this perception will be much weaker in the case of an
affiliate, especially one that has not advertised its links to the foreign parent. In either
case, the expectation of parental support is a bet and not a consequence of legal form as is
the case with branches. For the parent, the existence of limited liability is an option to
abandon with the strike price being the loss of reputation if it walks away. However, the
strike price is stochastic in that it depends on the reason behind the parent invoking
limited liability. The cases of Crédit Agricole, Scotiabank and MBK Mercobank in
Argentina are illuminating. In all three cases, the foreign shareholders or parents,
unwilling to recapitalize failed subsidiaries, turned them over to the Argentine
government for rescue. In the cases of Crédit Agricole and Scotiabank the reasons for failure were the Argentine government’s economic policy decisions. This is a very different matter than if the reason had been corporate mismanagement or malfeasance.

Scotiabank (formerly Bank of Nova Scotia) refused to pump in more capital and instead abandoned Scotiabank Quilmes, writing off C$540mn in the process. The government transferred Quilmes to Banco Comafi and Banco Bansud, which appeared to have roughly split it between them, and which took over all the liabilities, not just the deposits. Scotiabank did make a voluntary payment of 20 cents on the dollar to holders of its subsidiary’s medium term notes and other debt. It may have done so to shore-up its reputation in the global market for its debt. It also gave severance pay to the 500 employees (out of 1700) who lost their jobs.

Crédit Agricole exercised the option implicit in limited liability and walked away from its three subsidiaries in 2002. It simply refused to send the around 200mn pesos (US$61.5mn) they would require to stay afloat. The three subsidiaries—Banco Bisel, Banco del Suquia and Banco de Entre Rios—have 353 branches that serve farmers in the provinces. The government-owned Banco de la Nación Argentina, the largest bank in the country, temporarily stepped in to keep the three running.

Regardless of the arguments, the data suggests that the phenomenon of a flight to quality does not provide foreign banks with a long-term advantage. Market share shifts to foreign banks during most crises (absent acquisitions of local banks) appear to amount to only a per cent or two of the banking systems’ total assets and may be short-lived.
1.3 Regulation

The Basle Concordat of 1975 (amended in 1983), established that home country supervisory authorities are responsible for solvency supervision of the parent’s branches abroad. This is logical as it is the home country authorities that have legal access to the parent’s books, and because a branch fails when its parent fails. Host and parent country supervisory authorities are jointly responsible for solvency supervision of subsidiaries, with the host country having primary responsibility. Again this is logical as the subsidiary is a legal person of the host country and so the local authorities have access to its books. Also, a subsidiary can fail even when the parent is solvent. However, the home country authorities are responsible for supervision on a consolidated basis as subsidiaries affect the parent’s solvency and the parent cannot disclaim all responsibility for its subsidiaries. This provision for joint responsibility followed the collapse of Banco Ambrosiano in 1982.

When Banco Ambrosiano collapsed, the Italian authorities protected Italian depositors by transferring the bank’s business to a new Italian entity. However, they disclaimed responsibility for the obligations of Ambrosiano’s Luxembourg subsidiary and the Latin American subsidiaries.

When BCCI failed in 1991, the local regulators in such countries as Canada and Mauritius dealt with the local operations. The Bank of Canada closed Bank of Credit and Commerce Canada. Bank of Mauritius issued a license to the Somaia group to establish Delphis Bank to take over BCCI’s banking business. When Demirbank failed in Turkey in 2000, its subsidiary in Bulgaria continued to function and there was no run on the bank. Instead, the Bulgarian subsidiary was simply an asset that the Turkish authorities sold.
Again, countries differ in terms of whether they permit foreign banks to operate as branches, affiliates or subsidiaries. When banks use affiliates, frequently this is in response to host countries’ laws limiting foreign ownership in the banking sector. The laws force the foreign parent into minority ownership as a condition of entry or continuation of operations. Generally foreign banks convert affiliates to subsidiaries when they can. Still, in some cases foreign banks continue to maintain affiliates rather than subsidiaries, perhaps in order to limit the parent’s responsibility. Belgolaise, a subsidiary of Belgium’s Fortis Bank that specializes in banking in Africa, operates almost exclusively through affiliates.

Countries that have wished to open their banking sectors to foreign banks sufficiently to avoid reciprocity concerns while limiting the foreign banks’ scope, have opted to permit subsidiaries rather than branches (Tschoegl 1981). Canada would be a case in point, at least before the NAFTA treaty forced change. Countries that have wished to limit foreign banks to the wholesale and corporate markets and to keep them out of the retail market have permitted branches but not subsidiaries. Japan would be a case in point, at least before the need to recapitalize some large, failed banks forced change.

In addition to these basic considerations, countries have also had to decide whether or not to permit foreign banks to buy local banks. Even in cases where the country permits the foreign bank to establish a subsidiary it commonly still forbids it to acquire local banks. This has the effect of limiting the foreign bank to organic growth, something that can be quite slow. HSBC entered Canada in 1979 but only started to grow rapidly in 1986 when it acquired the failed Bank of British Columbia; HSBC
Canada followed this with seven more acquisitions, which between them had acquired six banks, mostly subsidiaries of other foreign banks (Tschoegl 2003). Similarly, the foreign banks that own the largest US subsidiaries or affiliates of foreign banks have all grown by acquisition (Tschoegl 2002b). The same appears generally to be the case in those transition and developing countries where there are large foreign banks. The primary exceptions are those cases where the foreign banks came when a country was a colony or before there were locally-owned banks. In these cases, the foreign banks have had the time to grow into a substantial presence, e.g., in Jamaica (Table 3), Malaysia (Table 4), and the Pacific Islands, though even here the foreign banks have been involved in mergers and acquisitions, especially among themselves.

2. Effect of Foreign Bank Presence in Crises

In general, foreign banks have had little effect in crises, primarily because they did not have a material presence before the crisis began. Of the following 12 countries (treating the Pacific Islands as one country), in eight (Bulgaria, Czech Republic, Hungary, Indonesia, Mexico, Norway, Tanzania and Thailand), the foreign banks’ share of banking system assets ranged from nil to well under 20 percent. In four countries (Argentina, Jamaica, Malaysia and the Pacific Islands), it was in excess of 20 percent.

One could well hypothesize that countries that had the sort of policies that would encourage the entry of foreign banks are not likely to have the sort of policies that lead to crises. Beck et al. (2003) found that crises were less likely in economies with fewer regulatory restrictions on bank competition and national institutions that encourage competition. At the very least, the empirical evidence suggested that developing-country banking systems that had lower entry barriers to foreign-owned banks gained directly and
indirectly. They were less vulnerable to crises and the domestic banks were more
efficient than in countries with greater barriers. Barth et al. (2003) found that the
negative correlation with the likelihood of a banking crisis is not with foreign bank
ownership per se, but rather with limitations on foreign bank entry and ownership.
Independent of actual foreign bank entry, the authors found that the likelihood of a major
banking crisis was positively associated with greater limitations on foreign bank
participation.

Even in those cases where foreign banks have had a large presence and there has
been a crisis, such as the Pacific islands in the Australian sphere of influence or Jamaica,
the crisis has been limited to the need to bail-out depositors in the government-owned
bank. The knock-on effects have been limited. All depositors in the foreign banks have
been unaffected and depositors in the government bank have at most only lost temporary
access to their deposits if that. There has been no material credit restriction because the
reason for the failure of the government bank was that its lending went to unproductive
purposes. The net effect of the crisis has been simply to transfer money from taxpayers
to the recipients of the political lending of the failed bank.

The great exception has been Argentina. Here part of the problem has been the
asymmetric pesification that acted as a tax on bank capital and transfer to depositors,
leading some foreign banks to pull out. For more complete treatments of the Argentine
case see Calomiris, Klingebiel, and Laeven (Chapter 2, this volume).

The foreign banks tend to have a stabilizing effect on the economy to the degree
that they are present. Subsidiaries of foreign banks tend not to be as affected by crises as
the domestic banks, in part because they have been more conservative in their lending.
Dages et al. (2000) concluded from their study of foreign banks in Argentina and Mexico over the 1994-99 period that foreign banks exhibited stronger and less volatile loan growth than domestic banks. However, it was the asset quality of bank portfolios and not ownership per se that appeared to be the decisive factor. Branches of foreign banks also benefit from having specialized in lending for trade, especially export trade, and in lending to foreign and large corporations. Because crises often result from or cause a depreciation of the host country currency, exporting firms benefit from the crisis. Thus, though foreign banks do suffer from the general downturn that occurs in economies in crisis, they often suffer less than do domestic banks.

In addition, branches certainly, and subsidiaries probably, benefit from the parents’ support. This has two linked consequences. First, when the foreign banks benefit from a flight to quality this reduces the demand for foreign exchange for flight capital and the consequent pressure on the exchange rate. Second, this gives the foreign banks the funds to continue to lend to host-country firms, which reduces the credit crunch effect of a crisis.

In Jamaica, as the problems in the banking sector grew, depositors engaged in a flight to quality, withdrawing their savings from what they perceived to be weak institutions, mainly indigenous ones, and depositing them in the branches of foreign banks (Kirkpatrick and Tennant 2002). If one examines the market share of the three banks that were foreign-owned before the crisis, all grew faster than the banks requiring government intervention. Furthermore, all gained at the expense of the formerly government-owned National Commercial Bank (Table 3).
When domestic banks are weak, the subsidiaries of foreign banks may have better access to funding in foreign exchange, especially in times of stress. However, the evidence suggests that strong domestic banks can do as well or even better than the foreign subsidiaries (Reynoso 2002).

Again, the primary constraint on these positive effects is the relatively small presence of foreign banks. A second constraint is that while the country is undergoing a crisis, risk managers at the foreign banks’ headquarters may require their banks to curtail lending. The need to match the currency of the assets to those of the liabilities will then have the foreign banks purchasing government bonds. This probably results in a trivial reduction in the governments’ funding costs but may crowd out private borrowing.

There is one last point about stabilization that is worth mentioning. The reverse of the coin that foreign banks may be less affected than host country banks by problems in the host country economy is that the foreign banks may be more affected by problems in the home country. Both Peek and Rosengren (2000) and Williams (1996), for instance, have documented how problems at home resulted in Japanese banks curtailing their lending abroad. Here the effect was more pronounced with branches than subsidiaries. Capital adequacy issues at the parent affect the ability of branches to lend but do not affect subsidiaries in the host countries. The Japanese parent banks’ problems led them to curtail the lending activities of their branches and agencies in California but did not affect the lending of their subsidiaries (Laderman 1999).

3. Roles of Foreign Banks in Resolving Crises

The experience of the 1990s brought an ever-widening recognition of the advantages of inviting foreign banks in (Buch 1997). Foreign banks can operate in two different roles:
in the microeconomic role of rehabilitators of troubled individual banks and in a systemwide role as instruments of reform of the banking system. However, here too foreign banks have their limitations.

3.1 Microeconomic rehabilitators

The restructurers acquire failed or laggard institutions that they then rehabilitate. The transformation process typically begins with the foreign acquirer recapitalizing the acquisition and includes both the closing of unprofitable branches and operations (and the redundancy of staff), and the introduction of systems and processes, especially what is known as “a credit culture”.

As mentioned earlier, frequently governments that have permitted some entry have still blocked foreign banks from acquiring control of domestic banks. It is not unusual for the governments to remove this restriction in crises. Foreigners frequently are the only parties able to recapitalize troubled banks as the other domestic banks are themselves not strong and the government wishes to limit its expenditures where it can. Examples of this abound; Mexico and Tanzania are cases in point.

After the 1994 Peso Crisis put Mexico’s newly privatized banks back into government hands, in 1998 the Mexican Congress finally permitted foreign ownership of up to 100 per cent in Mexican banks. Currently, the top three banks in Mexico—Banamex (Citibank), BBVA Bancomer and Santander Serfin—the fifth—Bital (HSBC)—and the seventh—Inverlat (Scotiabank)—are all foreign-owned and account for over 80 per cent of banking system assets. The degree of foreign ownership is as high as in some Eastern European countries and the ownership is concentrated in far fewer banks.
In 1996, the Tanzanian government began to privatize the largest government-owned banks, which between 1967 and 1991 had been the only banks in the country. In 2000 it privatized the National Commercial Bank to Amalgamated Banks of South Africa (ABSA). As of mid-2000 foreign-owned banks accounted for over 55 per cent of the assets in the Tanzanian banking system. The top 6 institutions, of which four are foreign-owned, accounted for 89 per cent of the assets in all banks and non-bank financial institutions.

As Claessens and Lee (2002) have found, foreign banks introduce improved risk management practices and “imported” bank supervision from parent country regulators. Also, as Lwiza and Nwankwo (2002) point out for Tanzania, and Guillén and Tschoegl (2000) for Argentina, Chile and Mexico, foreign banks frequently compete by introducing new financial products and services. That is, they introduce to the host country products and services that they have previously developed and deployed elsewhere. In a study of foreign bank ownership in Hungary, Majnoni et al. (2003) found that greenfield banks clearly outpaced other foreign-owned banks in terms of profitability. However, improvements in profitability derived from the introduction of new products and a broader array of financial services rather than from higher intermediation margins.

As worthwhile as these contributions are, they are not a panacea against the risk of crises. Competition between banks will tend to transfer efficiency gains to customers. Somewhat counter-intuitively, even better risk control will probably not affect the likelihood of crises. It may reduce the incidence of failure at individual banks, but will
be ineffective for the many cases where the problem is not the banks’ lack of ability to manage risk but rather a lack of will.

3.2 Instruments of systemwide reform

Foreign banks act as instruments of systemwide reform when governments admit them in order to change the structure of the banking system. There are two situations where allowing foreign banks to acquire domestic banks is likely to reduce the incidence of bank crises: when the foreigners take over formerly government-owned banks or when they take over owner-managed banks. Government ownership often results in sub-par average returns; owner-management often results in high variance of returns. Ownership by foreign banks can address both problems. However, in both situations the increasing role in the banking system of foreign banks is likely to be correlated with an apparent reduction in credit outstanding.

The first situation where foreign ownership of banks may help reduce the likelihood of a recurrence of crisis occurs when the foreign banks acquire formerly government-owned banks. That is, foreign ownership of the banks impedes a government’s exploitation of its banks to keep alive failing, but politically sensitive companies, and the concomitant need periodically to bail out the banks. As Gros (2003) points out, permitting foreign banks to acquire government banks can constitute a commitment and transparency device.

As part of a series of measures aimed at “limiting Leviathan”, in June 1997 the Bulgarian government adopted a currency board, which removed the government’s control over monetary policy and stabilized the currency (Koford 2000). The government also pushed forward privatization of the banking system to limit its own
power to use the banking system to support bankrupt firms. By privatizing the banks, the
government removed them from its own direct control. Furthermore, the government
reasoned that foreign banks could draw on their parents for liquidity when the currency
board system limited the BNB’s ability to act as a lender of last resort (Šević 2000). In
May 2003 the government completed the privatization process when it sold 100 per cent
of DSK, the state savings bank, to OTP (Országos Takarékpénztár és Kereskedelmi
Bank), itself the former Hungarian state savings bank. DSK accounts for about 14 per
cent of assets in the Bulgarian banking system so now foreign owners account for about
86 per cent of assets in the banking system (Table 5).

Limiting the government’s discretion was also the motivation for permitting
foreign banks to acquire domestic banks via privatizations in the cases of Hungary and
the Czech Republic. Hungary liberalized before Bulgaria, and the Czech Republic after.

In 1986-87, the Hungarian government authorized foreign banks to enter via
foreign majority-owned joint ventures with Hungarian banks. However, the great influx
of foreign banks began in 1990. The banking crisis of the early 1990s left the
government-owned banks and several private Hungarian banks in desperate straits. The
government decided not to rescue the banks through an infusion of capital, recognizing
that as long as the government owned the banks in whole or in part, borrowers and
managers would expect a bail-out, which in turn would lead to problems of moral hazard.
Also, the government recognized that conflicts of interest could arise when a bank’s
owners were also its largest customers.

Having decided on privatization, the government generally sought strategic
investors rather than dispersed ownership, except in the case of the state savings bank,
even though the only possible strategic investors were foreign firms as Hungarian non-financial firms lacked the capital and the skills. The government’s decision to permit foreign banks to acquire Hungarian private banks and to privatize the banking system led both to a deepening of entry and further entry (Bonin and Wachtel 1999). Currently, foreign banks account for about 70 per cent of banking system assets (Table 6).

Hasan and Marton (2003) examined the Hungarian banking sector during the transition process. They found that flexible approaches to privatization and liberal policies towards foreign banks' involvement with domestic institutions helped to build a relatively stable and increasingly efficient banking system. Furthermore, foreign banks and banks with higher foreign bank ownership involvement were associated with lower inefficiency.

The Czech government was reluctant to permit strategic investors, especially foreign ones. (This is part of a long-seated distrust. In 1920, after the dissolution of the Hapsburg Empire, Czechoslovakia passed a Nostrification Law that required firms with assets in Czechoslovakia to incorporate there.) The government nominally privatized the major banks by selling just under 50 per cent of each in voucher privatizations. The remaining shares remained with entities such as the National Pension Fund or the Ministry of Finance. Once the government bowed to necessity in 1998, things moved quickly. By the end of 1999 foreign institutions controlled almost 50 per cent of total bank assets (Table 7). That percentage may have reached more than 90 per cent with the privatization of Komercni Banka (Mathieson and Roldos 2001).

More generally, government ownership of banks can bring with it certain problems. La Porta et al. (2002) found that higher government ownership of banks in
1970 was associated with slower subsequent financial development and slower growth in per capita income and productivity. They argued that their evidence supported “political” theories that government ownership of banks politicizes resource allocation and reduces inefficiency. In a wide-ranging study, Dinç (2002) found that government-owned banks increased their lending in election years. Restructured and overdue loans also increased. Despite the claim that government-owned banks fund projects private banks cannot finance, government-owned banks tended to fund the government by holding more government debt than private banks did. Both government-owned and private banks held a similar share of loans to assets on average across the electoral cycle.

As Sevic (2001) points out, in small states the relationship between citizens, civil servants, and politicians is often close. There, government-owned banks are thus vulnerable to problems of cronyism, support buying, and corruption. Again, in the cases such as Jamaica, the Pacific Islands, and Tanzania, the solution has been the privatization of the government-owned bank after its restructuring.

The second reform situation involves owner-managed banks. In East Asia, family control of corporations is ubiquitous. The percentage of total market capitalization that the top 10 families control ranges from 2 per cent in Japan (which is almost an order of magnitude lower than the 18 per cent in Taiwan, the next lowest country) to 58 per cent in Indonesia (Claessens et al. 1999). The figure for Singapore is 27 per cent, almost identical to that in Korea and not much greater than the 25 per cent in Malaysia. In the Philippines, the figure is 53 per cent; one family, the Ayalas, alone accounts for 17 per cent.
Owner-managed firms have different governance problems from those of publicly owned firms. A key strength of owner-managed firms is the absence of principal-agent problems, and there is some evidence that owner-managed firms have a better performance than publicly owned firms do (Tan et al. 2001). However, owner-managed firms possibly also have a higher variance in their performance because the owner-manager does not have to persuade others, such as a board of directors, of his strategy. No one can say no, either to good ideas or to bad ones. In addition, often the owner-managed bank is part of an economic group. In these cases one can expect that top management will overrule cautious credit officers should the officers be reluctant to lend to a related company.

It is therefore not surprising that Laeven (1999) found that family-owned and company-owned banks were among the most risky banks, whereas foreign-owned banks took little risk relative to other banks in East Asia. Furthermore, the banks requiring restructuring after the 1997 Asian crisis were mostly family-owned or company-owned and tended to have had excessive credit growth. They were rarely foreign-owned.

When these owner-managed banks got into trouble frequently the only potential rescuers were foreign banks as even the sounder host country banks were still weakened by the crisis. For instance, related and crony lending was clearly a problem in Mexico to the point that one could describe the situation as one of looting (La Porta et al. 2003).

In Thailand too many of the banks had lent on the basis of cronyism, rather than credit assessment (Wiwattanakantang et al. 2002). What facilitated the cronyism was that 12 of the 15 commercial banks were family owned. Dealing with the crisis involved the government taking over six banks. Foreign banks acquired three banks from the
government. United Overseas Bank acquired Radanasin Bank, which had itself, under
duress from the regulatory authorities, taken over the defunct Laem Thong Bank.
Standard Chartered acquired Nakornthon Bank. In addition, Development Bank of
Singapore acquired Thai Danu Bank and ABN-AMRO purchased the Bank of Asia, on a
buy-now, set-the-price-later plan. The government still owns three banks, which account
for about 27 per cent of banking system assets and attempts to sell these to foreign banks
have fallen through. As a result, although the share of foreign owners in banking system
assets approximately doubled, relative to the situation in Latin America or Central
Europe, it remained small (Table 8). Still, even in banks where the owning families
managed to retain control, foreign ownership increased when the regulators forced the
banks to bring in additional capital. At Bangkok Bank, Bank of Ayudhya, Siam
Commercial Bank, Thai Farmer’s Bank foreign ownership was 25 per cent in 1997; it
was 48, 40, 49 and 49 per cent respectively at the end of 1999 (Hewison 2001).

Lastly, related and crony lending was also a problem in Indonesia. Government-
owned banks accounted for 34 per cent of banking system assets and 30 per cent of
deposits. By contrast, foreign JVs and branches accounted for 10 and 3 per cent. Since
the crisis, the government has permitted foreign banks to convert joint ventures to wholly
owned subsidiaries, and has started to move towards permitting foreign banks to acquire
domestic banks. However, impediments to foreign ownership meant that the government
generally had to acquire the failed banks. Even though assets and deposits in foreign
banks have grown, the number of foreign banks and branches has fallen, and the total
foreign share remains small (Table 9).
In both the government ownership and owner-management situations, transfer of the affected banks to foreign ownership may correlate with a decline in total loans outstanding in the banking system. One reason is an artifact of the rescue itself and the other is a consequence of the change in ownership.

To make a failed bank saleable, whether it is government owned or owner-managed, the regulatory authorities typically strip it of its worst assets, often putting them into an asset recovery unit. This was the pattern, for instance, in the privatizations of Argentine provincial banks in the mid-1990s (Clarke and Cull 2002). Any comparison of the failed bank before and after the advent of foreign ownership will show a decline in the size of the loan book, but the direction of the causality is from reduction to the change in ownership, not vice-versa. Also, the comparison conceals the fact that the accounts, by not marking the loans to their salvage value, overstated the loans outstanding before transfer. Clarke et al. (2003) found that privatization of Argentine provincial banks was associated with a temporary reduction in credit due to cleaning of the portfolios of the banks that were being privatized. Thereafter, growth in lending by the privatized and other banks restored credit to pre-privatization levels within a few years.

Still, foreign ownership will automatically bring a change in lending policy, completely apart from any effect of more stringent standards. The result will be that the new owners will reduce or even stop their lending to many of the acquired bank’s traditional customers. Until the bank can develop a new customer base, something that may take time, especially when the host country economy is in recession, the size of the loan book will drop and investments in securities, such as government bonds, will increase.
There is one situation where foreign bank entry could increase the likelihood of crisis even though the entry generates an expansion of credit. The problem occurs when the entry disrupts a cartel. One technology for protecting depositors is to reduce the probability of banks failing. Governments frequently accomplish this by permitting banks to cartelize. In their insightful paper, Breton and Wintrobe (1978) explain regulation by “moral suasion” as an exchange between the authorities and the commercial banks. The authorities provide information and other services that facilitate collusion, and deter entry. Weak banks survive and strong banks live comfortably. In return, the banks comply with the goals of the authorities, including submitting to implicit taxes such as social policies that build support for the authorities. The entry of foreign banks can undermine the exchange for at least two reasons. First, the increase in the number and variety of participants complicates the task of establishing agreement among the banks vis-à-vis the regulators. For the foreign banks, the operations in say, Trans-Amazonia, are only a small part of their total operations whereas operations there represent almost all of the activities of Trans-Amazonian banks. The foreign banks are also likely to have a different mix of activities than local banks. Foreign banks are, therefore, likely to react in different ways to the authorities’ strictures than will Trans-Amazonian banks. Second, the foreign banks, if they do not wish to cooperate, can appeal for support to their home governments, making domestic policy issues matters of international trade and investment policy. The net effect on lending of the entry of the foreign banks depends on the balance between two opposing effects. On the one hand, the disruption of the cartel should lead to higher rates on deposits, lower rates on loans, and increasing lending. Levine (2002) finds that countries that restrict foreign banks
from entering, even if they permit domestic entry, suffer from higher net interest margins. On the other hand, narrower margins may put some host country banks at risk. If they fail, this will, at least temporarily, disrupt banking relationships and may reduce lending. Still, Clarke et al. (2001) find some evidence that the net effect on credit is positive.

One last issue has to do with government-owned banks even when these have not failed. As Marichal (1997) points out, dominance of banking by government-owned banks, especially in Argentina, Brazil, Chile and Mexico, dates from the 19th century. The government favored these banks with its business and with other concessions, but at the same time assigned these banks a development or policy role. Today, this may take a variety of forms, including the maintenance of bank branches in rural areas and small towns where business would not normally justify a bank branch, lending for agriculture or other favored sectors on better-than-market terms, and sometimes, simply the provision of jobs. What has made this possible is an implicit cross-subsidy scheme. These government-owned banks have implicitly taxed the urban and competitive corporate sectors while subsidizing the policy targets. The tax has taken the form of wider than otherwise necessary spreads between deposit and lending rates. In this context, there may not be significant differences in the performance of private and government-owned banks. Sarkar et al. (1998) found that in the absence of well-functioning capital markets, public and private enterprises in India’s banking industry performed comparably.

The entry of foreign banks can undermine the cross-subsidy system. The foreign banks offer better deposit rates to urban middle and upper class customers, better lending rates to the same customers on credit cards and mortgages, and better lending rates to
profitable corporations. This leaves the government-owned banks with the burden of the policy branches and loans, but with a reduced ability to fund them. The result then is that the government-owned banks appear less profitable and less competent relative to the foreign-owned banks. The government-owned banks may be less well-run, but this is then a mandated inefficiency. Ultimately, the government faces the problem that if it privatizes these apparently unprofitable banks that it owns, the result will be that the new owners will close uneconomic rural branches, call-in unprofitable loans, and initiate mass redundancies among bank employees. These consequences may impede the privatization process by creating opponents. As Clarke and Cull (2002) found in the case of the privatization of Argentinean provincial banks, overstaffing, high levels of provincial unemployment and higher shares of public employment all correlated with a lower likelihood of privatization.

A possible positive outcome of the whole process may be an increased transparency for the costs of the government’s policies. The problem is that the benefits of the subsidies may be less quantifiable and some socially worthwhile policies such as the integration of rural areas into the modern economy may suffer. In principle, the government can initiate a system of explicit subsidies to banks, for instance, to maintain rural branches, or programs for them to act as administering agents for schemes for subsidized lending. However, such policies are easier to posit in the abstract than to establish in the face of political and practical difficulties.
3.3 Limitations

Although foreign banks can rescue ailing institutions, remove assets from direct government control, bring competition and transfer technology, they come with handicaps. One is the liability of foreignness and another is a liability of size.

The liability of foreignness simply refers to the fact that the foreign bank is operating at a distance and in an unfamiliar environment (Hymer 1960, 1976). Both of these factors are likely to degrade the quality of the decisions that the foreign bank makes, at least relative to those that host-country firms would make, because of their effect on the quality of information. This is the argument that Hymer and later Kindleberger (1969) made for why it is necessary for foreign firms to have an offsetting advantage if they are to survive the competition from domestic firms.

Of course, in acquiring a host country subsidiary the parent bank acquirers local managers who have local knowledge. However, it may be instructive to think about two extreme scenarios. If the parent gives the local managers no discretion, then it makes no use of their knowledge. If the foreign bank is competing with equally capable local banks the foreigner is at a disadvantage. If the parent gives the local managers complete discretion then the parent is conceding that its decisions add no value. The more capable its local managers become, the more authority the foreign parent should devolve. Ultimately, the question will arise as to the point of owning the foreign operation when shareholders could hold it directly. One can make the argument that foreign banks can bypass their need for local knowledge by using credit scoring approaches. Clarke et al. (2003) conjecture that it was foreign banks’ increased use of such models that enabled them to increase their lending in provinces outside of Buenos Aires. However, in time
capable local banks will come to use such models too, again leaving the foreign banks with no offsetting edge vis-à-vis the liability of foreignness.

The liability of size refers to the argument that large banks and small banks do different things. Berger et al. (2002) argue, on the basis of theories of incomplete contracting, that small banks may be better than large banks at processing soft information. Bank lending to small firms is one area that relies heavily on soft information in developed economies, and even more so in developing economies where the infrastructure to produce hard information is, at best, nascent. They find that large banks were less willing than small banks to lend to firms that do not keep formal financial records and were more likely to have impersonal, shorter, and less exclusive relationships with borrowers. Similarly, using data from Texas, Brickley et al. (2003) found that small locally-owned banks had a comparative advantage over large banks within specific environments.

By necessity, the foreign banks that participate in restructuring tend to be large. Much depends though on how much autonomy the foreign banks allow their subsidiaries to have. If the banks the foreign banks acquire act like even larger banks, it follows then that one can expect that foreign-owned banks will tend to neglect lending to small firms. If they act like autonomous entities, the effect may be muted, but then the parent’s ownership is not adding value.

To address this question, Clarke et al. (2001) used bank level data for Argentina, Chile, Colombia and Peru for the mid-1990s. They had mixed results, perhaps reflecting differing strategies of foreign banks and the varying duration of the foreign parent’s presence in the host country, something that may matter if the foreign parent’s first order
of business is to change the credit policy at its acquisition. Berger et al. (2001), using a
data set on Argentine banks, firms and loans, found evidence suggestive of the possibility
that large and foreign banks may have difficulty extending relationship loans to
informationally opaque small firms. Of course, even a finding that foreign banks do not
have a comparative advantage for smallscale lending does not imply that increased
market share of foreign banks would reduce systemwide credit access.

If foreign banks tend to lend to informationally less opaque firms, principally
foreign firms and large domestic firms, this can give rise to charges that the foreign banks
“cream skim” or “cherry pick”, leaving the worst risks to the domestic banks. Barajas et
al. (2000) found that foreign entry in Colombia’s banking sector improved bank behavior
by enhancing operating efficiency and competition, but may have resulted in increased
risk and a subsequent deterioration in loan quality, particularly among domestic banks.

However, this is precisely the result one would hope would occur. Each class of
banks is lending where it has a comparative advantage. As long as the domestic banks
charge appropriate risk-adjusted interest rates there is no issue.

One might then ask what about the risk to the system through deposit insurance?
If foreign and domestic banks pay the same deposit insurance premium, in that case one
may conjecture that domestic banks are under-paying for deposit insurance and the
foreign banks are over-paying for it. Then the outcome of the combination of “cherry
picking” and deposit insurance would be a transfer from foreign banks to domestic banks.

Furthermore, when foreign banks specialize in lending to good risks they are in
the long-run competing with commercial paper and bond markets, and therefore
specializing in the least profitable markets, leaving the more profitable markets to the
domestic banks. Lastly, the evidence for India for the 1995-96 to 2000-01 period is that foreign banks were aggressive in credit markets rather than “cherry picking” (Bhaumik and Piesse 2003).

4. Conclusions

What foreign banks can bring to banking systems that have undergone a crisis is two services. The most obvious service is that foreign banks can recapitalize and rehabilitate the failed banks that they acquire. In many cases the new foreign parent also accomplishes a skill transfer, inculcating a credit culture and risk management. The more important service that foreign banks can perform is to be instruments of systemwide reform. By taking over formerly government or owner-managed banks the foreign banks can reduce the likelihood of crises. Government ownership and owner-management are subject to specific weakness that ownership by foreign banks can obviate. Experience has shown that one does not have to induce foreign banks to provide these services.

As Nikolai Bukharin (1917) wrote:

“It is finance capital that appears to be the all-pervading form of capital, that form which, like nature, suffers from a horror vacui, since it rushes to fill every "vacuum," whether in a "tropical," "sub-tropical," or "polar" region, if only profits flow in sufficient quantities.”

Bukharin correctly identified that some foreign banks will react to opportunities. However, he elided over a pre-condition and failed to identify a consequence. The pre-condition is that foreign banks require that conditions be propitious. This means that foreign banks will take over cleaned up banks, but there are few signs that the foreigners themselves are willing to assume the burdens of writing off loans. It also means that foreign banks are more likely to enter after reforms that facilitate their operations.
The consequence that Bukharin missed is that the foreign banks’ initial entry is only a phase in a succession process. Some part of the entry is normal international banking activity that will persist indefinitely, but never be of much quantitative importance. A second part is a betting on the success of the transition or restructuring process. As their bets succeed or fail, the bettors will sell their shares, either for a gain or a loss. The third part, and the one that draws the most concern in many countries around the world, is the majority ownership of large commercial banks by foreign strategic investors, that is, investors that manage the banks and who entered either in an exploratory foray that led them further or who entered to restructure a major host country bank.

However, to the degree that the strategic investors are successful, any predominance in host economies is likely to erode over time. As the banks, foreign and domestic-owned alike, become more competitive and adept, the foreign owners will no longer have a comparative advantage in general retail and commercial banking, even if they retain an absolute advantage. Thus, in time, we can expect many foreign owners, if not all, to sell their retail banking activities to domestic owners. They may retain a branch in the national financial center to conduct corporate and wholesale banking but will leave retail and general commercial banking to local banks. More importantly, the reforms that accompanied the entry of the foreign banks will free the domestic banks to compete and grow, increasing their relative importance. This succession process will take decades at best, but it is ongoing.
Bibliography


Table 1a: Allied Irish Banks

<table>
<thead>
<tr>
<th>Year</th>
<th>Event</th>
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<tbody>
<tr>
<td>Late 1980s</td>
<td>AIB had a surplus of senior managers so it lent them out as consultants working in the transition economies, particularly the Czech Republic, Hungary and Poland.</td>
</tr>
<tr>
<td>1993</td>
<td>At the request of the IBRD and the EBRD, AIB agreed to a twinning arrangement with Wielkopolski Bank Kredytowy (WBK).</td>
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<tr>
<td>1995</td>
<td>AIB took a 16.3 per cent stake in WBK.</td>
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<tr>
<td>1996</td>
<td>It acquired a further 20 per cent from the Polish government.</td>
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<tr>
<td>1997</td>
<td>AIB acquired shares in WBK from the EBRD, bringing its ownership to 60 per cent.</td>
</tr>
<tr>
<td>1999</td>
<td>AIB reached an agreement with the Polish State Treasury to acquire an 80 per cent shareholding in Bank Zachodni.</td>
</tr>
<tr>
<td>2000</td>
<td>AIB merged Wielkopolski Bank Kredytowy and Bank Zachodni to form Bank Zachodni WBK.</td>
</tr>
<tr>
<td>Present</td>
<td>AIB currently owns 70.50 per cent of BZ WBK and the remaining shares are widely held. Both WBK and Zachodni were regional retail banks rather than banks to the corporate sector.</td>
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</table>

Note: Having sold its AllFirst subsidiary in the US (Tschoegl 2002b), AIB has no retail banking operation outside Ireland and the UK other than Bank Zachodni WBK.

Table 1b: Prager Handelsbank

<table>
<thead>
<tr>
<th>Year</th>
<th>Event</th>
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<tbody>
<tr>
<td>1989</td>
<td>Four banks established Prager Handelsbank (PH): Ceskoslovenska Obchodni Banka (CSOB; 45%), DG Bank (30%), Zivnostenska Banka (10%), Raiffeisen Zentralbank Oesterreich (Wien) (10%) and BHF Bank (5%). The plan was that PH would specialize in financing foreign trade transactions, especially between Germany, Czechoslovakia and Austria.</td>
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<tr>
<td>1990</td>
<td>PH opened its head office in Frankfurt.</td>
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<tr>
<td>1991</td>
<td>PH opened a rep office in Prague but for legal reasons could not open a branch.</td>
</tr>
<tr>
<td>1992</td>
<td>CSOB (55%) and DG Bank (35%) acquired the shares of Zivnostenska banka and BHF-Bank. BHF-Bank had acquired a 40% stake in Zivnostenska banka at the beginning of the year.</td>
</tr>
<tr>
<td>1997</td>
<td>CSOB bought out its partners in PH.</td>
</tr>
<tr>
<td>2000</td>
<td>CSOB sold PH to Belgium’s KBC Bank. KBC had acquired 66% of CSOB in May 1999. At the end of the 1999 it obtained another 16.66% during the sale of a stake in CSOB held by the National Bank of Slovakia. KBC integrated PH into KBC Deutschland and the name disappeared.</td>
</tr>
</tbody>
</table>

Note: Having sold its AllFirst subsidiary in the US (Tschoegl 2002b), AIB has no retail banking operation outside Ireland and the UK other than Bank Zachodni WBK.
Source: News reports.
Table 2: European banks’ patterns of acquisition in Central and Eastern Europe

<table>
<thead>
<tr>
<th>Country</th>
<th>Unicredito</th>
<th>Erste Bank</th>
<th>KBC</th>
<th>Société Générale</th>
</tr>
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<tbody>
<tr>
<td>Poland</td>
<td>Bank Pekao</td>
<td>Kredyt Bank</td>
<td></td>
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<tr>
<td>Czech Republic</td>
<td>Zivnostenska Banka</td>
<td>Ceska sporitelna</td>
<td>CSOB</td>
<td>Komercni banka</td>
</tr>
<tr>
<td>Slovakia</td>
<td>Unibanka</td>
<td>Slovenska sporitelna</td>
<td>CSOB</td>
<td>Komercni banka Bratislava</td>
</tr>
<tr>
<td>Slovenia</td>
<td></td>
<td></td>
<td>Nova Ljubljanska Banka¹</td>
<td>SKB Banka</td>
</tr>
<tr>
<td>Croatia</td>
<td>Zagrebacka Banka</td>
<td>Erste &amp; Steiermärkische Bank²</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Serbia</td>
<td></td>
<td></td>
<td></td>
<td>Société Générale Yougoslav Bank</td>
</tr>
<tr>
<td>Hungary</td>
<td>Erste Bank Hungary³</td>
<td>K&amp;H Bank</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Romania</td>
<td>Unicredit Romania</td>
<td></td>
<td>Banque Roumaine de Développement</td>
<td></td>
</tr>
<tr>
<td>Bulgaria</td>
<td>Bulbank</td>
<td></td>
<td></td>
<td>SG Expressbank</td>
</tr>
</tbody>
</table>

Note: (1) Associated bank. (2) ex- Bjelovarska banka, Trgovacka banka, Cakovecka banka, and Rijecka banka. (3) ex-Mezőbank. Sources: Bank websites.

Table 3: Ownership structure of Jamaica’s banking system before and after the crisis

<table>
<thead>
<tr>
<th>Bank</th>
<th>1998</th>
<th>2001</th>
<th>Per cent</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Assets</td>
<td>Per cent</td>
<td>Assets</td>
</tr>
<tr>
<td>Bank of Nova Scotia</td>
<td>57,087</td>
<td>34</td>
<td>87,279</td>
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<tr>
<td>Citibank</td>
<td>5,187</td>
<td>3</td>
<td>9,285</td>
</tr>
<tr>
<td>Canadian Imperial</td>
<td>11,138</td>
<td>7</td>
<td>16,618</td>
</tr>
<tr>
<td>Trafalgar Commercial</td>
<td>858</td>
<td>0.5</td>
<td></td>
</tr>
<tr>
<td>First Global Bank</td>
<td></td>
<td></td>
<td>2,991</td>
</tr>
<tr>
<td>Citizens Bank</td>
<td>12,870</td>
<td>8</td>
<td></td>
</tr>
<tr>
<td>Eagle Commercial Bank</td>
<td>3,295</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Island Victoria Bank</td>
<td>2,504</td>
<td>1.5</td>
<td></td>
</tr>
<tr>
<td>Workers Savings &amp; Loan</td>
<td>4,836</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>RBTT</td>
<td></td>
<td></td>
<td>33,298</td>
</tr>
<tr>
<td>National Commercial Bank</td>
<td>72,281</td>
<td>43</td>
<td>90,349</td>
</tr>
<tr>
<td>TOTAL Bank</td>
<td>170,058</td>
<td>100</td>
<td>239,820</td>
</tr>
<tr>
<td>Per cent foreign-owned</td>
<td>43.2</td>
<td></td>
<td>98.8</td>
</tr>
</tbody>
</table>

Notes: Figures in bold refer to assets in foreign-owned banks; Figures in italics refer to asset in banks with Financial Sector Adjustment Company (FINSAC) intervention that the government later privatized. Source: Bank of Jamaica.
Table 4: Foreign bank presence in Malaysia before and after the 1998 financial crisis

<table>
<thead>
<tr>
<th>Year</th>
<th>Domestic</th>
<th>Foreign</th>
<th>Total</th>
<th>Foreign/Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Assets</td>
<td>Per cent</td>
<td>Assets</td>
<td>Per cent</td>
</tr>
<tr>
<td>1996</td>
<td>279,986</td>
<td>80,141</td>
<td>360,127</td>
<td>22</td>
</tr>
<tr>
<td>1997</td>
<td>376,434</td>
<td>103,815</td>
<td>480,249</td>
<td>33.4</td>
</tr>
<tr>
<td>1998</td>
<td>352,765</td>
<td>101,748</td>
<td>454,513</td>
<td>-5.4</td>
</tr>
<tr>
<td>1999</td>
<td>373,646</td>
<td>109,961</td>
<td>483,607</td>
<td>6.4</td>
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<tr>
<td>2000</td>
<td>388,727</td>
<td>123,988</td>
<td>512,715</td>
<td>6.0</td>
</tr>
<tr>
<td>2001</td>
<td>398,156</td>
<td>131,580</td>
<td>529,736</td>
<td>3.3</td>
</tr>
<tr>
<td>2002</td>
<td>425,792</td>
<td>137,158</td>
<td>562,950</td>
<td>6.3</td>
</tr>
</tbody>
</table>

Notes: Assets are reported in RM Millions and percentages are year-on-year changes in total assets.
Source: Bank Negara Malaysia.

Table 5: Foreign ownership of banks in Bulgaria

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>State</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Savings</td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share (%)</td>
<td>98.5</td>
<td>96.8</td>
<td>93.6</td>
<td>84.4</td>
<td>76.9</td>
<td>82.5</td>
<td>51.1</td>
<td>17.6</td>
<td>18.1</td>
<td>14.2</td>
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</tr>
<tr>
<td>Bulgarian</td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>private</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share (%)</td>
<td>1.5</td>
<td>3.2</td>
<td>6.4</td>
<td>15.6</td>
<td>22.4</td>
<td>15.2</td>
<td>6.9</td>
<td>9.9</td>
<td>10.3</td>
<td>11.2</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Foreign</td>
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<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subsidiaries</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
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</tr>
<tr>
<td>Branches</td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
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<td></td>
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<td></td>
</tr>
<tr>
<td>Share (%)</td>
<td>0.1</td>
<td>0.6</td>
<td>2.3</td>
<td>25</td>
<td>42</td>
<td>73</td>
<td>72</td>
<td>74</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assets (BL Bn)</td>
<td>463</td>
<td>582</td>
<td>810</td>
<td>1072</td>
<td>1,089</td>
<td>3,301</td>
<td>8,076</td>
<td>7,589</td>
<td>8,223</td>
<td>9,774</td>
<td>11,908</td>
<td>14,558</td>
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<tr>
<td>Herfindahl</td>
<td>0.38</td>
<td>0.33</td>
<td>0.30</td>
<td>0.15</td>
<td>0.11</td>
<td>0.19</td>
<td>0.12</td>
<td>0.11</td>
<td>0.12</td>
<td>0.11</td>
<td>0.09</td>
<td>0.08</td>
<td></td>
</tr>
</tbody>
</table>

Notes: Herfindahl is the Hirschman-Herfindahl index, calculated as the sum of the squares of each bank’s share of the total assets in the banking system. The Herfindahl index ranges between 0, which represents complete dispersion, and 1, which represents a situation of monopoly.
### Table 6: Foreign bank presence in Hungary

<table>
<thead>
<tr>
<th>Rank</th>
<th>Bank</th>
<th>Owner</th>
<th>Country of origin</th>
<th>Assets (1)</th>
<th>Branches (2)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>of owner</td>
<td>(Ft Bn)</td>
<td>(#)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(%)</td>
<td>(%)</td>
</tr>
<tr>
<td>1</td>
<td>OTP</td>
<td></td>
<td></td>
<td>2,393</td>
<td>430</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>30</td>
<td>42</td>
</tr>
<tr>
<td>2</td>
<td>K+H</td>
<td>KBC Bank</td>
<td>Belgium</td>
<td>1,196</td>
<td>163</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>15</td>
<td>16</td>
</tr>
<tr>
<td>3</td>
<td>MKB</td>
<td>Bayerische Landesbank</td>
<td>Germany</td>
<td>964</td>
<td>30</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>12</td>
<td>3</td>
</tr>
<tr>
<td>4</td>
<td>CIB</td>
<td>IntesaBCI</td>
<td>Italy</td>
<td>831</td>
<td>45</td>
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<tr>
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<td></td>
<td></td>
<td></td>
<td>10</td>
<td>4</td>
</tr>
<tr>
<td>5</td>
<td>HVB</td>
<td>Bank Austria</td>
<td>Austria</td>
<td>579</td>
<td>38</td>
</tr>
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<td></td>
<td></td>
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<td>7</td>
<td>4</td>
</tr>
<tr>
<td>6</td>
<td>Raiffeisen Bank</td>
<td>Raiffeisen Bank</td>
<td>Austria</td>
<td>554</td>
<td>43</td>
</tr>
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<td></td>
<td></td>
<td></td>
<td></td>
<td>7</td>
<td>4</td>
</tr>
<tr>
<td>7</td>
<td>Postabank</td>
<td>Erste Bank</td>
<td>Austria</td>
<td>407</td>
<td>114</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>5</td>
<td>11</td>
</tr>
<tr>
<td>8</td>
<td>Erste Bank</td>
<td>Erste Bank</td>
<td>Austria</td>
<td>393</td>
<td>79</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>5</td>
<td>8</td>
</tr>
<tr>
<td>9</td>
<td>Budapest Bank</td>
<td>GE Capital</td>
<td>USA</td>
<td>332</td>
<td>56</td>
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<td></td>
<td></td>
<td></td>
<td>4</td>
<td>6</td>
</tr>
<tr>
<td>10</td>
<td>Citibank</td>
<td>Citibank</td>
<td>USA</td>
<td>322</td>
<td>19</td>
</tr>
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<td></td>
<td></td>
<td></td>
<td></td>
<td>4</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td></td>
<td></td>
<td>7,971</td>
<td>1017</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

Notes: 1) OTP is about 30-40 percent foreign owned, but the shares are widely held. Data as of end-2003. Source: Financial Times.

### Table 7: Foreign ownership of banks in the Czech Republic

<table>
<thead>
<tr>
<th>Year</th>
<th>State financial institutions</th>
<th>State-owned banks</th>
<th>Czech-controlled banks</th>
<th>Under conservatorship</th>
<th>Foreign controlled Banks</th>
<th>TOTAL Banks</th>
<th>TOTAL Branches</th>
<th>Unlicensed banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td></td>
<td>4</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>1990</td>
<td></td>
<td>4</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>1991</td>
<td></td>
<td>4</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>1992</td>
<td></td>
<td>4</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
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<td>1993</td>
<td></td>
<td>4</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>1994</td>
<td></td>
<td>4</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
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<td>1995</td>
<td></td>
<td>1</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>1996</td>
<td></td>
<td>1</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>1997</td>
<td></td>
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<td>2</td>
<td>13</td>
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<td>x</td>
<td></td>
</tr>
<tr>
<td>1998</td>
<td></td>
<td>1</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
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<tr>
<td>1999</td>
<td></td>
<td>1</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>2000</td>
<td></td>
<td>1</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>2001</td>
<td></td>
<td>1</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td></td>
<td>1</td>
<td>2</td>
<td>13</td>
<td></td>
<td>5</td>
<td>x</td>
<td></td>
</tr>
</tbody>
</table>

Notes: 1) Banks in liquidation, bankruptcy, non-commencement of operation, no longer operating due to merger, or transformed into a non-bank entity. Source: Česká Národní Banka.
Table 8: Foreign bank ownership in Thailand

<table>
<thead>
<tr>
<th></th>
<th>1996</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>Branches of foreign banks</td>
<td>14</td>
<td>18</td>
</tr>
<tr>
<td>Local banks w/majority foreign ownership</td>
<td>0</td>
<td>4</td>
</tr>
<tr>
<td>Number of local banks</td>
<td>15</td>
<td>12</td>
</tr>
<tr>
<td>Assets in branches or subsidiaries of foreign banks</td>
<td>8.5%</td>
<td>17.5%</td>
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</tbody>
</table>

Source: Thai Ministry of Finance.

Table 9: Foreign bank ownership in Indonesia

<table>
<thead>
<tr>
<th></th>
<th>Year</th>
<th>State-owned</th>
<th>Private</th>
<th>Regional Development</th>
<th>Foreign and joint-venture</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banks</td>
<td>1997</td>
<td>7</td>
<td>160</td>
<td>27</td>
<td>44</td>
</tr>
<tr>
<td></td>
<td>2000</td>
<td>5</td>
<td>83</td>
<td>26</td>
<td>39</td>
</tr>
<tr>
<td>Branches</td>
<td>1997</td>
<td>1,748</td>
<td>5,133</td>
<td>776</td>
<td>90</td>
</tr>
<tr>
<td></td>
<td>2000</td>
<td>1,734</td>
<td>3,777</td>
<td>798</td>
<td>71</td>
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<tr>
<td>Assets</td>
<td>1997</td>
<td>152.6</td>
<td>237.9</td>
<td>12.7</td>
<td>44.2</td>
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<tr>
<td></td>
<td>2000</td>
<td>458.7</td>
<td>331.9</td>
<td>23.2</td>
<td>113.9</td>
</tr>
<tr>
<td></td>
<td></td>
<td>34%</td>
<td>53%</td>
<td>3%</td>
<td>10%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>49%</td>
<td>36%</td>
<td>3%</td>
<td>12%</td>
</tr>
</tbody>
</table>

Source: Bank Indonesia.