# Euro Currency (Offshore) Market

## Summary

### 8.1 Definition / Introduction of Euro Currency Market

**Euro Currency market can be described as an international financial market which specializes in borrowing and lending of currencies (termed euro-currency deposits/credits) from / to non-residents outside the country of issue of the currencies. Remember Euro is a currency and Eurocurrency is deposits and loans in various currencies, including Euro**

### 8.2 Origin of Euro Currency (Offshore) Market

**Certain governments that were not politically sync with the US government and were always apprehensive about their USD assets being frozen by the US administration in case of adverse developments between the governments initiated Euro market. It provides an environment to create assets & liabilities outside the regulatory supervision of the monitoring authority pertaining to a currency.**

### 8.3 Factors Contributing Towards Growth of Euro Currency (offshore) Market.

**1] The ceiling on interest rate on deposits in the US. 2] US requirement for maintenance of reserves against deposits. 3] Mandatory insurance of deposits. 4] Interest equalization tax and 5.] US restrictions on international borrowing.**

### 8.4 Characteristics of Euro Currency Market

Unregulated market; Short term deposits and long term loans; opportunity for time deposits, ease of wholesale transactions based on Euro and LIBOR etc. mark this market.

### 8.5 Components (Compositions) of Euro-Currency Markets.

**Compositions of Euromarkets are described in three areas, viz., a] Market Participants - consisting of commercial banks, corporate banks, government and**

central banks and private individuals, b] Euro Financial Instruments and c] transactional structure of Euro Markets – the Euro Currency market is entirely a wholesale market.

## 8.6 Euro Currency Deposits Market

Euro Currency deposits are placed with banks in currencies outside their home country; deposits are accepted only in freely convertible currencies and most of them are for six months with minimum size of $ 50,000 or equivalent.

## 8.7 Euro Currency Credit (Loans) Market

Euro-credits are generally provided for short to medium term i.e. five to eight years and for large amounts on syndicated basis. They are assessed on the basis of credit rating of the borrower and the financial viability of the project and subject to floating interest rates guided by LIBOR.

## 8.8 Types of Euro Currency Bonds

This debt has a fixed maturity and a fixed coupon rates. It is repaid in one go at maturity called 'Bullet' repayment'. Bonds having varying interest rates or coupon rates over their life are called as floating rate notes. They have 5 – 7 years maturity and are linked to six-month LIBOR rate. Sinking Fund Bonds provide for repayment of the principal in installments during the lifetime of the bond. Such bonds are issued by companies with average credit rating. Companies with very poor credit rating or entering into high risk business ventures issue bonds that are termed 'Junk'. These bonds carry coupon rates of at least 3 – 4% above the normal rates. Zero Coupon bonds don't carry any interest rate and are issued at discount and repaid at face value.

## 8.10 Euro Currency Notes Market

Commercial paper is a short term security issued for maturity of less than one year without underwriting support from banks. Long term requirements of borrowers are met by issue of short term notes which are redeemed by issue of fresh notes. Bankers Acceptance (BA)is an instrument widely issued in the US money market to finance domestic as well as international trade. Under Repurchase Obligation (RO) transactions the borrower 'sells' securities to the lender with commitment to 'repurchase' the same at a predetermined rate on a fixed future date.

## 8.12 Syndication of Loans

For large loans, individual banks found it difficult to take the risk single handed. Regulatory authorities in most countries also limit the size of the individual exposures. Hence the risk was required to be shared by a group of banks termed 'syndicate'

## 8.13 Offshore Banking and tax havens

Offshore Financial centers conduct a wide range of business activities such as banking, insurance, securities transactions, trusts and some non-financial activities such as shipping, registries etc. A country that offers foreign individuals and businesses little or no tax liability in a politically and economically stable environment is known as a Tax Haven.

## 8.14 Petrodollars

The Organization of Petroleum Exporting Countries (OPEC) was formed in 1960 and prices of petro products were increased significantly. Surplus USD generated in OPEC by this move is known as Petrodollars.

## 8.16 LIBOR – (London Interbank Offered Rate)& SIBOR

The interest rate at which prime bank offers dollar deposit to other prime bank in London is known as LIBOR. The rate is used as the basis for pricing Eurodollars. SIBOR stands for Singapore Interbank Offered Rate and is a daily reference rate based on interest rates at which banks offer to lend unsecured funds to other banks in Singapore.

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