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“Constructing and Deconstructing the Global Payments System 1870-2000”

GloCoBank: Global Correspondent Banking 1870-2000

- Plumbing of the global payments system: prone to leakage, diversion, points of failure, patches
- Decline in correspondent banking since 2008 (Erbenova et al 2016):
  - Anti-Money-Laundering, Counter-Terrorist-Funding, Sanctions
  - Cost/Benefit of acting as a correspondent
- Challenge of other digital solutions, disintermediation, regulatory oversight, financial exclusion of poor countries (FSB/BIS attention)
- Response to financial crisis, conflict, technological innovation, changes in bank business models
- CHIPS (1970), SWIFT (1977)
  - ISO 20022

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Index of Number of Active Correspondents 2011=100

Northern America
Asia
Eastern Europe
Oceania
Africa
Americas (excl. North America)
Literature on Correspondent Banking

• USA
  • Richardson (2007)
  • James and Weiman (2010)
  • Das, Mitchener & Vossmeyer (2018)
  • Mitchener & Richardson (2019)
  • Calomiris, Jaremski & Wheelock (2019)

• International:
  • London: Mollen (2012), Mollen & Michie (2012)
  • SWIFT: Scott & Zachariadis (2014)

• Contemporary
  • Meinster & Mohindru (1975)
  • Palmer (1990)
  • Lawrence & Lougee (1970)
  • Naughton & Chan (1998)

• Current issues:
  • Gustitus, Bean & Roach (2001)
  • Grollman & Jutsra (2017)
  • von Peter & Rice (2020)
  • CPMS @ BIS/FSB
Bank of California 1968 Campaign: 2000 Correspondents around the world

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Context for 1960s-1970s

• Early 1960s – Eurodollar market surge in global payments, integrated cross-border inter-bank market
• Late 1960s – rush/panic among banks to internationalise
  • Branches
  • Subsidiaries
  • Cooperative Strategies
• Market Risk: floating exchange rates
• Operational Risk: weak internal controls, complexity
Number of Respondent Banks for Banks in London 1970 and 1975

- Australia and New Zealand Bank
- Bank of Scotland
- Barclays Bank Ltd
- Brown Shipley
- Coutts and Co
- Keyser Ullman
- Lloyds Bank
- Midland Bank
- Moscow Norodny
- National Westminster
- Royal Bank of Scotland
- Williams and Glyns

1970 vs. 1975
Correspondent Bank Deposits of US Banks: due to Foreign Banks

*Excluding* Edge Act Banks (USD billion)

Source: American Banker

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BEFORE 1970
Deutsche Bank buys Sterling against Dollars

Deutsche Bank Frankfurt

Telex

Dollar deposit

Morgan New York Correspondent

Dollar cheque

Midland London

Dollar deposit

Irving Trust New York Correspondent

Dollar credit

New York Clearing House International Payments Exchange (5 times daily)
Clearing House Interbank Payments System

- All day entries through computer terminals, final netting out at end of day, 30 minutes to meet any deficit, final payment through FRBNY
- 1970 – demand driven (too many cheques, too many messengers, too many clerks, focused on last daily clearing)

‘one New York bank had its payments staff drop from an average of 22 years in the bank to an average of 8 months in a two-year span’ (Crowley FRBNY 5 July ‘74)

- Technological innovation available (adapted from domestic use)

- New York Clearing House Members
  - Associated members, Edge Act subsidiaries
Burroughs B 2500 AND B 3500 ELECTRONIC DATA PROCESSING SYSTEMS A NEW LEVEL OF COMPUTER RESPONSIVENESS
Note: Gendered element to technology
Clerical tasks
CHIPS Average Daily Number of Transactions

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Average Daily Amount of Transactions USD billions

c. 85% of USD cross-border settlement

• FX payments immediately available but matching Dollars not available until next day: Clearing House Funds

• Friday funds not available until Monday: strategic holding over to put into money markets

• Daylight Overdrafts: float/deposits covers only a tiny proportion of turnover even for small respondents

• Time change NY-London-Europe: NY clearing not completed before European banks close

‘it is a business in which trust and confidence is essential’
Crowley FRBNY 5 July ‘74

• Associate members don’t have direct access: clearing through Clearing House members
Correspondent Banking Deposits of US Banks: due to foreign banks (USD billion)

- 6/30/80
- 6/30/81
- recalibrated
- 06/30/81
- 06/30/82
- 06/30/83

Edge Act Banks Included

1 Oct 1981
Same-day settlement

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CHIPS Average Total Net Credit Positions Through the Day
Feb 9 to Feb 22 1989 (USD billion)

Peak $54 billion
4:30pm European Time

Source: Dallas Fed
Herstatt Bank Collapse: July 1974

• Fraud, insolvency

• German authorities close Herstatt before dollar payments to cover FX payments on behalf of Herstatt (Mourlon-Druol 2015; Schenk 2014)

• Exposes counterparty risk in CHIPS

• Chase Manhattan: main correspondent bank

• Next day retrieval of FX payments (symmetric to dollar settlement)

• Sharp fall in turnover

• Sharp and sustained fall in average size of transaction
Average Size of Payment '000s

Deflated Avg Amount per Payment

Average Dollar Amount Per Payment '000

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GloCoBank 2021-2026

There is a lot still to learn about Correspondent Banking system

• Geopolitics
• International Trade
• Technological innovation (ICT, competing/complementary networks)
• Financial Crisis: response and role in
• Bank strategies (divergence)
• Governance (AML/CTF, transparency)
• Regulation (national and supranational)
• Regional as well as global dynamics

https://glocobank.web.ox.ac.uk/#/

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