Session 2: Financial Stability and Financial System Reforms - Discussion

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Competition and Credit Procyclicality in European Banking (authors: Leroy and Lucotte)

Aim

– Empirical assessment of competition effects on credit procyclicality in Europe

Methodology

– Country level analysis: Interacted panel VAR (IPVAR); 4 main variables: GDP, CPI, real outstanding credit and nominal short-term interest rate, using quarterly HP-filtered data, 1997Q1-2014Q4

– Bank specific analysis: Panel fixed effects model; 2005-2014; main variable of interest: output gap*Lerner Index; including total assets, loans/total assets, equity/total assets and Lerner Index*Monetary policy shock

– Both analysis examine 16 European countries

Competition and Credit Procyclicality in European Banking (authors: Leroy and Lucotte)

Main findings

- Credit is procyclical
- Procyclicality of credit is higher in economies where competition among banks is relatively low
- Cross-country heterogeneity in credit procyclicality
- A higher credit procyclicality is a feature of a more bank-based economies
- Supporting "competition-stability" view

Policy recommendations

- A pro-competitive policy is expected to reduce macroeconomic volatility (relatively less sensitivity of investment and consumption to the business cycle).
- Supporting the recent initiative by the European Commission to implement policies to develop markets for corporate debt securities.

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Strengths

– The topic is of high relevance

– Comprehensive literature review tackling different strands of the literature

– Use of the most recent econometric models in terms of VAR analysis, Interacted panel VAR

– Two-level analysis: country-level and bank-level analysis

– Extensive checks for robustness

– Relevant results for policy-makers – contributing to "competition-stability" view and promotion of market-based financial structure.

Comments

- Lerner Index discussion

  - Why only one output? Why total assets? Why not loans and/or other earning assets?

  - Trend is used to account for technical change over time … No need for country by country estimation?

  - Which model/approach is used for estimation of SFA?

  - Inclusion of equity?

  - The score is a result of estimation process, hence Lerner index includes an error element. Any adjustment procedure?

- Why not using the Boone indicator (2000, 2001, 2004) as a measure for competition.

  - Higher levels of efficiency are mapped with higher relative profits.

Comments

Country-level analysis

- What is total credit? Banks credit+?

- The assumption that competition level is exogenous is too strong (NEIO – Bresnahan, 1989 and Sutton, 1991)

- Any control for structural breaks (the financial crisis)?

- How do you interpret the contemporaneous negative effect of the exogenous GDP shock on the credit cycle in the four biggest economies: France, Germany, UK and Sweden?

- Controlling for regulatory and supervisory practices

- Lending standards and screening (Dell'Ariccia and Marquez, 2006 and Ruckes, 2004)

Comments

Bank-level analysis

- All bank-specific variables treated as endogenous, competition as well?

- The lagged dependent is insignificant. Any explanation?

- Any environmental variables to control for cross-country differences?

- Why the chosen set of bank-specific variables?

- Lagged values to control for endogeneity

  - Any possible available instruments?

- Interaction term: Output gap*Lerner Index

  - Test for joint significance?

  - Graphical presentation of the marginal effects would be useful given both variables are continuous

Minor points for possible discussion/consideration:

- Divide Introduction in two separate sections, Introduction and Literature Review

- Lerner index could be explained in a separate section prior to Section 2, given that banking competition is in the focus of this paper.

  - Other measures for competition to be considered such as the Boone Indicator

- For better illustration the proportion of banks per country included in the analysis to be presented along with the number of banks per country

Pension funds and their contribution to long-term investment: the case of infrastructure (author: Bernard H Casey)

Questions for discussion:

- What type of investment model? Direct investment in infrastructure projects or via investment funds etc?
  - Only in projects that generate regular cash-flow
- Is this proposal for the pension fund pillar 1, pillar 2 or pillar 3?
- What is the advantage compared to government bonds? Higher yield?
- Is there any limitation of the level of funds invested in infrastructure projects?
- Any particular idea for the case of Macedonia?

Thank you for your attention!