

2021 EBA Policy Research Workshop

Discussion of "Informational Asymmetries and Interbank Competition:
Evidence from Branch Pruning" by Maddalena Galardo and Paolo
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Outline

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The issue and the paper

- Research question: what is the impact of bank branch closures on interbank competition, the credit market and the probability of looking for a new credit relationship?
- Important contributions of this paper:
 - Nice identification strategy based on a difference-in-difference approach and the use of the heterogeneity between firms that borrow from closing branches (treated group) and other firms (control group) within the same municipality;
 - Interesting combination of individual-level data (credit register) and granular fixed effects at the local level to control for local credit demand effects and firm-specific characteristics.

Main findings

- Main findings:
 - Critical role of bank branches for the acquisition of soft information on borrowers \Rightarrow closures lead to informational loss;
 - Branch closures raise the probability that a borrower looks for a new lending relationship (2.2 percent higher probability);
 - Temporary discount benefiting firm switching bank after a branch closure compared to normal switchers, vanishing after three years;
 - Higher impact on more opaque corporate borrowers, identified on the basis of a Z-score.

Theoretical model?

- Need for a short theoretical model to better understand the net welfare effects of a bank closure, and the terms of the trade-off between increased interbank competition and the loss of soft information;
- What are the consequences in terms of market imperfections (incentives, screening, moral hazard and adverse selection)?

Empirical model

- Set-up of the diff-in-diff estimation:
 - Robust identification strategy based on detailed borrower-branch-level data and inclusion of municipality*time fixed effects
 - But what about the parallel trend between the treated group and the control group before the closure? Need for some evidence about that.
 - Crucial role of SMEs: could be more analyzed, group most likely to be impacted by soft information and lending relationship
 - \Rightarrow Introducing a dummy variable is fine but why not interacting it with the variable of interest or running the regression on a sample limited to SME lending?
 - How to explain the low level of the R-square of the equations (around 10 percent) in the baseline estimation?

Empirical model

- Problems with the database, highlighted in the paper:
 - No loan denials and acceptances reported in the credit register (CR). Loan acceptances inferred from the CR through observation of appearance of a loan in the CR after firm application.
 - \Rightarrow What if the firm decides to drop its application in the meantime due to disagreement with loan terms? How are undrawn credit lines treated, can you identify available but undrawn credit lines? Any information, statistics about the length of the application procedure?
 - Lending branch not observed in the CR, problem for firms served by branches staying on a different postal code from that of the firms: approximation made by the authors (closest branch) would make more sense if sample restricted to SMEs.

Policy implications

- Suggestion: adding some policy implications in terms of prudential supervision, banking competition policy and banks' profitability assessment

Conclusion

- Solid and interesting paper relying on a rigorous empirical strategy;
- Empirical findings could focus more on SME lending;
- More work could be done to explain the transmission channels between branch closures and the imperfections of the credit market, as well as the policy implications.