



Discussion: Reallocation of banks' portfolio during a liquidity shock: Evidence from the 2007 and 2009 financial crisis by P. Pessarossi and F. Vinas

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** The views expressed are those of the discussant and do not necessarily reflect the official position of the EBA*

Content of the paper

The paper aims to:

- Analyse how banks adjust their lending during a liquidity shock and,
- Assess causal effects between the liquidity profile of banks prior to the crisis and the change in the volume and in the maturity of credit between 2007q2 and 2009q4.
- Focus on the French banking sector and on the French economy.

The methodology uses:

- Descriptive statistics from three different databases (Credit registry of BdF, Supervisory reporting and, Database on firms),
- Cross-sectional regressions using banks' liquidity risks as the main independent variables (*ie.* Deposits ratio, ASF, RSF, NSFR) and the change in the volume and in the maturity of lending as dependant variables,
- Control for bias on lending demand.

The results show that:

- Banks with lower liquidity risks provided more loans during the crisis and kept higher credit supply towards small firms,
- However, taking into account the maturity of loans, banks with lower liquidity risks prior to the crisis increase long-term lending only to large firms.

The main conclusions are that:

- Even resilient banks shortened the maturity of credit during the crisis,
- A robust, regulation on liquidity would make lending supply more resilient to liquidity shock but would not eliminate entirely the negative effects on the real economy.

Comments

- The paper is well-structured and both the demonstration and the conclusions are clear and straight-forward.
- The analysis benefits from a very granular database which enable to assess the lending relationship between banks and non-financial firms at an individual level.
- The paper provides a comprehensive assessment of the impact on lending by focusing not only on volume but also on the type of counterparts and the maturity of credit.
- Use of the NSFR (proxy) as an ex-ante explanatory variables of the change in lending during the crisis provides added value to the literature and new insights to regulators.

Suggested improvements and extensions

Suggested improvements in the paper

- The RSF may not be an adequate proxy to capture market liquidity risk (HQLA/ Total Asset may be a better proxy).
- A clarification of the use (or the removal of the concept) of the difference-in-difference is necessary as the analysis does not include a control group.
- Further explanation on the use of the fixed effect model in the absence of panel data and in terms of the model exploited in line with Khwaja and Mian (2008).

Suggested extensions for the empirical study

- Account for the constraints on credit supply (i.e. quantitative constraints on long term funding) in the regression equations.
- If possible, assess the impact on the different sector of the economy (real estate, trade...) and not only by type of counterparts (small, medium, large firms).

Reflection on the policy implications

- Should the liquidity regulation also be aimed at reducing credit crunch?
- Takeaways for the EBA ongoing work on the calibration of the NSFR?
 - use of the suggested NSFR proxy to extend the current EBA QIS sample?
 - use of the suggested methodology to control for credit demand bias?



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