



EUROPEAN CENTRAL BANK

EUROSYSTEM

The impact of negative rates on bank balance sheets: Evidence from the euro area

discussion by

Angela Maddaloni (ECB) and

José-Luis Peydró (ICREA-UPF, CREI, Barcelona GSE, CEPR)

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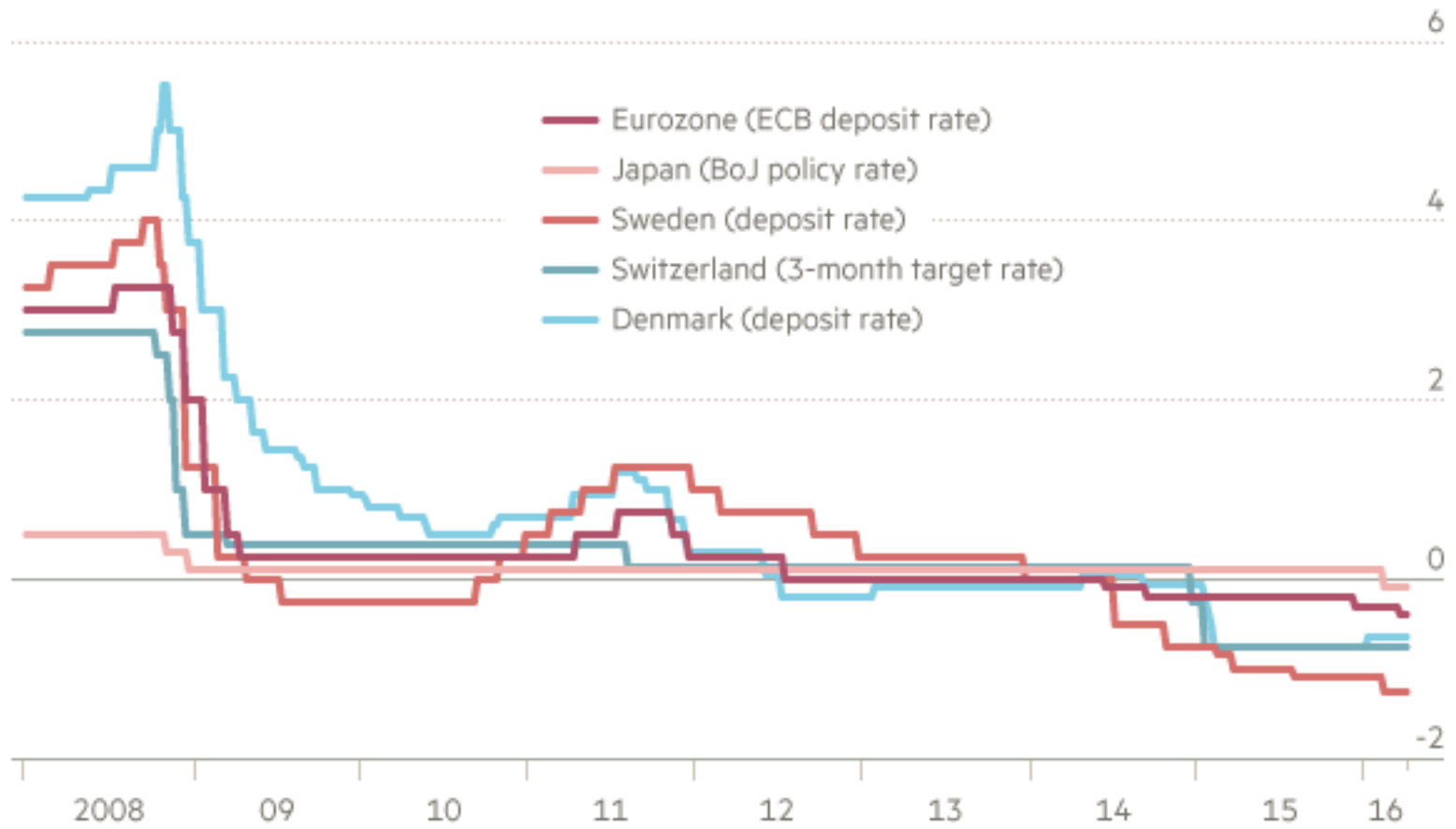
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Negative interest rates

- The European Central Bank, the Bank of Japan and other central banks around the world have introduced overnight negative interest rates
- Negative rates on deposits are one of many non-standard monetary policy tools employed by the ECB
- Negative rates are not “exceptional” anymore in financial markets and are an important feature of economies that account for a large part of global GDP

Central bank policy rates

Per cent

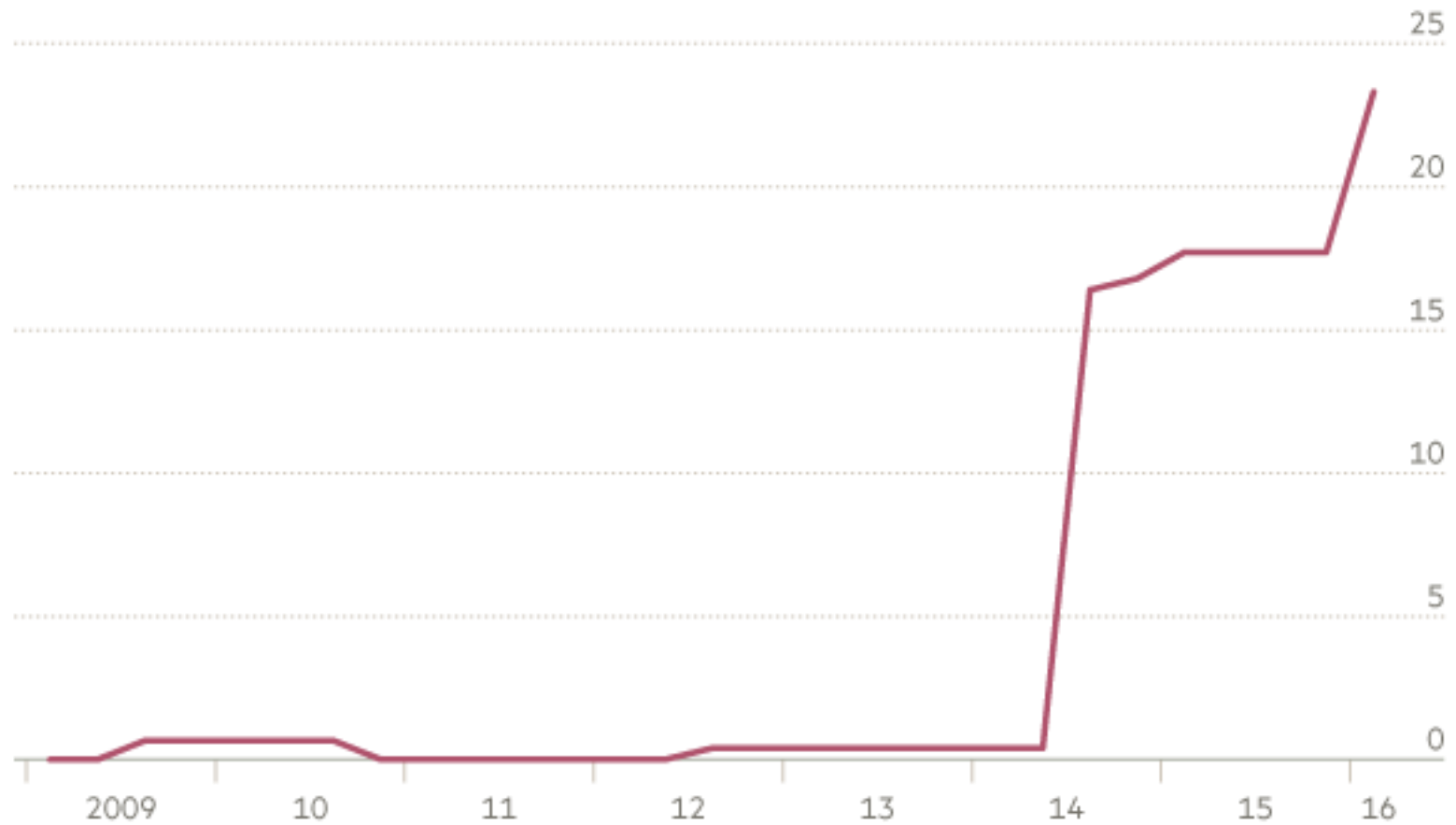


Source: Thomson Reuters Datastream

FT

Rates go negative

% of global GDP of economies with a negative central bank interest rate*



* Eurozone, Japan, Switzerland, Sweden, Denmark

Source: FT research

FT

Negative yielding government bonds

JPM Global GBI Broad Index (\$bn)

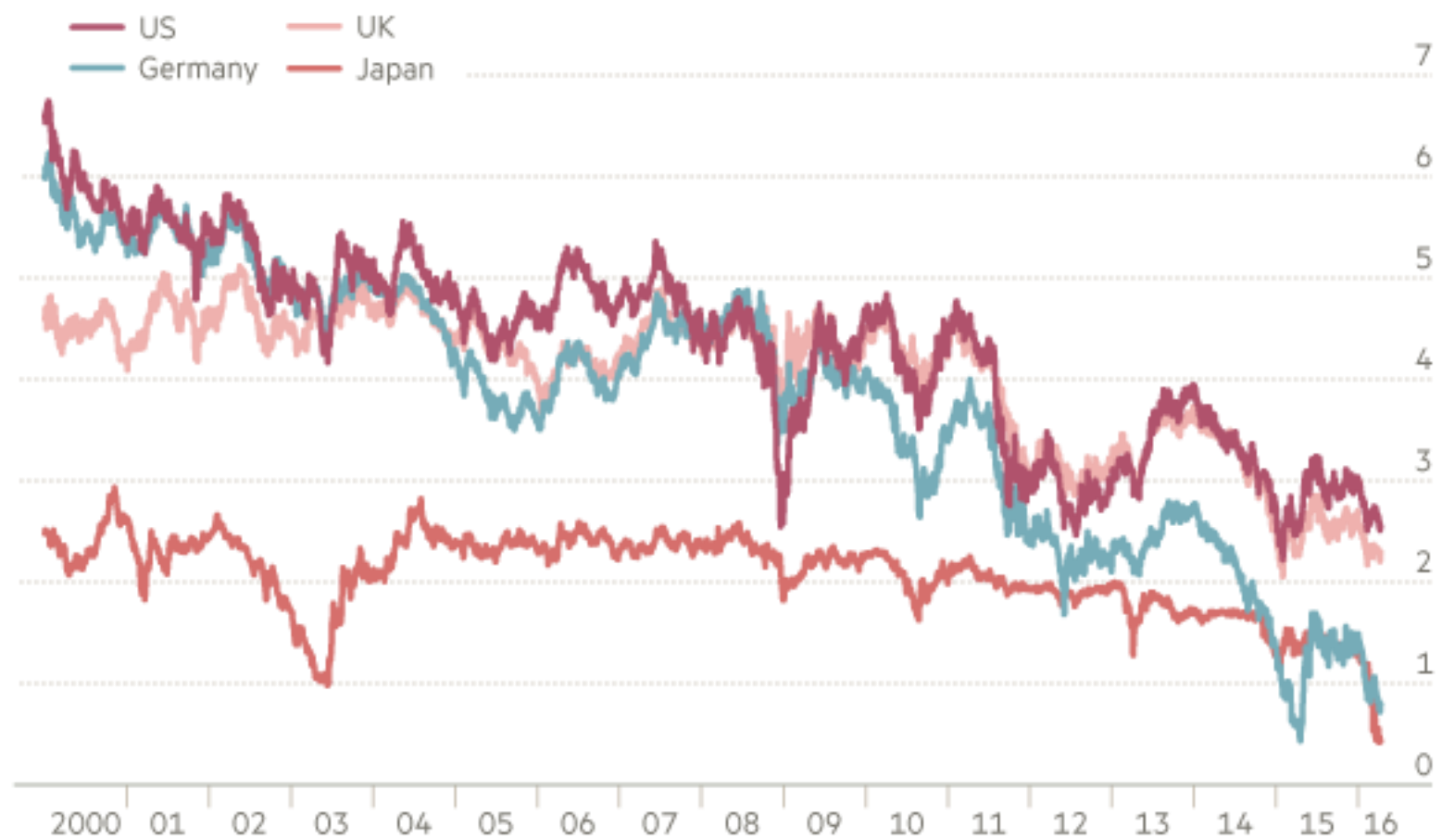


Source: JPMorgan

FT

Yield collapse

30-year bond yields (%)



Source: Thomson Reuters Datastream



Negative interest rates: the objective

- This stance of monetary policy aims at encouraging banks to lend (directly and indirectly), but there are doubts over its effectiveness, concerns about possible negative effects on bank profitability and the widespread volatility in financial markets.
- BoJ governor Haruhiko Kuroda: “The policy’s effects are showing in falling benchmark lending rates and mortgage rates,” ... “They will eventually spread to the real economy and consumer prices, and people will see the policy in a positive light.”
- Others, as Larry Fink, chief executive of BlackRock, said that there is not enough attention to negative effects of negative rates (e.g., on saving habits).

Negative interest rates: what does the data tell us?

- Are negative rates “special”?
- What are the implications?
- We need empirical analysis to understand the effects, and this is exactly what this paper is trying to do. The issue addressed in the paper is topical and important.

Impact of negative rates and identification

- The impact of negative interest rates on bank balance sheets. Are negative rates “special”?
 - Difficult to pass completely negative rates to customers (legal constraints, competition, etc...)
- Identification relies on the amount of excess liquidity that banks hold at the ECB, through their excess reserves and balances at the deposit facility.

What are the findings of the paper?

- Banks adjust their assets and liabilities in response to negative interest rates
- On average, banks increase their holdings of sovereign bonds, increase lending and decrease wholesale funding

First take on the paper

- Very well written paper, hypothesis and testing assumptions are well explained
- The empirical analysis and identification methodology is clearly explained

What are the findings of the paper?

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Identification through excess liquidity

- The analysis in the paper relies critically on the identification through excess liquidity
 - A bank having more excess liquidity in (t-1) is hurt the most by negative rates and therefore needs to adjust its balance sheet
- But excess liquidity is a highly endogenous variable
 - why do banks have excess liquidity in the first place?
- A detailed analysis of bank observable characteristics associated to higher and lower excess liquidity is needed
- What are the banks with higher excess liquidity? Presumably...
 - Big banks, with a lot of brokerage activities
 - Small, less sophisticated banks
 - Banks that are not part of big groups and cannot move liquidity freely inside the group

Identification through excess liquidity

- For the identification the use of the dummy is not enough, even with robustness checks
 - The authors compare periods of extreme volatility and crisis events (2008-June 2014) with a more financially stable period (post June 2014)
- Some suggestions:
 - Use event studies?
 - A difference in difference analysis around the policy shock?

What are the findings of the paper?

- Banks adjust their assets and liabilities in response to negative interest rates
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Increase in sovereign bond holdings

- The authors are looking at sovereign bond holdings, because they have the data on this
 - what about other similar assets? (like private debt for example)
 - what about higher and lower yield securities?
- The current analysis provides only some suggestive evidence on these issues (vulnerable and less vulnerable countries for example)

Back to the paper that I discuss

- What is the economic significance of the increase in loans?
- Do banks with different excess liquidity have the same lending opportunities? Do they get a similar number of loan applications and from similar borrowers? [the controls from the BLS are at aggregate level. Possible to use some bank-level data?]
- It is interesting that in more vulnerable countries lending actually decreases. Any intuition? [maybe in these countries banks' profitability is more negatively affected by negative rates...]

Back to the paper that I discuss

- The results on the decrease of wholesale funding are as expected
- ...but concerning this issue it seems that the analysis should be enriched with a control for banking groups. Banks that are part of groups should be able to move liquidity inside the group, therefore possibly biasing the results related to wholesale funding
- Aggregating by banking groups seems more important than looking at listed/non-listed banks

All in all...

- a very interesting and timely paper

Thank you!