Comments on Buch and Goldberg, “International Banking and Liquidity Risk Transmission: Lessons from across Countries”

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*The views expressed are my own and do not necessarily reflect those of the Federal Reserve Bank of Boston or the Federal Reserve System.
International Banking Research Network

• The IBRN is undertaking a commendable effort with a noble goal
• As multinational banks play an increasing role and as financial shocks are increasingly transmitted both rapidly and widely, it is extremely important to improve our understanding of the mechanisms underlying the international transmission of shocks.
IBRN Country Studies about the Transmission of Liquidity Shocks

- Bank-level micro data
- Common research method
  - Same baseline regression model
  - To produce comparable cross-country evidence
- Recognizing that banks are not homogeneous
  - Domestic banks with foreign operations
  - Domestic banks without foreign operations
  - Foreign bank branches and subsidiaries in host countries
  - In addition, there are differences in balance sheet characteristics
- Importance of internal capital markets (internal liquidity management) for multinational banks
- Importance of official sector liquidity provision
Dream the Impossible Dream

• But it’s complicated. . . very, very complicated.
  – Too much heterogeneity, both across banks and countries
  – Too many moving parts: banks make tradeoffs across many dimensions
  – Impossible to produce a simple story

• For example:
  – Domestic bank: Does it have foreign operations?
  – Domestic bank without foreign operations: Does it rely only on local funding or also on foreign funding?
    • If foreign funding, provider likely is less committed to an unaffiliated bank than to an affiliated branch or subsidiary (also information asymmetry between borrower and lender).
  – Foreign branch/sub in host country
    • A funding source for its parent FBO, or a loan origination source?
    • Relative importance for FBO; commitment to host country
    • Differences between branch and subsidiary operations
  – Direct cross-border lending into a country not done through a branch/sub in the country
  – Nature of shock
    • Global (systemic)
    • The parent (home country)
    • The host country (or even a host country other than the one being studied)
  – Availability of alternatives to bank credit (for example, bond market, nonbank lenders) differ across countries
Multi-Country vs. Individual-Country Studies

• There are major tradeoffs in terms of
  – Data detail and public availability of data
    • level of disaggregation
    • Bank coverage
  – Ability to control for loan demand, and thus isolate loan supply factors
    • Loan demand faced by a multinational bank not captured by host country loan demand
  – Questions that can be asked and potentially answered
    • FBO shock unlikely to be transmitted to all of its host countries to the same degree
    • Direct cross-border lending from HQ vs. through local affiliates in host countries (Equation 4 tries to pick some of this up). There is substantial evidence that direct cross-border lending shrank more than lending through affiliates in a host country during the crisis.
Concerns about the Specific Studies on Liquidity Shock Transmission

- LIBOR-OIS Spread: Can it be acting almost like a dummy variable for a short window of time?
- The effects of the crisis on banks, the financial system, and the real economy persisted much longer than the spike in the LIBOR-OIS spread.
Official Liquidity Facilities

• Using the facility certainly can alter a bank’s behavior.
• But, even if the facility is not used by a bank, knowing that access is available if needed can affect the bank’s behavior.
• Given the importance of internal capital markets, for multinational banking organizations it is access to a liquidity facility in it’s home country (or another host country) as well as in the country being studied that can matter.
  – For example, during the crisis, the U.S. provided substantial dollar funding to foreign banks.
Results

• Results make sense
• Easier to explain domestic loan growth insofar as determinants are more closely related to conditions in the country being analyzed, while cross-border lending depends on additional factors unrelated (or less related) to conditions in the country being analyzed. A multinational bank is pulled in many directions and must make tradeoffs across a number of dimensions.
• Access to official liquidity facilities affect bank behavior insofar as it relieves pressure on banks and can make differences across banks’ balance sheet characteristics less relevant.
Results

• Multinational banks make use of internal capital markets to adjust to shocks.

• Cross-border lending growth is more sensitive to liquidity risk. This can be related to the degree of a parent bank’s commitment to a host country as well as pressure from the home country’s government/regulators to have a home bias. It also may reflect that during the crisis, local affiliate lending declined by much less than direct cross-border lending from the banking organization’s headquarters.
Final Comments

• I applaud the formation of IBRN and the contributions that they have made, and will make, to our understanding of the international transmission of financial shocks.

• An additional benefit may be the added incentives for countries to collect more and better data on their own banks, with the benefits of further improving our understanding of important banking issues and perhaps contributing to better regulatory and policy decisions due to the additional information and understanding acquired.