

Can Unlimited Liquidity Provision Help to Avoid a Credit Crunch? Evidence from the Eurosystem's LTROs

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The views expressed in this discussions are my own and not those of the ECB or Eurosystem

Summary of the paper – Objectives

- Did the two LTROs have an effect on the supply of credit to French firms?
- Address two identification issues:
 - Disentangle credit supply and credit demand → *firm fixed effects*
 - Endogenous in-take of LTRO funding by banks → *bank balance sheets*
- Understand the transmission channels:
 - To which type of firms?
 - Through which type of banks?
- Effort to quantify aggregate effects

Summary of the paper – Results

- LTROs had a positive impact on the supply of credit:
 - To large firms, and to firms with many banks
 - Through capital-rich banks
- The first LTRO (December 2011) had a bigger impact than the second LTRO (March 2012)
- Overall, the net effect on firms was positive:
 - Firms did not substitute credit across banks
 - Back-of-the-envelope calculations suggest that every EUR-billion of funding resulted in a EUR107 million increase in loans to NFCs

Comment 1: Better understand the transmission channels of the LTROs

- Since October 2008, the Eurosystem has been implementing a FRFA policy: banks have their bids fully satisfied and can roll over “unlimited” funding
- Not so obvious why LTROs would have had an effect *above and beyond the FRFA MROs*: What is the specificity of LTROs?
- LTROs improve the “quality” of funding over FRFA MROs:
 - Safer funding: less uncertainty as to rolling over Eurosystem funding
 - Cheaper funding: interests paid out at the end and not compounded
 - LTROs helps bank comply with new liquidity regulation (?)

Comment 2: Specification

- Main specification in the paper focuses on the *intensive* margin only (i.e. on the degree of loan roll-over):

$$\log(L_{f,g,2012}) - \log(L_{f,g,2011}) = \alpha_f + \beta \frac{LTRO_g}{Assets_{g,2011}} + \gamma BS_{g,2011} + \varepsilon_{f,g}$$

- Why not look at *both intensive and extensive* margins?

$$\frac{L_{f,g,2012} - L_{f,g,2011}}{L_{g,2011}} = \alpha_f + \beta \frac{LTRO_g}{Assets_{g,2011}} + \gamma BS_{g,2011} + \varepsilon_{f,g}$$

$$\frac{L_{f,g,2012} - L_{f,g,2011}}{Assets_{g,2011}} = \alpha_f + \beta \frac{LTRO_g}{Assets_{g,2011}} + \gamma BS_{g,2011} + \varepsilon_{f,g}$$

Comment 2: Specification

- Why not look at $LTRO_g + MRO_g$?

$$\frac{L_{f,g,2012} - L_{f,g,2011}}{Assets_{g,2011}} = \alpha_f + \beta \frac{LTRO_g + MRO_{g,after}}{Assets_{g,2011}} + \gamma BS_{g,2011} + \varepsilon_{f,g}$$

- Funding quality versus funding quantity

$$\frac{L_{f,g,2012} - L_{f,g,2011}}{Assets_{g,2011}} = \alpha_f + \beta_M \underbrace{\frac{MRO_{g,before} - MRO_{g,after}}{Assets_{g,2011}}}_{\text{MRO replaced by LTRO (quality effect)}} +$$

$$\beta_L \frac{LTRO_g + MRO_{g,after}}{Assets_{g,2011}} + \gamma BS_{g,2011} + \varepsilon_{f,g}$$

Comment 3: Some results are hard to explain

- The first LTRO had a positive effect but not the second one. Is it really a “stigma” effect?
- LTRO–banks gave more credit to large firms that have short relationships with many banks. Could it reflect an increase in syndicated loans?
- LTRO–banks gave more credit but reduced credit lines
 - It looks like the banks with the most credit line exposures in Sept 2011 went to the LTRO in anticipation of those credit lines being drawn

Comment 4: Endogeneity of LTRO in-takes

	Total Credit		
	(1)	(2)	(3)
Bank LTRO	0.18 (0.36)	0.01 (0.47)	0.62*** (0.21)
Bank Size			0.10 (0.78)
Bank Liquid Assets			-0.13*** (0.04)
Bank Capital			0.17*** (0.06)
Bank Interbank Liabilities			0.22*** (0.05)
Bank ECB Dependence			-0.20** (0.09)
Bank Bond Rollover			-0.09 (0.14)
ECB MRO User			7.29** (3.32)
Foreign Bank			-2.53 (2.45)
Public Bank			-10.47*** (2.53)
Firm fixed effects	No	Yes	Yes

Comment 4: Endogeneity of LTRO in-takes

- Instrument $LTRO_g$
- Rule out reverse causality by checking that LTRO in-takes are independent of banks' *ex ante* loan portfolio characteristics, e.g.:
 - Banks' *ex ante* exposures to credit lines
 - Banks' *ex ante* loan portfolio quality (e.g. borrower size, profitability, rating)

Comment 5: Aggregate effects

- The estimations and back-of-the-envelope calculations are based on a particular sub-sample of (relatively large?) firms: those with bank loans in both 2011 and 2012
 - Small firms may be missing and the effects are hardly significant for small firms
 - Large firms are also the most likely to have direct access to markets and there may be a substitution between bank financing and bonds
 - ⇒ The effects may be over-estimated

Conclusion

- Difficult task
- Some more robustness checks needed
- Very nice paper