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# "Restoring Confidence in Systemically Important Banks: SSM Effects on Bank Performance"

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Disclaimer: The opinions expressed are those of the author and do not necessarily reflect those of the ECB or the Eurosystem

#### Motivation

- European banks dangerously weak in the early 2010s
  - Largely due to (and contributing to) sovereign debt crisis
  - Permanent doom loop
- Bank weakness has multiple consequences
  - Individual / systemic financial stability
  - Reduced ability to support real economic activity
- Banking Union (SSM, SRM, EDIS) aimed at stabilizing banks
  - Not yet complete
  - Evidence still not fully conclusive

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### This paper

- Positive effect of SSM on key bank parameters
  - Return on assets, income, lending, risk-taking
- Result mostly direct
  - Via higher profitability and lower risk, rather than via portfolio reallocation
- Stronger in peripheral than in core countries
- Does not pre-date the SSM
- Conclusion: "[..] the SSM has contributed to the recovery and stability of SSM banks by enhancing confidence in their soundness."

#### Assessment

- Interesting paper on an important question
- Generally solid analysis
- Believable results
- Some quibbles (two types)

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#### Absent-minded philosopher



Chapter 1. Theory

- What do we expect to find? Theory ambiguous
- On the one hand, supervision by local entities may be more rigorous
  - Local supervisors can monitor better (Laffont & Tirole 1993)
  - Local supervisors may extract superior information (Colliard 2020)
- On the other hand, centralized supervision may be more effective
  - Reduce the risk of cross-country arbitrage (Dell'Arricia & Maques 2006)
  - Higher supervisory independence (Rochet 2008)
- Discuss your results against this theoretical ambiguity

## Chapter 2. Sample

- <u>Comment 1.</u> Non-random selection of banks into treatment and control group
  - SSM banks many fewer and much larger than non-SSM banks
  - Need to make the sample more symmetric
    - Choose banks close to SSM threshold size-wise
  - Table 6, column 1: should be the baseline sample
- <u>Comment 2.</u> SSM and non-SSM banks different across multiple dimensions
  - We need to see this
    - Summary stats by group in Table 1, statistical differences
  - Propensity Score Matching procedure to choose pair-wise similar banks

Comment 3. Empirical model

• <u>Comment 1.</u> Time-varying variations common to SSM and non-SSM banks in a country

 $y_{it} = \mu_i + \lambda_t + \delta \cdot SSM_{it} + X'_{it}\beta + \epsilon_{it}$ 

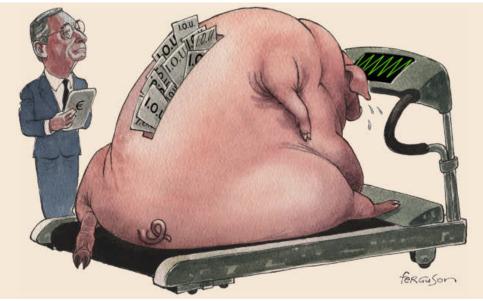
- Need to include country X time fixed effects
- Else, effect contaminated by, e.g., demand and growth opportunities
- <u>Comment 2.</u> Some effects observed already in 2013
  - Effect of Comprehensive Assessment (not discussed)
  - Compare to 2011-2012, as opposed to 2005-20012
- <u>Comment 3.</u> Effect may be driven by a global trend in increased soundness by large banks
  - Placebo test: EU but non-EA countries
  - Does effect obtain for pseudo-SSM vs. pseudo non-SSM banks?

# Chapter 4. Real effects

- Growth and stability: complements or substitutes?
  - Stability generates growth by increasing return to investment (Ramey and Ramey 1995)
  - Maintaining high growth necessitates the occasional crisis (Ranciere et al. 2008)
- Can we use the SSM implementation to learn something about this?
  - "Too feeble to spur growth" (FT 2014)
  - European banks safer and more

profitable (your results) ...

- ... but have they become more willing to support the right growth project?
- Or did the SSM spur a flight to safety?



• Put differently: Does higher bank safety stimulate or hinder growth?

### Conclusion

- Important and timely: Does supranational supervision work better than local one?
- Main result: SSM banks safer and more profitable
- We need more work like this to fully quantify the effect of the BU
- A few obvious loose ends to tighten (econometrics, trade-offs)
- Good luck! 🙂