

Discussion of

The Cyclical Behaviour of Bank Capital Buffers in an Emerging Economy: Size Does Matter

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The problem:

Cyclical downturn

- > more rating downgrades
- > higher capital requirements (as counterparty risk \uparrow)
- $> \downarrow$ loans
- > amplification of economic cycle



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Questions:

- How serious is this problem?
- Does the response depend on the size of banks?





Very well written introduction & presentation of theory

Nice and clean dataset

 (all inclusive unbalanced panel, quarterly & annual, 15 years)
 → you have it all (!): large and small, bust and boom
 (complete cycle and "major banking crisis", 1998 2000)



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$$\Delta B_{i,t} = \lambda \left(B_{i,t}^{*} - B_{i,t-1} \right) + \varepsilon_{i,t}$$

$$B_{i,t} = \lambda B_{i,t}^{*} + (1 - \lambda)B_{i,t-1} + \mathcal{E}_{i,t}$$

where $B_{i,t}$ is capital in excess of the 9%.





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estimate

$$B_{i,t} = \alpha + \beta \cdot B_{i,t-1} + X'_{i,t} \cdot \theta + \varepsilon_{i,t}$$
$$X' = [\Delta gdp, roe, NPL / L, \Delta loans, loans / asset]$$

dynamic GMM estimator (Blundell and Bond (1998))

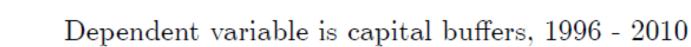




Dependent variable is capital buffers, 1996 - 2010

Variable	Coefficient	Standard Error
BUF(t-1)	-0.0785***	0.0181
ROE	0.0657	0.0901
RISK	1.012	1.091
DLOAN	-0.012**	0.006
LOANS	-0.005**	0.003
GDP	-0.132***	0.030
DUMMYSARC	0.523	0.498
DUMMYSIZE	-1.051**	0.489
INTERACT1	1.121***	0.211
INTERACT2	0.035***	0.004
INTERACT3	0.029***	0.005
CONSTANT	0.854	0.795
SARGANTEST (p-value)	0.79	
m1 (p-value)	0.00	
m2 (p-value)	0.86	





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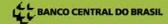
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DUMMYSIZE	-1.051**	0.489	
INTERACT1 (GDP*LARGE)	1.121***	0.211	
INTERACT2	0.035***	0.004	
INTERACT3	0.029***	0.005	



Dependent variable is capital buffers

	1996:3 - 2010:3		1993:3-2008:4	
Variable	Coeffi cient	Standard Error	Coefficient	Standard Error
BUF(t-1)	-0.0855***	0.0261	-0.0855***	0.0244
ROE	0.0799	0.0907	0.0740	0.0858
RISK	1.712	1.090	1.717*	0.676
DLOAN	-0.113**	0.049	-0.106**	0.045
LOANS	-1.640	1.402	-1.269	1.193
GDP	-1.210**	0.601	-1.231**	0.0601
DUMMYSIZE	-1.054**	0.495	-1.002	0.396
INTERACT1	1.151***	0.213	1.025	0.310
INTERACT2	0.047***	0.008	0.051	800.0
INTERACT3	0.051***	0.009	0.079	0.012
CONSTANT	0.964	0.886	0.682	0.756
SARGANTEST (p-value)	0.91		0.88	
m1 (p-value)	0.00		0.00	
m2 (p - value)	0.89		0.94	



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Finally,

when comparing the statistics of large and small banks over the years, you seem to have "natural selection" going on

- show size distribution;

- perhaps, compare subsample of those that were always large with those that were always small, as a robustness check.





In summary:

A nice paper that uses a comprehensive dataset to address an important issue within the context of an emerging market

Smoothing the rough edges on the estimation could strenghten your case for cyclical capital buffers.





Cyclical Buffers

Questions:

should they be top-down (system wide) or bottom-up (bank-specific) ? if they are system wide, should they vary as the bank size distribution varies ?

to which extent can cyclical reserve requirements in EMs do the job that cyclical capital buffers are expected to do ?



