

Discussion of “Managing Regulatory Pressure: Bank Regulation and Corporate Bond Intermediation”

by Andreas Rapp and Martin Waibel
(Federal Reserve Board)

Filippo De Marco
(Bocconi University & CEPR)

Big Picture – Dealers and liquidity

- Bank dealers are key in OTC markets, where search costs are high, but their intermediation ability is constrained post crisis
 - Basel III (re)introduced a simple **supplementary leverage ratio** (SLR) on top of risk-based requirements for large banks
- Because the SLR does not differentiate between safe or risky assets, it may lead to **risk-shifting**, by **shedding low-yielding safe assets**
 - Particularly the case for Treasury
 - Most of the literature has focused on the lower liquidity in U.S. Treasury market because of these requirements (Duffie, 2018; Du et al., 2023; Infante et al., 2025...)
- This paper: focuses on intermediation in the **corporate bond** market instead

Big Picture – Dealers and liquidity

- Corporate bonds are **risky**
 - Corporate bonds were already subject to risk-weighted capital requirements before
- In money markets, dealers can drain reserves to extend lending without expanding balance sheets (Correa et al., 2025), but not in corporate bonds.
- SLR still binds (and same effect on low-yielding investment-grade bonds)

Cash (20) (RW = 0%)	Equity (8)
Other Assets (200) (RW = 50%)	Debt (212)

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Bond (10) (RW = 20%)	Repo (10)

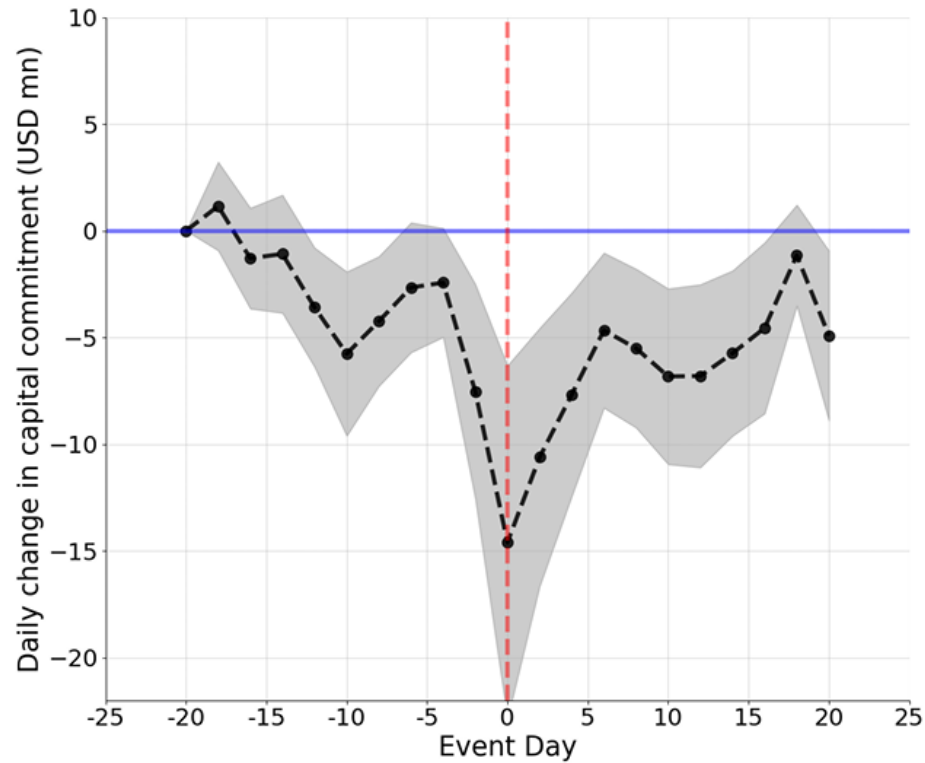
$$\text{LR} = \frac{8}{200+20+20} = 3.3\%$$

This paper

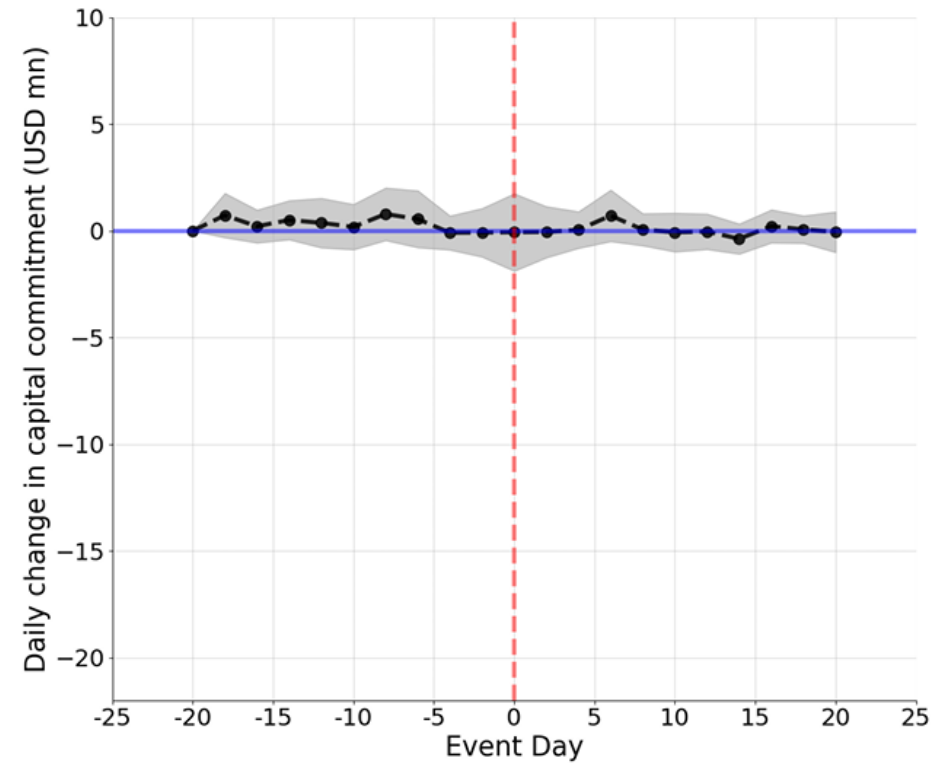
- Does Basel III (SLR in particular) reduce bond intermediation?
- Data: Regulatory TRACE (trades with dealer identity) + Mergent FISD
 - 135 million bond trades, 161 dealers (90 banks) for 30k bonds
- Identification based on Diff-in-diff at **quarter-end (QE)** reporting of regulatory capital ratios vs. non-bank dealers (not subject to any requirement)
- Heterogeneity of effects by:
 - US (average over quarter) vs. JP+EU bank dealers (end-of-quarter snapshot)
 - Investment-grade (IG) vs. high-yield (HY) bonds
 - Distance from regulatory minimum
 - ...

Results – event study

$$\text{Capital Commitment}_{i,t} = \sum_{k=-20}^{k+20} \beta_k D_k + \theta' \mathbf{M}_t + \alpha_{i,q} + \epsilon_{i,t},$$

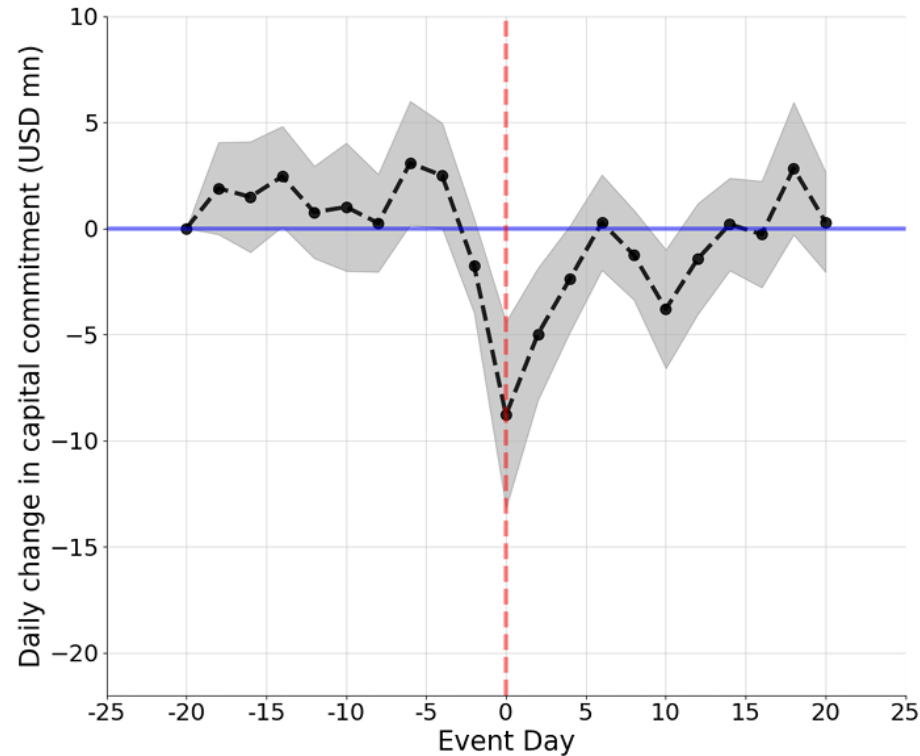


(a) Bank Dealers

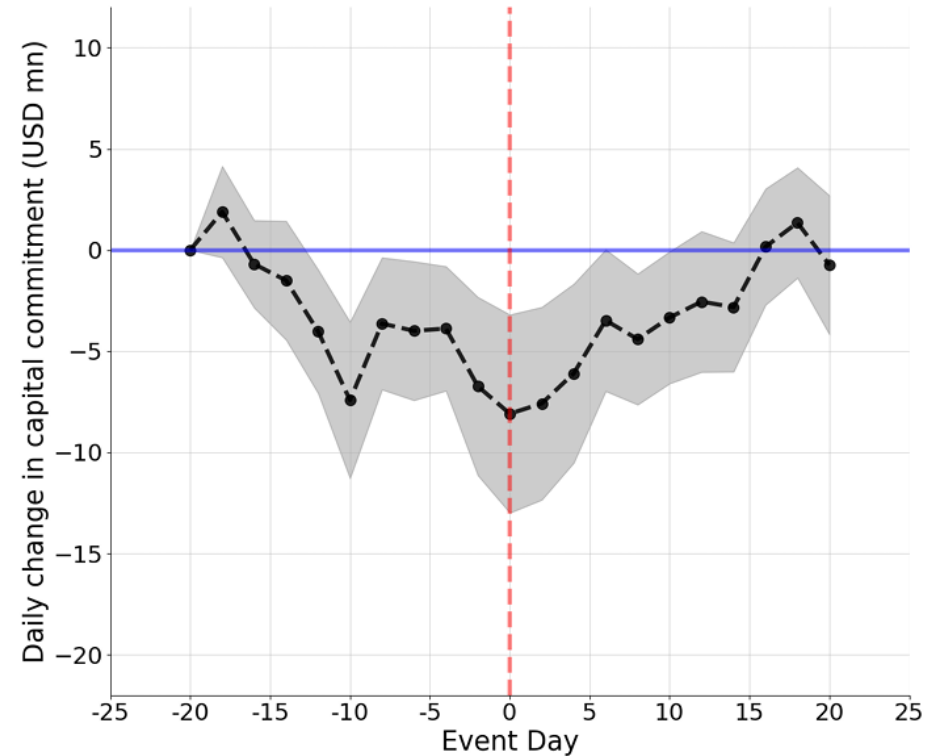


(b) Nonbank Dealers

Results – event study



Bank Dealers during
(c) Pre-Leverage Ratio Period



Bank Dealers during
(d) Leverage Ratio Period

- Visually, not immediately clear, but cumulative sell-off of about 12% before QE in panel c) vs. 40% in panel d)

Comments

- Very polished paper, with great data, important question and convincing empirical design
- Two main comments on the interpretation of the results:
 1. Quantification
 2. Implications for financial stability

1. Quantification of the effects

- “*daily reduction of around 6% of a standard deviation in dealer capital commitment*” – not very clear
- Can you quantify the effects with back-of-the-envelope calculations?
- Right now, coefficient of interest is the interaction of two dummies: $1[QE] \times 1[SLR]$: how much does +1pp in SLR affect bond selling? What is the effect on TotA and RWA?
- The event study evidence shows that the before QE sell-off is rapidly undone: Before SLR it was only a few days, afterwards about 2 weeks. **But is it really costly?**
- Table 10 goes in that direction: For large trades, bank dealers **increase transaction costs by 7.5%** relative to costs outside QE

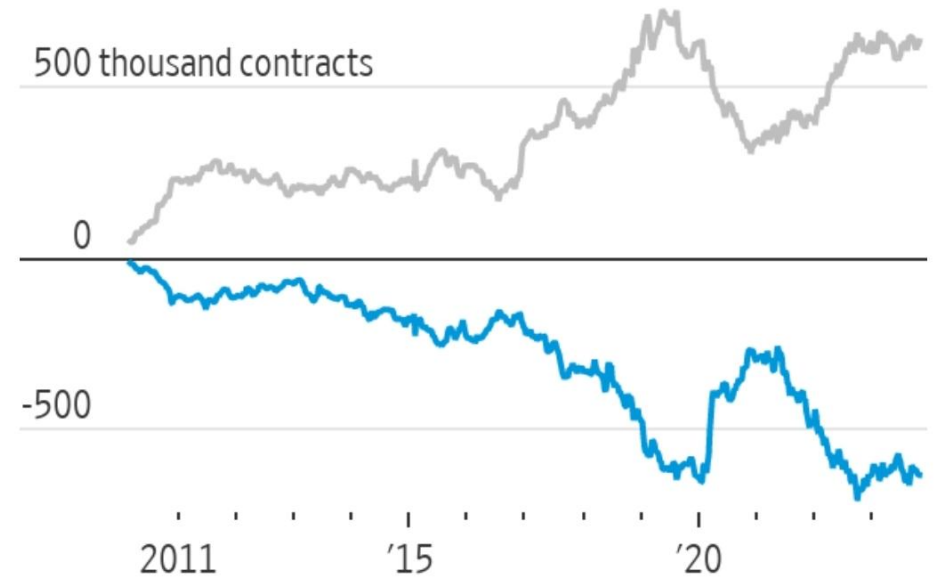
2. Implications of selling to non-bank dealers

- In the Treasury market, concern that hedge funds (highly leveraged, runnable, repo-funded, lightly regulated) have taken up the role of primary dealers
- But in the corporate bond market, insurance companies are the biggest holders ($\approx 40\%$)
- This paper: insurance companies step in and buy IG bonds preQE in leverage period
- Insurance companies become **liquidity-suppliers in corporate bond market**
- What are the financial stability implications? No concern as insurance are regulated, buy-and-hold?

Hedge funds have taken up the role of Treasury dealers, intermediating between sellers of the bonds and real-money investors

Treasury futures and options, net position

■ Leveraged funds ■ Asset managers



2. Implications of selling to non-bank dealers

- [Comerton-Forde, Ford, Foucault and Jurkatis](#) (2025) show that, during the March 2020 Dash-for-Cash, some investors stopped providing liquidity
- They study trading costs around downgrades from IG to HY (“fallen angels”)
- Dealers relying on **hedge funds are more resilient** to liquidity shocks
- In contrast, dealers relying **more on insurance companies** as a source of liquidity experience a significantly **larger increase in their trading cost**
- Why? Because insurance companies face constraints when investing in HY bonds
- So insurers may stabilize ordinary IG liquidity, but they may **create a different fragility**, amplifying cliff effects around downgrades

Conclusions

- Strong paper, relevant questions and very rich set of results
- At the margin, I would just discuss the magnitudes of the effects and add something on financial stability implications
- I recommend everyone to read it and best of luck with the publication process!