Discussion of Bank Bold Holdings and Bail-in Regulatory Changes

Tiago Pinheiro

Financial Stability Department
Banco de Portugal

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The views expressed in this presentation are those of the author and do not necessarily reflect the views of Banco de Portugal or the Eurosystem.

Summary of the paper

- How does the composition of bank bonds held by credit institutions change with MREL and TLAC?
- Credit institutions increase the holdings of bank bonds eligible for MREL relative to the total holdings of bank bonds.
  - The effect is stronger for self-holdings: Banks increase more their exposure to their own MREL eligible bonds than to other banks' MREL eligible bonds.
- Credit institutions also increase the holdings of TLAC-eligible instruments relative to non-eligible ones.
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  - The question is about the impact of bank liability policies beyond bank capital policies.
  - The question can be informative about who bears the bail-in risk associated with MREL-eligible bonds.
- The analysis is well executed. Granular data with diff-in-diff approach. Allows for analysis about home bias, self-ownership, etc.

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  - The paper's hypotheses and the interpretation of results are written around credit institutions' incentives to hold bank bonds after MREL and TLAC.
  - The actual change in bank holdings of these exposures may have nothing to do with their incentives changing but with other market forces.
- Supply or demand effect?
  - The authors argue that using issuer-quarter fixed effects controls for the supply effect.
  - Issuer-quarter fixed effects controls for the overall supply of bonds of a given issuer. It does not control for changes in the composition of that supply.
  - Control for each issuer's change in the issuance of other liabilities that can also be used in bail-ins? Control for each issuer's MREL shortfall?

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- Is May 2016 the key policy date for the demand side effect of MREL?
  - Expectation that certain liabilities will be used in a bail-in were shaped in June 2012 at the time of the Commission's proposal.
  - Around June 2012 starts the sharp decrease in the weight of debt securities in euro area banks' main liabilities.
  - Perhaps the policy change in May 2016 is mostly a supply side shock as banks become informed about their MREL shortfalls.
- Policy changes affect incentives to issue and hold different types of liabilities, not just bonds.
  - Having this in mind is critical for inferences about the implication of results.
  - For example, the inter-linkages across banks may have decreased despite the increase in the exposure to MREL-eligible bonds because the exposure of credit institutions to the equity of other banks decreased.
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- Hard to generalize results to the banking sector (banks) when only 26 banking groups are observed – most of them G-SII.
- The number of observations stays constant across different specifications of each regression model.
  - This is unexpected. As issuer-quarter and holder-quarter fixed effects are added, I expect some observations to drop.
- In results related to the notional amounts there is a significant change in the magnitude of the coefficient on the post-policy dummy when issuer-quarter fixed effects are added.

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  - Nominal values are not directly comparable across different bonds. Terms and conditions are different.
  - MREL-eligible bonds may have a large nominal value but may also be sold at a significant discount such that banks' exposure to MREL-eligible bonds may actually decrease after the policy.
  - A discount is likely if MREL-eligible bonds become riskier after the policy and no adjustment in other credit terms is made to compensate for the additional risk.
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  - In section 3.3, p.25: '...MREL requirements contributes to increase the home bias in banks' cross-holdings...'.
  - Table 7 results show that the introduction of MREL reduces the likelihood of holding bonds in the same country but less so if bonds are MREL-eligible.
  - To look at the impact of MREL on same country holdings you need to look at both the post*same_country coefficient and the post*same_country_eligible and then you need to weight them according to the share of eligible bonds relative to total bonds.

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