# Discussion of "Macroprudential Policies, Capital Flows, and the Structure of the Banking Sector"

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*Usual disclaimer applies*

# Summary

- **Objective**:

  Examining the role of macroprudential policies to contain cross-border bank inflows and how the structure of the banking sector may affect the effectiveness of respective policies.

- **Methodology:**

  Panel Least Square on data of 66 countries over the period of 1999-2012.

# Summary

**Key findings**:

- Strong and robust evidence for marginal effectiveness of MPPs to contain international bank inflows.
- Higher regulatory quality, a higher loan-to-deposit ratio, and a lower cost-to-income ratio strengthen the effectiveness of MPPs.
- Externalities of MPPs in forms of spillovers across asset classes and across countries are also depends on similar characteristics of the domestic banking sector.

**Contribution:**

- This study highlights that the structure of domestic banking sector is an important factor for effectiveness as well as externalities of MPPs

# Comment 1

- Regulatory quality, profitability, intermediation behavior, concentration, and foreign bank penetration to characterize the structure of the banking sector.
- However, the resilience/ soundness and risk-taking behavior of the banking sector are not included.
- Hermann & Mihaljek (2010), Brunneirmeir, *et al*. (2012), and Cerutti, *et al*. (2015): resilience or soundness of the financial sector and perceived risk-taking behavior are determinant of investors' appetite that may affect capital flows.
- Suggest to include either leverage level of banking sector as a proxy for banking risk-taking behavior or capitalization level (eg. CAR or Equity/TA) as a proxy for banking resilience.

# Comment 2

- Cost-to-income as a proxy for profitability which is also a measure of operational efficiency.
- Suggest to have net interest margin (NIM) or spread between credit and deposit interest rates (Hermann & Mihaljek ,2010) as another robustness check for banking profitability.
- NIM is also a measure of price efficiency, that is more inline with the credit-to-deposit ratio as a proxy for interest rates based of intermediation activities.
- Moreover, the standard transmission channel of the monetary policy is closely related to the impact of interest rates changes on credits and deposits.

# Comment 3

- There is a potential two-way causality effect between domestic intermediation activity and cross-border bank inflow (eg. Lane & McQuade, 2013).
- Authors utilize lagged credit-to-deposit and credit growth.
- Another method to overcome this concern as well as to control for potential omitted-variables bias is two stages IV regressions.
- 1st stage, credit-to-deposit ratio or credit growth could be instrumented with variables such as banking capitalization (CAR), risk-taking behavior (loan loss provision ratio), and domestic MPPs on intermediary activities (eg. LTV, debt-to-income ratio, reserve requirement, etc).
- 2nd stage, the estimated credit-to-deposit ratio or credit growth will be employed as an explanatory variable in the main regressions.

# Comment 4

- Authors utilize a dummy of domestic banking crises (pull factor) to check if the results are driven by crises periods.
- It is also possible that the 2007/08 global financial crisis-GFC (push factor) may affect the cross-border bank flows as in Hermann & Mihaljek (2010).
- Suggest to set a time dummy variable of post GFC and to interact it with financial variables.
- Next, to distinguish the analysis between emerging markets and advanced economies as the crisis started in some of developed markets with spillover impact on emerging markets.
- Is there any difference in the role of domestic banking structure on the bank capital flows: pre and post the 2007/08 GFC in each group?

# References


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- Banks and cross-border capital flows: Policy challenges and Regulatory Responses, Committee on International Economic Policy and reform. (Brunnermeier, *et al*. 2012)
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- Domestic credit growth and international capital flows. (Lane, P. R. and McQuade, P., ECB Working Paper Series No.1566, 2013)
- Global liquidity and drivers of cross-border bank flows. (Cerutti, E., Claessens, S., and Ratnovsky, L., 2015)