Discussion of
Haoyu Gao, Hong Ru, Robert Townsend, and Xiaoguang Yang
Rise of Bank Competition: Evidence from Banking Deregulation in China

By

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A good empirical paper might need

- A nice data set

- A shock

- A good question

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- A nice data set
  - Loan level data from 19 largest banks as reported to China Banking Regulatory Commission
- A shock
  - A relaxation of the bank branching rules
- A good question
  - What are the effects of greater competition among banks on efficiency and financial stability?

- The paper’s answer:

Greater bank competition leads simultaneously to

(a) Better loan terms to borrowing firms (benefit)
(b) More loans to SOEs with political connections (which the authors interpret as bad outcome)

1. Confounding Factors?

- Massive stimulus package during end of 2008-end of 2010
  - 1 trillion extra fiscal package
  - 3 trillion extra bank loans
- Could the stimulus package affect the lending by the two types?
- For example, the stimulus package might require all banks to make more loans to SOEs
- How the city banks do that? By stealing clients from majority state owned banks

2. Sample Bias?

- Underlying Loan Data: 19 banks
- Sample used in the paper: big 4 + 12 city banks (joint equity banks)
- Why excluding two other banks
  - In particular, Bank of Communication in particular
  - Does it behave like Big 4 or City 12 or neither?

3. Heterogeneity across Banks?

- Heterogeneity among the city-12?

  How special is China Merchant Bank?

  Which of the conclusions regarding the city-12 hold once CMB is excluded?

- Heterogeneity among the Big-4
  - ICRC is said to be more market oriented, and BOC is said to be more politically motivated
  - Are such differences reflected in their lending behavior?

4. Interpretation of the results

- Does the fact that City-12 make more loans to SOEs socially inefficient?

- Not necessarily
  - SOEs are heterogeneous
  - Do City-12 make more loans to the relatively good risks among the SOEs?
  - Would be more helpful to explicitly measure borrower heterogeneity in terms of risk profile beyond the SOEs and non-SOEs classification

5. Generalizability?

- The motivating statement: financial liberalization could simultaneously raise efficiency but undermine financial stability
- The authors would like to sell the paper as offering empirical evidence supporting this general proposition
- Is this general or China-specific?
- However, if the source of distortion in the economy is SOEs receiving more bailout help, then the nature of "outcomes" following the financial liberalization might not apply to other countries

Summary

The data set is very rich (envy by many)

The analysis might be further enriched with attention to various kinds of heterogeneity across cities, banks, and borrowers.