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Research Newsletter

DeNederlandscheBank
EUROSYSTEEM

Latest news

Andreas Pick has become Director of Graduate Studies at the Tinbergen institute.

The paper 'Cyclical Changes in Firm Volatility' by Emmanuel De Veirman (DNB) and Andrew Levin (Dartmouth College) has been accepted for publication in the *Journal of Money, Credit and Banking*. Using a new measure for firm-specific volatility in sales and earnings growth, this paper finds that the negative association between firm-specific volatility and the business cycle is weaker than earlier research suggests. During the Great Recession of 2007-2009, firm-specific volatility increased moderately but never substantially exceeded its sample mean. These results are inconsistent with the hypothesis that firm-specific volatility is an important driver of the business cycle, as it theoretically could be through an effect of default risk on credit spreads. While earlier literature has emphasized a trend increase in the volatility of publicly traded firms, the authors find that a typical publicly traded firm has become more stable.

A paper by Razvan Vlahu (jointly with Martin Brown, University of St. Gallen, and ››

DNB at ASSA conference San Francisco

This year only a small delegation of DNB (Jakob de Haan, Natalya Martynova and Iman van Lelyveld) visited the ASSA conference as we were not hiring new staff this year.

Iman presented a paper entitled 'A Dynamic Network Model of Unsecured Interbank Lending Market' (joint work with Bräuning and Blasques (VU University, Amsterdam)). In this paper the authors introduce a dynamic network model of interbank lending and estimate the parameters using network statistics of the Dutch interbank market from 2008 to 2011. They find that credit risk uncertainty and peer monitoring are significant factors in explaining the sparse core-periphery structure of the market and the presence of relationship lending. Shocks to credit risk uncertainty lead to extended periods of low market activity, amplified by a reduction in peer monitoring. Moreover, changes in the central bank's interest rate corridor have both a direct effect on the market as well as an indirect effect by changing banks' monitoring efforts. This is very important for the discussion about where and how to set the corridor.

Natalya presented her paper (joint work with Enrico Perotti, University of Amsterdam) in which they study how contingent capital (CoCos) that converts in equity ahead of default affects bank risk-shifting. Going concern conversion restores equity value in highly levered states, thus reducing heightened risk incentives. In contrast, conversion at default for traditional bail-inable debt has no effect on endogenous risk. The main beneficial effect comes from reduced leverage at conversion. In contrast to traditional convertible debt, equity dilution under going concern conversion has the opposite effect. Any value transfer to equity holders upon conversion provides better incentives. CoCo capital may be less risky than bail-inable debt when lower priority is compensated by lower endogenous risk, which is beneficial as a lower bond yield improves incentives. However, the highest risk reduction effect can be achieved with pure equity.

In one of the sessions, Linda Goldberg (Federal Reserve Bank of New York) presented a paper based on a joint research project of the International Banking Research Network (IBRN), in which also DNB participates. In this paper, 'Cross-border regulatory spillovers: How much? How important?' (co-author: Claudia Buch of the Bundesbank) the authors report on the outcomes of the second project of the IBRN, examining spillover effects of changes in prudential policies. Two types of spillover effects are considered: inward and outward. The analysis for the Netherlands (written by Jon Frost, Neeltje ››

van Horen and Jakob de Haan) focuses on outward spillovers. The Netherlands presents a unique testing ground for analyzing the outward transmission of prudential regulation, i.e. the impact of changing prudential regulation in country j on lending by foreign banks to country j. The Dutch economy has a large banking sector relative to GDP and several banks have significant foreign activities. In contrast to many other national banking sectors, which often have a strong regional focus, Dutch banks have a global footprint. While the European Union (EU) accounts for 58% of foreign activities, Dutch banks are also active across North American, Asian and Latin American markets. The authors report evidence that Dutch banks increase their foreign lending in countries that tighten prudential regulation, and decrease such lending when regulation is loosened. Looking at relevant sub-samples, they find that this result is driven particularly by larger banks, lending to advanced economies, and the post-crisis period.

Latest news

Stefan Trautmann, University of Heidelberg) titled 'Understanding Bank-Run Contagion' has been accepted for publication in *Management Science*. The paper examines through which channels and under which information conditions a panic-based run by depositors at one bank may trigger a panic-based run at another bank. A clear message emerging from the analysis is that when banks are economically related (i.e., through asset commonality), the observed behavior of well-informed depositors influences the behavior of less-informed depositors by providing a noisy signal of bank fundamentals. However, the main channel through which contagion occurs is not through an updating of beliefs about bank fundamentals, but through an updating of beliefs about the other depositors' withdrawal behavior. Thus observed withdrawals can become contagious even if they only have a modest impact on beliefs about bank fundamentals. From a policy perspective these findings suggest that economic linkages across banks due to common asset exposure and/or similar portfolio characteristics may have a further negative impact on financial stability beyond their direct economic impact on banks' financial statements and equity returns.

Newton meets Van Leeuwenhoek

Martijn Boermans en Robert Vermeulen.

In a forthcoming article titled 'Newton meets van Leeuwenhoek: Identifying international investors' common currency preferences' Martijn Boermans and Robert Vermeulen show the importance of the currency denomination of bonds for euro area investors. First, the authors investigate whether euro area investors prefer euro denominated bonds over bonds denominated in a foreign currency. Second, the authors investigate whether it matters whether a bond is issued by a company or government from a euro area country or a company or government from a non-euro area country. The main results show that euro area investors find it very important whether a bond is denominated in euros. In fact, euro area investors double their holdings of a bond if it is denominated in euros, all else equal. On the other hand, whether a bond is issued by a company or sovereign from a euro area or non-euro area country does not seem to be so important, all else equal.

The main innovation of this study is the ability to distinguish between the importance of currency denomination and the home country of the issuer, which in this setting no study has been able to do before. The authors were able to make this distinction by using the ECB's Securities Holdings Statistics. This database contains highly detailed information on the ownership of individual bonds. So, a microscope was needed to analyse this dataset. On the other hand, the authors had to take into account that investors prefer bonds which are issued by companies and governments close to their home country. To take these investor preferences into account, a so called gravity model was estimated, which is a very common model to explain international asset holdings in the academic literature.

There are several explanations for the strong preference of investors to hold euro denominated bonds. Probably the most important reason is the desire of large institutional investors to match their assets with their liabilities and avoid currency risk. For example, banks attract euro denominated deposits, so they have a strong preference to hold euro denominated bonds to avoid currency risk when depositors withdraw their funds and banks need to sell assets. In the same vein insurers and pension funds promise their clients an income stream in euros, so they prefer assets in euros. Therefore, euro denominated bonds issued by non-euro area companies and governments are an attractive asset class. However, investors need to assure themselves that the bond issuer also has an income stream in euros and/or that the firm/government has a healthy

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debt level. Otherwise, the bond may be riskier than first thought, for example, emerging market debt issued in euros may become riskier when emerging economies stagnate irrespective of the bond's currency denomination.
For more details, the full article can be accessed online via http://dx.doi.org/10.1016/j.frl.2016.01.005
Boermans, M. and Vermeulen, R. (2016), Newton meets Van Leeuwenhoek: Identifying international investors' common currency preferences, Finance Research Letters, forthcoming.

Introducing: Sweder van Wijnbergen

We are very proud that Sweder van Wijnbergen has joined DNB as special advisor. Below Sweder introduces himself.

I was trained as a physicist but got my PhD in Economics, at MIT in the US. I have always been interested in the challenges posed by real world problems and policy questions, which explains why I joined the World Bank after graduating from MIT. At the Bank I worked as chief economist for Central and Eastern Europe after the fall of the Wall, and before that in the same position for Mexico and Central America during the Brady deal debt restructuring and the NAFTA negotiations. After leaving the World Bank in 1993 I was extensively involved in the reform and transition process in Eastern Europe and Central Asia, and later again in Mexico and the Middle East, as advisor to Central Banks and Finance ministers in the region. I also spent several years as an active policy maker as Secretary General of the Ministry of Economic Affairs. Since about five years I have been full time involved in teaching and academic research at the University of Amsterdam.

During all those years I have been actively publishing academic work, mostly in fields like macroeconomics, international economics and public finance. More recently I have redirected my attention to corporate finance, asset pricing and financial intermediation. And since the Lehman tidal wave hit the world economy, I have had a special interest in the interface between finance and macroeconomics, which happens also to have been the topic of my PhD thesis years ago. Examples are recent papers on Contingent Capital and Systemic Risk, on Bank Recapitalization and the duration of recessions, and on the link between financial sector fragility and the effectiveness of Keynesian demand stimuli.

Hence my interest in DNB: basically all difficult policy questions today involve one way or another Central Banks, and those are also exactly the issues that academic research has neglected in the past decennia. What should we think of QE, is it just a modern day exchange rate war or an effective strategy for economic recovery benefitting everybody? How can we strengthen commercial banks' loss absorption capacity without negatively affecting credit to the corporate sector? What exactly should policy makers think of the new buzz word, macroprudential policy? So I am starting with enthusiasm in my new position as an advisor within DNB, a unique place to be for anybody with an interest in real world policy making and the research necessary to make those policies effective in the challenging new environment the world is in these days.

Conferences

Forthcoming:

21-22 April 2016:
DNB Payments Conference 2016, Retail Payments: Mapping Out The Road Ahead. Location: De Nederlandsche Bank, Amsterdam
Call for papers: Link

22-23 April 2016:
Economic Policy Meeting

9-10 June
DNB-CEPR Conference on Bank Equity over the Cycle Link to CEPR
Deadline call for papers 15 February 2016.
avincentrous@cepr.org

7-8 September
Adaptive Learning Conference

DNB working-papers

Since the end of 2015 the following Working Papers have been published (no. 486-497), please use the following link:
DNB Working Papers no. 486-497

- **No 497** - Price level convergence within the euro area: How Europe caught up with the US and lost terrain again Marco Hoeberichts and Ad Stokman - 27 January 2016
- **No 496** - Consumption uncertainty and precautionary saving Dimitris Christelis, Dimitris Georgarakos, Tullio Jappelli and Maarten van Rooij - 26 January 2016
- **No 495** - Measuring financial cycles with a model-based filter: Empirical evidence for the United States and the euro area Gabriele Galati, Irma Hindrayanto, Siem Jan Koopman and Marente Vlekke - 26 January 2016

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- **No 494** - Why risk is so hard to measure Jon Danielsson and Chen Zhou - 5 January 2016
- **No 493** - Competing for savings: how important is creditworthiness during the crisis? Jacob Bikker, Dirk Gerritsen and Steffie Schwillens - 5 January 2016
- **No 492** - What drives public acceptance of reforms? Longitudinal evidence from the run-up of the increase of the Dutch retirement age Jante Parlevliet - 29 December 2015
- **No 491** - Family, friends and framing: A cross-country study of subjective survival expectations Federica Teppa, Susan Thorp and Hazel Bateman - 23 December 2015
- **No 490** - Banking products: you can take them with you, so why don't you? Carin van der Cruijsen and Maaike Diepstraten - 21 December 2015
- **No 488** - Pawn or Vigilant Watchdog? How board vigilance and board tenure moderate the effects of executive tenure on board functioning Irene Mostert, Dennis Veltrop, Paula van Veen-Dirks and Jakob de Haan - 21 December 2015
- **No 487** - Decision making in times of uncertainty: An info-gap perspective Yakov Ben-Haim and Maria Demertzis - 26 November 2015
- **No 486** - Demand and supply of mortgage credit Alex van de Minne and Federica Teppa - 17 November 2015

DNB Occasional Studies

Since November 2015 the following occasional studies have been published, please use the following link: Occasional Studies

- **Nr. 6 (2015):** Biases in supervision: what are they and how can we deal with them? December 2015. Remy Jansen and Margot Aelen
- **Nr. 5 (2015):** Longevity Risk Transfer activities by European insurers and pension funds. November 2015. Patty Duijm

Published contributions

Since November 2015 the following contributions have been published. Please use the following links:
Published Articles
Published Articles in Books

- **A macroprudential approach to address liquidity risk with the Loan-to-Deposit ratio**, Jan Willem van den End, The European Journal of Finance, 2016, 22(3), 237-253
- **Credit ratings and bond spreads of the GIIPS**, Tim de Vries and Jakob de Haan, Applied Economics Letters, 2016, 23(2), 107-111
- **Supervisory powers and bank risk taking**, Tanveer Shehzad and Jakob de Haan, Journal of International Financial Markets, Institutions & Money, 2015, 39, 15-24
- **An empirical analysis of excess interbank liquidity: A case study of Pakistan**, Muhammad Omer, Jakob de Haan and Bert Scholtens, Applied Economics, 2015, 47(44), 4754-4776
- **Banks' liquidity buffers and the role of liquidity regulation**, Clemens Bonner, Iman van Lelyveld and Robert Zymek, Journal of Financial Services Research, 2015, 48(3), 215-234
- **Bank regulation and financial fragility in developing countries: Does bank structure matter?**, Jeroen Klomp and Jakob de Haan, Review of Development Finance, 2015, 5, 82-90
- **How much does the public know about the ECB's monetary policy? Evidence from a survey of Dutch consumers**, Carin van der Cruijsen, David-Jan Jansen and Jakob de Haan, International Journal of Central Banking, 2015, 11(4), 169-218
- **The multi-layer network nature of systemic risk and its implications for the costs of financial crises**, Sebastian Poledna, José Luis Molina-Borboa, Sefarín Martínez-Jaramillo, Marco van der Leij and Stefan Thurner, Journal of Financial Stability, 2015, 20, 70-81
- **Firm entry, endogenous markups and the dynamics of the labor share of income**, Andrea Colgiaco and Lorenza Rossi, Macroeconomic Dynamics, 2015, 19(6), 1309-1331
- **A multiplex network analysis of the Mexican banking system: link persistence, overlap, and waiting times**, José-Luis Molina-Borboa, Serafin Martinez-Jaramillo, Fabrizio López-Gallo and Marco van der Leij, The Journal of Network Theory in Finance, 2015, 1(1), 99-138
- **The inclusive growth concept: Strengths, weaknesses, and a research agenda for Indonesia**, Pande N.L. Kusumawati, Paul Elhorst and Jakob de Haan, In: R.L. Holzhacker, R. Wittek and J. Woltjer (eds.), Decentralization and Governance in Indonesia, 2015, Heidelberg: Springer, 145-168
- **Reforming the architecture of EMU: Ensuring stability in Europe**, Jakob de Haan, Jeroen Hessel and Niels Gilbert, in: H. Badinger and V. Nitsch (eds.), Handbook of the Economics of European Integration, 2015, New York: Routledge
- **Managing Liquidity Risk: The LCR and Beyond**, Clemens Bonner, Paul Hilbers and Iman van Lelyveld (eds.), Risk Books, 2015

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- **Putting liquidity risk management into a wider context**, Jan Willem van den End, Iman van Lelyveld and Stefan W. Schmitz, in: C. Bonner, P. Hilbers and I. van Lelyveld (eds.), Managing Liquidity Risk: The LCR and Beyond, Risk Books, 2015, 215-238

- **The process of liquidity supervision**, Patrick de Neef, in: C. Bonner, P. Hilbers and I. van Lelyveld (eds.), Managing Liquidity Risk: The LCR and Beyond, Risk Books, 2015, 63-76

- **Liquidity regulation, the 2007-9 crisis and the regulatory response**, Clemens Bonner and Paul Hilbers, in: C. Bonner, P. Hilbers and I. van Lelyveld (Eds.), Managing Liquidity Risk: The LCR and Beyond, Risk Books, 2015, 13-34

- **Financial Markets and Institutions: A European Perspective**, Jakob de Haan, Sander Oosterloo and Dirk Schoenmaker, 2015 (3rd edition), Cambridge University Press

Forthcoming contributions

Since November 2015 the following contributions have been accepted for publication. Please use the following links:
Forthcoming Articles
Forthcoming Articles in Books

- **Adapting extreme value statistics to financial time series: dealing with bias and serial dependence**, Laurence de Haan, Cécile Mercadier and Chen Zhou, Finance and Stochastics

- **Cash versus debit card: the role of budget control**, Lola Hernandez, Nicole Jonker and Anneke Kosse, Journal of Consumer Affairs

- **Business cycle and vertical integration in Europe and Asia**, Ayako Saiki, International Journal of Economics and Finance

- **Newton meets Van Leeuwenhoek: Identifying international investors' common currency preferences**, Martijn Boermans and Robert Vermeulen, Finance Research Letters

- **The level effect of bank lending standards on business lending**, Koen van der Veer and Marco Hoeberichts, Journal of Banking and Finance

- **Preferential regulatory treatment and banks' demand for government bonds**, Clemens Bonner, Journal of Money, Credit and Banking

- **The impact of liquidity regulation on bank intermediation**, Clemens Bonner and Sylvester Eijffinger, Review of Finance

- **Household saving behaviour in the euro area**, Julia Le Blanc, Alessandro Porpiglia, Federica Teppa, Michael Ziegelmeyer and Junyi Zhu, International Journal of Central Banking

- **Introduction: Understanding global banking**, Jakob de Haan, Galina Hale and Kathryn Russ, IMF Economic Review

- **Market reactions to the ECB's Comprehensive Assessment**, Cenkhan Sahin and Jakob de Haan, Economics Letters

- **Understanding bank-run contagion**, Martin Brown, Stefan Trautmann and Razvan Vlahu, Management Science

- **Competition and prices by bank service line**, Wilko Bolt and David Humphrey, in: J. Bikker and L. Spierdijk (eds.), Handbook on Competition in Banking and Finance, Edward Elgar

- **European payment systems: Pricing, regulation and innovation**, Wilko Bolt, Nicole Jonker and Mirjam Plooij, in: T. Beck and B. Casu (Eds.), The Palgrave Handbook of European Banking, Palgrave Macmillan

- **Regulating interchange fees of card payments**, Nicole Jonker, in: J. Górka (Ed.), Transforming Payment Systems in Europe, Palgrave Macmillan

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