September 2021

DNB Research Newsletter

DeNederlandscheBank
EUROSYSTEEM

Research highlights

1. Bank interest rate margins in a negative interest rate environment

Negative policy rates

In recent years, the ECB and other central banks have reduced their policy rates below zero. Since then, an intense debate has emerged on the impact of negative rates on banks and monetary transmission. One of the key issues is that banks are reluctant to reduce deposit rates below zero. Because of this lower bound on deposit rates, negative policy rates hurt bank interest rate margins. This in turn could hinder monetary transmission. There may even be a "reversal interest rate" below which further rate cuts have a contractionary impact on the economy. Using bank-specific panel data, this paper investigates the impact of negative rates on euro area banks' interest rate margin.
Read more

2. Public trust only partly immune to COVID-19 pandemic

Public trust in banks, insurers, BigTechs and other people (generalised trust) is key. It is crucial for the adoption of financial products and services. Moreover, low trust in financial institutions may undermine financial stability. Public trust is especially important in turbulent times. However, little is known about the impact of the COVID-19 pandemic on public trust. Using two large-scale surveys among households in the United States and the Netherlands, DNB research sheds light on this topic. The results suggest that the pandemic did not have much effect on trust in banks and insurers. However, trust in BigTechs and trust in other people declined, especially in the US.
Read more

3. Heterogeneous wealth effects

New research shows significant heterogeneity of consumption responses to housing wealth shocks. Consumption responses are stronger for households with low cash-on-hand and households with high mortgage debt compared to the value of their house.
Read more

Publications (since mid-July 2021)

Working Papers

725 - Business dynamism, sectoral reallocation and productivity in a pandemic
Guido Ascari, Andrea Colciago, Riccardo Silvestrini

724 - The rise in the cross-sectoral dispersion of earnings expectations during COVID-19
Joost Bats, William Greif, Daniel Kapp

723 - Has the COVID-19 pandemic affected public trust? Evidence for the US and the Netherlands
Carin van der Cruijsen, Jakob de Haan, Nicole Jonker

722 - Trust in the ECB in turbulent times
Carin van der Cruijsen, Anna Samarina

721 - Bank interest rate margins in a negative interest rate environment
Jorien Freriks, Jan Kakes

720 - Determinants of trust in banks' payment services during COVID: an exploration using daily data
Michiel Bijlsma, Carin van der Cruijsen, Jester Koldijk

DNB Analyse

The impact of carbon pricing and a CBAM on EU competitiveness
Guido Schotten, Yannick Hemmerlé, Guus Brouwer, Maurice Bun, Moutaz Altaghlibi

Published journal articles

Sovereign debt ratings and the country composition of cross-border holdings of euro area sovereign debt
Leo de Haan, Robert Vermeulen
Journal of International Money and Finance, 2021, 119, 102473

Quantitative Easing and exuberance in stock markets: Evidence from the euro area
Tom Hudepohl, Ryan van Lamoen, Nander de Vette
Journal of International Money and Finance, 2021, 118, 102471

Effects of credit restrictions in the Netherlands and lessons for macroprudential policy
Gabriele Galati, Jan Kakes, Richhild Moessner
Financial History Review, 2021, 28(2), 237-258

The international spillovers of the 2010 U.S. flash crash
David-Jan Jansen
Journal of Money, Credit and Banking 53, 1573-1586

The heat is on: A framework for measuring financial stress under disruptive energy transition scenarios
Robert Vermeulen, Edo Schets, Melanie Lohuis, Barbara Kölbl, David-Jan Jansen, Willem Heeringa
Ecological Economics, 2021, 190, 107205

Financial stability and the Fed: Evidence from congressional hearings
Arina Wischnewsky, David-Jan Jansen, Matthias Neuenkirch
Economic Inquiry, 2021, 59(3), 1192-1214

Financial knowledge and trust in financial institutions
Carin van der Cruijsen, Jakob de Haan, Ria Roerink
Journal of Consumer Affairs, 2021, 55(2), 680-714

Do fiscal rules constrain political budget cycles?
Bram Gootjes, Jakob de Haan, Richard Jong-A-Pin
Public Choice, 2021, 188, 1–30

Trends in extreme value indices
Laurens de Haan, Chen Zhou
Journal of the American Statistical Association, 2021, 116(535)

Forthcoming journal articles

Dynamics and heterogeneity of subjective stock market expectations
Florian Heiss, Michael Hurd, Maarten van Rooij, Tobias Rossmann, Joachim Winter
Journal of Econometrics

Credit policy and the 'debt shift' in advanced economies
Dirk Bezemer, Josh Ryan-Collins, Frank van Lerven, Lu Zhang
Socio-Economic Review

Trust in financial institutions: A survey
Carin van der Cruijsen, Jakob de Haan, Ria Roerink
Journal of Economic Surveys

The long-run effects of pandemics on inflation: Will this time be different?
Dennis Bonam, Andra Smădu
Economics Letters

Joint decomposition of business and financial cycles: Evidence from eight advanced economies
Jasper de Winter, Siem Jan Koopman, Irma Hindrayanto
Oxford Bulletin of Economics and Statistics

Other publications

Pension funds' portfolio choices and investment beliefs
Dirk Broeders, Kristy Jansen
SUERF Policy Briefs No 170, September 2021

Prijsniveaus in oorspronkelijke twaalf eurolanden divergeren al jaren
Ad Stokman
Economisch Statistische Berichten, Kort online, 4 August 2021

Digital euro has potential in the Netherlands
Michiel Bijlsma, Carin van der Cruijsen, Nicole Jonker, Jelmer Reijerink
SUERF Policy Briefs No. 150, August 2021

Cross-sectoral dispersion in firms' earnings expectations during the COVID-19 crisis
Joost Bats, William Greif, Daniel Kapp

ECB Economic Bulletin, 2021(5), Box 2

The long-run effects of pandemics on inflation: Why this time may be different
Dennis Bonam, Andra Smădu
VoxEU, 18 July 2021

For a complete list of publications see our website

Events

Research seminars

Past

07 Sept 2021: How do People Respond to Small Probability Events with Large, Negative Consequences?
Mathias Trabandt (Goethe University Frankfurt)
09 Sept 2021: On the effectiveness of climate policiesConny Olovsson (Riksbank)
14 Sept 2021: Credit Fire Sales: Captive Lending as Liquidity in Distress
Sergio Mayordomo (Bank of Spain)
21 Sept 2021: US trade policy and the US dollar
Felix Strobel (Deutsche Bundesbank)
28 Sept 2021: Measuring Regulatory Complexity
Jean-Edouard Colliard (HEC Paris - Finance Department)

Forthcoming

05 Oct 2021: Time Variation in the News-Returns Relationship
Harry Mamaysky (Columbia Business School Directory)
30 Nov 2021: tba
Olivier de Jonghe (National Bank of Belgium)

Workshops and conferences

Forthcoming

05 November 2021: DNB Annual Research Conference

The DNB Annual Research Conference will take place online on November 5th. This year's conference aims to investigate how macroeconomic policies affect business dynamism and how that affects macroeconomic aggregates. Of particular interest are papers that study these issues in light of the current challenges posed by the ongoing Covid-19 crisis and the broader discussions around the transition to a low-carbon economy. The conference will feature five papers, a keynote speech, and a policy panel. John Cochrane will give the keynote talk. The panelists are Lucrezia Reichlin, Rick van der Ploeg and Eric Bartelsman. Soon, we will provide details for registration to this event. The preliminary program of the conference is available via this link.

Research highlights, details

1. Bank interest rate margins in a negative interest rate environment

Squeezed interest margin …

The paper presents a decomposition of banks' interest income into three parts: a lending margin, a funding margin and maturity transformation. This distinction is important to understand how banks are affected by negative rates and how they may respond. The decomposition provides important added value to the existing literature, which mostly focuses on broad profitability measures. The paper finds that banks' funding margins are reduced significantly, particularly for banks that rely on deposit funding. This is a gradual process: it may take several years before the full impact has materialized.

… but transmission to lending rates

At the same time, banks do pass on declining interest rates to their lending rates, which is a key component of monetary transmission. Together with the squeezed funding margin, however, net interest income is shrinking, which can undermine bank profitability and lending capacity.

Read more?

See DNB Working Paper 721 Bank interest rate margins in a negative interest rate environment by Jorien Freriks and Jan Kakes

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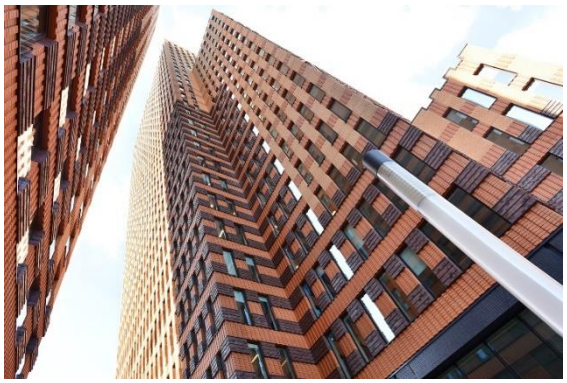
2. Public trust only partly immune to COVID-19 pandemic

Trust in BigTechs is low

Trust in BigTechs is lower than trust in banks, insurers and other people (trust in other people is often referred to as generalised trust). Only 26% of the Americans and 22% of the Dutch have pretty much or a lot of trust in BigTechs. All the others have not so much trust or absolutely no trust. In the US, trust in banks ranks first. 63% of the people have trust in banks, whereas fewer people have trust in other people and in insurers. In the Netherlands, generalised trust ranks first. 77% of Dutch people have trust in other people.



Trust only partly immune

The COVID-19 pandemic reduced trust in BigTechs and other people, especially in the US. Some 33% of Americans and 19% of the Dutch self-reported that they experienced a decline of trust in BigTechs. The share of people that experienced a trust increase is much smaller. The pandemic did not have much effect on trust in financial institutions in the US and the Netherlands.

People with poor health have lower trust

For both countries, we find evidence that people with poor health have lower levels of trust than healthy people, and that trust among less healthy people dropped more during the pandemic. The relationship between various other personal characteristics and trust differs across the US and the Netherlands. For instance, for the US, trust in other people, banks, insurers and BigTechs is lower for males than females, where the strongest gender effect is visible for trust in BigTechs. For the Netherlands the gender effect is only present for generalised trust and trust in BigTechs.

Read more?

See DNB Working Paper Has the COVID-19 pandemic affected public trust? Evidence for the US and the Netherlands by Carin van der Cruijsen, Jakob de Haan and Nicole Jonker.

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3. Heterogeneous wealth effects

House price developments and consumption: correlation or causation?

The impact of housing price shocks on consumption is not undisputed. Macro data do show a strong correlation between house price developments and changes in consumption. However, when studying this relation, researchers have to deal with endogeneity issues related to reverse causality and third (unobserved) factors driving the co-movement between house prices and consumer spending. The present study uses a novel survey approach and elicits information from hypothetical questions on exogenous housing wealth shocks (positive as well as negative). Inspired by similar studies on exogenous income shocks, this approach enables an investigation of individual marginal propensities to consume (MPC's) out of housing wealth shocks and its relation to sociodemographic and economic background characteristics.

MPC's out of housing wealth shocks are very heterogenous

While the average wealth effect is in the 2-5% range, the estimates reveal significant heterogeneity. Over 90% of the households in our sample reports no consumption adjustment to wealth shocks.

Households that do adjust report substantial consumption responses. Moreover, the consumption response to positive wealth shocks is greater than the response to negative shocks. This difference is consistent with a collateral channel mechanism. Increases in home values allow additional borrowing and spending, while decreases in home values do not necessarily require households to reduce borrowing given that the constraint binds only at the time of loan origination. In line with predictions of models with precautionary savings and liquidity constraints, we find a negative association between the wealth effect and cash-on-hand. Furthermore, homeowners with high loan to value (LTV) ratios are particularly responsive to adverse shocks.

The way forward

This research quantifies MPC's out of positive or negative house price shocks and provides information on several mechanisms by which house price shocks impact household consumption decisions. This information is relevant for economic analysis as well as for the design of housing policies. An interesting avenue for future research is to extend this approach to other countries with possibly different institutional features for the housing and mortgage market. One of the policy implications is that reducing high LTV's contributes to the mitigation of consumption responses to house price shocks and thereby alleviating boom-bust patterns in the Dutch economy.

Read more?

See publication in Europen Economic Review - Heterogeneous wealth effects by Dimitris Christelis, Dimitris Georgarakos, Tullio Jappelli, Luigi Pistaferri, and Maarten van Rooij

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