Newsletter no. 40, March 2019

Research Newsletter

DeNederlandscheBank
EUROSYSTEEM

Latest news

Theses successfully defended

On February 1, 2019, **Dorinth van Dijk** successfully defended his PhD thesis titled "Commercial and residential real estate market liquidity" at the University of Amsterdam (UvA). His dissertation explores several issues regarding the role of market liquidity in real estate assets, in particular for the Dutch residential and U.S. commercial real estate markets. Three main topics are addressed throughout all chapters. The first topic concerns the development of new ways to measure real estate market liquidity. The second topic addresses the link between changes in market liquidity and price developments. The third topic focusses on how market liquidity can be used by policymakers and market participants to get a better grasp on real estate markets.

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Report on DNB Research Programme 2018

The report about the DNB Research Programme 2018 is available here. In 2018 5 (out of 80) projects were stopped for various reasons, mostly due to lack of sufficient results or the fact that some researchers have left DNB. In 2019, 43 projects of the research programme 2018 will be continued. In 2018 38 DNB working papers have been published, compared to 27 in 2017. In 2018, 4 A publications, 18 B publications and 11 C publications have been published. At the beginning of 2018, 6 A and 27 B papers had been accepted for publication.

New A Publications

Bank Profitability, Leverage Constraints, and Risk-Taking

Authors Natalya Martynova, Lev Ratnovski and Razvan Vlahu; forthcoming in *Journal of Financial Intermediation*.

Traditional theory suggests that higher bank profitability (or franchise value) dissuades bank risk-taking. We highlight in this paper an opposing effect: higher profitability loosens bank borrowing constraints. This enables profitable banks to take risk on a larger scale, inducing risk-taking.
Our starting observation is that in Jensen and Meckling-type models, firms choose the risk of a portfolio of an exogenous (fixed) size. We show that bank risk-taking may take a different form when bank balance sheet size is endogenous. In our model, banks are endowed with a stable 'core business'. They use the implicit equity associated with the profitability of the core business to fund 'side activities' undertaken alongside the core business. Higher core profitability enables banks to borrow more and engage in side activities on a larger scale. Larger scale makes risk-taking in side activities more attractive. When higher core profitability enables an exceeding scale of side activities, even very profitable banks may choose to take risk. This effect is more pronounced when bank leverage constraints are looser, or when new investments can be financed with senior funding (such as repos).
The key implication of our analysis is that higher bank profitability (or, similarly, higher bank capital or franchise value) is not by itself a panacea against risk-taking. Profitable banks have superior capacity to borrow and therefore can rapidly accumulate risks.

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This dissertation is the result of a collaboration between the UvA and DNB. The advisors were Marc Francke (UvA) and Jakob De Haan (DNB and University of Groningen). During his PhD Dorinth was a visiting research at MIT and he is currently working as an economist at the Econometrics and Models department within the Economics and Policy division of DNB. An interview with Dorinth on his thesis is available here (in Dutch) and his thesis can be found here.

On 7 February **Irina Stanga** successfully defended her thesis entitled "Bank fragility and financial stability policies" at the University of Groningen. In this dissertation I investigate various causes of bank fragility and the effectiveness of key macro-prudential tools and bailout policies in preserving or restoring stability in the banking system. The results indicate that a high reliance on wholesale funding is associated with lower bank stability and the negative effects are amplified in a competitive environment. The liquidity risk of banks increases as they become susceptible to bank runs by wholesale financiers.

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Bank risk-taking should be understood as a dynamic concept. Regulators need to consider not only contemporaneous bank risks, but also the banks' ability to increase risk going forward. Such dynamic effects are particularly relevant when banks have easy access to scalable market-based investments.

Mining Matters: Natural Resource Extraction and Firm-level Constraints

Authors Ralph de Haas and Steven Poelhekke; *Journal of International Economics*, 117, 109-124

The extraordinary expansion in global mining activity over the last two decades, and its increasing concentration in emerging markets, has reignited the debate over the impact of mining on local economic activity. This paper analyses how the presence of nearby mines influences firms in nine countries with large manufacturing and mining sectors. Mines are found to out-compete local manufacturing firms for inputs, labour, and infrastructure. However, mining activity is found to improve the business environment on a wider geographic scale

Forthcoming Conferences

CALL FOR PAPERS
The 16th Corporate Finance Day

We invite paper submissions for the 16th Corporate Finance Day that will take place on September 19, 2019 at the University of Groningen, the Netherlands. Sponsored by De Nederlandsche Bank

Keynote Speaker:
Renée Adams is currently Professor at Saïd Business School, University of Oxford. Her research interests include corporate governance, group decision-making, and gender diversity. She has published multiple papers in top journals in finance and economics including JF, JFE, and RFS. Prof. Adams currently sits on the council of Society for Financial Studies, serves as a Finance Department Editor at Management Science and chairs the co-founded American Finance Association's "Academic Female Finance Committee"

Programme:
The conference will cover a broad range of topics in theoretical and empirical corporate finance. We welcome the global finance community: professors, postgraduate students, researchers, and government officials. The conference is also open to researchers who do not plan to present a paper.

Submission:
Please submit papers in PDF format to cfday@rug.nl. The deadline for paper submissions is May 26, 2019. Submitting authors will be notified within three weeks after this deadline. Authors of accepted papers may be asked to discuss a paper.

Logistics:
The conference fee is € 60, which covers documentation, lunch, and coffee breaks. Participants are responsible for their own travel expenses.

Conference website

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Therefore, a loan portfolio financed with high leverage implies higher overall risk even if it consists of safe assets. From a policy perspective, the analysis suggests that macro-prudential policies, and in particular lower regulatory loan-to-value ratios, are associated with a reduction in mortgage defaults. Finally, the results show that bailout policies were effective in reducing the default risk of banks, however they generated a risk transfer from banks to governments and amplified the bank-sovereign contagion channels in Europe.

22nd Annual Research Conference De Nederlandsche Bank

Uncertainty and Non-linearities: Policy Challenges and New Perspectives

Amsterdam, 30th September-1st October 2019

Keynote Speakers:
Jesus Fernandez-Villaverde (University of Pennsylvania) and Lars Peter Hansen (University of Chicago)

Uncertainty has received substantial attention recently. The Federal Open Market Committee identified uncertainty as a key factor in the 2001 and 2007–2009 recessions. Similarly, concerns about policy uncertainty have intensified in recent years. The International Monetary Fund suggested that uncertainty about U.S. and European fiscal and monetary policies contributed to a steep economic decline in 2008-2009 and slow recoveries afterward. Time variation and non-linearities in fundamental economic relationships imply that decision makers face new challenges and need new tools. Additionally, policy makers need criteria to select and interpret information coming from several, potentially misspecified, models.

We invite the submission of high quality theoretical and empirical papers that study the role of uncertainty and non-linearities for economic and policy analysis. Topics of interest include, but are not limited to:

- Model uncertainty, ambiguity;
- The conduct of monetary policy under uncertainty;
- Uncertainty shocks, time varying second moments, stochastic volatility;
- Incomplete information, higher order beliefs;
- Measures of uncertainty;
- Combining information from several models, model misspecification;
- Forecasting with non-linear models.

Manuscripts should be submitted to DNB_ResearchConference@dnb.nl by the 30th of May 2019. Authors of accepted papers will be notified by the 15th of June 2019.

DNB workingpapers

Since December 2018 the following Working Papers have been published, please use the following link

- **619** - Do information contagion and business model similarities explain bank credit risk commonalities? by Dieter Wang, Iman van Lelyveld, Julia Schaumburg 20 December 2018
- **620** - The impact of sovereign debt ratings on euro area cross-border holdings of euro area sovereign debt by Leo de Haan and Robert Vermeulen 28 December 2018
- **621** - The single supervisory mechanism: Competitive implications for the banking sectors in the euro area by Iryna Okolelova and Jacob Bikker 31 December 2018
- **622** - Did spillovers from Europe indeed contribute to the 2010 U.S. Flash Crash? by David-Jan Jansen 28 January 2019
- **623** - The global macroeconomics of a trade war. The EAGLE model on the US-China trade conflict by Wilko Bolt, Kostas Mavromatis and Sweder van Wijnbergen 1 February 2019
- **624** - Outlier detection in TARGET2 risk indicators by Ronald Heijmans and Chen Zhou 7 February 2019
- **625** - The heat is on: A framework for measuring financial stress under disruptive energy transition scenarios by Robert Vermeulen, Edo Schets, Melanie Lohuis, Barbara Kölbl, David-Jan Jansen and Willem Heeringa 25 February 2019
- **626** - Does monetary policy affect income inequality in the euro area? by Anna Samarina and Anh Nguyen 8 March 2019
- **627** - The impact of size, composition and duration of the central bank balance sheet on inflation expectations and market prices by Stephanie Titzck and Jan Willem van den End 8 March 2019
- **628** - Who creates and destroys jobs over the business cycle? by Andrea Colciago, Volker Lindenthal and Antonella Trigari 14 March 2019

DNB occasional studies (new since December 2018)

Since December 2018 the following occasional studies have been

published, please use the following link

Nr. 8 (2018): The price of transition: an analysis of the economic implications of carbon taxing by Gerbert Hebbink, Laurien Berkvens, Maurice Bun, Henk van Kerkhoff, Juho Koistinen, Guido Schotten en Ad Stokman (October 2018)

Published Articles in Journals

- **Mining matters: Natural resource extraction and firm-level constraints**
  Ralph de Haas and Steven Poelhekke *Journal of International Economics, 2019, 117, 109-124*
- **Loss shocks in export credit insurance markets: Evidence from a global insurance group**
  Koen van der Veer *Journal of Risk & Insurance, 2019, 86(1), 73-102*
- **Pension profile preferences: The influence of trust and expected expenses**
  Carin van der Cruijsen and Nicole Jonker *Applied Economics, 2019, 51(12), 1212-1231*

For published articles in journals please use the following link

Forthcoming Articles in Journals

- **System risk and bank business models**, Maarten van Oordt and Chen Zhou, *Journal of Applied Econometrics*
- **Endpoint estimation for observations with normal measurement errors**, Xuan Leng, Liang Peng, Xing Wang and Chen Zhou, *Extremes*
- **Consumption uncertainty and precautionary saving**, Dimitris Christelis, Dimitris Georgarakos, Tullio Jappelli and Maarten van Rooij, *Review of Economics and Statistics*
- **How competitiveness shocks affect macroeconomic performance across euro area countries**, Karsten Staehr and Robert Vermeulen, *The World Economy*
- **The cyclicality of R&D investment revisited**, Maurice Bun, Noud van Giersbergen, Kees Jan van Garderen en Hans van Ophem, *Journal of Applied Econometrics*
- **Cartel dating**, Maurice Bun, Peter Boswijk en Maarten Pieter Schinkel, *Journal of Applied Econometrics*
- **On the value of virtual currencies**, Wilko Bolt and Maarten van Oordt, *Journal of Money, Credit and Banking*
- **Is fiscal policy in the euro area Ricardian?**, Nikki Panjer, Leo de Haan and Jan Jacobs, *Empirica*
- **Central bank policies and income and wealth inequality: A survey**, Andrea Colciago, Anna Samarina and Jakob de Haan, *Journal of Economic Surveys*

For forthcoming articles in journals please use the following link

Forthcoming Articles in Books

- **ECB communication: Effects on expectations**
  Jakob de Haan
  In: Jaques Ziller (ed.), *The European Central Bank's Communication: An Instrument of Monetary Policy and a Vector of Accountability*, Giappichelli

For forthcoming articles in books please use the following link

Published Articles in Books

- **Detection and explanation of anomalies in real-time gross settlement systems**
  Ron Triepels, Hennie Daniels and Ronald Heijmans
  In: Hammoudi S., Śmiałek M., Camp O., Filipe J. (eds) *Enterprise Information Systems*. ICEIS 2017. Lecture Notes in Business Information Processing, 2018, vol 321. Springer, Cham
- **Utility-equivalence of pension security mechanisms**
  Dirk Broeders, An Chen and Birgit Koos
  In: J.A. Bikker, *Pension Fund Economics and Finance*, 2018, Routledge, London, 233-250
- **Pension fund economics and finance: efficiency, investments and risk-taking**
  Jacob Bikker (ed.) Routledge, 2018

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