Shock Absorbers and Transmitters: The Dual Facets of Bank Specialization

Rajkamal Iyer
Imperial, CEPR

Sotirios Kokas
U of Essex

Alex Michaelides
Imperial, CEPR

José-Luis Peydró
Imperial, CEPR

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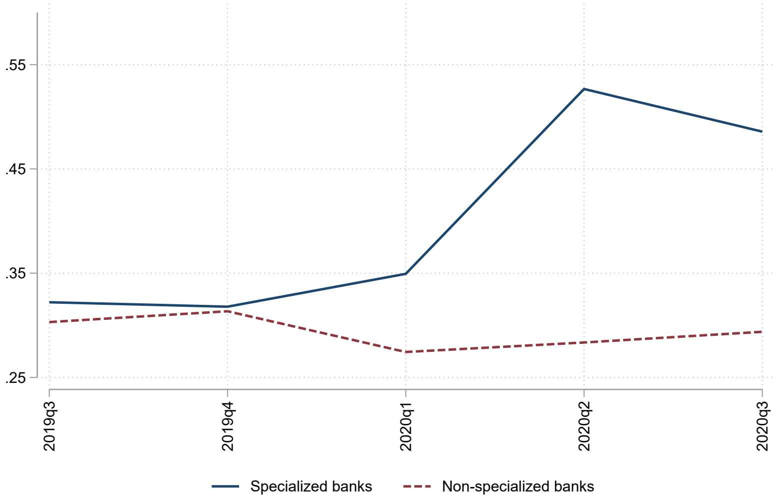
This paper

Research question

How does bank's lending specialization affect credit supply in the presence of industry specific shocks?

- We examine the role of bank specialization in the provision of credit post negative shocks to affected and unaffected sectors.
- We evaluate banks as shock absorbers **and** transmitters.
- We investigate the conditions under which this propagation has an effect on real economic activity.

Figure: Credit Shares in Hospitality and Aviation



Motivation

In the presence of negative sector-specific shocks:

+ Banks specialized in an affected sector will reduce lending to this sector due to lower (expected) profits (Freixas and Rochet, 08).

  $\longrightarrow$ *credit reallocation towards unaffected sectors*

- Loan pricing can increase sufficiently for banks specializing in the affected sector to make it attractive and secure a higher yield relative to lending to firms in unaffected sectors (Stein, 2013).

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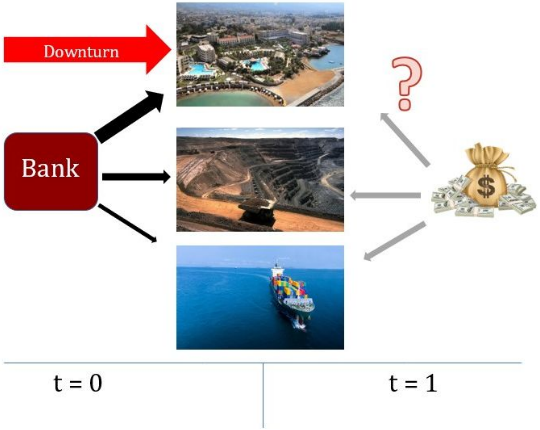
Framework



Preview of the main results #1

A. Loan-level

Specialized banks in distressed sectors:

- Increase credit to firms (by 5%) and charge higher lending rates (7-19 bps) in the distressed sectors.
- Lending to firm with better profitability outcomes up to 3 years after the loan origination.
- Reduce lending to firms in non-distressed and unrelated sectors by 2.3% (pass-through).

Preview of the results #2

B. Firm-level: Real effects

- Firms in the unaffected sectors do not experience any significant change in their total bank credit, total debt, size and employment.
- However, when financing frictions are high, firms in unaffected sectors experience an overall reduction in their bank credit, total debt, and employment.

C. Industry-level: Real effects

- We find that there is a reduction in bank credit and industry level real outcomes during turmoil.

Thank you!

For comments or questions please use:

skokas@essex.ac.uk
@skokas01