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Making room for the needy: The credit-reallocation effects of the ECB's Corporate QE

Oscar Arce, Ricardo Gimeno, Sergio Mayordomo

Discussion by

Diana Bonfim

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These are my views and not those of Banco de Portugal or the Eurosystem.

The one million dollar question:

How effective was QE?

The contribution of this paper:

How effective was CSPP?

How effective was CSPP (in Spain)?

Looking at it through two angles:

1) **Direct effects:**

- announcement and implementation dates
- quantity and price effects

2) **Indirect effects:**

- spillovers on access to bank loans from non-eligible firms (challenging task!)

Summary of the paper

Direct effects

Indirect effects

Main findings

1) **Direct effects:**

- announcement effects were larger than implementation effects.
- eligible firms issued more bonds, at lower costs.

2) **Indirect effects:**

- some banks experienced loan outflows from eligible firms.
- new loans channeled to other firms (mainly large and low risk firms).

1. What is missing from the picture?

Direct effects

Indirect effects

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1) Financing of Spanish firms abroad

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2) Holdings of corporate bonds by Spanish banks

Indirect effects

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Indirect effects

Direct effects

1) Financing of Spanish firms abroad

3) Details on outflows

1. What is missing from the picture?

1) Financing of Spanish firms abroad

- Eligible Spanish firms may be special.
- A Spanish investment grade firm that was able to issue bonds during the crisis, was probably **not very dependent** on Spanish banks.
- The **cost** of domestic bank financing probably exceeded significantly that of (international) bond financing.
- Often these firms borrow from **many banks** simultaneously.

It would be important to show evidence on all this.

1. What is missing from the picture?

2) Holdings of corporate bonds by Spanish banks

- How much? Where? From whom?
- **If banks sell** the bonds they're holding, this should be part of the **outflow** measure in the regressions.
- **If they do not sell**, the **price and liquidity effects** generated by CSPP might also offer room to grant new credit.

It's critical to control for all this (or show that it is not relevant).

1. What is missing from the picture?

3) Details on outflows

- How does CSPP affect lending **to eligible firms**?
- "The credit balance of groups that issue bonds in the quarter following the CSPP announcement diminished, on average, by around 20%." What are these "**loan cancelations**"?
  - Early redemptions?
  - Loans that are not renewed?
  - Regular loan payments?

1. What is missing from the picture?

3) Details on outflows

Suggestions:

- Illustrate, on aggregate terms, the substitution of bank loans by bonds in **banks** and **firms balance sheets** (before diving into the regressions).
- Show that funds released from **outflows are not going to bond issuers**, by running a modified version of equation 4 with another dependent variable.

2. What else is going on?

Monetary policy decisions

10 March 2016

At today's meeting the Governing Council of the ECB took the following monetary policy decisions:

(1) The interest rate on the main refinancing operations of the Eurosystem will be decreased by 5 basis points to 0.00%, starting from the operation to be settled on 16 March 2016.

(2) The interest rate on the marginal lending facility will be decreased by 5 basis points to 0.25%, with effect from 16 March 2016.

(3) The interest rate on the deposit facility will be decreased by 10 basis points to -0.40%, with effect from 16 March 2016.

(4) The monthly purchases under the asset purchase programme will be expanded to €80 billion starting in April.

(5) Investment grade euro-denominated bonds issued by non-bank corporations established in the euro area will be included in the list of assets that are eligible for regular purchases.

(6) A new series of four targeted longer-term refinancing operations (TLTRO II), each with a maturity of four years, will be launched, starting in June 2016. Borrowing conditions in these operations can be as low as the interest rate on the deposit facility.

2. What else is going on?

- There is an attempt to take the TLTROs on board.

However:

- This does not reflect the changes announced on **TLTRO II**;

- The variable TLTRO is defined as the amount of funds used up to January 2016 relative to the overall limit, but what it matters is **how far are banks from their benchmark** (when they face a penalty).

- For some banks, the way this benchmark is computed **changed** significantly in March 2016.

3. The control and treatment groups

- To examine the spillovers to non-affected firms, the authors examine the universe of 145,244 **non-issuing firms** in Spain (*out of 500,000?)*.

  Outflows are computed for **all bond issuers**.

$$Credit_{j,b} = \alpha + \beta_1 Outflows/TA_b + \beta_2 D.Size_j + \beta_3 D.Size_j x Outflows/TA_b + \delta F_j + \gamma B_b + \theta FB_{jb} + \varepsilon_{j,b} \quad (4)$$

- Some questions:

  - should all bond issuers be treated alike? (**eligible vs non-eligible**)

  - The ECB only bought bonds from **13 Spanish firms**.

  - What about **1st time bond issuers**? (11 out of 33 issues)

4. Estimation window

- Announcement date: March 2016
- Implementation date: June 2016

- Estimation window: February 2016 – June 2016

- Why leave out all that happened after the program actually started?

5. Are demand effects truly being controlled for?

- How can the pick-up in lending be disentangled from the overall recovery of the Spanish economy?

- One possible story is that **non-eligible/non-issuer firms are probably more dependent on the domestic economy** (and on domestic banks) than large, more internationally diversified firms. These firms might thus be starting to **ask for more credit**, compared to the other ones.

- A related intriguing **question**: why do non-eligible firms increase bond issuance? Why are the effects larger in some cases?

6. Minor comments

- Figure 1 shows that there was also a large effect on the bond yields of financial corporations – why?
- Are there bond upgrades from junk to investment grade during this period?
- Running weighted regressions could provide some more insights on aggregate effects.
- Show regressions without the interactions with firm size.

Overall assessment

- Very interesting and complete analysis.

- Important policy contribution.

- Tying some loose ends can provide even deeper insights.