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BANK CAPITAL AND BALANCE SHEET MANAGEMENT DURING TIMES OF DISTRESS: INTERNATIONAL EVIDENCE

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THE PAPER IN BRIEF

Da Rocha Lopes et al. (2025) Bank capital and balance sheet management during times of distress: international evidence

- **Do banks actively manage their equity capital and balance sheets in the short run?**

Bank equity capital → **Balance sheet managment**

Some of the previous models	• Bank capital is **exogenous** in the short run
This paper	• Bank capital is **endogenous** in the short run • Active forward-looking role of bank management

- **Empirical analysis: Two exercises**
  1. Partial adjustment model:
     1. *Estimation of each bank's target capital asset ratio* → $\hat{Z}$
     2. *Simultaneous equations: Δln(Balance Sheet) and* $\hat{Z}$
  2. Endogeneity of Management Action on Capital (MAC)
     1. *Single-equation model: MAC = f(distress,* $\hat{Z}_{t-1}$*…)*
     2. *Simultaneous equations system: Δln(RWA) and MAC*

- **Advances in modeling: Applicable to stress testing within a dynamic approach**

- **On the models**

$$\hat{Z}_{b,c,t} = 100 \times \left[\left(\frac{k_{b,c,t}}{\hat{k}^*_{b,c,t}}\right) - 1\right].$$

- $\hat{Z}$ is a crucial variable, but few explanatory variables are significant in the model for the reported CET1
    - *Should the model be revised? Consider dropping non-significant variables*

- Is it feasible to use <u>reported</u> target capital asset ratios [Couaillier (2021)] instead of <u>estimated</u> ratios?

- Are bank <u>fixed effects</u> truly necessary? If included, interpret with caution: avoid cross-sectional comparisons

- The baseline model addresses Nickell bias (GMM estimates)…but not the rest
    - *Also with lagged dependent variable and fixed effects*

SCOPE FOR IMPROVEMENT?

Da Rocha Lopes et al. (2025) Bank capital and balance sheet management during times of distress: international evidence

- **On the research design:**
  - Dataset: 172 banks, 26 countries. Further characterize and explore the sample
    - *Banks' size (Group 1/ Group 2)*
    - *Listed vs. non listed banks*
    - *Cross-country differences*
  - The Covid period is deliberately excluded, which limits the coverage of times of distress
    - *Why not expand the sample to include data from 2020 onward?*

- **On the distress definition**
  - Based on large unexpected loses (=negative profits). Potential limitations of this measure
  - Other forms of distress are not captured
    - *(e.g.: market volatility)*

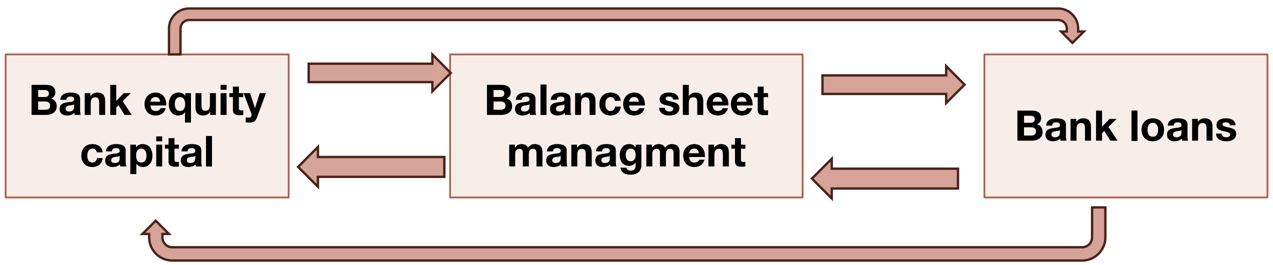
- **On the database**
  - QIS maintained on an anonymous basis. Difficult to match with external datasets. Is it a limiting factor?

SOME ISSUES TO CLARIFY

Da Rocha Lopes et al. (2025) Bank capital and balance sheet management during times of distress: international evidence

- **Further motivation for the definition of Management Action on Capital (MAC)**
  - MAC_3: ΔCET1 adjusted by the passive component of retained earnings…rationale behind?
  - Additional mechanisms of capital adjustment
    - *Dividend policies, equity issuance, asset sales (de-risking portfolios)*

- **There is no link to lending…Is an extension of the analysis in this direction feasible?**
  - The paper focused on the link between *Δln(RWA) and MAC*
  - How capital management decisions affect loan growth and credit availability?



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THANKS FOR YOUR ATTENTION!