

## de Andoain/Heider/Hoerova: “Excess liquidity and interbank market functioning under stress: Evidence from TARGET2 transactions”

Discussion by Kim Abildgren

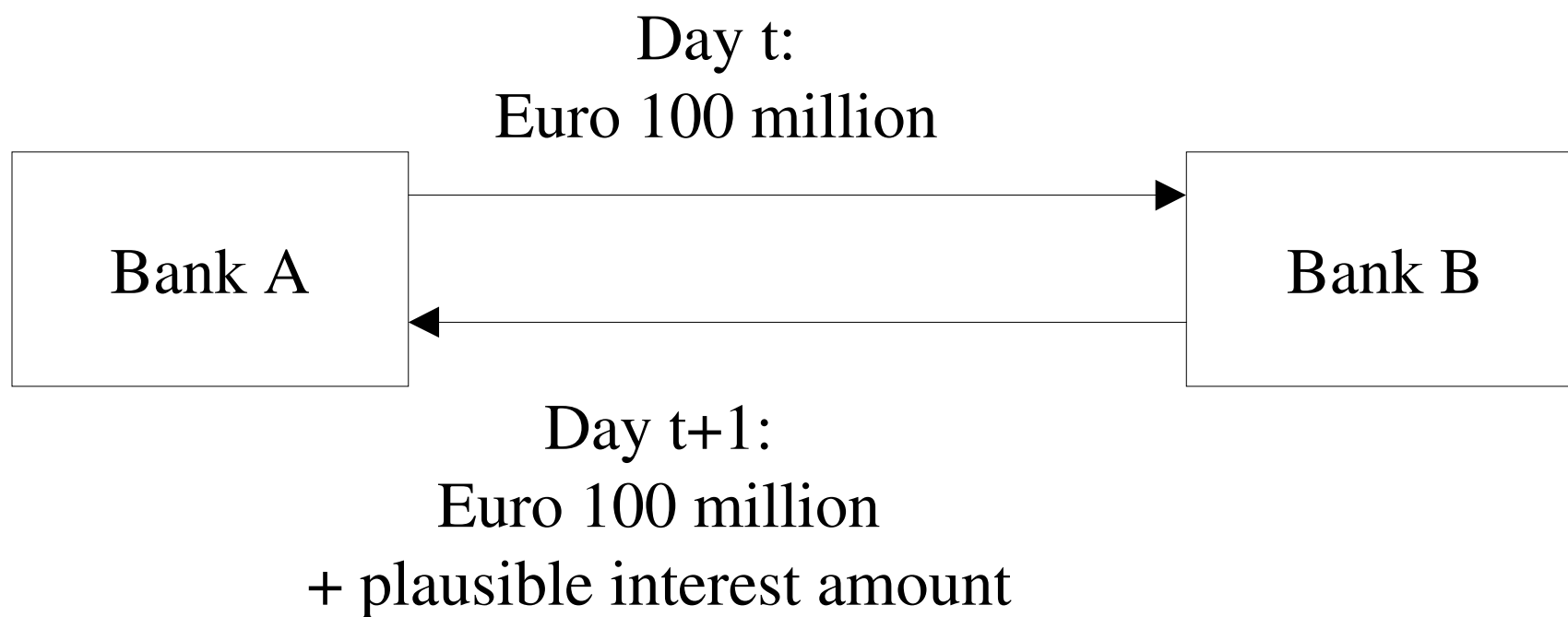


# General assessment and outline of discussion

- A very interesting paper of high relevance in relation to assessment of the functioning of the euro area money market, monetary transmission and monetary policy implementation in stress and non-stress periods.
- Based on unique transaction-level data for the euro area money market derived from Target2 payment data.
- Outline of the discussion:
  - Brief review of the approach and main findings of the paper.
  - Suggestions regarding data description *etc.*
  - Scope for further research on the Target2 data.

# Data

- Interbank transactions on uncollateralised overnight loans 2008-2013 derived from TARGET2 payment flows using a Furfine-type algorithm



# Main findings

- Low stress markets
  - Higher supply of central-bank liquidity (excess liquidity) leads to lower money market interest rates (spread to the ECB deposit rate) and vice versa.
  - Higher supply of central-bank liquidity leads to lower money-market turnover of loans.
- High stress markets
  - No simple relationship between excess liquidity and changes in money market interest rates.
  - Might reflect concern about counterparty risks as well as liquidity hoarding as insurance against negative shocks to own liquidity needs.

## Suggestions regarding data description *etc.*

- Comment on the reliability of overnight loan transactions in the euro area identified via the Furfine-type algorithm.
  - The precision of the algorithm has recently been a major topic in relation to US payment data.
  - However, as reported in the final MaRs Report the algorithm seems to work fairly well for the euro area, at least for overnight transactions as used in the paper.
- “The key to identification is that in between central bank market operations, which happen once a week, the amount of excess liquidity is fixed...” (page 2, see also page 6)
- Might deserve a comment on the marginal lending facility (the insignificant use of the facility in the sample period).

# Scope for further research on the Target2 data - 1

- Combine Furfine-type data with bank-level accounting information to analyse the importance of bank-specific characteristics on trading volumes and interest rates.
- Are banks with a low solvency ratio, high loan impairment charge ratios or banks that later exit by default paying higher interest rates in the overnight market than other banks? (i.e. analysis of credit-risk premiums in the money market)
- Are banks with a decline in their liquidity buffer relative to the statutory requirement reducing their supply of interbank loans?
- Are banks with an increase in their liquidity buffer increasing their supply of interbank loans?
- Were small banks (measured by e.g. the balance-sheet total) paying a premium on uncollateralised overnight loans during the crisis? Even after control for the banks' economic performance?

## **Scope for further research on the Target2 data - 2**

- Combine Furfine-type payment data with bank-level information on the use of the monetary-policy instruments.
  - Are banks with a low level of excess central-bank liquidity paying higher interest rates on loans than other banks?
  - Are banks with a high level of excess liquidity charging lower interest rates on loans than other banks?
  - Is the level of the overnight interest rate higher when the total outstanding amount of excess central-bank liquidity is concentrated on relatively few monetary-policy counterparties?
  - What was the impact on the money market microstructure during the crisis of changes in the width of the interest-rate corridor (determined by the rates on the standing facilities) or changes in the collateral base for monetary-policy loans?
  - What was the impact of a negative rate on the standing deposit facility on the money market microstructure?

## Scope for further research on the Target2 data - 3

- The impact on government guarantee schemes vis-à-vis the banking sector on individual banks' access to the interbank market and the interest rate they pay.
  - Did the guarantees lower the interest rate paid by banks in financial distress?
  - Did the guarantees facilitate access to the money market for banks in financial distress?
- Are systemically important financial institutions (SIFIs) paying lower interest rates in the money market than other banks? Even after control for the banks' economic performance?



## Scope for further research on the Target2 data - 4

- Interconnectedness in the interbank market (measured e.g. by the number of counterparties, other quantitative measures of interconnectedness, network charts, *etc.*)
  - The impact on trading networks of bank failures. Can structural breaks in interconnectedness measures be detected?
  - Were announcements of “bad news” for individual banks expected in the market, for instance indicated by reduced exposure vis-à-vis the banks in question prior to the announcement?
  - The impact of other specific events on the network structure.
  - Are interbank network structures time or regime dependent?
  - Are there cyclical patterns in the degree of interconnectedness and thereby systemic risks?