Discussion of Buchak et al. "Secular Decline of Bank Balance Sheet Lending"

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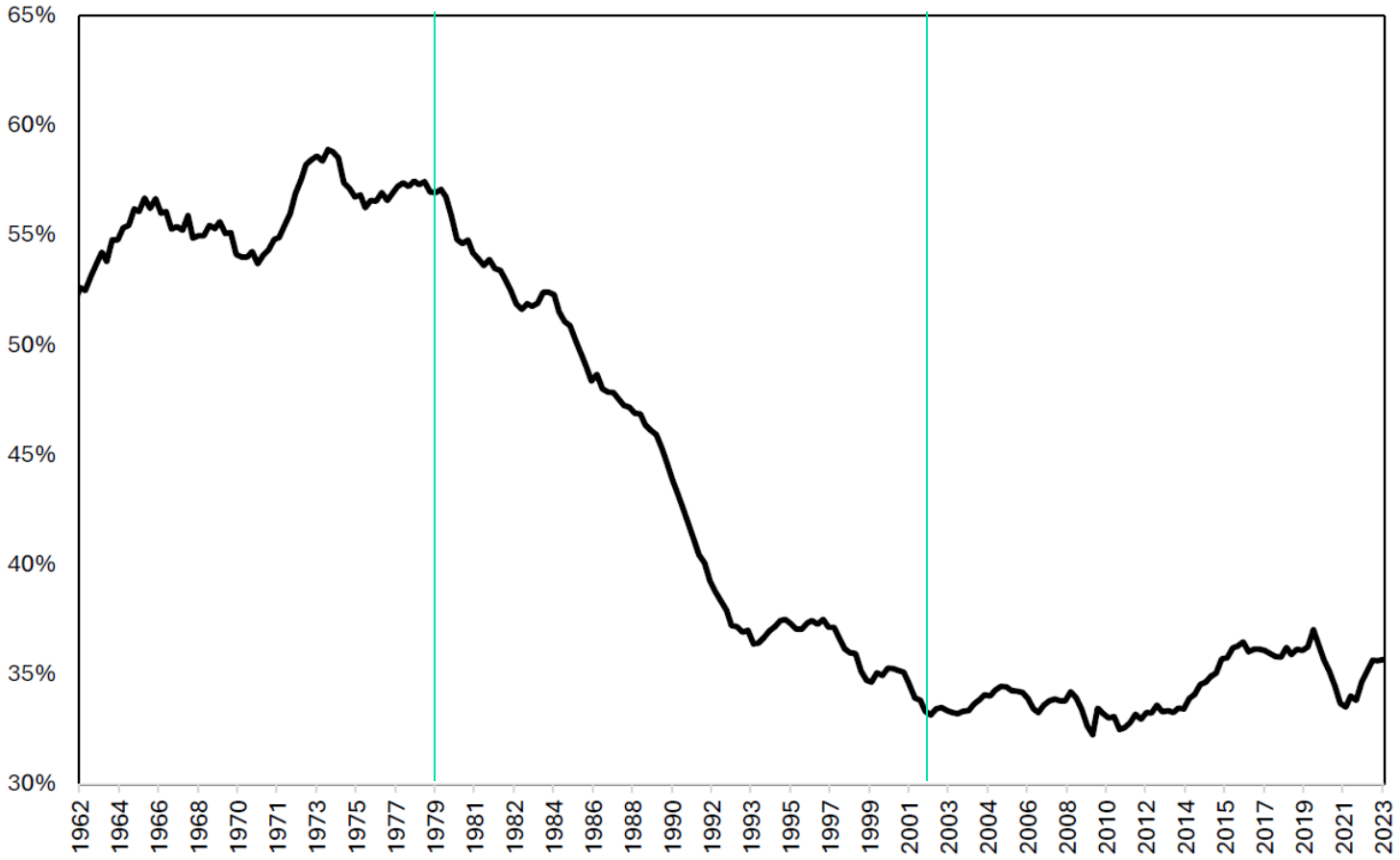
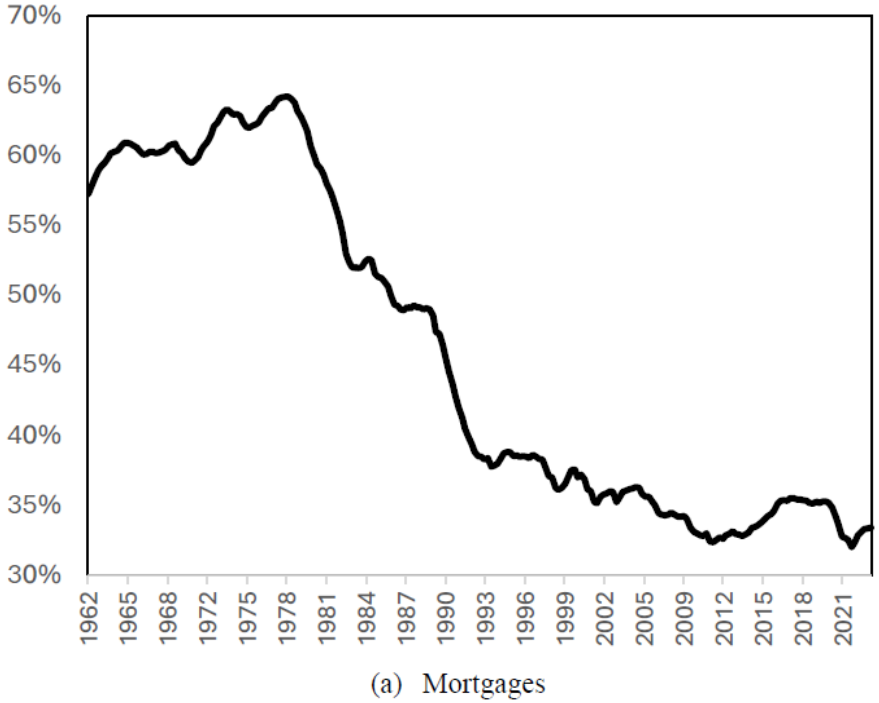
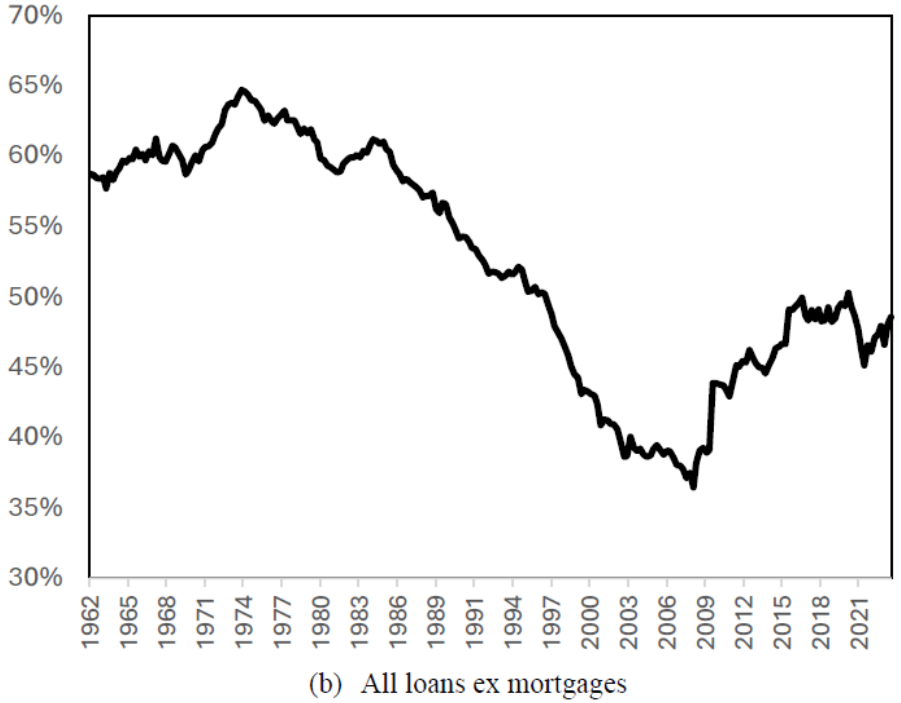
Bank balance sheet loans to total borrowing



Not just mortgages

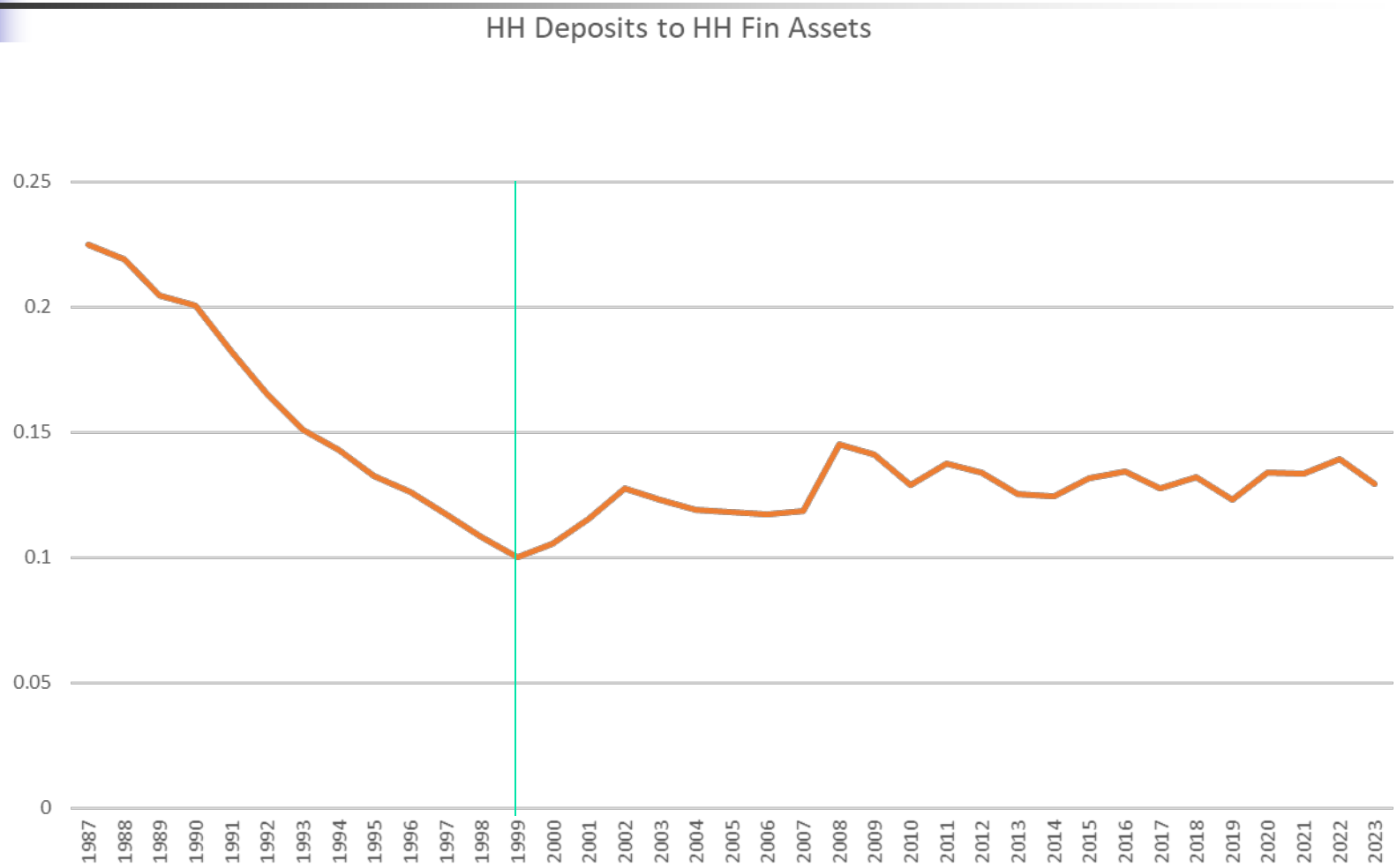


(a) Mortgages



(b) All loans ex mortgages

Household deposits to financial assets



Bottom line

- Something happened to banks and banking between 1980 and 2000

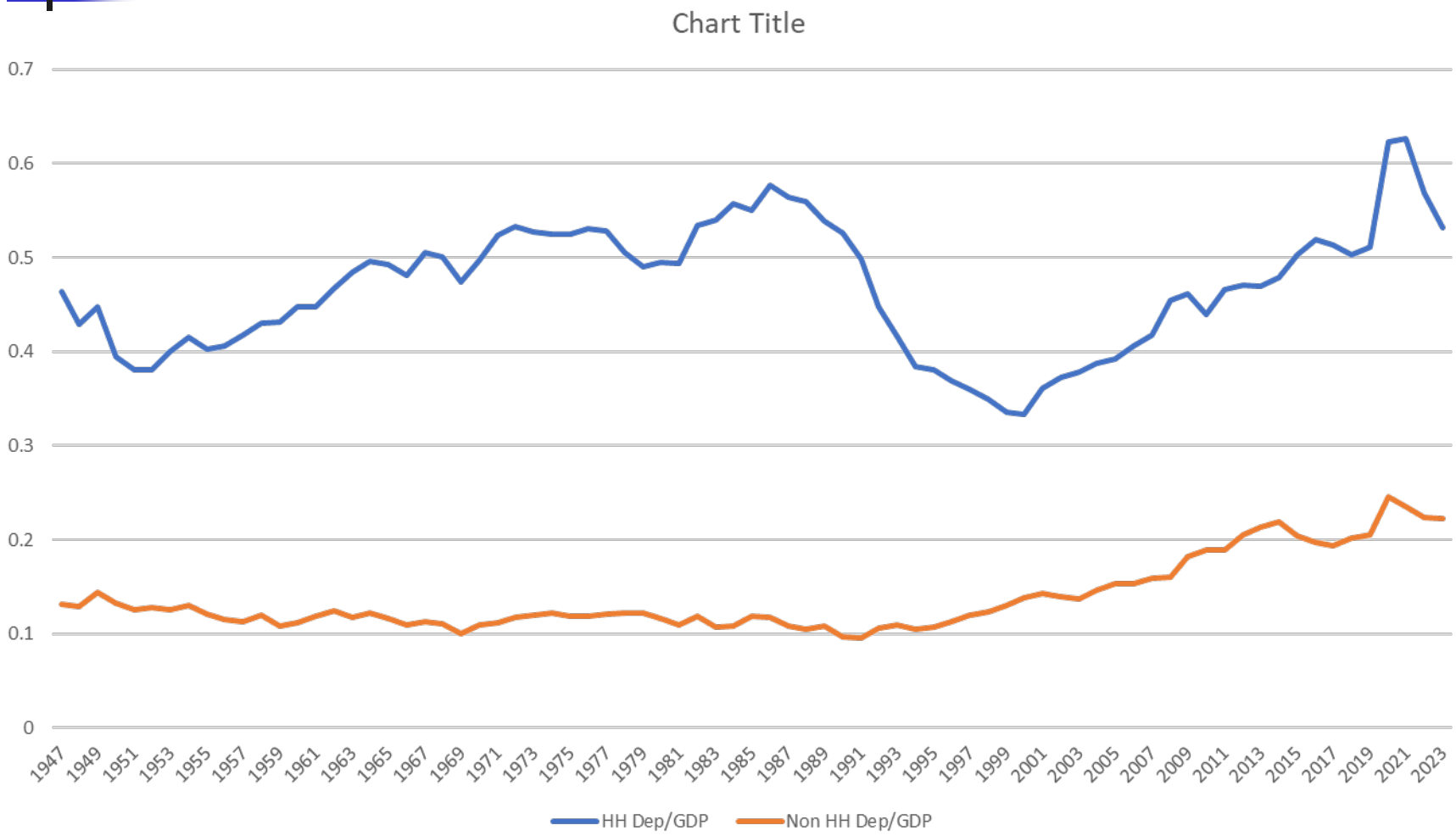
Also

- Spreads have not changed significantly, quantities have.
- Bank assets more oriented to securities
  - Loans 70% of bank assets in 1970, 55% in 2023

Interestingly

- Banks have not shrunk relative to GDP.

Deposits to GDP



This paper: Why the (relative) decline in bank balance sheets?

Explanations this paper focuses on

- Technological change: e.g., securitization, credit scoring, computerization, government guarantees
- Saver preferences: e.g., changes in household and pension fund behavior
- Borrower preferences
- Implicit regulatory bank subsidies/costs

How do you tell these apart?

- Structural model: use prices, quantities, and timing to elicit parameter estimates
  - Still requires assumptions:

"we attribute changes in the quantities of informationally insensitive loans in the economy that are unexplained by changes in securities prices to changes in the implicit cost of securitization and not to changes in borrower preferences"

  - High inflation => savers want higher nominal rates and fewer low interest deposits (preferences) => changes in technology (MM funds started), regulations (regulation Q).

Big picture results

- Technological change in favor of securitization primary driver of total lending (Fig 5 a)
- Saver preferences for deposits primary driver of bank balance sheet size contraction (Fig 5 b)
- Implicit subsidies or costs to bank loans primary driver of allocation of bank balance sheets between loans and securities (Fig 5d).
- Why quantity effects seemingly largely between 1980 and 2000?
  - CLOs, private credit, BDCs take off post 2007.

Thought experiment made possible by estimates

- What will a 25% increase in capital requirements have on aggregate lending in 2023 vs 1960?
- Not much
  - Share of "bank specific" loans smaller on bank BS, so less effect of balance sheet shrinkage on lending.
  - Substitution from market based informationally insensitive securities for lost lending.
  - Substitution by banks between securities and loans.
- Interesting implication: Can impose more regulations on banks to make them safer still.
- MM view of banking?

What is going on?
Conjecture 1: Natural optimization

- Bank balance sheet space is costly, especially as households find alternatives to deposits, and capital requirements go up.
- How do bank assets change as alternatives become available
  - What is off loaded/sold
    - Plain vanilla stuff
    - Loans that require screening not monitoring
      - Worries about credit score sufficient to reduce strategic default
  - What is kept
    - Lending where screening & monitoring important
    - Liquidity provision as part of relationship (lines of credit)
    - Contingent lending – lending when the going gets tough
    - Lending to financial intermediaries (why add layer?)

Implications.

- Could "optimized" informationally sensitive lending be different from its past avatar? Are the marginal costs of substitution changing?
  - Can we treat the products as the same over time in the estimation or in policy experiments?
- Are the products independent of each other?
  - If lending has an element of liquidity provision … need securities holding?
  - Similarly if banks offer more demandable claims on liability side…

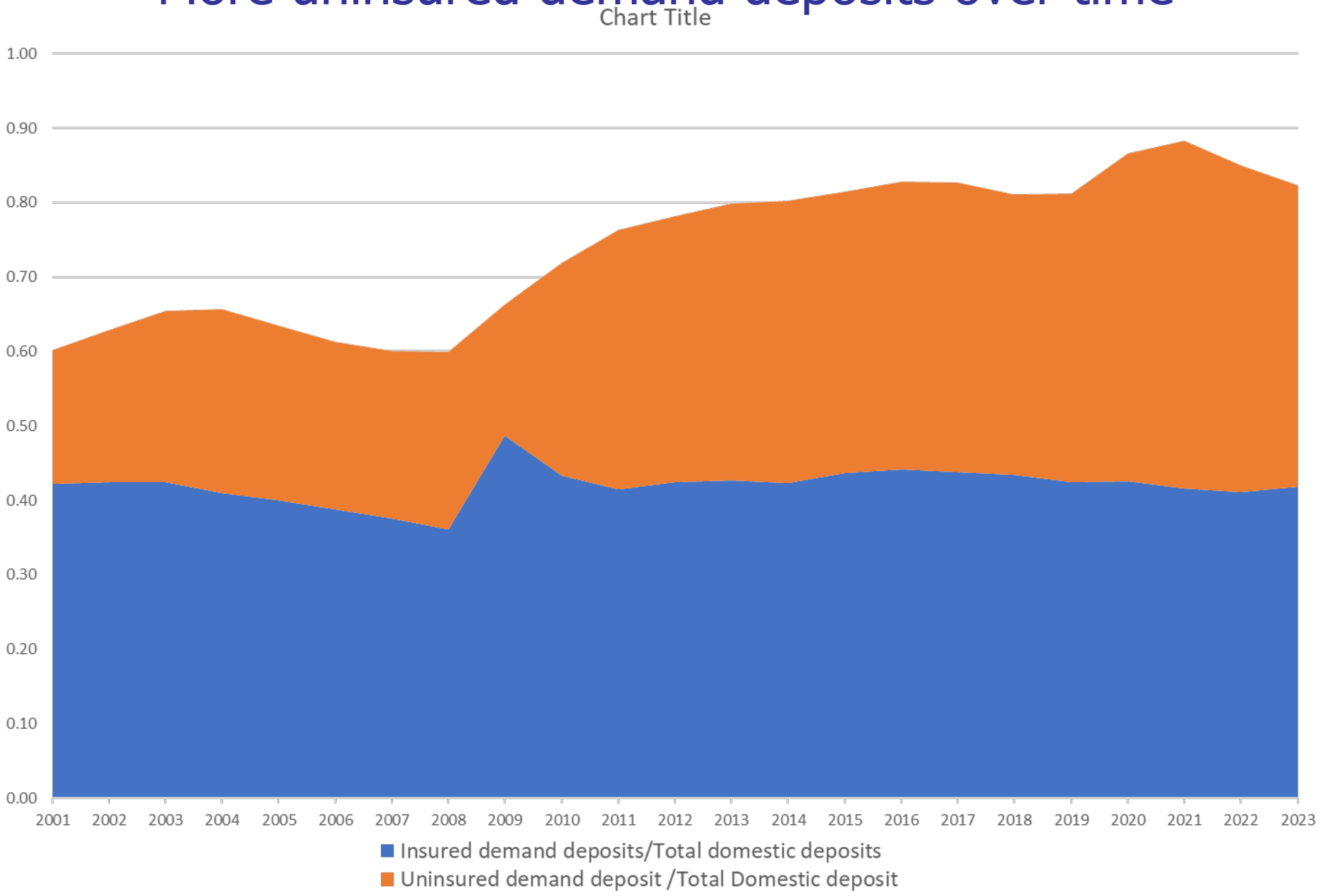
Conjecture 2: Banks are different based on 1980-2000

- Large banks are different from small banks
  - More securities, fewer relationship loans
  - More focus on liquidity provision
    - Lines of credit, demandable claims
- Economies of scale in banking – deregulation in 1980s and 1990s prompt mergers => shifts within banking sector independent of outside forces (technology of banking?)
- Not all banks are the same, changes within banking system could explain some of the effects.

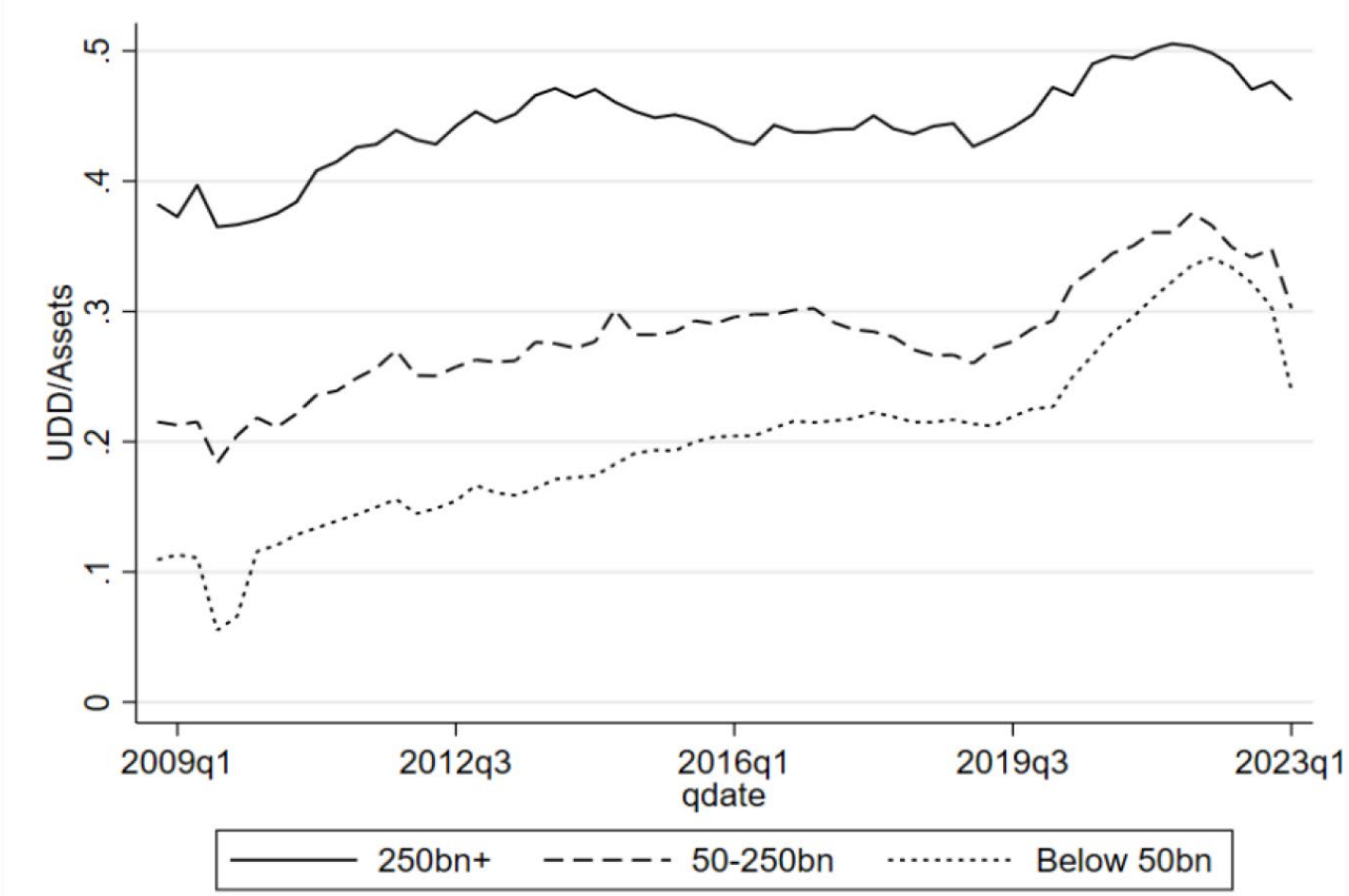
Conjecture 3: Policy shift changes bank products

- Monetary policy such as quantitative easing has an effect on assets and liabilities of banks (Acharya et al. (2023))
  - Deposits change: become more uninsured and demandable
- Has differential effect across banks based on differentiated regulation
  - Not necessarily in a way to make the system safer
- Caveat: Would not explain changes before the late 1990s.

More uninsured demand deposits over time

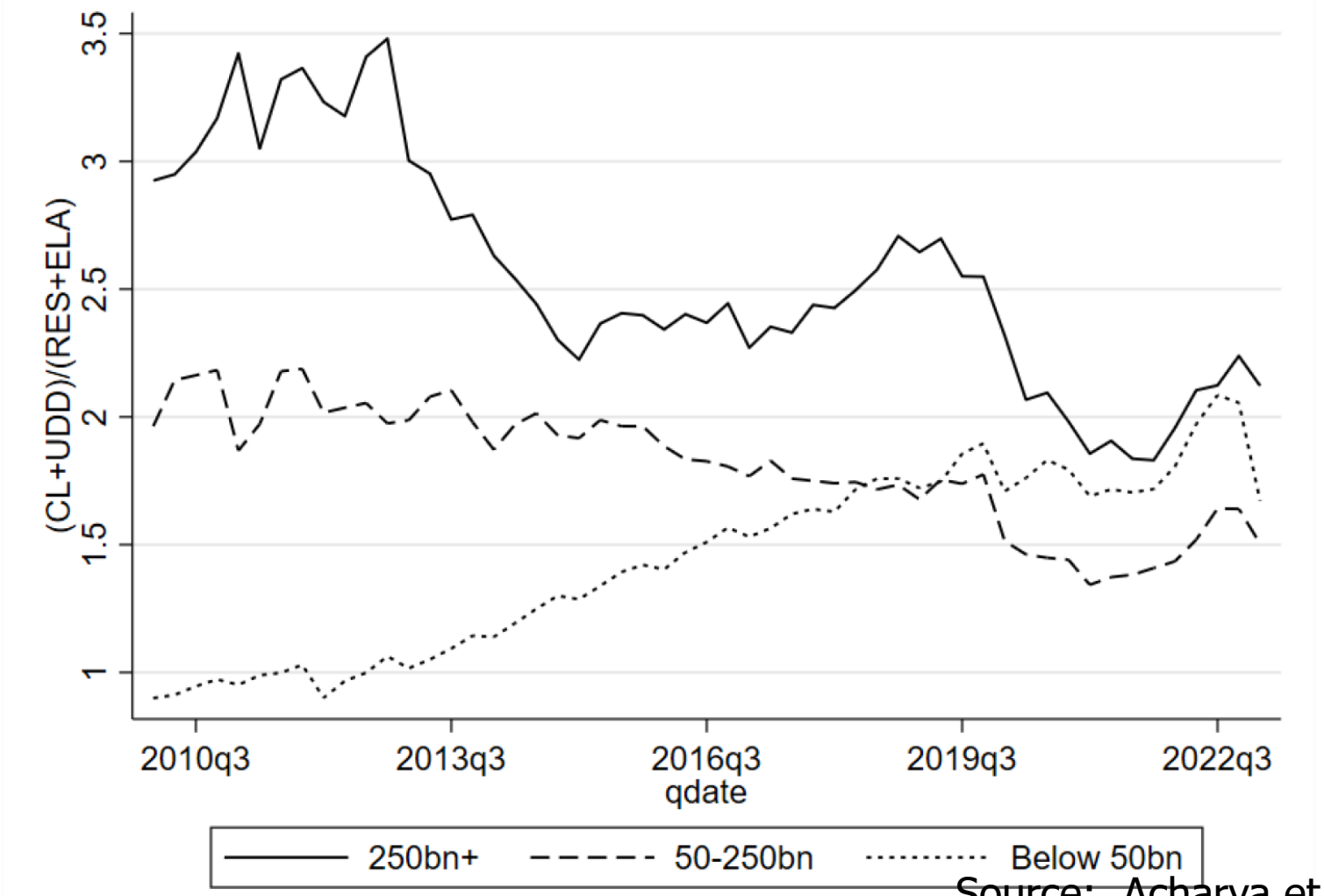


Uninsured demand deposits/assets for banks of different size



Source: Acharya et al. (2023)

(Cl+UDD)/(Res+Elg Sec)



Source: Acharya et al. (2023)

So big balance sheet changes within banks 2009-2024

- Time deposits down, uninsured demand up, lines of credit up
- Bank balance sheets up relative to GDP (adding to earlier rise)
- Differences between banks
- What explains these changes?
  - Fed policy + regulation + preferences?

Bottom line

- Great paper on an interesting topic.
- Has to make assumptions about what forces to concentrate on.
  - Interesting implication about limited effect of policy/regulatory changes
  - Surely the focus on "migration margin" and "retention margin" is right. But what are they as banks re-optimize in the face of change?
- Other forces also affect bank balance sheets.
- Scope for future research!