

Discussion of:

**Lending-of-last-resort is as Lending-of-last-resort  
Does: Central Bank Liquidity Provision and Interbank  
Market Functioning in the Euro Area**

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# Summary

What is the impact of the ECB liquidity provision from 2008 to 2014 on unsecured interbank market?

- ▶ Setting and empirical strategy
  - 2008-14: large liquidity provision (repos) by ECB
  - Novel data on o/n unsecured interbank transactions
  - Identification: liquidity fixed for a week after allotment
  - Structural VAR
- ▶ Findings: ↑ central bank liquidity
  - 2008-10: ↓ rates, ↓ volumes
  - 2011-13: ↓ rates in stressed countries
- ▶ Economics
  - ECB liquidity: ↓ *demand*; ↑ *supply* in stressed countries
  - ECB acts as a de facto LOLR

# Discussion

- 1) ECB as a LOLR
- 2) Which Friction(s)/Market Failure(s) Fixed?
- 3) The Role of Maturity

# 1) ECB as a LOLR in 2008-14: Core Vs. GIIPS

Bagehot: *“to avert panic, central banks should lend early and freely, to solvent firms, against **good collateral**, and at **high rates**”*

## ▶ Collateral subsidy in GIIPS

- Haircut are security specific, *not* bank specific
  - **ECB haircut on PT govt bonds 4.0%**; LCH Clearnet: 10.0%
  - ECB haircut on DE govt bonds 3.0%; **LCH Clearnet: 2.0%**
- Data from late 2010 (Drechsler et al (forthcoming))

## ▶ Risky collateral is mainly in GIIPS

- Banks pledge risky collateral first

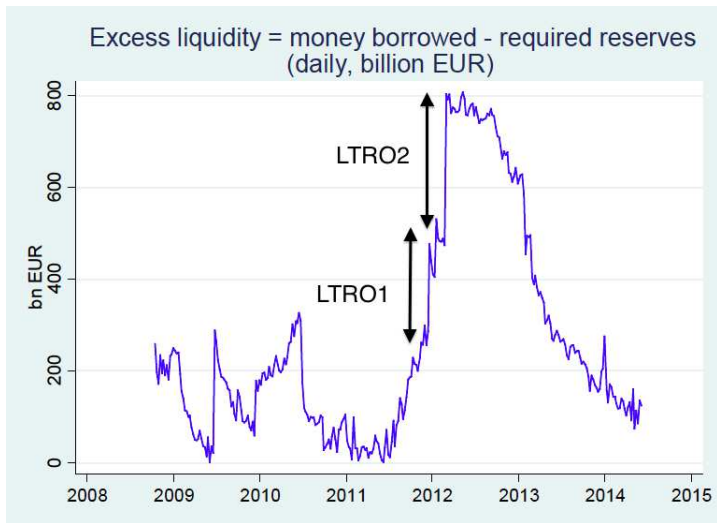
⇒ ECB liquidity mainly to GIIPS (2/3 of 3YLTRO in IT+ES)

**Bagehotian LOLR in core countries, something more in GIIPS**

## 2) Which Friction?

- ▶ “ECB did continue to lend only to solvent banks and against appropriate collateral”
    - Illiquidity story
    - Why private markets are not working?
    - Hard to rule out insolvency
  
  - ▶ Analysis is at country level
    - DE/PT different patients treated with different medicines
    - Probably different transmission channels at work
  
  - ▶ Exploit bank heterogeneity within a country
    - *Which* banks are reducing demand the most?
    - *Which* GIIPS banks are increasing supply the most?
    - *Which* banks deposited extra cash at deposit facility?
- ⇒ Look at bank balance sheet characteristics

# Excess Liquidity



### 3) Does Maturity of LOLR Loans Matter?

- ▶ LTRO maturity extended during crisis
  - Normal times: one-week (MRO) or three-month (LTRO)
  - From mid-09: longer LTROs (e.g., 4 1Y-LTROs, 2 3Y-LTROs)
- ▶ Does not matter in theory
  - Rollover short term liquidity = long term liquidity (if no uncertainty and FRFA)
- ▶ In practice?
  - Large uptakes of longer term liquidity provisions
  - What's special about long term maturity liquidity?

# Overall

This paper:

- Important first step in understanding effect of LOLR liquidity on unsecured interbank markets
- Opens up new interesting questions, especially on the economic forces driving the transmission



Thank you!