

Economics Lunch

Wednesday, September 25, 2019, 12:30 – 13:15 pm, WWZ, HG, S 15

Aakriti Mathur, PhD student Graduate Institute in Geneva and BIS

"In the dangerzone! Regulatory uncertainty and voluntary bank capital surpluses"

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Abstract

Banks voluntarily hold substantially more capital than required by regulators. Understanding why is important for forecasting the extent to which banks would use this surplus to support lending in a crisis, and therefore for calibrating macro-prudential policy. This paper studies the role of uncertainty about the regulations themselves, which could heighten any precautionary motive to avoid accidental breach of minimum requirements. We introduce two new measures of regulatory uncertainty: one at bank level based on confidential regulatory data; another at sector-level based on news-media text. These correlate with more general uncertainty measures from the literature, but also contain distinct information. Using regulatory data on UK banks between 1989-2013, we find that a one standard deviation increase in regulatory uncertainty increases banks' voluntary capital surpluses by 0.8 to 2 percentage points on average, and this effect is stronger when surpluses are smaller, that is, for banks in the "dangerzone". Given a Basel I minimum capital requirement of 8%, our results are economically meaningful.

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