

Discussion of "Banking when Inflation Surges:
Headwinds or Tailwinds"
by Bergant, Hakamada, Kirti, Mano

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ASSA Meetings

Overview

- ▶ **Research Question:** Are banks subject to inflation risk?
- ▶ **Approach:**
 1. Use international panel data to assess risk exposure
 2. Study direct and indirect exposures via interest rates
- ▶ **Main Results:**
 1. Return on assets and net interest margins show little exposure
 2. This result holds across countries and banks with few exceptions

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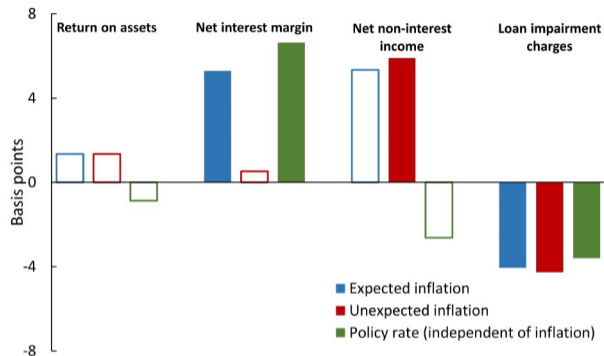
Main Empirical Approach

- ▶ The main regression takes the form

$$Y_{b,i,t} = \alpha^1 \pi_{i,t}^e + \alpha^2 \pi_{i,t-1}^e + \sigma^1 \pi_{i,t}^s + \sigma^2 \pi_{i,t-1}^s + \beta i_{i,t}^o + \phi X_{i,t} + \gamma_b + \gamma_t + \epsilon_{b,i,t}$$

- ▶ where $Y_{b,i,t}$ is return on assets, net interest margin, etc.
- ▶ $i_{i,t}^o$ is the interest rate orthogonalized to other regressors
→ α 's and σ 's give total effect of inflation (direct and through i_t)

Key Results



- ▶ Shows small exposure of ROA & NIM to 100bps change in inflation
- ▶ Result is a variation of finding in Drechsler, Savov, and Schnabl (2021)
- ▶ **Intuitive:** inflation risk mainly takes the form of interest rate risk for banks

Comments & Suggestions

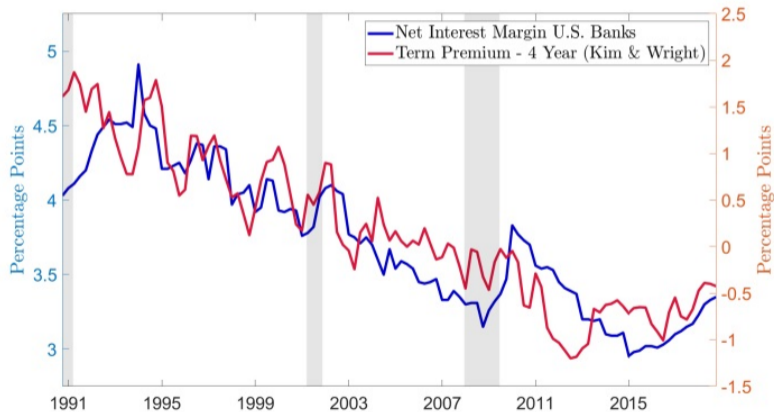
Comment (1)

Differentiate between interest rate risk affecting bank profit margins vs. balance sheets:

- ▶ Paper mainly focuses on profit margins → little exposure, stable NIMs
- ▶ But March 2023 crisis showed that banks' balance sheets can be heavily exposed
- ▶ Long-duration assets + uninsured deposits can lead to runs when rates ↑
- ▶ **Suggestion:** extend analysis to balance sheet exposures

Comment (2)

1. Not only changes in inflation can affect profit margins, but also inflation volatility
2. Inflation volatility $\uparrow \rightarrow$ interest rate volatility $\uparrow \rightarrow$ term premium $\uparrow \rightarrow$ NIM \uparrow



Comment (3)

- ▶ As opposed to pre-step orthogonalization, you can just exclude/include variables
- ▶ For example, total and direct effect of inflation can be obtained via:

$$Y_{b,i,t} = \alpha\pi_{i,t} + \dots + \epsilon_{b,i,t}$$

$$Y_{b,i,t} = \alpha\pi_{i,t} + \beta i_{i,t} + \dots + \tilde{\epsilon}_{b,i,t}$$

- ▶ Similarly, total and direct effect of interest rates can be obtained via:

$$Y_{b,i,t} = \beta i_{i,t} + \dots + \epsilon_{b,i,t}$$

$$Y_{b,i,t} = \beta i_{i,t} + \alpha\pi_{i,t} + \dots + \tilde{\epsilon}_{b,i,t}$$

Summary

- ▶ Nice paper with valuable numbers for policy
- ▶ **Some suggestions:**
 1. Effect of interest rate risk on bank balance sheets
 2. Analyze implications of inflation volatility
 3. Simplify identification approach

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