DISCUSSION:

“WHAT EXPLAINS THE CRASH OF BANK STOCK PRICES DURING COVID-19?”

ACHARYA, ENGEL & STEFFEN

“LIQUIDITY INSURANCE VS. CREDIT PROVISION”

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**Effects of Credit Lines Drawdowns on Banks**

Credit lines from banks key source of liquidity for firms

- Salient during COVID crisis $\implies$ pressure on banking sector

1. **Big picture question:** Do drawdowns on existing credit lines affect banks’ decisions going forward?
   - First order: key part of liquidity transformation by banking sector
   - But traditionally focus on capital, liquid assets, deposits
   - Hard question: why would bank decision be inefficient when crisis comes from outside financial sector?
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2 Main fact: Negative correlation between drawdowns and lending

   - I believe it: repeatedly emerge from the data
     (also Ivashina Scharfstein 2010, Greenwald et al. 2020)
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2. **Main fact:** Negative correlation between drawdowns and lending
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3. **Underlying mechanism:**
   - Paper 1: probably capital (stock price evidence)
   - Paper 2: probably not capital (survey evidence)
Off-balance sheet commitments have lower capital charges than on-balance sheet loans

- The smaller the conversion ratio, the larger the effect, i.e. if off-balance sheet capital charge is only 20% relative to on-balance sheet, required capital is multiplied by 5 if loan is fully drawn

- Not all drawdowns are created equal

- Ex-post drawdowns on short-term loans create more risk (because paradoxically they are safer commitments ex-ante)

- Unambiguously true: mechanical effect of current regulation
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Suggestion: leverage variation from drawdowns on different loans exploiting differences in capital charges

Natural follow-up: what kind of loans are drawn during these times?
Maturity and Drawdowns

(A) Assets < $250M
(B) Assets > $1 B

Source: “Bank Liquidity Provision Across the Firm Size Distribution”
Chodorow-Reich, Darmouni, Luck & Plosser

Similar effect with collateral
**Risk Tolerance Channel**

Not mechanical rule: not as easy to explain

“Change credit risk make-up of banks’ loan portfolio and thus banks’ expectations of future losses”

- By far most common answer in banking survey data
- Also in line with low-take up of Main Street Lending Program
- Relates to bank optimal balance sheet management (multi-dimensional, lending is just one margin)
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Natural follow-up: what kind of firms draw-down during these times?
INDUSTRY EXPOSURE AND CREDIT LINE DRAWDOWNS
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Larger shock $\implies$ higher drawdowns at large but not small firms

Source: “Bank Liquidity Provision Across the Firm Size Distribution”
Chodorow-Reich, Darmouni, Luck & Plosser
What Drives Aggregate Drawdowns?

Aggregate draw-down rates are not exogenous
i.e. 2020 draw-down different than in GFC, reversal in 2020Q2, etc

1 Nature of the shock: banking sector, firm cash-flow, uncertainty..
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Adding the effect of draw-downs to stress tests is good first step; Ideal would be corporate finance model of draw-downs
Paycheck Protection Program and Drawdowns

PPP funds to Y-14 borrowers largely used to repay credit line balances

- PPP recipients had higher repayment propensity in 2020Q2
- Credit line repayments equal 72% of disbursement to small SMEs, over 100% for large SMEs, 95% pooled across all firms

(a) Q1 drawdowns
(b) Q2 drawdowns

Source: “Bank Liquidity Provision Across the Firm Size Distribution”
Chodorow-Reich, Darmouni, Luck & Plosser
ISSUING BONDS TO PAY BACK CREDIT LINES

Source: “Crowding-Out Bank Loans: Liquidity-Driven Bond Issuance” Darmouni-Siani

- \( \frac{2}{3} \) HY bond issuers repaid some bank loan (40% in full)
- 85% IG bond issuers that drew down in 2020Q1 repaid their bank