Discussion of:
Paying banks to lend? Evidence from the Eurosystem's TLTRO and the EA credit registry

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The paper in a nutshell

- **Very timely and clear assessment of the impact of TLTRO III on bank loan volumes**

- **Identification:**

  - IV structure exploiting unanticipated increase in borrowing allowance on 10 December 2020.

  - Khwaja & Mian (2008) firm fixed effects to control for loan demand exploiting newly established euro area credit register.

- **Mechanisms of transmission**:

  - "Targeted" channel: lending performance criteria stimulate lending

  - "Profitability" channel: interest rate spread between TLTRO rate and DFR
    - I would expect profitability channel to be much broader than just the dual interest rate element.

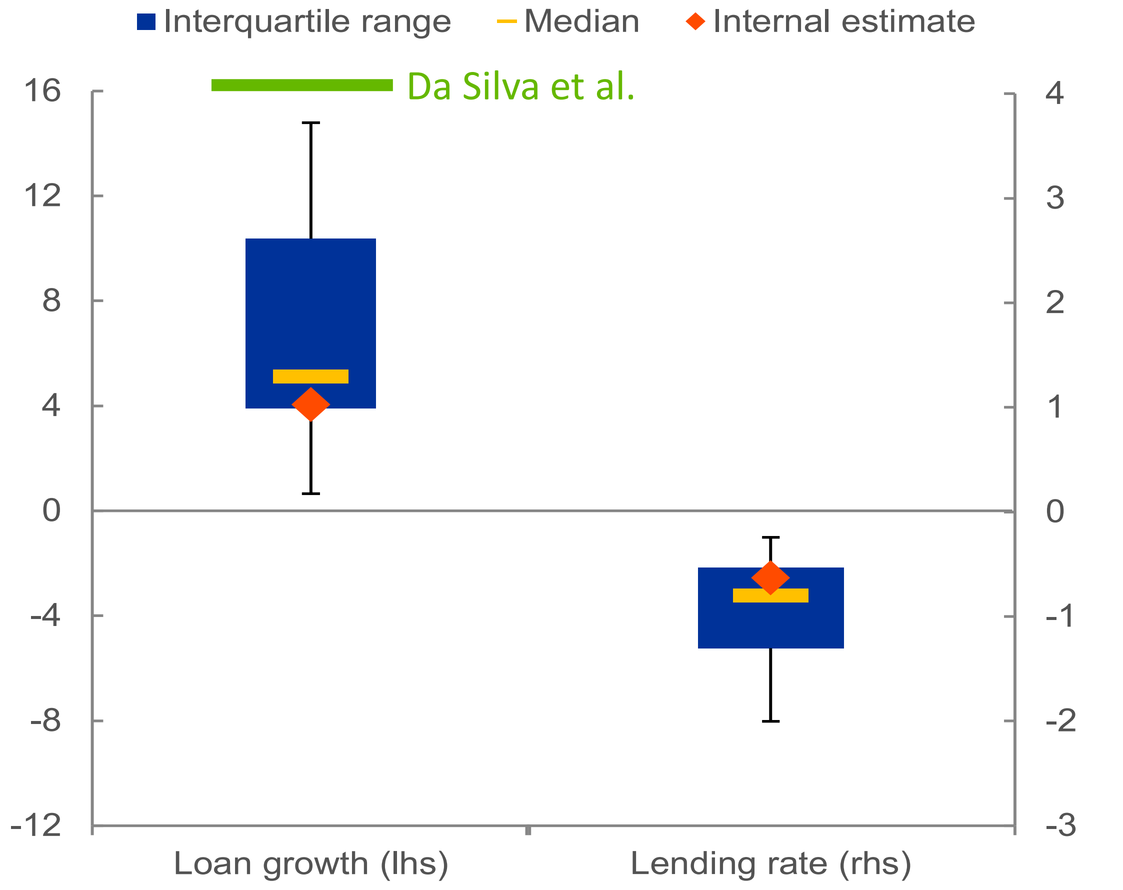
The paper in a nutshell

- **Results (my reading):**
  - If external validity holds, (very) strong difference in new loans over 2021 associated with higher take-up
    - **800bn-2400bn more loans if applied to overall TLTRO III take-up, 16%-50% of ex-ante volume.**
  - Profitability channel accounts for 90%-94% of the impact (non-eligible lending/eligible lending, non-achievers/achievers).
- **Conclusion (puzzling at first sight)**:

  "TLTRO with dual interest rates were no more effective than previous programs, despite causing all things equal explicit transfers from CB to banks."

The impact on lending conditions of TLTRO III across studies

(lhs: percentage points; rhs: percentage points p.a.)



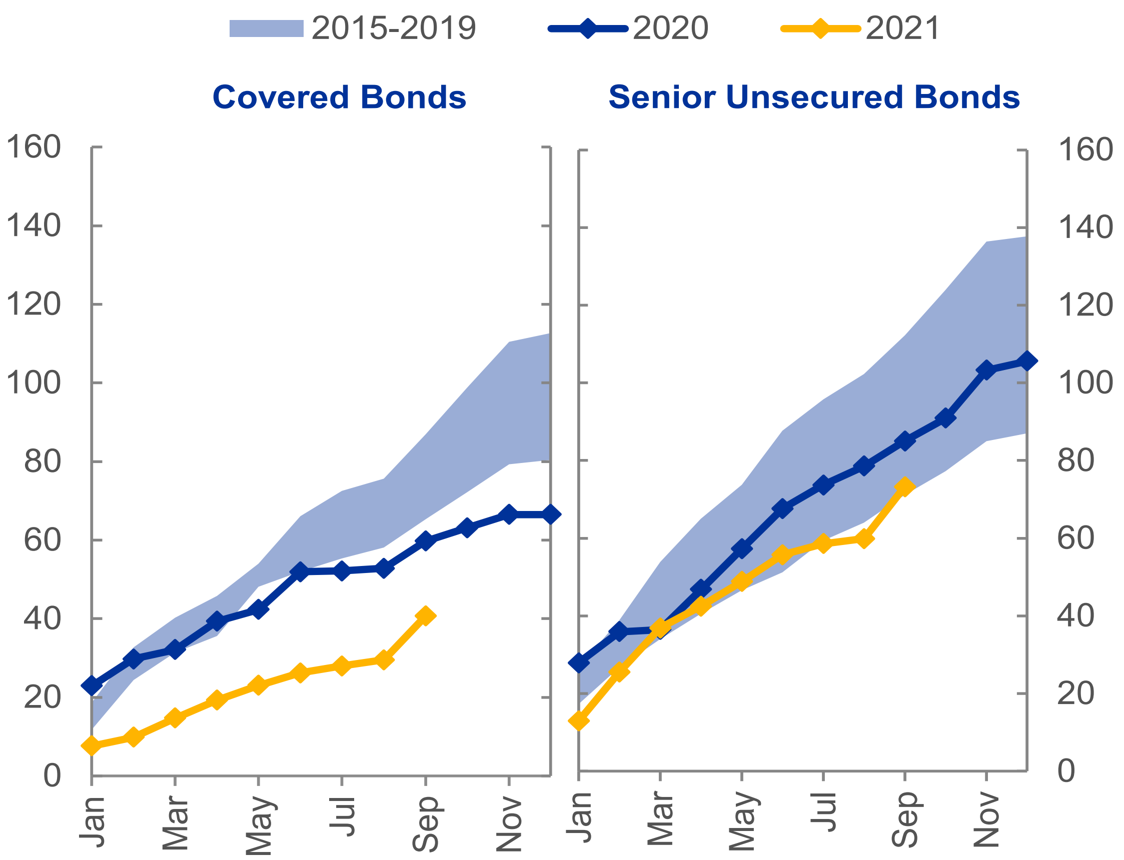
Sources: Afonso et al. (2019), Altavilla et al (2020a), Altavilla et al. (2020b), Andreeva, García-Posada (2021); Arce et al (2020), Balfoussia et al (2016); Barbiero et al. (2022), Bats, Hudepohl (2019); Benetton, Fantino (2021); Boeckx et al (2020); Cravo Ferreira (2019); Esposito et al (2020); Flanagan (2019); Gibson et al. (2020); Laine (2021); Offermans, Blaes (2021); Rostagno et al. (2021); van Dijk, Dubovik (2018). Notes: The box plot shows the interquartile and 10th-to-90th percentile ranges of estimates coming from 18 studies. Latest observation: June 2021.

Three comments

- ❑ **Transmission channels**
- ❑ **Was the dual interest rate element useful?**
- ❑ **Identification and measurement**

Transmission channels

Bank bond issuance
(gross monthly flows, EUR bn)



Sources: Dealogic DCM and ECB calculations.
Latest observation: September 2021.

❑ Incentive scheme embedded in the design

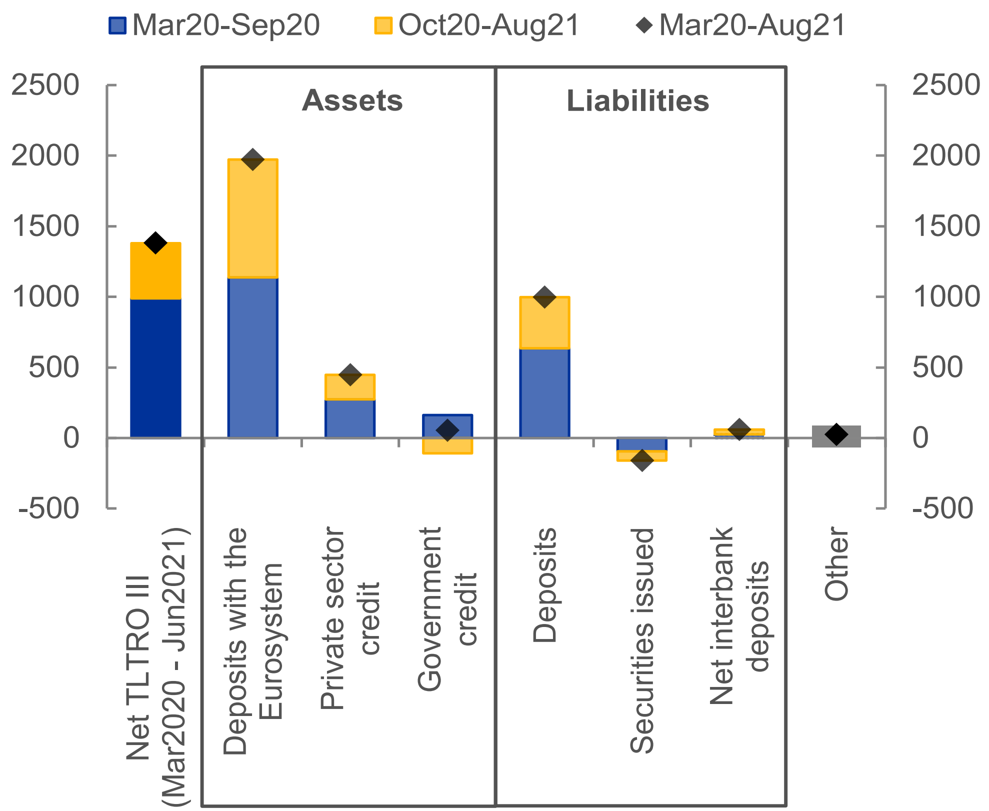
❑ Funding cost relief

- **Direct effect** via individual take-up
- **Indirect effect** via aggregate take-up and scarcity effects on other sources of funding

Transmission channels

Developments in assets and liabilities of TLTRO III bidders

(EUR bn)



Sources: ECB (iBSI) and ECB calculations. Notes: The chart shows the cumulated flows in the main assets and liabilities from March 2020 until September 2020 (blue bars) and from October 2020 until August 2021 (yellow bars) for bidders in TLTRO III covered in the iBSI sample. On the asset side, private sector credit includes loans to NFCs and households as well as holdings of private sector securities; government credit includes holdings of sovereign securities and credit to the government. On the liability side, deposits are vis-a-vis non-MFIs; (net) interbank funding are deposits minus loans from other MFIs excluding the Eurosystem.

❑ Incentive scheme embedded in the design

❑ Funding cost relief

- **Direct effect** via individual take-up
- **Indirect effect** via aggregate take-up and scarcity effects on other sources of funding

❑ Pandemic-specific impacts

- **Need to provide funding certainty**: Risk perceptions exceptionally high
- **Compression of lending margins:** Surge in deposits paired with long period of low and even negative interest rates

❑ Other impacts:

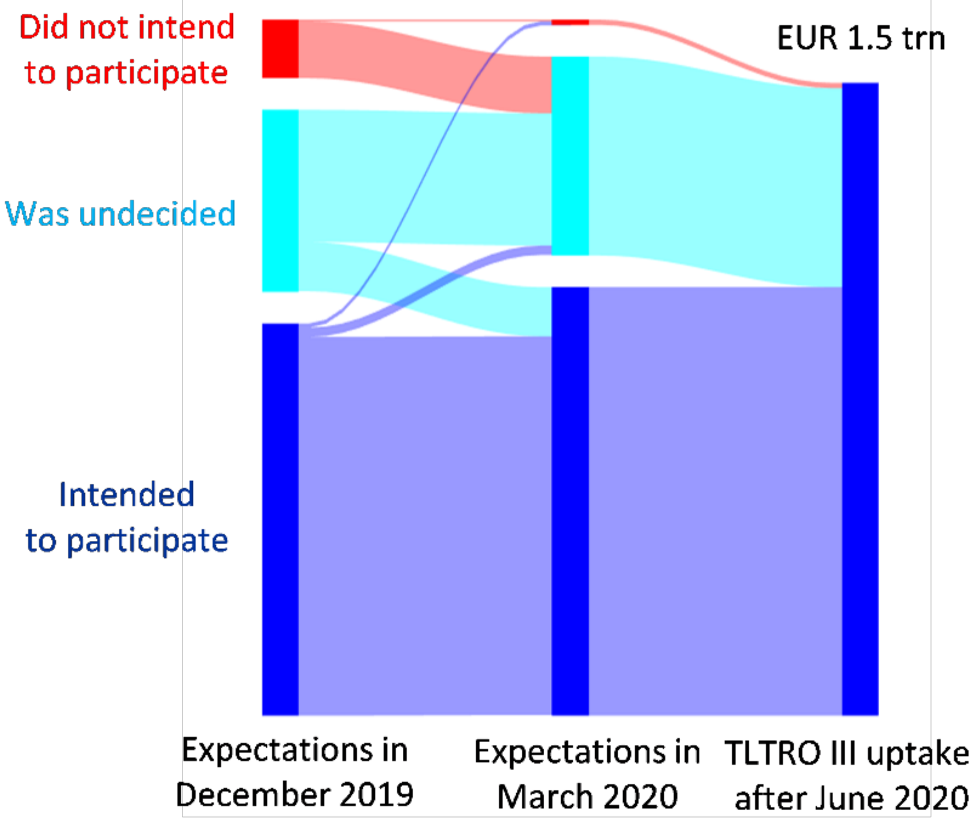
- **Mitigate procyclicality** by easing regulatory constraints
- **Downward pressure on money market rates** via injection of CB liquidity.

❑ Most prominently: Reducing the chance of financial amplification.

Was the dual interest rate useful? It was useful to avoid stigma

Evolution of intentions to participate for TLTRO participants as of June 2020

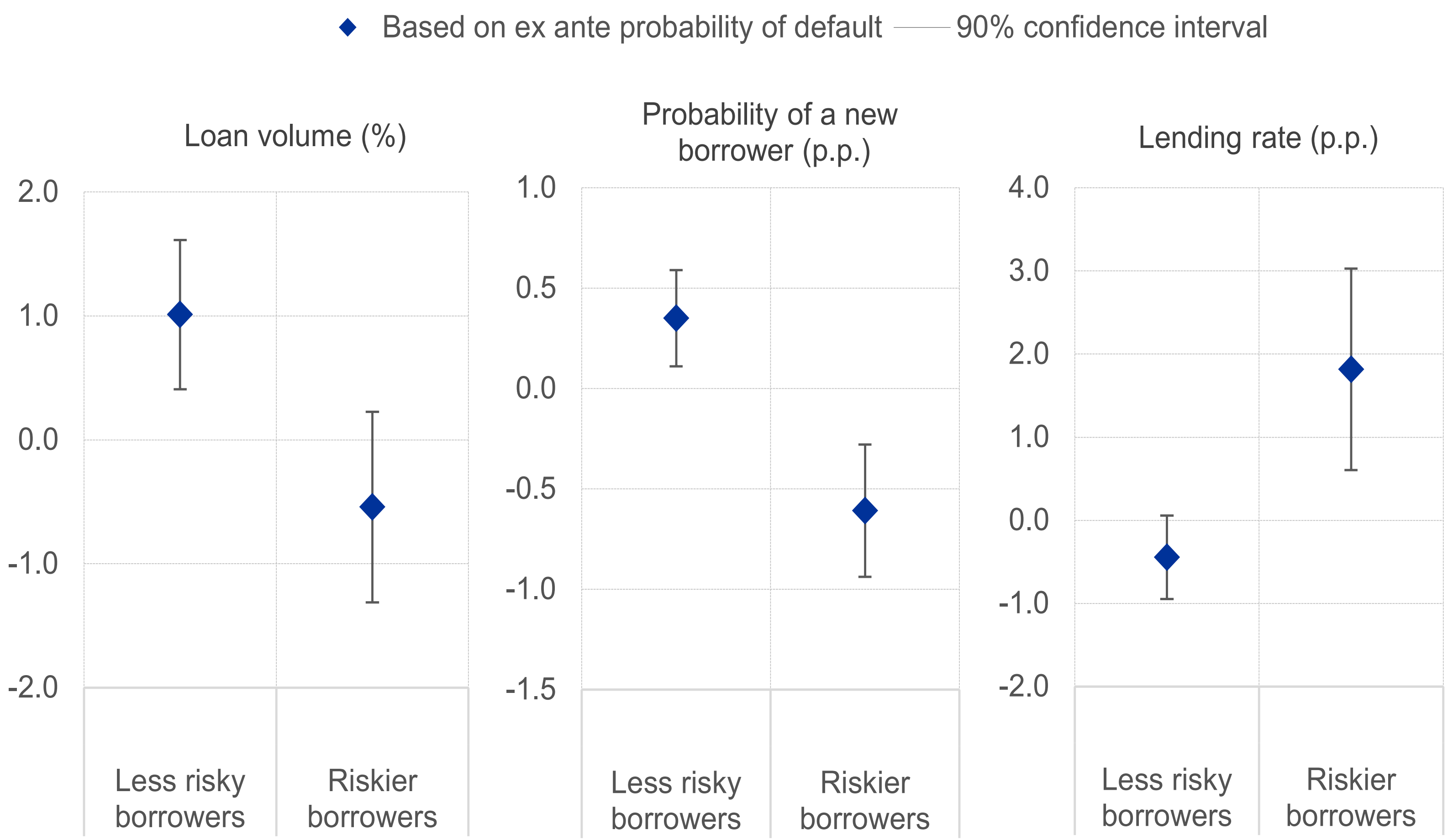
(share of respondents weighted by volume of TLTRO III uptake in June 2020)



Sources: ECB (MOPDB, BLS). Notes: The blue bar on the right column measures the EUR 1.5 trillion of participation after the June TLTRO operation. The three bars on the left column measure the eventual participation in the June operation by banks that, in December 2019 (January 2020 BLS), reported that they intended to participate (blue bar), were undecided (cyan bar) or did not intend to participate (red bar). The three bars on the central column measure the same participation in the June operation but based on responses given in March 2020 (April 2020 BLS). The shaded areas between the left and central columns measure transitions from one response to the other between survey waves.

Was the dual interest rate useful? It had welcome side effects

Exposure to TLTROs with dual interest rate and qualitative composition of credit



Source: Barbiero, F., Burlon, L., Dimou, M., Toczynski, J., "Targeted monetary policy, dual rates and bank risk taking", ECB working paper, 2682, 2022.

Identification and measurement

❑ Identification:

- **Recalibration of 10 December 2020 was not exogenous to bank circumstances**, and in particular to the bank-based transmission mechanism of monetary policy.
- It “prolonged” the support from “past few months” in a “time of high stress”
- Key elements: Previous take-up, past lending performance, persistent risk perceptions.

- **Unused borrowing allowance** affects lending beyond actual participation

❑ Measurement:

- **Exposure to TLTROs** hardly only a matter of take-up, and take-up hardly only a matter of borrowing allowance

- **Lending performance** is about net lending, not just new loans: rollover of the emergency lending during the pandemic was critical. Estimates might be a lower bound.

- **“Profitability” channel** is about much more than just the spread below the DFR, it should be measured relative to all alternative funding sources.