

# International Conference on the Global Financial Crisis: European Financial Markets and Institutions

25 – 26 April 2013



**International Conference on the Global Financial  
Crisis: European Financial Markets and Institutions**

**April 25-26, 2013  
Chilworth Manor  
Southampton, UK**

## **Welcome to the International Conference on the Global Financial Crisis: European Financial Markets and Institutions – University of Southampton**

When we started to plan this conference, we were somewhat unsure about the topic. The main concern was that the *Global Financial Crisis* might be over by the time we will hold the conference in April 2013. After the initial shock to the financial system and subsequent bailouts, it seemed that the crisis ran out of steam. The Euro seemed to have been saved, and there were glimmers of hope.

As it turns out, while writing this welcome note, the *Global Financial Crisis* is fighting back. Cypriot banks remained closed for days, and capital controls are looming amid the next round of imminent bank bailouts. The *Global Financial Crisis* remains as topical as last year and the year before.

Apart from destroying the faith in financial markets, the corporate elite and the ability of states to tackle the fallout, the *Global Financial Crisis* has revealed the inadequacy of our understanding of finance and economics in general. This is also a crisis of our way of thinking about finance and economics. However, it is also a chance to improve our theoretical constructs and to move on. We hope that this conference will provide a breeding ground for new ideas and innovative thoughts.

Apart from presenting and discussing your research, papers presented at the conference can be submitted to a Special Issue published in the *Journal of International Money and Finance*. The Special Issue will be edited by the guest editors Professor Taufiq Choudhry, Dr Gerhard Kling and Dr Ranadeva Jayasekera. Additional details concerning the submission procedure will be provided in due course. We hope that this Special Issue will inform the wider academic community and provide new insights into the financial crisis and its consequences.

We also would like to thank the *Money Macro and Finance Research Group* for their support in organising this conference. We are very pleased and grateful that Professor James Lothian (Fordham University, USA) will deliver the keynote speech, and Professor Charles Goodhart (London Business School) will present the lunch time seminar.

We are very grateful to our sponsors, the *Journal of International Money and Finance*, the *Money Macro and Finance Research Group*, *Amplify Trading*, the *Bank of England*, *Bloomberg*, *Oxford University Press*, *International Financial Society* and the *School of Management, University of Southampton*. We wish you all a successful and exciting conference.

Kind regards,

The Conference Committee:

Prof Taufiq Choudhry, University of Southampton  
Dr Gerhard Kling, University of Southampton  
Dr Ranadeva Jayasekera, University of Southampton

## **CONFERENCE PROGRAMME**

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**Opening Ceremony 8.30-8.55 Cedar Suite**  
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**Session 1: Non-European Markets I**

**Time and date: 9.00-10.45, 25 April Thursday**  
**Room: Seeley**  
**Chair Person: Ranadeva Jayasekera**

**“Fool Me Once...”**  
**U.S. Investors’ Responses to the European Debt Crisis**

Carol C. Bertaut, Fang Cai and Nyssa Kim  
Board of Governors of the Federal Reserve System

**The Gold Price in Times of Crisis: Is There a Speculative Bubble?**

Jedrzej Bialkowski<sup>1</sup>, Martin T. Bohl<sup>2</sup>, Patrick M. Stephan<sup>2</sup> and Tomasz P. Wisniewski<sup>3</sup>  
<sup>1</sup>Presenting Author; University of Canterbury, Department of Economics and Finance,  
<sup>2</sup>WestphalianWilhelminian University of Münster, Department of Economics, Germany, <sup>3</sup>  
University of Leicester, School of Management, Great Britain

**Regulatory Change and Capital Adjustment of Cooperative Financial Institutions**

John Goddard, DonalMcKillop and John O.S. Wilson  
Goddard: Bangor University; McKillop: Queen’s University Belfast; Wilson: University of St  
Andrews

**Do Bubbles occur in Gold Prices? An application of Gold Lease Rates and Markov  
Switching Models.**

Brian M Lucey and Fergal A. O’Connor  
Trinity College Dublin, Dublin 2, Ireland.

## Session 2: **Risk I**

**Time and date: 9.00-10.45, 25 April Thursday**

**Room: Earl Jellicoe**

**Chair Person: Chris Adcock**

### **Bank and sovereign credit ratings during the European debt crisis**

RashaAlsakka<sup>a</sup>, Owain apGwilym<sup>a</sup>, Tuyet Nhung Vu<sup>a</sup>

<sup>a</sup> Bangor Business School, Bangor University, UK

### **Assessing the impact of sovereign credit re-ratings on financial return distributions using a multivariate regime switching long memory approach**

Hung Do<sup>a</sup>, Robert Brooks<sup>a</sup>, SirimonTreepongkaruna<sup>b</sup>, Eliza Wu<sup>c</sup>

<sup>a</sup>Department of Econometrics and Business Statistics, Monash University, Australia,

<sup>b</sup>Accounting and Finance, UWA Business School, The University of Western Australia, Australia, <sup>c</sup>Finance Discipline Group, UTS Business School, University of Technology

Sydney, Australia

### **Bank dividends, real GDP growth, and default risk**

Angelos Kanas

University of Piraeus

### **A Structural Credit Risk Model for the Analysis of Sovereign Default**

Z Purewsuren and C J Adcock

Sheffield University Management School

## Session 3: Macroeconomics I

**Time and date: 9.00-10.45, 25 April Thursday**

**Room: Tanners**

**Chair Person: Taufiq Choudhry**

### **The impact of monetary policy shocks on financially constrained firms' returns: Comprehensive evidence from the UK market**

Nikolaos Balafas<sup>a</sup> and Alexandros Kostakis<sup>b</sup>

<sup>a</sup> University of Liverpool Management School, Liverpool, UK , <sup>b</sup> Corresponding author.  
Manchester Business School, University of Manchester, UK.

### **The International Transmission of Monetary Policy Shocks on Stock Returns: Does Foreign Policymakers' Reaction Make a Difference?**

Georgios Chortareas<sup>a</sup> and Emmanouil Noikokyris<sup>b</sup>

<sup>a</sup> Department of Economics, University of Athens, Greece, <sup>b</sup> Kingston Business School,  
Kingston University London, UK

### **The effect of monetary policy interventions on stock markets and G-SIFIs during the crisis**

Franco Fiordelisi<sup>a,b\*</sup>, Giuseppe Galloppo<sup>c</sup>, Ornella Ricci<sup>a</sup>

<sup>a</sup> University of Roma Tre, Italy <sup>b</sup> Bangor Business School, UK <sup>c</sup> University of Viterbo La  
Tuscia, Italy

### **The real effects of financial stress in the Eurozone**

Sushanta K. Mallick<sup>1</sup> and Ricardo M. Sousa<sup>2</sup>

<sup>1</sup> Queen Mary University of London, <sup>2</sup> University of Minho and LSE, FMG

## Session 4: **Banking I**

**Time and date: 9.00-10.45, 25 April Thursday**

**Room: Mill Room**

**Chair Person: Silviu Ursu**

### **The determinants of long-term bank funding conditions**

Andrea Cardillo<sup>1</sup> and Andrea Zaghini<sup>2</sup>

<sup>1</sup> Bancad'Italia, Economic and Financial Statistics Department, Italy, <sup>2</sup>Bancad'Italia, Economic Policy and Monetary Policy Department, Italia

### **A simulation model of the UK “CHAPS” interbank payment system with payment prioritisation**

Robert De Caux, Markus Brede and Frank McGroarty  
School of Management, University of Southampton, UK

### **Cooperative Banking in Poland: A Post-Crisis Record of Stability and Efficiency**

Ewa Miklaszewska and Krzysztof Kil  
Cracow University of Economics

### **IMPACT OF GLOBAL FINANCIAL CRISIS ON TRADITIONAL AND SHADOW BANKING PERFORMANCE: EVIDENCE FROM EUROPE**

Silviu Ursu<sup>a</sup> and AlinAndries<sup>b</sup>

AlexandruIoanCuza University of Iasi, Department of Finance, Money and Public Administration

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**TEA BREAK 10.45 -11.00**

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## Session 5: Contagion/Linkage I

**Time and date: 11.00-12.45, 25 April Thursday**

**Room: Seeley**

**Chair Person: Janusz Brzeszczyński**

**On the linkages between stock prices and exchange rates: Evidence from the banking crisis of 2007–2010**

Guglielmo Maria Caporale<sup>a</sup>, John Hunter<sup>a</sup>, FaekMenla Ali<sup>a</sup>

<sup>a</sup>Department of Economics and Finance, School of Social Sciences, Brunel University, UK

**CONTAGION IN GOVERNMENT BOND SPREADS AMONG EURO AREA COUNTRIES**

George Hondroyiannis, Harry H. Kelejian, PurbaMukerji and George S. Tavlak  
Bank of Greece and Harokopio University, University of Maryland, College Park,  
Connecticut College, New London, Bank of Greece

**Interdependence of Stock Markets Before and After the Global Financial Crisis of 2007**

Boulis M. Ibrahim and Janusz Brzeszczyński  
Heriot-Watt University, Edinburgh

**Investor Induced Contagion during the Banking and Sovereign Debt Crisis: Wealth Effect versus Portfolio Rebalancing**

Dimitris Petmezas<sup>a</sup> and Daniel Santamaria<sup>b\*</sup>

a Surrey Business School, University of Surrey, b\* (Presenter) Canterbury Business School, Canterbury Christ Church University

## Session 6: **Banking II**

**Time and date: 11.00-12.45, 25 April Thursday**

**Room: Earl Jellicoe**

**Chair Person: Gerhard Kling**

### **How Does the State Affect Bank Fragility in the EMU?**

Stefan Eichler and Karol Sobanski

TechnischeUniversitaet Dresden, Faculty of Business and Economics, Germany

### **Market Perceptions of US and European Policy Actions Around the Subprime Crisis**

TheoharryGrammatikos, Thorsten Lehnert and Yoichi Otsubo

Luxembourg School of Finance, University of Luxembourg

### **Central Bank Transparency and Financial Stability: Measurement, Determinants and Effects**

Roman Horváth and Dan Vaško

Institute of Economic Studies, Charles University, Czech Republic

### **Has the financial crisis had an adverse effect on bank competition?**

Ali Mirzaei and Tomoe Moore

Department of Economics and Finance, Brunel University, UK

Special Session I: **The consequences of the crisis on the performance of  
European cooperative banking**

**Time and date: 11.00-12.45, 25 April Thursday**

**Room: Tanners**

**Chair Person: Silvio Goglio**

**Discussant: Yiorgos Alexopoulos**

**Organizational Structure and Exposure to Crisis among European Banks: Evidence  
from Rating Changes**

Giovanni Ferri (University of Bari), Panu Kalmi (University of Vaasa), Eeva Kerola (Aalto School of Economics)

**Bank lending procyclicality and credit quality during the crisis of 2008-2009**

Stefano Di Colli <sup>(a), (c)</sup>

Juan Sergio Lopez <sup>(a)</sup>

<sup>(a)</sup>FederCasse Economic Research Department and International relations Via Lucrezia Romana Rome, <sup>(d)</sup> University of Teramo,

**Persistent cooperative stabilizers in the lingering financial and economic misery**

Hans Groeneveld

Senior Vice President Cooperative and Sustainable Business at Rabobank Nederland

**Cooperative *versus* conventional (joint-stock) banking in Europe:  
comparative resistance and resilience during the recent financial crisis**

Yasmina LEMZERI and Mireille JAEGER, Jean-Noel ORY  
CEREFIGE - University of Lorraine, France

Special Session II: *Money Macro Finance Research Group Session*

**Time and date: 11.00-12.45, 25 April Thursday**

**Room: Mill Room**

**Chair Person: Andrew Mullineux**

**Discussant: Charles Goodhart**

**Supranational regulation - how much and for whom?**

Thorsten Beck and Wolf Wagner  
European Banking Center

**The Eurozone Crisis: Escaping the ‘Doom Loop’**

Andy Mullineux  
Bournemouth University

**The European crisis: Causes and Solutions - An Application of the Quantity Theory of Credit**

Richard Werner  
University of Southampton

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**LUNCH 12.45 – 1.45 COACH HOUSE SUITE**  
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**Presentation by Bloomberg 1.45 – 2.05 Cedar Suite**  
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**Lunch Time Presentation by Professor Charles Goodhart 2.10 – 2.50 Cedar Suite**  
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**Tea Break 2.50 – 3.00**  
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## Session 9: **Bond Markets**

**Time and date: 3.00-5.00, 25 April Thursday**

**Room: Seeley**

**Chair Person: Marco Committeri**

**Does gold offer a better protection against sovereign debt crisis than other metals?**

Sam Agyei-Ampomah<sup>1</sup>, Dimitrios Gounopoulos<sup>2</sup>, Khelifa Mazouz<sup>3</sup>

<sup>1</sup>Cranfield School of Management, University of Cranfield, Bedford, UK., <sup>2</sup>Surrey Business School, University of Surrey, UK, <sup>3</sup>Management School, University of Bradford, Bradford, UK

**You Never Give Me Your Money? Sovereign Debt Crises, Collective Action Problems, and IMF Lending**

Marco Committeri\* and Francesco Spadafora\*\*

\* Bank of Italy, Department of International Economic Analysis and Relations, \*\* Bank of Italy

**Foreign investors and risk shocks: seeking a safe haven or running for the exit?**

Maurizio Michael HABIB and Livio STRACCA

European Central Bank, Kaiserstrasse, Frankfurt am Main, Germany

**Entering the Public Bond Market during the Financial Crisis**

Eilnaz Kashefi-Pour

Birmingham Business School, UK

**Vine copulas and applications to the European Union sovereign debt analysis**

Dalu Zhang

School of Economics, University of East Anglia, UK

## Session 10: Equity Markets I

**Time and date: 3.00-5.00, 25 April Thursday**

**Room: Earl Jellicoe**

**Chair Person: Gishan Dissanaik**

### **Does the Stock Market Reward Innovation: Market Reactions to Negative News During the 2007–2012 Global Financial Crisis**

Christopher Adcock<sup>(1)</sup>, XiupingHua<sup>(2)</sup> and Shuxing Yin<sup>(1)</sup>

(1) Sheffield University Management School, Sheffield, UK; (2) University of Nottingham, Ningbo, China

### **Global Financial Crisis and Multiscale Systematic Risk: Evidence from Selected European Markets**

Antonios K. Alexandridis<sup>1</sup> and Mohammad S. Hasan<sup>2</sup>

<sup>1</sup> University of Kent, School of Mathematics, Statistics and Actuarial Science, <sup>2</sup> Kent Business School, University of Kent

### **European ‘fear’ indices – evidence before and after the financial crisis**

Wolfgang Aussenegg<sup>(a)</sup>, Lukas Goetz<sup>(b)</sup>, and Ranko Jelic<sup>(c)\*</sup>

(a) Department of Finance and Corporate Control, Vienna University of Technology, Austria, (b) UNIQA Capital Markets GmbH, Vienna, Austria, (c)\*Corresponding author; Department of Accounting and Finance, University of Birmingham, UK

### **Efficiency Characteristics of the European banking sector and the Global Financial Crisis of 2007-2012**

Taufiq Choudhry and Ranadeva Jayasekera

School of Management, University of Southampton, UK

### **Signalling Quality of UK firms during the global financial crisis: Clinical study of theory and Evidences**

Gishan Dissanaik, Jonathan Faasse, Ranadeva Jayasekera

Cambridge Judge Business School; University of Cambridge, School of Management, University of Southampton

## Session 11: Risk II

**Time and date: 3.00-5.00, 25 April Thursday**

**Room: Tanners**

**Chair Person: Owain apGwilyn**

### **The Greek Effect? Default Risk Transfer between Eurozone Sovereign and Financial Sectors**

Anurag Banerjee<sup>a,1</sup>, Chi-Hsiou Hung<sup>b,2</sup>, Kai Lisa Lo<sup>a,\*</sup>,

<sup>a</sup> Durham Business School, University of Durham, United Kingdom, <sup>b</sup>School of Business, University of Dundee, United Kingdom

### **The Determinants of the source of Debt and Debt Diversification: Empirical Evidence from European Non-Financial Firms 2000-2011**

Debolina Banerjee and Amrit Judge

Department of Economics and International Development, Middlesex University Business School

### **A Theory of Sovereign Risk Premia and Financial Intermediation in the Euro Area**

Philipp Englerand Christoph Grosse Steffen

### **Financial Factors and the International Transmission Mechanism**

Abigail Haddow and MariyaMilev

### **Liquidity and Credit Risks in the UK's Financial Crisis: How QE changed the relationship**

Woon Wong, Wanru Yao and Peter Howells

Centre for Global Finance, Bristol Business School, UWE Bristol



## Session 12: Exchange Rates

**Time and date: 3.00-5.00, 25 April Thursday**

**Room: Mill Room**

**Chair Person: Taufiq Choudhry**

### **UK Imports from Germany, Japan and the US: Empirical Investigation of the Third Country effect and the Global Financial Crisis**

Taufiq Choudhry, Syed Shabi Ul Hassan and Fotios I. Papadimitriou  
School of Management, University of Southampton, UK

### **Are the effects of market news on asset prices and exchange rates changing?**

Linda Goldberg<sup>1</sup> and Christian Grisse<sup>2</sup>

<sup>1</sup> Federal Reserve Bank of New York, Research Department, USA, <sup>2</sup> Swiss National Bank, Zürich

### **On financial risk and the safe haven characteristics of Swiss franc exchange rates**

Christian Grisse and Thomas Nitschk  
Swiss National Bank, Monetary Policy Analysis, Zurich, Switzerland.

### **The euro exchange rate during the European sovereign debt crisis – dancing to its own tune?**

Michael Ehrmann<sup>1</sup>, Chiara Osbat<sup>2</sup>, Jan Strasky<sup>3</sup> and Lenno Uusküla<sup>4</sup>

<sup>1</sup> European Central Bank. <sup>2</sup> European Central Bank. <sup>3</sup> Organisation for Economic Co-operation and Development. <sup>4</sup> Bank of Estonia.

### **Credit Risk, Liquidity or Funding Access? Foreign-Exchange Forwards in a Post-2008 World**

Justin Yap

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**Key Note Speech Professor James Lothian 5.15 – 6.15 Cedar Suite**  
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**Conference Dinner 6.30 – 10.30 Lord Selbourne**  
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## Session 13: Non-European Markets II

**Time and date: 8.30-10.15, 26 April Friday**

**Room: Seeley**

**Chair Person: David G. McMillan**

### **Business Cycles, International Trade and Capital Flows: Evidence from Latin America**

Guglielmo Maria Caporale\* and Alessandro Girardi\*\*

\*Department of Economics and Finance, and Centre for Empirical Finance, Brunel University \*\*ISTAT, Via Cesare Balbo, Rome, Italy

### **Stock Market Reaction to Fed Funds Rate Surprises: State Dependence and the Financial Crisis**

Alexandros Kontonikias, Ronald MacDonald and Aman Saggi  
Economics Subject, Adam Smith Business School

### **Firm-level Contagion - An Asset Pricing Perspective**

Woon Sau Leung and Nicholas Taylor  
Cardiff University, UK

### **How Much Does Market Structure Matter? Evidence from US Bank Profit and Risk**

David G. McMillan<sup>a</sup> and Fiona J McMillan<sup>b</sup>

<sup>a</sup> Accounting and Finance Division, Stirling Management School, University of Stirling,

<sup>b</sup>School of Management, University of St Andrews

## Session 14: Macroeconomics II

**Time and date: 8.30-10.15, 26 April Friday**

**Room: Earl Jellicoe**

**Chair Person: Christopher A. Hartwell**

***Perseverare Diabolicum*: the shortcomings of pre-crisis financial regulation, and the repetition of the same mistakes in the regulatory response to the crisis**

Riccardo de Caria

University of Torino – Italy

**Financial Liberalization and Crises in Transition Economies: What Have 20+ Years Taught Us?**

Christopher A. Hartwell

Institute for Emerging Market Studies (IEMS), Moscow School of Management – SKOLKOVO, Russia

**Monetary Policy and Bank Lending in the Euro Area: Is there a Stock Market Channel or an Interest Rate Channel?**

Robert E. Krainer

University of Wisconsin-Madison, U.S.A.,

**The relationship between interest rates and nominal GDP growth in the U.S., U.K., Germany and Japan from the 1960s to 2008**

Richard A. Werner and Min Zhu

School of Management, University of Southampton, UK

## Session 15: Contagion/Linkage II

**Time and date: 8.30-10.15, 26 April Friday**

**Room: Tanners**

**Chair Person: Ranadeva Jayaserka**

### **Integration and Contagion: Global Evidence from Recent Crises**

Sungjun Cho, Stuart Hyde and Ngoc Nguyen  
Manchester Business School, University of Manchester

### **Linkages between European national stock markets during the years 1997-2012: The impact of financial crises and EU expansions**

Malgorzata Doman and Ryszard Doman  
<sup>1</sup>Poznan University of Economics, Department of Applied Mathematics, POLAND, <sup>2</sup> Adam Mickiewicz University in Poznan, Faculty of Mathematics and Computer Science, Laboratory of Financial Econometrics, POLAND

### **The Contagion Effect in Lending and Economic Stability: A Study of the European Sovereign-Debt Crisis and its Global Impact**

Yuki Masujima<sup>1</sup> and Winnie P. H. Poon<sup>2</sup>  
<sup>1</sup> Presenting Author; Japan Center for Economic Research, Japan, <sup>2</sup> Department of Finance and Insurance, Lingnan University, Hong Kong

### **Contagion Risk and Spillover Effects within the Eurozone Countries: How serious is the effect of the current sovereign debt crisis**

Andreas Tsopanakis  
University of Glasgow, Department of Economics, UK

## Session 16: **Banking III**

**Time and date: 8.30-10.15, 26 April Friday**

**Room: Mill Room**

**Chair Person: Gerhard Kling**

### **The impact of the euro crisis on deposit rate convergence and pass-through**

Ivo J.M. Arnold <sup>a,b</sup>, Saskia E. van Ewijk<sup>b</sup>

a Erasmus School of Economics, Rotterdam, the Netherlands, <sup>b</sup>Nyenrode Business University, Breukelen, the Netherlands

### **Financial stability implication of securitization: evidence from Italy**

Francesca Battagli<sup>1</sup>, Angela Gallo<sup>2</sup> and Maria Mazzuca<sup>3</sup>

<sup>1</sup> Assistant Professor, Dipartimento di Studi Aziendali, Università Parthenope, Italy,

<sup>2</sup> Assistant Professor, Dipartimento di Studi Aziendali, Università degli Studi di Salerno, Italy,

<sup>3</sup> Assistant Professor, Dipartimento di Scienze Aziendali, Università della Calabria, Italy

### **Banks' responses to funding liquidity shocks: Lending adjustment, liquidity hoarding and fire sales**

Jan Willem van den End and Leo de Haan

De Nederlandsche Bank, Amsterdam

### **The Interest Rate Pass-Through in the Euro Area during the Global Financial Crisis**

Nikolay Hristov<sup>1</sup>, Oliver Hülsewig<sup>2</sup> and Timo Wollmershäuser<sup>1</sup>

<sup>1</sup>Ifo Institute – Leibniz-Institute for Economic Research at the University of Munich, Germany,

<sup>2</sup>University of Applied Sciences, Germany

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**Tea Break 10.15-10.30**

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## Session 17: CDS

**Time and date: 10.30-12.30, 26 April Friday**

**Room: Seeley**

**Chair Person: Ghulam Sorwar**

### **Price discovery of credit spreads in tranquil and crisis periods**

Davide Avino, Emese Lazar and Simone Varotto

### **Fear or fundamentals? Speculative behaviour in the European CDS market**

Carl Chiarella<sup>1</sup>, Saskiater Ellen<sup>2</sup>, Tony He<sup>1</sup> and Eliza Wu<sup>1</sup>

<sup>1</sup> University of Technology, Sydney, <sup>2</sup> Corresponding author: Erasmus School of Economics, Erasmus University Rotterdam

### **CDS Spreads and Option Volatility during Crises**

José Da Fonseca & Katrin Gottschalk

Auckland University of Technology, Business School, New Zealand.

### **Sovereign Default Swap Market Efficiency and Country Risk in the Eurozone**

Yalin Gunduz<sup>1</sup> and Orcun Kaya<sup>2</sup>

Deutsche Bundesbank, Goethe University Frankfurt

### **Behaviour of the CDS spreads during the Eurozone crisis**

John Pereira<sup>1</sup>, Mohamed Nurullah<sup>1</sup> and Ghulam Sorwar<sup>2</sup>

<sup>1</sup> Kingston Business School, UK, <sup>2</sup> Nottingham University Business School, UK

## Session 18: Equity Markets II

**Time and date: 10.30-12.30, 26 April Friday**

**Room: Earl Jellicoe**

**Chair Person: Utz Weitzel**

**Can the information content of share repurchases improve the accuracy of equity premium predictions?**

Dimitris Andriosopoulos<sup>1</sup>, Dimitris K. Chronopoulos<sup>2</sup> and Fotios I. Papadimitriou<sup>3</sup>  
<sup>1</sup>School of Business and Economics, Swansea University, UK, <sup>2</sup>School of Management, University of St Andrews, UK, <sup>3</sup>School of Management, University of Southampton, UK

**European Equity Investing Strategy through the Financial Crisis: the role of Momentum and Trend Following**

Andrew Clare\*, James Seaton\*, Peter N. Smith† and Stephen Thomas\*

\*Faculty of Finance, Cass Business School, London, †Department of Economics, University of York.

**Momentum strategies in a group of European countries during the 2008 financial crisis**

Taufiq Choudhry and Yuan Wu  
School of Management, University of Southampton

**When the going gets tough: Insights into individuals' trading behaviour during, and their likelihood of 'surviving', the global financial crisis**

Johnnie E. V. Johnson, Peter A. F. Fraser-Mackenzie, Ming-Chien Sung, Tiejun Ma and Alexander Dolia  
Centre for Risk Research, School of Management, University of Southampton, UK.

**Fire-sale opportunities or flight to quality? Cross border takeovers in Europe and the crisis.**

Gerhard Kling<sup>1</sup>, Utz Weitzel<sup>2</sup> and Dirk Gerritsen<sup>3</sup>  
<sup>1</sup> Southampton University, Southampton, UK, <sup>2</sup> Radboud University Nijmegen, IMR, Department of Economics, Nijmegen, The Netherlands, <sup>3</sup> University Utrecht School of Economics, Utrecht, The Netherlands



## Session 19: **Banking IV**

**Time and date: 10.30-12.30, 26 April Friday**

**Room: Tanners**

**Chair Person: Simon Wolfe**

### **Bank bailouts, competition, and the disparate effects for borrower and depositor welfare**

Cesar Calderon<sup>a</sup> and Klaus Schaeck<sup>b</sup>

<sup>a</sup> The World Bank, <sup>b</sup> Bangor University

### **Towards a New Model for Early Warning Signals for Systemic Financial Fragility and Near Crises: An Application to OECD Countries**

Barbara Casu, Andrew Clare and NashwaSaleh  
Cass Business School, City University London

### **Banking branch network, local contestability and consumer welfare during the financial crisis**

Marta Degl'Innocenti<sup>1</sup>, Claudia Girardone<sup>2</sup>, Giuseppe Torluccio<sup>3</sup> and Simon Wolfe<sup>1</sup>

<sup>1</sup> School of Management, University of Southampton, Highfield Southampton, United Kingdom, <sup>2</sup> Essex Business School, University of Essex, Wivenhoe Park, Colchester, United Kingdom, <sup>3</sup> Department of Management, University of Bologna, Via Capo di Lucca, Italy

### **'Too Systemically Important to Fail' in Banking – Evidence from Banking Mergers and Acquisitions**

Philip Molyneux<sup>a\*</sup>, Klaus Schaeck<sup>a</sup>, Tim Mi Zhou<sup>b</sup>

<sup>a</sup> Bangor Business School, Bangor University, Wales, UK, <sup>b</sup> Sunderland Business School, Sunderland University, England, UK

### **Asymmetric information and the behaviour of bank default risk in a financial crisis**

Peter Spencer  
University of York, UK

## Session 20: Economic Growth and Wealth Effects

**Time and date: 10.30-12.30, 26 April Friday**

**Room: Mill Room**

**Chair Person: Yaz Gulnur Muradoglu**

### **The Value of Government Ownership during the Global Financial Crisis**

Christof Beuselinck<sup>1</sup>, Lihong Cao<sup>2</sup>, Marc Deloof<sup>3</sup> and Xiping Xia<sup>4</sup>

<sup>1</sup> IESEG School of Management and LEM, <sup>2</sup>Huazhong University of Science and Technology and University of Antwerp, <sup>3</sup> Presenting author; University of Antwerp,

<sup>4</sup>University of Science and Technology

### **The Recent Financial Crisis and Europe's Economic Growth and Convergence**

René Cabral and Jorge Jaramillo

Tecnológico de Monterrey, Campus Monterrey, Escuela de Graduados en Administración Pública y Política Pública, Ave. Rufino Tamayo, Garza García, NL, México

### **Economic and Financial Growth in Europe. Is Euro Beneficial for all Countries?**

Kalaitzoglou Iordanis and Beatrice Durgheu

Audencia PRES-LUNAM, School of Management, Centre for Financial and Risk Management, Department of Economics, Finance and Accounting, Coventry Business School, Birmingham

### **Wealth Effects of the Eurozone Crisis: Evidence from European Financial Markets**

Walter Matthias Kirsten<sup>a,f</sup>, Ali M. Kutan<sup>b,c,d</sup> and YazGulnurMuradoglu<sup>c,e,f</sup>

<sup>a</sup> Cass Business School, City University, London, UK, <sup>b</sup>Department of Economics and Finance, Southern Illinois University Edwardsville, USA, <sup>c</sup>The Emerging Markets Group, Cass Business School, City University London, UK, <sup>d</sup>The William Davidson Institute, Michigan, USA, <sup>e</sup>School of Business and Management, Queen Mary, University of London, UK, <sup>f</sup>Behavioural Finance Working Group, UK

## **ABSTRACTS**

## Session 1: **Non-European Markets I**

Time and date: 9.00-10.45, 25 April Thursday

Room: Seeley

Chair Person: **Ranadeva Jayasekera**

### **“Fool Me Once...” U.S. Investors’ Responses to the European Debt Crisis**

**Carol C. Bertaut, Fang Cai and Nyssa Kim**

Board of Governors of the Federal Reserve System

#### **Abstract**

This paper examines U.S. investors’ portfolio investment patterns since the global financial crisis with particular focus on responses to the European debt crisis that began in late 2009. The global financial crisis of 2007-2008 was accompanied by dramatic changes in U.S. investors’ portfolio investment abroad. U.S. investors experienced significant valuation losses, and pulled back notably from their foreign investment, especially from foreign debt. In contrast, while they have again incurred sizable losses on cross-border investment – especially in equity – during the European debt crisis, U.S. investors so far have not pulled back from their long-term cross-border investments, even from Europe. Holdings data show that U.S. investors have continued to invest in European debt, particularly in government debt, although they have made little new investment in the financial sector. This continued interest in European securities could owe to the fact that most of U.S. holdings of European debt have been concentrated in dollar-denominated debt issued by core euro area countries and the United Kingdom, which are deemed relatively safe. Changes in the composition of holdings over the past couple years suggest that U.S. investors have behaved in a way that reflects their diversity and differing objectives: many looked for safer investments, but on the margin some investors appear to have also reached for higher yields.

# The Gold Price in Times of Crisis: Is There a Speculative Bubble?

**Jedrzej Bialkowski<sup>1</sup>, Martin T. Bohl<sup>2</sup>, Patrick M. Stephan<sup>2</sup> and  
Tomasz P. Wisniewski<sup>3</sup>**

<sup>1</sup> Presenting Author; University of Canterbury, Department of Economics and Finance

<sup>2</sup> Westphalian Wilhelminian University of Münster, Department of Economics, Germany

<sup>3</sup> University of Leicester, School of Management Great Britain

## **Abstract**

Motivated by the current gold price boom, this paper investigates whether rapidly growing investment activities have caused a new asset price bubble. Drawing on gold's role as dollar hedge, inflation hedge, portfolio diversifier and safe haven, we calculate fundamentally justified returns and approximate gold's fundamental value. Based on the deviations of the actual gold price from its fitted value, we then apply a Markov regime-switching Augmented Dickey-Fuller (ADF) test, which has substantial power for detecting explosive behavior. Our empirical evidence is favorable for a fundamentally justified price level even during the recent world financial and the current European sovereign debt crisis.

# **Regulatory Change and Capital Adjustment of Cooperative Financial Institutions**

**John Goddard, DonalMcKillop and John O.S. Wilson**

Goddard: Bangor University; McKillop: Queen's University Belfast; Wilson: University of St Andrews

## **Abstract.**

We investigate the determinants of US credit union capital-to-assets ratios, before and after the implementation of the current capital adequacy regulatory framework in 2000. Capitalization varies pro-cyclically, and credit unions classified as adequately capitalized or below followed a faster adjustment path than well capitalized credit unions. Credit unions managed their capital more actively following the change in regulation. During the recent financial crisis, large credit unions experienced a smaller reduction in capitalization, on average, than small credit unions. The z-score risk measure was a more reliable predictor of survival or non-survival during the crisis than several other financial-health indicators.

## **Do Bubbles occur in Gold Prices? An application of Gold Lease Rates and Markov Switching Models.**

**Brian M Lucey and Fergal A. O'Connor**

Trinity College Dublin, Dublin 2, Ireland.

### **Abstract**

We assess whether two classes of bubbles occur in the spot price of gold, rational speculative and periodically bursting bubbles, using gold's lease rates for the first time in the literature as a measure of its fundamental value. This question is of particular significance as these are the only observable market measures of a yield that can be earned by owning gold. We use traditional unit root and cointegration tests for rational speculative bubbles and Markov Switching Augmented Dickey-Fuller tests for periodically bursting bubbles. Bubbles are found to possibly exist for in ADF and cointegration bubble tests, but under the Markov switching model no bubble found to be present.

## Session 2: Risk I

Time and date: 9.00-10.45, 25 April Thursday

Room: Earl Jellicoe

Chair Person: **Chris Adcock**

### **Bank and sovereign credit ratings during the European debt crisis**

**Rasha Alsakka<sup>a</sup>, Owain apGwilym<sup>a</sup>, TuyetNhungVu<sup>a</sup>**

<sup>a</sup> Bangor Business School, Bangor University, UK

#### **Abstract**

The paper analyses the behaviour of European sovereign and bank ratings assigned by the larger credit rating agencies (Moody's, S&P and Fitch) during the current debt crisis. We find that sovereign rating downgrades and negative watch signals have strong effects on bank rating downgrades. The impact is more pronounced in PIIGS countries and stronger for negative watch signals than for actual downgrades. We find significant differences in rating policies across the three credit rating agencies, and show evidence of interdependence in bank rating actions. S&P and Fitch credit actions tend to be the more independent ones, while Moody's appears to be more cautious, although it is by far the most likely to assign multiple-notch downgrades.



# **Assessing the impact of sovereign credit re-ratings on financial return distributions using a multivariate regime switching long memory approach**

**Hung Do<sup>a</sup>, Robert Brooks<sup>a</sup>, Sirimon Treepongkaruna<sup>b</sup>, Eliza Wu<sup>c</sup>**

<sup>a</sup>Department of Econometrics and Business Statistics, Monash University, Australia

<sup>b</sup>Accounting and Finance, UWA Business School, The University of Western Australia, Australia

<sup>c</sup>Finance Discipline Group, UTS Business School, University of Technology Sydney, Australia

## **Abstract**

We investigate the effects of credit rating agencies (CRAs)' sovereign credit assessments on stock and currency return distributions by developing a framework that allows a multivariate system of long memory processes to be conditional on specific credit rating regimes. We find heterogeneous effects of sovereign rating actions across regimes. Furthermore, we reveal that the total effects (both direct and indirect forces) of sovereign credit assessments can be different to their direct effects. We find that the rank orders of CRAs are not unique across rating regimes nor for each realized moment.

# **Bank dividends, real GDP growth, and default risk**

**Angelos Kanas**

University of Piraeus

## **Abstract**

We reveal evidence that the U.S. aggregate bank dividends exercise a causal impact on the U.S. real GDP growth during the period from the introduction of the Prompt Corrective Action (PCA) framework in 1992 until the outburst of the recent financial crisis in 2007. Over this period, the positive signaling effects of bank dividends outperform the negative effect of dividends on default risk. During the pre-PCA and the recent post-2007 periods, bank dividends do not affect GDP growth. This regime-dependent relation is due to an asymmetric role of bank default risk. These findings are of interest to bank regulators in reassessing the role of bank dividends within Basel III, and carry important policy implications as bank dividends constitute an important tool available to policy makers for strengthening real activity.

# **A Structural Credit Risk Model for the Analysis of Sovereign Default**

**Z Purewsuren and C J Adcock**

Sheffield University Management School

## **Abstract**

The issue of sovereign credit risk and sovereign balance sheet are more important today than ever before, given the recent financial crisis and the current sovereign debt crisis in Europe. This paper has three objectives. The first is to apply a structural credit risk model, which depends on the Black-Scholes-Merton option pricing formula, to estimate sovereign default probabilities for both European and other countries which account for around 70% of global GDP and over 70% of sovereign debt. The model also results in estimates of distance to default and sovereign credit spread. The empirical performance of this model applied to sovereigns confirms the findings reported for its application to corporate debt. Default probabilities are seriously under-estimated, as are the values of sovereign spread. The second objective of the paper is to report an investigation into the standard but arbitrary assumptions conventionally made about the use of national accounts data as inputs to the model. The paper shows that estimates of default probabilities and related parameters are sensitive to these assumptions.

The third objective is to report a theoretical contribution to structural credit risk models. A new model is presented in which the market value of sovereign credit spread is an input to the model rather than an output. The new model is used in conjunction with Itô's lemma to derive the Wiener process for sovereign spread. This approach has not been reported in the literature previously. Using this model, the paper shows that the implied probabilities of default are larger than those obtained using the standard structural model. This new model also results in revised values for domestic currency liabilities and its volatility. These are larger than the actual values reported by national agencies and are interpreted as the market's implicit valuation of debt.

The empirical analysis is presented in two parts: for (i) the fourteen European Union countries for which national accounts data is available and (ii) for eleven non-EU countries, which include Brazil, Japan, Russia and the United States. Two key and topical outputs from the model are default rankings for Eurozone and non-Eurozone countries.

## Session 3: Macroeconomics I

Time and date: 9.00-10.45, 25 April Thursday

Room: Tanners

Chair Person: **Taufiq Choudhry**

### **The impact of monetary policy shocks on financially constrained firms' returns: Comprehensive evidence from the UK market**

**Nikolaos Balafas<sup>a</sup> and Alexandros Kostakis<sup>b</sup>**

<sup>a</sup> University of Liverpool Management School, Liverpool, UK

<sup>b</sup> Corresponding author. Manchester Business School, University of Manchester, UK.

#### **Abstract**

This study provides comprehensive evidence on the return response of financially constrained firms listed on London Stock Exchange (LSE) to UK monetary policy shocks, extracted on Bank of England's MPC meetings relative to expectations embedded in interest rate futures prices, during the period June 1999- December 2011. Using a large number of financial constraints proxies, we find no significant evidence that the most constrained firms' returns are more responsive to monetary policy shocks relative to the least constrained ones, as the credit channel of the monetary policy transmission mechanism would suggest. We also show that the inverse relationship between interest rate shocks and UK stock returns reversed its sign and became significantly positive during the recent financial crisis period. Finally, we provide extensive evidence on the state dependence of the interest rate shocks- returns relationship, showing that UK stock returns were much more responsive to monetary policy shocks during periods of tight credit market conditions.

# **The International Transmission of Monetary Policy Shocks on Stock Returns: Does Foreign Policymakers' Reaction Make a Difference?**

**Georgios Chortareas<sup>a</sup> and Emmanouil Noikokyris<sup>b</sup>**

<sup>a</sup>*Department of Economics, University of Athens, Greece*

<sup>b</sup>*Kingston Business School, Kingston University London, UK*

## **Abstract**

With this empirical study we have a twofold objective; namely, firstly, to analyse the effects of the Fed's monetary policy announcements on global equity markets, and secondly, to investigate the extent to which foreign monetary policymakers' response to the U.S. monetary policy action influences the magnitude and the way U.S. monetary policy feeds through to global stock markets. We find significant spillover effects of the Fed's actions on foreign stock prices. Moreover, foreign policymakers' reactions to Fed's actions determine the way the U.S. monetary policy shocks are transmitted to the global equity markets.

# **The effect of monetary policy interventions on stock markets and G-SIFIs during the crisis**

**Franco Fiordelisi<sup>a,b\*</sup>, Giuseppe Galloppo<sup>c</sup>, Ornella Ricci<sup>a</sup>**

*<sup>a</sup> University of Roma Tre, Italy*

*<sup>b</sup> Bangor Business School, UK*

*<sup>c</sup> University of Viterbo La Tuscia, Italy*

## **Abstract**

Central banks have run during the crisis a wide set of monetary policy interventions using new instruments and techniques to restore the monetary stability and thus re-establish the stability of financial (and banking) systems. We analyze the effect of monetary policy interventions on stock markets in the most advanced monetary areas (Euro area, Japan, U.S., U.K., and Switzerland). We estimate cumulated abnormal returns (CARs) around the announcement of each monetary policy intervention focusing on: 1) interbank credit market; 2) stock markets; and 3) Global-Systematically Important Financial Institutions (G-SIFIs). We show that different monetary policy interventions from single central banks have produced a diverse market reaction. Non-conventional measures have been more effective than traditional ones in restoring the stability of financial and banking sectors. Dividing the sample period into three different time intervals, we also show that the impact of expansionary interventions was particularly significant during the subprime crisis, while the effect of restrictive interventions was more relevant during the sovereign debt crisis.

# The real effects of financial stress in the Eurozone

Sushanta K. Mallick<sup>1</sup> and Ricardo M. Sousa<sup>2</sup>

<sup>1</sup> Queen Mary University of London

<sup>2</sup> University of Minho and LSE, FMG

## Abstract

This paper examines the real effects of financial stress in the Euro-zone, using two identification strategies based on a Bayesian Structural VAR and a Sign-Restriction VAR. As expansionary monetary policy has been blamed to have fuelled asset price bubble, it is important to assess the macroeconomic impact of both a financial stress shock and a monetary policy shock. We find that unexpected variation in financial stress conditions plays an important role in explaining output fluctuations and, therefore, demands an aggressive response by the monetary authority to stabilise output. This, in turn, indicates a preference shift from inflation targeting. We also show that a monetary policy contraction strongly deteriorates financial stress conditions. As a result, rapid credit growth due to a long period of low interest rates possibly contributed to an increase in asset prices and encouraged unsustainable demand growth as observed in the recent financial crisis.

## Session 4: **Banking I**

Time and date: 9.00-10.45, 25 April Thursday

Room: Mill Room

Chair Person: **Silviu Ursu**

### **The determinants of long-term bank funding conditions**

**Andrea Cardillo<sup>1</sup> and Andrea Zaghini<sup>2</sup>**

<sup>1</sup> Bancad'Italia, Economic and Financial Statistics Department, Italy

<sup>2</sup> Bancad'Italia, Economic Policy and Monetary Policy Department, Italy

#### **Abstract**

We assess the long-term funding conditions for banks in the US, euro area and the UK and, separately, for the group of global systemically important financial institutions (G-SIFIs), over the period 1997-2011. In particular, after the outbreak of the subprime crisis in 2007 there was a considerable reshuffling of the relative weight of banks' funding sources – also due to non-conventional monetary policy interventions and government support measures – and a significant increase in wholesale funding cost. By looking at 6400 bank bonds we find that both implicit and explicit guarantees by the sovereign have a substantial role in shaping the wholesale cost of bond issuance with significant differences between AAA-rated and lower rated countries. However, when a bank CDS exists the role of the government is significantly reduced with the market giving more weight to the soundness and creditworthiness of the issuing institution.



# **A simulation model of the UK “CHAPS” interbank payment system with payment prioritisation**

**Robert De Caux, Markus Brede and Frank McGroarty**

School of Management, University of Southampton, UK

## **Abstract**

At £575bn, the average daily throughput of the two main UK interbank payment systems is roughly equivalent to one-third of UK annual GDP. However, that understates the importance of interbank payment dynamics. During the recent banking crisis, trust between banks was greatly reduced, with a fear that payments would not be made in a timely manner. Under current liquidity regulations, banks were able to alleviate this operational risk by obtaining liquidity from the Bank of England at negligible opportunity cost, but if and when these regulations change, the associated costs of raising liquidity will substantially increase and lead to a heightened danger of systemic operational risk. We model the incentives to banks in the UK CHAPS interbank payment system and further existing models by incorporating more realistic assumptions about bank behaviour, specifically with regards to payment prioritisation.

Within interbank payment systems, banks are incentivised to minimise their cost of borrowing liquidity from the central bank and the reputational cost of payment delays, but these incentives may not produce the most socially beneficial outcome for the system as a whole. Using a game-theoretic approach in the context of a multi-agent simulation model of CHAPS, we allow banks autonomy over their liquidity borrowing and payment prioritisation on a daily basis. These decisions are made to minimize the trade-off between payment delay costs and liquidity costs, subject to assumptions about a stochastic flow of incoming payments and payment requests. We then compare the equilibrium of our strategizing banks with the socially optimal strategy that a central planner would invoke to minimise system-wide cost. Finally we draw some general conclusions from these results about what measures financial regulators should employ to improve performance of the system under stress conditions, in terms of liquidity pricing and throughput management.

# **Cooperative Banking in Poland: A Post-Crisis Record of Stability and Efficiency**

**Ewa Miklaszewska and Krzysztof Kil**

Cracow University of Economics

## **Abstract**

Globalisation and the growing complexity of banking firms, and post-crisis bank restructuring, based on massive public assistance to the largest banks, pose the question of whether in the global post-crisis environment there is still a role for locally based cooperative banks, with their traditional intermediation model. Facing fewer competitive pressures from the environment/shareholders, and with a traditional business model with long-term objectives, cooperative banks should in principle behave more prudently and take fewer risks. The aim of the paper is to determine whether Polish cooperative banks have a post-crisis performance record superior to that of universal banks, due to their safer business model.

Using the bank stability index and Z-score indicator, the paper concludes that the Polish cooperative banking sector is safe, profitable, but slightly inefficient, and needs pressure exerting on it in order to expand. The “niche bank status quo” seems to fulfill the needs of both universal banks, which do not intend to operate in rural areas, and cooperative banks, which feel comfortable with their traditional functions. Thus, the policy conclusion of the paper is that although the current performance of the Polish cooperative sector is sound, regulatory support for this sector will be necessary in the long run, either through strengthening the position of associating banks, or by creating incentives for the largest cooperative banks to demutualize.

# IMPACT OF GLOBAL FINANCIAL CRISIS ON TRADITIONAL AND SHADOW BANKING PERFORMANCE: EVIDENCE FROM EUROPE

Silviu Ursu<sup>a</sup> and Alin Andries<sup>b</sup>

Alexandru Ioan Cuza University of Iasi, Department of Finance, Money and Public Administration

## Abstract

The global financial crisis of 2007-2012 restores the issue of how sensitive is the performance of banks and other entities within the financial system to macroeconomic conditions. A major concern is on the part of the financial system called shadow banking that refers, according to the Financial Stability Board's work, to the activities related to credit intermediation and involving liquidity and maturity transformation and leverage that take place outside the regular banking system. This experienced a significant growth in the years before the financial crisis, rivaling the traditional banking system in the intermediation of credit to households and businesses. Though the crisis had a major impact on overall profitability of both traditional and shadow banking, there is significant variation in the different measures of performance of financial intermediaries across countries during that period.

This paper seeks to investigate the main factors that determine the performance of commercial banks and shadow banking entities across European countries before and during the current financial crisis. The aim is to assess the differences between internal (bank level) and external (macroeconomics and financial system level) variables. We also intend to highlight and explain any potential differences between various groups of countries according to their European Union or Eurozone membership, and, more important, between commercial banks and financial intermediaries within the shadow-banking perimeter. We use the Eurosystem's approach, according to which the grouping other financial intermediaries (OFI) sector in ESA 95 includes many of the entities that could be involved in shadow banking activities and obtain the micro-level data from the Bankscope database for the period 2004-2010. The data on financial crisis, financial systems characteristics and macroeconomic variables is taken from World Bank, EBRD, ECB reports and recently updated database of Laeven and Valencia (2012).

We use a linear model estimated using the panel least square fixed effects methodology. Performance is proxied alternatively by several variables - return of average assets, distance to default or cost efficiency, which are regressed on a set of common explanatory variables, following the empirical literature on bank performance.

Our findings show that the global financial crisis has exerted a negative and significant impact of the performance of both traditional and shadow credit intermediaries, with differences in magnitude at country-level and also between commercial banks and other financial intermediaries.

## Session 5: Contagion/Linkage I

Time and date: 11.00-12.45, 25 April Thursday

Room: Seeley

Chair Person: **Janusz Brzeszczynski**

### **On the linkages between stock prices and exchange rates: Evidence from the banking crisis of 2007–2010**

**Guglielmo Maria Caporale<sup>a</sup>, John Hunter<sup>a</sup>, FaekMenla Ali<sup>a</sup>**

<sup>a</sup>Department of Economics and Finance, School of Social Sciences, Brunel University, UK

#### **Abstract**

This study examines the nature of the linkages between stock market prices and exchange rates in six advanced economies, namely the US, the UK, Canada, Japan, the euro area, and Switzerland, using data on the banking crisis between 2007 and 2010. Bivariate GARCH-BEKK models are estimated producing evidence of unidirectional spillovers from stock returns to exchange rate changes in the US and the UK, in the opposite direction in Canada, and of bidirectional spillovers in the euro area and Switzerland. Furthermore, causality-invariance from stock returns to exchange rates changes is found in Japan and in the opposite direction in the euro area and Switzerland, whilst there is evidence of bidirectional feedback in the US and Canada. These findings imply limited opportunities for investors to diversify their assets during this period.

# **CONTAGION IN GOVERNMENT BOND SPREADS AMONG EURO AREA COUNTRIES**

**George Hondroyiannis**

Bank of Greece and Harokopio University

**Harry H. Kelejian**

University of Maryland, College Park

**Purba Mukerji**

Connecticut College, New London

**George S. Tavlas**

Bank of Greece

## **Abstract**

This paper takes a spatial modeling approach in specifying and testing for contagion in government bond spreads among euro area countries. Our approach enables us to estimate certain asymmetries such as the magnitude of bond spread contagion of one country upon others, as well as how that country, in turn, is affected by events in neighboring countries. The approach also enables us to test for the significance of contagion, and then estimate its extent, in a formal, straightforward way. As a preview, we find that contagion is a statistically significant factor in explaining the level of government bond spreads and, furthermore, its effects are not uniform across the countries considered. We also identify a set of fundamental factors determining government bond spreads in euro area countries, and describe their consequence spatial interactions. As a corollary, we suggest policies that can be undertaken for medium term reductions of government bond spreads.

# **Interdependence of Stock Markets Before and After the Global Financial Crisis of 2007**

**Boulis M. Ibrahim and Janusz Brzeszczyński**

Heriot-Watt University, Edinburgh

## **Abstract**

In this paper we analyse the evolution of interdependence and influence of major international stock markets (New York, London and Tokyo) before and after the Global Financial Crisis (GFC) of 2007. Using the framework of the Foreign Information Transmission (FIT) model of Ibrahim and Brzeszczyński (2009) we investigate first the direction and strength of simple meteor shower effects across those three markets and then focus our attention on other factors which may impact on the relations between the largest stock trading centres, namely: differentials in trading volume, differentials in stock price volatility and interest rate differentials. The results are robust to different models' specifications and they clearly indicate that the role of the US market as the influencer of the stock price movements in other markets has weakened after the GFC in 2007 while the role of the other two trading centres in the UK and Japan has strengthened. Our findings are consistent with the explanation related to the shift in balance of economic powers between countries.

# **Investor Induced Contagion during the Banking and Sovereign Debt Crisis: Wealth Effect versus Portfolio Rebalancing**

**Dimitris Petmezas<sup>a</sup> and Daniel Santamaria<sup>b\*</sup>**

a Surrey Business School, University of Surrey

b\* (Presenter) Canterbury Business School, Canterbury Christ Church University

## **Abstract**

We examine the wealth effect versus the portfolio rebalancing hypothesis before and during the banking crisis followed by the sovereign debt crisis on U.S. and European stock-bond relationships. We find an increase in stock-bond correlation during the crisis, a result that is consistent with the investor induced contagion hypothesis through the wealth effect. Only stock-bond relationships involving Euro-zone short term bond returns confirm the portfolio rebalancing hypothesis during the sovereign debt crisis caused by a “flight from quality”. Additionally, we identify a tightening of credit conditions as the main driver of contagion during the banking crisis which, coupled with bouts of investor risk aversion, induces a portfolio rebalancing effect during the early stages of the crisis. This appears to coincide with a manifestation of the wealth effect at the height of the banking crisis, a finding that is repeated at the start of the sovereign debt crisis. Further evidence in favor of the portfolio rebalancing hypothesis is reported in specific stages of the sovereign debt crisis, although it is seen more as a temporary phenomenon.

## Session 6: **Banking II**

Time and date: 11.00-12.45, 25 April Thursday

Room: Earl Jellicoe

Chair Person: **Gerhard Kling**

### **How Does the State Affect Bank Fragility in the EMU?**

**Stefan Eichler and Karol Sobanski**

Technische Universitaet Dresden, Faculty of Business and Economics, Germany

#### **Abstract**

We study the impact the state has on bank default risk in the eurozone using the Distance to Default derived from stock prices of 115 banks in 11 EMU member countries in the period 1999-2010. We find that EMU member states may reduce the default risk of their banks by implementing more stringent diversification and capital requirements, by improving overall regulatory quality, and by reducing public debt. Moreover, we find that several political factors such as electoral cycles, the political power (i.e. parliament majority and fractionalization) of the government, and political ideology significantly affect the stability of EMU banks.



# **Market Perceptions of US and European Policy Actions Around the Subprime Crisis**

**Theoharry Grammatikos, Thorsten Lehnert and Yoichi Otsubo**

Luxembourg School of Finance, University of Luxembourg

## **Abstract**

This paper explores the impacts of key policy actions by US and European authorities on stock returns of systemically important banks in Europe and US around the subprime crisis. We find that the US policy announcements had a stronger impact on the European and US banking industry than the European policy announcements. In particular, the announcements of monetary policies and financial sector policies by the US authorities were accompanied by higher abnormal returns compared to related announcements of European authorities while the announcements of the US liability guarantees had the most favorable impact on the banking stock returns during the crisis. The lead role of US policies compared to European policies was strengthened after the collapse of Lehman brothers. We also find that the policy announcements, regardless of which side of the Atlantic the news arrived from, has increased the return volatility during the crisis. Our results lend additional support to the literature documenting event-induced volatility increases.

# **Central Bank Transparency and Financial Stability: Measurement, Determinants and Effects**

**Roman Horváth and Dan Vaško**

Institute of Economic Studies, Charles University, Czech Republic

## **Abstract**

We develop a comprehensive index of the transparency of central banks regarding their policy framework to promote financial stability for 110 countries from 2000 to 2011 and examine the determinants and effects of this transparency. We find that the degree of transparency increased in the 2000s, though it still varied greatly across the countries in our study. Our regression results suggest that more developed countries exhibit greater transparency, that episodes of high financial stress have a negative effect on transparency and that the legal origin matters, too. Importantly, we find that the level of transparency regarding the financial stability is strongly affected by monetary policy transparency. The central banks that have a transparent monetary policy are more likely to show increased transparency in their framework for financial stability. Our results also suggest a non-linear effect of central bank financial stability transparency on financial stress. Unless the financial sector experiences severe distress, greater transparency is beneficial for financial stability.

# **Has the financial crisis had an adverse effect on bank competition?**

**Ali Mirzaei and Tomoe Moore**

Department of Economics and Finance, Brunel University, UK

## **Abstract**

This article investigates whether the recent financial crisis has had any adverse impact on bank competition for 24 emerging and 25 advanced countries with large and small-size banks over the sample period 2001-2010. The H-statistic advocated by Panzar and Rosse (1987) is employed as the measure of competition. We find that the adverse effect of the financial crisis on bank competition seems to be trivial and on the contrary, competition is marginally boosted during the crisis period. This applies to both types of economies, irrespective of bank size. This suggests that currently ongoing policies to avert further crises in the banking sector have not exerted so great an adverse effect on competition. In the individual countries' study, the recent global financial crisis, however, led to a significant decline in competition in some countries.

Special Session 1: *The consequences of the crisis on the performance of European cooperative banking*

Time and date: 11.00-12.45, 25 April Thursday

Room: Tanners

Chair Person: **Silvio Goglio**

Discussant: **Yiorgos Alexopoulos**

**Organizational Structure and Exposure to Crisis among European Banks:  
Evidence from Rating Changes**

**Giovanni Ferri** (University of Bari), **Panu Kalmi** (University of Vaasa), **Eeva Kerola** (Aalto School of Economics)

**Abstract**

The Great Crisis started in 2007 deeply affected banks throughout Europe. Using the assessment of the two global rating agencies (Fitch and Moody's) publishing ratings on the financial strength of individual banks, we study whether the crisis hit the European banks differently across their mission/ownership/organizational structure. In particular, moving from general to specific, we consider three breakdowns of the banks: i) a "mission-based" breakdown of shareholder (profit maximizing) banks vs. stakeholder banks (catering not only for their shareholders); ii) an "ownership-based" categorization of the stakeholder banks differentiating cooperative banks from savings banks; iii) an "organizational/ownership-based" breakdown of the stakeholder banks where cooperative banks are further subdivided into tightly federated vs. loosely federated and savings banks are also split into private vs. public.

We also subdivide the entire crisis period 2007-2011 into three separate phases: 1) the 2007-2008 phase, mostly limited to the financial sector; 2) the 2009 stint, when the action moved to the real sector triggering recession and then recovery; 3) the 2010-2011 phase, dominated again by a financial shock, this time the European sovereign debt crisis. Our "mission-based" breakdown suggests us that shareholder banks – with their vocation to financial investment – be more vulnerable to financial shocks while stakeholder banks – inclined toward nonfinancial lending – be more exposed to real shocks. Then, we would expect that the stakeholder banks were less severely hit than the shareholder banks at least in phase 1 and 3, whereas we are unsure about holding that expectation for phase 2. We have instead no strong a priori on how the impact of the different phases of the crisis might have impinged on the two additional "ownership-based" and "organizational/ownership-based" breakdowns of the stakeholder banks. We employ country-level and balance-sheet controls in our econometric analysis to analyze the changes in ratings. Our initial results lend support to the hypothesis that rating changes differ across ownership structures. Our paper is among the first statistically-based evidence on relative merits of different organizational structures during the recent financial and economic crisis.

# **Bank lending procyclicality and credit quality during the crisis of 2008-2009**

**Stefano Di Colli** <sup>(a), (c)</sup>

**Juan Sergio Lopez** <sup>(a)</sup>

<sup>(a)</sup> *Federcasse*

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Via Lucrezia Romana 41/47, 00178 Rome

<sup>(d)</sup> University of Teramo,

## **Abstract**

The financial crisis occurred in 2008 led to a sharp growth of the suffering loan losses, a reduction in bank profitability and a series of bank failures. This work aims to understand what is the relationship, if any, between loan growth in the positive phases of the business cycle and loan losses increase during the recessions. Some analysts argue that increased competition in the banking sector has led to lower lending rates and lower lending criteria. Where periods of economic growth follow one after the other, banks tend to thin out the memory of the credit losses that have arisen in the past, becoming more willing to extend credit. In this case, the credit selection process may become less strict, credit quality goes down and, when the economic cycle is reversed, the bad loans increased more than proportionally. This paper tries to explain if the loan growth in the period before the crisis affected the size of the loan losses once it has occurred.

# **Persistent cooperative stabilizers in the lingering financial and economic misery**

**Hans Groeneveld**

Senior Vice President Cooperative and Sustainable Business at Rabobank Nederland

## **Abstract**

The global financial sector has been hit by various subsequent shocks. Now, the worldwide economy is particularly negatively impacted by the unfolding sovereign debt crisis in the Eurozone. Many banking systems are fairly fragile and aim to increase their resistance to new shocks by rising liquidity and solvency ratios. Many banks are also refocusing on traditional retail banking activities. Cooperative banking groups have been exposed to all these shocks and adjustments in banking as well. However, they were not so severely affected by the initial credit crisis originating in the United States in 2007. They did not need large scale state support a few years ago. The aim of this paper is threefold. Firstly, the main cause for their relatively good performance in the recent past is explored. It appears that the cooperative governance is a major explanation for this observation. Secondly, it will be investigated whether cooperative banks still stand out regarding their financial solidity and performance after almost five years of consecutive financial turbulences which are now translating into severe repercussions for the real economies. To this end, new data up to and including 2011 are used. Thirdly, the prospects and ‘presence value’ of cooperative banking groups in national financial systems are tentatively explored.

# **Cooperative *versus* conventional (joint-stock) banking in Europe: comparative resistance and resilience during the recent financial crisis**

**Yasmina LEMZERI and Mireille JAEGER, Jean-Noel ORY**  
CEREFIGE - University of Lorraine  
France

## **Abstract**

During the banking crisis of the 1990s', French cooperative banks turned out to be more resistant and more efficient than the conventional banks (i.e, "joint-stock"), which allowed them to improve their market shares and to increase their reserve capital. Finally, they have become the core of external restructurings that led them to transform into large universal banking groups, with a large scope of joint-stock subsidiaries under control. At that time, their competitive advantage was mainly relying on a different behavior in risk-taking and risk management, that could be associated with their cooperative legal form and their specific governance model (Gurtner, Jaeger, Ory, 2009).

Obviously, the same features have not clearly prevailed during the financial phasis of thecrisis (2007-10). Whereas the whole governance model has been deeply questioned in banking sector, the original cooperative model has evolved differently in European countries, with a high level of hybridization in some of them (listed vehicles, very large scope of activities in joint-stock subsidiaries...etc...), and a still very diffuse and deconcentrated network in some others. Moreover, it is a fact that some European cooperative groups have been hurt by the crisis, mainly because of the *corporate and investment banking (CIB)*, that was part of their activity.

Yet, the recent crisis has revealed the importance of a worlwide resisant and resilient banking system. And the diversity of legal forms and organizations may contribute to achieve this goal. We consider the resistance as "the relative insensivity to the crisis" where as the resilience is defined as "the ability to quickly recover after being affected by the crisis". In this regard, we aim to compare the resistance and the resilience of major joint-stock (*plc*) banks to the crisis, compared to that of cooperative banking, in different European countries and Canada. Our analysis is led at an aggregated/consolidated level for these two categories of banks, controlled by the country they belong to. Using different types of indicators (such as *z-score, loans to economic sector, return on equity...*) as independent variables, we try to show whether the cooperative form is synonymous with better resistance or resilience in banking sector, and whether the results may be explained by different organizational schemes and features in cooperative banking.

## Special Session 2: *Money Macro Finance Research Group Session*

Time and date: 11.00-12.45, 25 April Thursday

Room: Mill Room

Chair Person: **Andrew Mullineux**

Discussant: **Charles Goodhart**

### **Supranational regulation - how much and for whom?**

**Thorsten Beck and Wolf Wagner**

European Banking Center

#### **Abstract.**

We argue that a one-size-fits-all approach to international bank regulation is not warranted. Rather, we identify two factors that determine the extent to which supervision and resolution should move to a supra-national level: cross-border externalities from financial instability and country heterogeneity. The case for a supranational solution is the strongest among countries that display high cross-border externalities and are fairly homogenous, and is the lowest for heterogeneous countries with limited cross-border externalities. Based on this externality-heterogeneity trade-off we present six distinct solutions and associate them with different regions of the world. These region-specific solutions are to be complemented by universal minimum requirements and standards in order to address regulatory arbitrage and divergence of regulatory architectures.



## **The Eurozone Crisis: Escaping the ‘Doom Loop’**

**Andy Mullineux**

Bournemouth University

### **Abstract**

The paper reviews the origins and complexity of the ongoing Eurozone debt crisis in which bank bad debts and government debts have become intertwined in a ‘Doom Loop’. It reports on a ‘Round Table’ (panel) discussion chaired by the author on behalf of the UK’s Money, Macro, Finance Research Group (MMFRG) as part of the Groupement de Recherche Européen (GdRE) on Money, Banking and Finance annual conference in Nantes, 28-29 June 2012. The panel included Charles Calomiris (University of Columbia), Charles Goodhart (LSE) and Olivier de Bandt (Banque de France). The proposals of the panel for resolving the Spanish debt crisis and for the establishment of a ‘Banking Union’ in the EU to resolve the wider crisis and prevent future crises are then explored further. It concludes that the economists have proposed the solutions and it is now the responsibility of the politicians to action them.

# **The European crisis: Causes and Solutions - An Application of the Quantity Theory of Credit**

**Richard Werner**  
University of Southampton

## **Abstract**

This paper applies the Quantity Theory of Credit, which was originally proposed in 1992, and has been empirically well supported in the twenty years since. The theory provides the missing link that allows the incorporation of the banking sector into a macroeconomic framework, showing the impact of bank behaviour on economic growth, asset prices and financial stability. After a brief analysis of the causes of the fiscal, banking and economic crises in Europe, post-crisis recovery policies are derived from the Quantity Theory of Credit. Necessary and sufficient condition for a recovery is shown to be an expansion in broad credit creation – which I originally called ‘quantitative easing’ in 1994, an expression that was later used by central banks to refer to the type of traditional monetarist policy (bank reserve expansion) that I had warned would fail. The Japanese government and central bank failed to implement the recommendations, insisting on interest rate policies for the first post-crisis decade and, later, bank reserve expansion policies (which it misleadingly called ‘quantitative easing’). It is argued that the European (including UK) economies could rapidly move from the current debt-deflationary contraction and worsening fiscal crisis to economic growth and fiscal and economic stability by applying ‘true quantitative easing’.

## Session 9: **Bond Markets**

Time and date: 3.00-5.00, 25 April Thursday

Room: Seeley

Chair Person: **Marco Committeri**

### **Does gold offer a better protection against sovereign debt crisis than other metals?**

**Sam Agyei-Ampomah<sup>1</sup>, Dimitrios Gounopoulos<sup>2</sup>, KhelifaMazouz<sup>3</sup>**

<sup>1</sup>Cranfield School of Management, University of Cranfield, Bedford, UK.,

<sup>2</sup>Surrey Business School, University of Surrey, UK.

<sup>3</sup>Management School, University of Bradford, Bradford, UK

#### **Abstract**

It is a commonly held view that gold protects investors' wealth in the event of negative economic conditions. In this study, we test whether other metals offer similar or better investment opportunities in periods of crisis. Using a sample of 13 sovereign bonds, we show that other precious metals, palladium in particular, offer investors greater compensation for their bond market losses than gold. We also find that industrial metals, especially copper, tend to outperform gold and other precious metals as hedging vehicles and safe haven assets against sovereign bonds. However, the outcome of the hedge and safe haven properties is not always consistent across the different bonds. Finally, our analysis suggests that copper (palladium) is the best performing industrial (precious) metal in the period immediately after negative bond price shocks.

# **You Never Give Me Your Money? Sovereign Debt Crises, Collective Action Problems, and IMF Lending**

**Marco Committeri<sup>\*</sup> and Francesco Spadafora<sup>\*\*</sup>**

<sup>\*</sup> Bank of Italy, Department of International Economic Analysis and Relations  
<sup>\*\*</sup> Bank of Italy and International Monetary Fund

## **Abstract**

We review the impact of the global financial crisis, and its consequences for the sovereign sector of the euro area, on the international “rules of the game” for dealing with sovereign debt crises. These rules rest on two main pillars. The most important is the IMF’s lending framework (policies, financing facilities, and financial resources), which is designed to support macroeconomic adjustment packages based on the key notion of public debt sustainability. The complementary pillar is represented by such contractual provisions as Collective Action Clauses (CACs) in sovereign bonds, which aim to facilitate coordination among private creditors in order to contain the costs of a debt default or restructuring. We analyze the most significant changes (and their consequences) prompted by the recent crises to the Fund’s lending framework, not only in terms of additional financial resources, new financing facilities (including precautionary ones), and cooperation with euro-area institutions, but also as regards the criteria governing exceptional access to the Fund’s financial resources. We highlight a crucial innovation to these criteria, namely that, for the first time, they now explicitly take account of the risk of international systemic spillovers. Finally, we discuss how the recent crises have provided new political support for a broader dissemination of CACs in euro-area sovereign bonds. Importantly, in the first case involving an advanced economy, CACs were activated in the debt exchange undertaken by Greece in Spring 2012.

# **Foreign investors and risk shocks: seeking a safe haven or running for the exit?**

**Maurizio Michael HABIB and Livio STRACCA**

European Central Bank, Kaiserstrasse, Frankfurt am Main, Germany

## **Abstract**

In this paper we set out to study the impact of shocks to global risk aversion (such as after Lehman) as well as shocks with a clearer geographical connotation (such as the European debt crisis) on cross border portfolio flows, taking the perspective of foreign investors. We find robust evidence of a systematic retrenchment of foreign investors after both types of shocks, but more so for global shocks. There are no securities which consistently safe haven, attracting foreign investors when risk is perceived to be higher. In market stress periods, only occasionally do foreigners buy short-dated debt instruments, or government bonds, of other countries. Our results suggest that information asymmetries that have been highlighted in the literature as potential explanations of the home bias in finance are also important to understand the behaviour of international investors, conditional to risk shocks.

# **Entering the Public Bond Market during the Financial Crisis**

**Elnaz Kashefi-Pour**

Birmingham Business School, University House, Birmingham, B15 2TT

## **Abstract**

The aim of this paper is to investigate the determinants of a firm's decision to enter the public bond market during the financial crisis. Using a sample of non-convertible public bonds made by UK public and private companies between 2007 and 2011, the results show that companies with a higher demand for external financing are likely to enter the public bond market earlier than those with a limited need for external funds. Similarly, the results for credit history and market reputation show that creditworthy companies with established track records are more likely to undertake bond IPOs during the crisis. Unlike private companies, the agency cost in the form of underinvestment problems delays a firm's entry to the bond public market, suggesting that high-growth firms with risky debt wait longer to issue their first public bonds, in order to mitigate the underinvestment problem. Finally, the impact of leverage, bank relationships, and the industry in which a company is operating, on the timing of bond IPOs is mixed for public and private companies.

# **Vine copulas and applications to the European Union sovereign debt analysis**

**Dalu Zhang**

School of Economics, University of East Anglia, UK

## **Abstract**

European sovereign debt crisis has become a very popular topic since late 2009. This paper investigates sovereign debt crisis by calculating the probabilities of the potential future crisis of 11 countries in the European Union. I use sovereign spreads against Germany as targets and apply the GARCH based vine copula simulation technique. The methodology solves the difficulties of calculating the probabilities of rarely happening events and takes sovereign debt movement dependence, especially tail dependence, into consideration. Results indicate that Italy and Spain are the most likely next victims of the sovereign debt crisis, followed by France, Belgium and Austria. Sweden and Denmark, which are outside EMU are the most financially stable countries in the sample.

## Session 10: Equity Markets I

Time and date: 3.00-5.00, 25 April Thursday

Room: Earl Jellicoe

Chair Person: **Gishan Dissanaik**e

### **Does the Stock Market Reward Innovation: Market Reactions to Negative News During the 2007–2012 Global Financial Crisis**

**Christopher Adcock<sup>(1)</sup>, XiupingHua<sup>(2)</sup> and Shuxing Yin<sup>(1)</sup>**

(1) Sheffield University Management School, Sheffield, UK; (2) University of Nottingham, Ningbo, China

#### **Abstract**

This study investigates the interaction between stock markets and R&D innovations by examining the reactions to major negative news during the current financial crisis. We hypothesize that given the importance of intangible assets in today's world investors can foresee the reward from long-term innovations arising from R&D. Our results show that, at both country and firm levels, stock prices for countries/firms invested less in innovations experience significantly worse abnormal returns around negative news events. At the country level, innovations can alleviate the information asymmetry by showing that stock prices are efficient in absorbing negative news. At the firm level, however, R&D intensity fails to reduce information asymmetry between firms and investors, as high/low R&D intensive firms experience similar price continuations after negative events.



# Global Financial Crisis and Multiscale Systematic Risk: Evidence from Selected European Markets

Antonios K. Alexandridis<sup>1</sup> and Mohammad S. Hasan<sup>2</sup>

<sup>1</sup> Lecturer in Finance, University of Kent, School of Mathematics, Statistics and Actuarial Science

<sup>2</sup> Senior Lecturer in Finance, Kent Business School, University of Kent

## Abstract

There is tremendous interest among financial analysts, researchers, policy makers and the general public regarding the impact of the recent United States subprime crisis on the global financial markets ensued by a prolonged and deep global recession. In this paper, we are investigating the impact of the crisis on the stock markets of selected European markets within the framework of Capital Asset Pricing Model. The behavior and performance of the CAPM during the pre-crisis, crisis, and two post-crisis periods provides a convenient and powerful framework for an empirical assessment of the impact of the crisis on the European stock markets. Given the mixed results regarding the inference about the CAPM and betas, and the multi-scale nature of the systematic risk, in this paper, we have employed a recent and powerful method to estimate the systematic risk of CAPM using wavelet analysis to examine the meteor shower effects of the global financial crisis on selected European stock markets. Our results support the CAPM at medium scales, however, the behavior of beta is different for the two groups. Finally, the  $vaR$  was estimated at different time-scales for the four time-periods. Our results indicate that for all periods the risk is concentrated at higher frequencies (lower scales) of the data. Moreover, the  $vaR$  was increased for all countries during the crisis and the two post-crisis periods however the difference between the two groups is evident.

# European ‘fear’ indices – evidence before and after the financial crisis

**Wolfgang Aussenegg<sup>(a)</sup>, Lukas Goetz<sup>(b)</sup>, and Ranko Jelic<sup>(c)\*</sup>**

(a) Department of Finance and Corporate Control, Vienna University of Technology, Austria

(b) UNIQA Capital Markets GmbH, Vienna, Austria

(c)\*Corresponding author; Department of Accounting and Finance, University of Birmingham, UK

## Abstract

We document negative and asymmetric relation of European stock market returns and implied volatility. The negative relation is significantly more pronounced at the highest quantile (i.e. decrease in prices) of the equity market distribution. The main European volatility markets exhibit differences consistent with institutional and cultural clusters identified in the previous literature. The degree of integration between leading European (UK, Germany and France) volatility markets, however, is very high and shocks on the implied volatility spread die out within a few days. Our Markov switching model distinguishes three volatility regimes. Large changes in both, implied volatility and returns increase the probability that volatility enters a higher (from low to middle and from middle to high) volatility regime. In the high volatility regime, first three factors (level, slope, and curvature) identified by principal component analysis (PCA) explain 97% of the complete European volatility term structure. Our findings lend support to the behaviour explanation of the return-implied volatility relation and have implications for risk management.

# **Efficiency Characteristics of the European banking sector and the Global Financial Crisis of 2007-2012**

**Taufiq Choudhry and Ranadeva Jayasekera**

School of Management, University of Southampton, Highfield, Southampton, SO17 1BJ, UK,

## **Abstract**

This paper investigates the effect of bad or good news (asymmetric effect) on the time-varying beta of firms in the banking industries of several European during good periods (booms) and bad periods (recessions). Daily data from thirteen large banks from France, Germany, Greece, Ireland, Italy, Portugal and Spain are applied in the empirical tests. The data ranges from 2003 to 2012, which includes the global financial crisis of 2007-2012. The time-varying betas are created by means of the bivariate BEKK GARCH model and then linear regressions are applied to test for the asymmetric effect of news on the beta. The asymmetric effects are investigated based on both market and non-market shocks. We find that most banks in our sample seem to support the market efficiency hypothesis or declining levels of asset mispricing during both periods. These results shed light on the level of market efficiency and hedging strategies.

# **Signalling Quality of UK firms during the global financial crisis: Clinical study of theory and Evidences**

**Gishan Dissanaïke**

Cambridge Judge Business School; University of Cambridge; Trumpington Street;  
Cambridge CB2 1AG;

**Jonathan Faasse**

Cambridge Judge Business School; University of Cambridge; Trumpington Street;  
Cambridge CB2 1AG; UK;

**Ranadeva Jayasekera**

School of Management, University of Southampton, Highfield, Southampton, SO17 1BJ, UK,

## **Abstract**

This paper investigates seasoned equity offerings made by in the UK during the period from 2006 to 2012, which incorporates the global financial crisis. The financial crisis provides an ideal setting to study the quality-signalling hypothesis of seasoned equity offerings. Elevated information asymmetry levels during the GFC (especially among the financial sector) enhance the importance of capital raising choices, and provide a fruitful cross-section of firm and investor behaviour. We formulate a set of hypotheses from a quality signalling perspective, examining the key relationships between renounceability, control dilution/private benefits of control, current shareholders expected takeup and subscription price discount. We find that information asymmetry has a heightened influence during the crisis period presenting important financial implications to issuers and investors.

## Session 11: Risk II

Time and date: 3.00-5.00, 25 April Thursday

Room: Tanners

Chair Person: **Owain apGwilyn**

### **The Greek Effect? Default Risk Transfer between Eurozone Sovereign and Financial Sectors**

**Anurag Banerjee<sup>a,1</sup>, Chi-Hsiou Hung<sup>b,2</sup>, Kai Lisa Lo<sup>a,\*</sup>,**

<sup>a</sup> Durham Business School, University of Durham, United Kingdom

<sup>b</sup> School of Business, University of Dundee, United Kingdom

#### **Abstract**

We find evidence that the risk of default has been transmitted from the financial sector to the sovereign sector in the Eurozone during the early part of 2010. In the period before the first Greece bailout, the default risk had a “two-way feedback” effect between the sovereign and financial debt sectors for the European Financial Stability Facility (EFSF) guarantee countries. After the first Greek bailout, the impacts of a shock transmission from the financial sector to the sovereign default risk become negative or less significant in both the short- and long-runs, especially for the countries suffering the debt crisis, including Greece. However, such effect disappeared when the other countries requested for their own bailouts. This indicates that the market has learned from the Greek bailout by the EFSF. We call this the “Greek effect”.

# **The Determinants of the source of Debt and Debt Diversification: Empirical Evidence from European Non-Financial Firms 2000-2011**

**Debolina Banerjee and Amrit Judge**

Department of Economics and International Development, Middlesex University Business School,

## **ABSTRACT**

This paper examines the role played by credit ratings in determining firms' capital structure and debt mix choices in 43 European countries from the years 1999 to 2011 using both firm level as well as country level factors. We employ a sample of 48304 firm year observations drawn from European countries. Due to the availability of recent data in our study we are able to include the years, which incorporate the sovereign debt crisis and the financial crisis in our analysis. To the best of our knowledge this paper is the first study to employ data on the debt financing mix from several European countries. Previous studies on European firm's capital structure choices and debt mix have employed far smaller samples. For example, Bancel and Mitto (2004) employ a small sample of only 87 firms from 16 European countries and Antoniou, Guney and Paudyal (2008) focus on only 2 European economies, one bank based and the other market based. But with Europe having considerable variation in the development of its banking and financial institutions, degree of sophistication of its equity and bond markets, its legal systems, bankruptcy codes, corporate governance rules, this study is more representative of Europe as a whole at the same time trying to establish the importance of credit ratings in European firm- financing decisions. We thus bring together a range of firm characteristics as well as country factors in our study.

# **A Theory of Sovereign Risk Premia and Financial Intermediation in the Euro Area**

**Philipp Engler and Christoph Grosse Steffen**

## **Abstract**

The European sovereign debt crisis has highlighted the role of spillovers from sovereign default risk to financial intermediation in shaping macroeconomic dynamics. We propose a quantitative model which captures this feedback mechanism by allowing simultaneously for optimal default on public debt and occasionally binding collateral constraints on the interbank market in a general equilibrium setting. A link to the real economy is established by a working capital assumption. It emerges a role of government debt policy for the provision of a safe asset to insure efficient intermediation on interbank markets. Spillovers from sovereign default risk lead to non-Ricardian effects of public debt. We replicate central features of the European sovereign debt crisis through numerical simulations: hikes in sovereign risk impede the financial intermediation process, risk premia are countercyclical, and a home bias in government debt allows higher average debt levels. The preliminary findings of the paper indicate that during times of high sovereign default risk fiscal consolidation may become expansionary.

# **Financial Factors and the International Transmission Mechanism**

**Abigail Haddow and Mariya Milev**

## **Abstract**

The aim of this paper is to investigate theoretically how financial factors affect the international transmission mechanism. We build a two-country dynamic stochastic general equilibrium model with sticky prices and financial frictions. To add to the literature we extend the model to include two types of credit spread shocks that are micro-founded; a mean preserving shock to the dispersion of firms idiosyncratic productivity (risk shock) and a shock to financial agents net worth (financial wealth shock). We find that the source of the shock to the credit spread matters; credit spread shocks of equivalent size, but driven by different innovations, have different consequences for output and inflation in the home and foreign economy. In general risk shocks generate more realistic spillovers to activity than a financial wealth shock.



# **Liquidity and Credit Risks in the UK's Financial Crisis: How QE changed the relationship**

**Woon Wong, Wanru Yao and Peter Howells**

Centre for Global Finance, Bristol Business School, UWE Bristol

## **Abstract**

This paper investigates the relationship between credit risk and liquidity components in the interbank spread and how this relationship unfolded during the recent financial crisis. We find that prior to the central bank's Bank of England's intervention counterpart risk was a major factor in the widening of the spread and also caused a rise in liquidity risk. However, this relationship was reversed after central bank started quantitative easing (QE). Using the accumulated value of asset purchases as a proxy for central bank's liquidity provisions, we provide evidence that the QE operations were successful in reducing liquidity premia and ultimately, indirectly, credit risk.

## Session 12: Exchange Rates

Time and date: 3.00-5.00, 25 April Thursday

Room: Mill Room

Chair Person: **Taufiq Choudhry**

### **UK Imports from Germany, Japan and the US: Empirical Investigation of the Third Country effect and the Global Financial Crisis**

**Taufiq Choudhry, Syed Shabi Ul Hassan and Fotios I. Papadimitriou**

School of Management, University of Southampton, UK

#### **Abstract**

This paper investigates the influence of exchange rate volatility on the real imports of the United Kingdom from Germany, Japan and the US during the period 1991:01-2011:12. The sample applied also includes the current global financial crisis. Thus, this paper also investigates the potential impact of the crisis on UK imports from these three major trading partners. The paper further explores the third country effect on the UK imports. The ARDL cointegration method and the constrained error correction (general-to-specific) methods are applied to study the relationship between real imports and its determinants (including exchange rate volatility). The conditional variance from the GARCH(p,q) model is applied as exchange rate volatility. Both nominal and real exchange rates are employed in the empirical analysis. Our results indicate a significant effect of the current financial crisis on the exchange rate volatility and some effect on the UK imports from these countries. This finding is also true when we test for the third country volatility effect.

# **Are the effects of market news on asset prices and exchange rates changing?**

**Linda Goldberg<sup>1</sup> and Christian Grisse<sup>2</sup>**

<sup>1</sup>Federal Reserve Bank of New York, Research Department, USA

<sup>2</sup>Swiss National Bank, Zürich

## **Abstract**

Although effects of economic news announcements on asset prices and exchange rates are well established, these relationships need not be stable. We document the time variation in consequences of news on the yield curves and exchange rates of the United States, United Kingdom, Germany, France, Switzerland, and Japan using high frequency data from January 1999 through December 2010. We show that significant time variation in news effects is present in the data and explore alternative explanations for these evolving effects. Particularly interesting are the roles of central bank credibility, uncertainty in the economic outlook, and the interaction of monetary policy and financial stability objectives of central banks in periods of market turmoil.

# **On financial risk and the safe haven characteristics of Swiss franc exchange rates**

**Christian Grisse and Thomas Nitschk**

Swiss National Bank, Monetary Policy Analysis, Zurich, Switzerland.

## **Abstract**

We analyse bilateral Swiss franc exchange rate returns in an asset pricing framework to evaluate the Swiss franc's safe haven characteristics. A "safe haven" currency is a currency that offers hedging value against global risk, both on average and in particular in crisis episodes. To explore these issues we estimate the relationship between exchange rate returns and risk factors in augmented UIP regressions, using recently developed econometric methods to account for the possibility that the regression coefficients may be changing over time. Our results highlight that the Swiss franc is not a safe haven currency per se: in response to increases in global risk the franc appreciates against the euro as well as against typical carry trade investment currencies such as the Australian dollar, but depreciates against the US dollar, the Yen and the British pound. We find statistically significant time variation in the relationship between Swiss franc returns and risk factors, with this link becoming stronger in times of stress.

# **The euro exchange rate during the European sovereign debt crisis – dancing to its own tune?**

**Michael Ehrmann<sup>1</sup>, Chiara Osbat<sup>2</sup>, Jan Strasky<sup>3</sup> and Lenno Uusküla<sup>4</sup>**

<sup>1</sup> European Central Bank, michael.ehrmann@ecb.europa.eu.

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<sup>3</sup> Organisation for Economic Co-operation and Development, jan.strasky@oecd.org

<sup>4</sup> Bank of Estonia, lenno.uuskyla@eestipank.ee

## **Abstract**

This paper studies the determinants of the euro exchange rate during the European sovereign debt crisis, allowing a role for macroeconomic fundamentals, policy actions and the public debate by policy makers. It finds that the euro exchange rate mainly danced to its own tune, with a particularly low explanatory power for macroeconomic fundamentals. Among the few factors that are found to have affected changes in exchanges rate levels are policy actions at the EU level and by the ECB. The findings of the paper also suggest that financial markets might have been less reactive to the public debate by policy makers than previously feared. Still, there are instances where exchange rate volatility was increasing in response to news, such as on days when several politicians from AAA-rated countries went public with negative statements, suggesting that communication by policy makers at times of crisis should be cautious about triggering undesirable financial market reactions.

# **Credit Risk, Liquidity or Funding Access? Foreign-Exchange Forwards in a Post-2008 World**

**Justin Yap**

## **Abstract**

Covered interest rate parity allows one to price foreign exchange forwards using no-arbitrage arguments, such that given the rate of risk-free return in both currencies, the forward discount/premium can be determined precisely. This largely held true until mid 2007, when the U.S. sub-prime crisis and subsequent global financial crisis led to U.S. dollar funding constraints that significantly impacted forward prices. We find that factors related to credit risk, funding costs and liquidity influence the forward exchange rate of AUD/USD, EUR/USD and GBP/USD in the post-Lehman period from July 2009 to June 2012, for tenors of 1, 2, 3, 6 months and 1 year.

## Session 13: **Non-European Markets II**

Time and date: 8.30-10.15, 26 April Friday

Room: Seeley

Chair Person: **David G. McMillan**

### **Business Cycles, International Trade and Capital Flows: Evidence from Latin America**

**Guglielmo Maria Caporale\* and Alessandro Girardi\*\***

\* **Presenter.** Department of Economics and Finance, and Centre for Empirical Finance, Brunel University

\*\*ISTAT, Via Cesare Balbo, Rome, Italy

#### **Abstract**

This paper adopts a flexible framework to assess both short- and long-run business cycle linkages between six Latin American (LA) countries and the four largest economies in the world (namely the US, the Euro area, Japan and China) over the period 1980:I-2011:IV. The result indicate that within the LA region there are considerable differences between countries, success stories coexisting with extremely vulnerable economies. They also show that the LA region as a whole is largely dependent on external developments, especially in the years after the great recession of 2008 and 2009. The trade channel appears to be the most important source of business cycle co-movement, whilst capital flows are found to have a limited role, especially in the very short run.

# **Stock Market Reaction to Fed Funds Rate Surprises: State Dependence and the Financial Crisis**

**Alexandros Kontonikas, Ronald MacDonald and Aman Saggu**  
Economics Subject, Adam Smith Business School

## **Abstract**

This paper examines the impact of Federal Funds rate (FFR) surprises on stock returns in the United States over the period 1989-2012, focusing on the impact of the recent financial crisis. We find that prior to the crisis, stock prices increased as a response to unexpected FFR cuts. State dependence is also identified with stocks exhibiting larger increases when interest rate easing coincided with recessions, bear stock markets, and tightening credit market conditions. However, an important structural shift took place during the financial crisis, which changed the stock market response to FFR shocks, as well as the nature of state dependence. Specifically, during the crisis period stock market participants did not react positively to unexpected FFR cuts. Our results highlight the severity of the recent financial turmoil episode and the ineffectiveness of conventional monetary policy close to the zero lower bound for nominal interest rates.



# **Firm-level Contagion - An Asset Pricing Perspective**

**Woon Sau Leung and Nicholas Taylor**

Cardiff University, UK

## **Abstract**

While a large volume of empirical contagion studies focus on the roles played by international markets and use them as units of analysis, we differentiate our study by investigating contagion in the US equity market using firm-level information motivated from an asset pricing perspective. We contribute to the contagion and asset pricing literature by providing strong evidences of contagion in the US equity market related to the structured finance market (referenced by the ABX indexes, which track an equally-weighted portfolio of 20 residential mortgage-backed securities (RMBS)) using a scaled asset pricing model during year 2007 consistent with Longstaff (2010). We show that the contagious effects were systematically priced and that the orthogonalized ABX factor explains cross-sectional expected returns. In particular, the Carhart (1997) four-factor model augmented with the ABX factor holds when the subprime crisis subsample is used. Our paper is the first study that examines the time variations of individual stocks' systematic risk exposure to the structured finance market given the increasing importance and size of the structured fixed income market. To this end, we compute an innovative and simple measure of time-varying ABX systematic risk exposure and document significant increases in ABX AAA systematic risk levels during February, July and October 2007. Granger-causality test results show that the ABX AAA systematic risk levels were driven by the market and funding illiquidity and value-weighted average idiosyncratic volatilities. Lastly, we examine the determinants of significant ABX systematic exposure using firm-specific accounting variables and find that return volatilities, market systematic risks, market size, turnover ratios and book-to-market ratios are important determinants of individual stocks' ABX systematic risk exposure.

# How Much Does Market Structure Matter? Evidence from US Bank Profit and Risk

**David G. McMillan<sup>a</sup> and Fiona J McMillan<sup>b</sup>**

<sup>a</sup> Accounting and Finance Division, Stirling Management School, University of Stirling

<sup>b</sup> School of Management, University of St Andrews

## **Abstract**

This paper documents the changing structure of the US bank market since the late 1970s but specifically asks how this has affect bank behaviour as it relates to profits and risk. Using a variety of approaches, such as the HHI, Lerner and Zipf measures, we document a general increase in concentration and market power, at least until the recent crisis period. Importantly, we then consider whether these changes, or whether bank specific and general economic conditions have a greater impact on bank profit and risk. Results support the view that changes to the degree and level of market power, market concentration, size distribution as well as regulatory changes has an impact on bank profit and risk, although, that effect differs across the measures of bank performance. However, the results show that market structure is not the only determining factor for these characteristics. In particular, output growth plays a prominent role in determining bank behaviour with significant pro-cyclical movements in profit and risk. These results are robust to several model specifications, including quantile regression, which also highlights some non-linear dynamics. An examination of large banks highlights that they differ from smaller banks through the degree to which they are affected by market structure and GDP growth. Finally, a simple analysis demonstrates that increased market power and concentration may have a negative impact on output growth.

## Session 14: Macroeconomics II

Time and date: 8.30-10.15, 26 April Friday

Room: Earl Jellicoe

Chair Person: **Christopher A. Hartwell**

### ***Perseverare Diabolicum: the shortcomings of pre-crisis financial regulation, and the repetition of the same mistakes in the regulatory response to the crisis***

**Riccardo de Caria**

University of Torino – Italy

#### **Abstract**

The paper addresses two issues: how poor regulation has contributed to the crisis, and how current regulatory responses to the crisis are (not) differing from the poor regulation that originated it. In the first part, the paper offers an overview of the most relevant examples of poor regulation that have arguably played a role in determining the crisis, with a focus on the US and the EU: from the institutional design of central banks (that influences the type of monetary policy they implement), to the rules at the basis of fractional reserve banking (a source of great systemic instability, according to the perspective adopted in the paper); from the prescriptions in the Basel Accords I and II (that strongly encouraged banks to invest in the "wrong" assets), to the several policies adopted by the US authorities to encourage the purchase of a house by American households (resulted in a bubble whose burst triggered the global financial turmoil); from the regulatory requirements entrenching the oligopoly of credit rating agencies (more competition might have meant improved overall rating abilities), to the deposit insurance schemes (a source of great moral hazard and financial irresponsibility of consumers); from some shortcomings that can be identified in the way the institutions of the EU and of the Eurozone were designed (a major source of the current turmoil in this area), to the policies making the size of government grow, resulting in an increase of spending, taxation, deficit and public debt (something highly unhealthy for the economy from the perspective adopted in the paper), to some features of "regulation" narrowly meant (at best, an obstacle to the proper functioning of the markets). The concluding paragraph explains how all these failures might have led to the crisis, and reflects on what lessons can be derived from the inquiry made, what would be appropriate responses from legislators and regulators, and what mistakes it should be wise to avoid repeating: in particular, it is argued that definitely not more, but less regulation (and government intervention in general) is needed.

In the second part, the lessons summarized in the former one are contrasted with the actual legislative and regulatory responses adopted by the US and the EU: from the changes in central banking (that not only have fallen short of reducing the power of central banks to manipulate money, but have instead entrusted these institutions with even more power), to (non-existent) changes in fractional reserve banking (that unfortunately has not been subject to any rethinking in the mainstream thought); from the rules of Basel III (that do not seem to be truly capturing what went wrong with its two predecessors), to the still ongoing distortions of the real estate sector (GSEs were eventually bailed out and not surprisingly subprime

mortgages seem to have resumed); from the legislative proposals in the field of credit rating agencies (that go as far as proposing the establishment of a public European-wide credit rating agency), to the EU agreement to set up a common deposit-insurance scheme (that will probably encourage consumers' recklessness to an even greater extent than national schemes); from the many attempts to fine-tune the European architecture (that do not seem bound to remedy the identified pre-crisis shortcomings), to the many decisions further increasing spending, taxation, deficit and public debt (thus putting recovery at stake), to the new flood of "regulation" (narrowly meant) that has struck the markets (all but helping them to restore their ordinary functioning). The final paragraph offers some reflections on what is the role that law and regulation should instead play in financial markets, and argues that it should be confined to a set of clear, broad and general principles, giving up the idea of pre-determining the outcome of the competitive game, but simply dictating its rules, in the spirit of Hayek's lesson in the first volume of *Law, Legislation and Liberty*.

# **Financial Liberalization and Crises in Transition Economies: What Have 20+ Years Taught Us?**

**Christopher A. Hartwell**

Institute for Emerging Market Studies (IEMS),  
Moscow School of Management – SKOLKOVO, Russia

## **Abstract**

Financial liberalization, whether internal or external, has facilitated the creation of market economies, but it also has exposed transition countries and their real economies to volatility from international financial markets. With uneven financial liberalization across the transition space, a key question is, does increasing the level and pace of financial liberalization unduly expose countries to crises? And if a crisis does strike, does a liberalized financial sector help countries to weather crises better they would have otherwise? Using a database of 28 transition economies from 1989-2010 compiled from World Bank and Global Insight data, we examine the performance of several economic indicators (including private sector share of GDP, per capita savings, and FDI inflows) in periods of crisis as a function of financial sector liberalization and other institutional factors. Using Prais-Winsten and GMM estimators, results show a strong correlation between banking reform and/or financial openness and positive economic outcomes, even during crisis periods. The complete results point to the fact that while liberalization and integration in international financial markets carries a risk of contagion, the benefits of liberalization outweigh these risks; more importantly, liberalization can help to moderate the effects of a crisis if and when it does strike.

# **Monetary Policy and Bank Lending in the Euro Area: Is there a Stock Market Channel or an Interest Rate Channel?**

**Robert E. Krainer**

University of Wisconsin-Madison, 975 University Avenue, Madison, WI 53706-1323, U.S.A.,

## **Abstract**

In this paper I compare a traditional demand oriented model of bank lending with its focus on short-term interest rates in the money market, to a non-traditional capital budgeting model of bank lending based on equity share valuations for the Euro area. Using non-nested hypothesis tests, omitted variables tests, and Granger causality tests I reject the traditional demand oriented model of bank lending and fail to reject the capital budgeting model of bank lending for Monetary Financial Institutions in the Euro area. These results parallel results obtained for bank lending in the U.S. Even though Europe is a bank-based financial system, it appears the stock market plays a key role in the lending decision and the allocation of capital in Europe. One possible policy implication of this study is that central banks should control credit going into the stock market through selective controls and/or carry out open market operations in a well-diversified portfolio of equities in order to stabilize equity valuations and bank lending.

# **The relationship between interest rates and nominal GDP growth in the U.S., U.K., Germany and Japan from the 1960s to 2008**

**Richard A. Werner and Min Zhu**

School of Management, University of Southampton, UK

## **Abstract**

Monetary policy procedures make a number of assumptions concerning the role of interest rates in markets and the economy. We are interested in examining the empirical relationship between interest rates and nominal GDP growth. We conduct Granger causality tests and estimate a VAR model. The Granger causality tests suggest that interest rates do not Granger cause nominal GDP growth, while nominal GDP growth does Granger cause interest rates. Interest rates appear to follow nominal GDP growth rather than lead it. When estimating a VAR model that includes monetary aggregates, we find that money aggregates should be more appropriate in order to target nominal GDP than short-term interest rates. Given these findings, it is surprising that central banks have chosen to focus on interest rates as their main policy tool.

## Session 15: Contagion/Linkage II

Time and date: 8.30-10.15, 26 April Friday

Room: Tanners

Chair Person: **Ranadeva Jayaserka**

### **Integration and Contagion: Global Evidence from Recent Crises**

**Sungjun Cho, Stuart Hyde and Ngoc Nguyen**

Manchester Business School  
University of Manchester

#### **Abstract**

Increased integration between global equity markets and recent financial crises have resulted in fresh investigations of the transmission mechanisms and the propagation of shocks between markets. In this paper we examine the time varying nature of integration and the patterns of contagion over four recent crisis periods including the global financial crisis and the European debt crisis. We investigate a large sample of 30,838 common stocks from thirty one markets across the globe establishing the key differences in the transmission of shocks between country, size, book-to-market, and liquidity constructed portfolios. Our findings point to distinct differences in the impact on integration and level of contagion from each crisis. Results also indicate significant contagion effects during the subprime crisis for small firm, growth firm and illiquid firm portfolios.



# **Linkages between European national stock markets during the years 1997-2012: The impact of financial crises and EU expansions**

**Malgorzata Doman and Ryszard Doman**

<sup>1</sup>Poznan University of Economics, Department of Applied Mathematics, POLAND

<sup>2</sup>Adam Mickiewicz University in Poznan, Faculty of Mathematics and Computer Science, Laboratory of Financial Econometrics, POLAND

## **Abstract**

In the paper, we give a detailed description of the dynamic conditional dependencies between pairs from among fourteen selected European stock markets during the years 1997-2012. The markets are represented by their main stock indices. The analysis is performed by means of Markov-switching copula models with three regimes. Since the period under scrutiny is relatively long, we are able to take into account events of great consequence for our investigation, including two subperiods of severe financial crisis (1997-1999 and 2007-2012), introduction of the euro, the Eastern extension of the European Union, and consolidation of stock markets.

We analyze three types of dependencies by considering the stock indices returns that correspond to different parts of a day. First we apply the most popular approach based on the close-to-close returns. Next we analyze the dependencies between close-to-open returns and between open-to-close returns. The analysis allows us to assess how the information from global financial market is reflected in stock prices and compare the dependencies during the periods when markets are open with those when the markets are closed. The applied flexible Markov-switching copula models with three regimes make possible to describe and explain the changes in the dynamics of the dependencies caused by information flow. Additional advantages of the models are connected with using copulas instead of correlation. First of all, copulas allow to separate dependence structure from the marginal univariate distributions. Moreover, this approach enables us to avoid limiting ourselves to elliptical distributions for the bivariate returns, and gets possibility to assess dependence in tails of the bivariate distributions, what is especially important when dealing with periods of turmoil in financial markets.

The contribution of the paper is thus threefold. First, we investigate in detail the impact of financial crises, the introduction of the euro and the EU extension on the dynamics of dependencies between the European national stock markets. Next, we give results showing how the dynamics of linkages during the trading part of a day differs from that observed when markets are closed. The remaining part of our results concerns the dynamics of linkages between markets from different groups of European countries (e.g. emerging and developed, those that have suffered from the recent crises and those that have survived them relatively easy). Moreover, as a by-product of estimation procedure, we obtain volatility estimates for the considered stock indices, what allows us to better determine the periods of turmoil in particular markets.

# **The Contagion Effect in Lending and Economic Stability: A Study of the European Sovereign-Debt Crisis and its Global Impact**

**Yuki Masujima<sup>1</sup> and Winnie P. H. Poon<sup>2</sup>**

<sup>1</sup> Presenting Author; Japan Center for Economic Research, Japan

<sup>2</sup> Department of Finance and Insurance, Lingnan University, Hong Kong

## **Abstract**

This paper investigates whether a lender's nationality and issuing currency of loans matter for the gross domestic product (GDP) growth volatility of 153 loan-receiving countries from seven major lending countries including Italian and Spanish banks in 1981-2011. The results suggest that foreign banks' local currency credit appears to dampen a host country's GDP growth volatility which is used to indicate economic stability (or instability). The nationality of lenders does not appear to have a significant impact on the GDP growth volatility of borrowers. Instead, the currency of loans, including switches to the Euro, is probably more important than the nationality of lenders. Specifically, the finding of the study suggests that deleveraging in Euro credit leads to a rise in a host country's GDP growth volatility in Euro zone. Results from the contagion effect in lending and economic stability provide insights about the potential impacts of the current European Financial Crisis on the global financial markets through international credit channel.

# **Contagion Risk and Spillover Effects within the Eurozone Countries: How serious is the effect of the current sovereign debt crisis**

**Andreas Tsopanakis**

University of Glasgow, Department of Economics, UK

## **Abstract**

Eurozone is getting through its most serious financial crisis, since its creation. This situation put at stake the whole European integration project and set a number of crucial questions for the viability of the Eurozone as an economic and political entity and of the euro as a common currency. One of the most interesting aspects of this financial turmoil in Eurozone is the identification of the sources of the instability. More precisely, it is important for policymakers and market participants to be able to spot the channels through which the crisis has affected European markets. Such a work can help on the creation of the most appropriate policy framework, in order to establish the best possible framework for financial markets' regulation and supervision, along with the necessary macro-prudential policies. In order to achieve the aforementioned, we focus on the main source of this financial crisis, that is, the financial and banking markets. Here, instead of focusing to single indicators of financial instability, we move one step forward, by using financial stress indices, in order to have a clear-cut idea of the size and the severity of the financial turmoil through time. Using a wide number of series, we first proceed to the construction of financial stress indicators for the money market, bond market, banking sector and the stock market of each Eurozone country, while an overall index for each country is also provided. By employing these indices, it is possible to have a clear narrative of the evolution of the current crisis for the whole Eurozone, as well as for each country and, even more important, for the markets that drove the crisis in each country. In order to be able to identify the spillover effects between Eurozone countries and their markets, a battery of multivariate GARCH models have been utilized. The results provide a clearer picture, regarding the countries and, more importantly, the specific markets that worked as the main propagators of the financial crisis.

## Session 16: **Banking III**

Time and date: 8.30-10.15, 26 April Friday

Room: Mill Room

Chair Person: **Gerhard Kling**

### **The impact of the euro crisis on deposit rate convergence and pass-through**

**Ivo J.M. Arnold<sup>a,b</sup>, Saskia E. van Ewijk<sup>b</sup>**

a Erasmus School of Economics, Rotterdam, the Netherlands

bNyenrode Business University, Breukelen, the Netherlands

#### **Abstract**

Following the introduction of the euro, the pace of retail banking integration in the euro area has been slow. Since 2007, expectations of a gradual convergence in euro area retail interest rates have been thwarted by the credit crisis and the euro crisis. These twin crises have threatened both the integration of European money markets and the soundness of individual financial institutions. As a result, policymakers are increasingly concerned about financial fragmentation and the singleness of the monetary policy transmission. The present study focuses on retail savings and investigates the impact of the crisis on convergence and pass-through of deposit interest rates in the euro area. We find that both  $\beta$ - and  $\sigma$ -convergence have been adversely affected by the crisis. Our estimates of a time-varying state space model for interest rate pass-through show that the pass-through coefficient rises more strongly in countries most affected by the sovereign debt crisis. We also show that, since October 2009, movements in deposit rates and pass-through coefficients can be linked to deposits flows, sovereign risk and banking risk. We conclude that the heterogeneity in sovereign and banking risk across the euro area has disrupted convergence in deposit rates and increased pass-through in highly indebted countries.

# **Financial stability implication of securitization: evidence from Italy**

**Francesca Battagli<sup>1</sup>, Angela Gallo<sup>2</sup> and Maria Mazzuca<sup>3</sup>**

<sup>1</sup> Assistant Professor, Dipartimento di Studi Aziendali, Università Parthenope, Italy

<sup>2</sup> Assistant Professor, Dipartimento di Studi Aziendali, Università degli Studi di Salerno, Italy

<sup>3</sup> Assistant Professor, Dipartimento di Scienze Aziendali, Università della Calabria, Italy

## **Abstract**

This research examines the effects of securitization on the bank's equity risk decomposed in systematic risk and idiosyncratic risk. Since the financial crisis illustrated the financial stability implication of securitization activity, we also provide empirical evidence of the potential effect on the systemic risk, measured as the Marginal Expected Shortfall as defined by Acharya et al. (2010). Using a sample of Italian listed banks over the period 2000-2009, we find evidence of increasing systematic and idiosyncratic risk associated with originator banks and that after the 2007 these increases are even higher. We also find that securitization increases the probability of the analyzed banks to become "systematically" riskier, but we find no difference in the comparison of pre-crisis and after crisis period. This suggests that the systemic exposures of these banks are still as high as before the crisis with severe implications for financial stability.

# **Banks' responses to funding liquidity shocks: Lending adjustment, liquidity hoarding and fire sales**

Jan Willem van den End and Leo de Haan  
De Nederlandsche Bank, Amsterdam

## **Abstract**

The crisis of 2007-2009 has shown that financial market turbulence can lead to huge funding liquidity problems for banks. This paper provides empirical evidence on banks' responses to market funding shocks, using data of seventeen of the largest Dutch banks over the period January 2004 to April 2010. The dynamic interrelations among instruments of bank liquidity management are modelled in a panel Vector Autoregressive (p-VAR) framework. Orthogonalized impulse responses reveal that banks respond to a negative funding liquidity shock in a number of ways. First, banks reduce lending, especially wholesale lending. Second, banks hoard liquidity in the form of liquid bonds and central bank reserves. Third, banks conduct fire sales of securities, especially equity. Fourth, fire sales are triggered by liquidity constraints rather than by solvency constraints. Finally, there is some causality running from fire sales of equity to wholesale lending and liquidity hoarding.

# The Interest Rate Pass-Through in the Euro Area during the Global Financial Crisis

**Nikolay Hristov<sup>1</sup>, Oliver Hülsewig<sup>2</sup> and Timo Wollmershäuser<sup>1</sup>**

<sup>1</sup>Ifo Institute – Leibniz-Institute for Economic Research at the University of Munich, Germany

<sup>2</sup>University of Applied Sciences, Germany

## **Abstract**

This paper uses panel vector autoregressive models and simulations of an estimated DSGE model to explore the reaction of Euro-area banks to the global financial crisis. We focus on their interest-rate setting behavior in response to standard macroeconomic shocks. Our main empirical finding is that the pass-through from changes in the money market rate to retail bank rates became significantly less complete during the crisis. Model simulations show that this result can be well explained by a significant increase in the frictions that the banks' business is subject to.

## Session 17: CDS

Time and date: 10.30-12.30, 26 April Friday

Room: Seeley

Chair Person: **Ghulam Sorwar**

### **Price discovery of credit spreads in tranquil and crisis periods**

**Davide Avino, Emese Lazar and Simone Varotto**

#### **Abstract**

In this paper we investigate the price discovery process in single-name credit spreads obtained from bond, credit default swap (CDS), equity and equity option prices. We analyse short term price discovery by modelling daily changes in credit spreads in the four markets with a vector autoregressive model (VAR). We also look at price discovery in the long run with a vector error correction model (VECM). We find that in the short term the option market clearly leads the other markets in the sub-prime crisis (2007-2009). During the less severe sovereign debt crisis (2009-2012) and the pre-crisis period, options are still important but CDSs become more prominent. In the long run, deviations from the equilibrium relationship with the option market still lead to adjustments in the credit spreads observed or implied from other markets. However, options no longer dominate price discovery in any of the periods considered. Our findings have implications for traders, credit risk managers and financial regulators.



# **Fear or fundamentals? Speculative behaviour in the European CDS market**

**Carl Chiarella<sup>1</sup>, Saskiater Ellen<sup>2</sup>, Tony He<sup>1</sup> and Eliza Wu<sup>1</sup>**

<sup>1</sup> University of Technology, Sydney

<sup>2</sup> Corresponding author: Erasmus School of Economics, Erasmus University Rotterdam

## **Abstract**

Since the beginning of the financial crisis European CDS spreads have risen significantly and cross-sectional differences have magnified. We investigate whether this can be attributed to deteriorating fundamentals or speculative behaviour of market participants. To model dynamics and speculation in the European CDS market, we propose a heterogeneous agent model with two types of agents: 'chartist' investors who follow trends and 'fundamentalist' investors who use a theoretical model based on economic fundamentals. Agents can choose to switch between these groups based on relative past performance. We find that credit risk was underpriced before the financial crisis. Although some of the spikes in CDS spreads in the run up to and during the European debt crisis can be explained by deteriorating fundamentals, trend following speculation has also had a destabilizing effect on spreads.

# **CDS Spreads and Option Volatility during Crises**

**José Da Fonseca & Katrin Gottschalk**

Auckland University of Technology, Business School, Department of Finance, Private Bag  
92006, 1142 Auckland, New Zealand.

## **Abstract**

This paper presents a joint analysis of the term structure of credit default swap (CDS) spreads and the implied volatility surface for European countries during 2007-2012, a sample period covering both the Global Financial Crisis and the European debt crisis. We analyze to which extent cross-hedges can be performed between the credit and volatility markets during these two crises. We find that during a crisis we may experience a breakdown of the relationship between credit and volatility markets which jeopardizes any cross-hedging strategy. Consequently, an impairment of this intrinsic relationship may occur depending on the underlying crisis.

# **Sovereign Default Swap Market Efficiency and Country Risk in the Eurozone**

**Yalin Gunduz<sup>1</sup> and Orcun Kaya<sup>2</sup>**

Deutsche Bundesbank  
Goethe University Frankfurt

## **Abstract**

This paper uses sovereign CDS spread changes and their volatilities to investigate the informational efficiency of the sovereign markets and persistency of country risks. Specifically, we apply semi-parametric and parametric methods to the sovereign CDSs of 10 eurozone countries. It is shown that there is no evidence of long memory for the spread changes, indicating that price discovery process functions efficiently for sovereign CDS markets even during the crisis. In contrast, both methods imply persistent behavior in the volatility of changes for Greece, Portugal, Ireland, Italy, Spain, and Belgium addressing the fact that, in causal terms, the less stable economies in the euro area have a high extent of sovereign risk. We furthermore demonstrate the potential spillover effects of spread changes among eurozone countries by estimating dynamic conditional correlations.

## **Behaviour of the CDS spreads during the Eurozone crisis**

**John Pereira<sup>1</sup>, Mohamed Nurullah<sup>1</sup> and Ghulam Sorwar<sup>2</sup>**

<sup>1</sup> Kingston Business School, UK

<sup>2</sup> Nottingham University Business School, UK

### **Abstract**

This paper examines the determinants of 2990 quarterly CDS spreads in the Eurozone area during the recent crisis, across all industrial sectors excluding the Banking sector. Our initial analysis shows a significant increase in CDS spread during the crisis period, which has failed to decline during the post crisis period. Based on the findings of Das et al. (2009), we regress the CDS spread against both accounting and market based variables, as a jointly they provide a better fit to the data. Our analysis reveals that majority of the accounting based variables are not significant in explaining the CDS spread both for the whole study period and the crisis period and that overall market based variables are more significant in explaining the CDS spread. Moreover, we find that during the crisis period, standard assumptions regarding many of the explanatory variables are not valid.

## Session 18: Equity Markets II

Time and date: 10.30-12.30, 26 April Friday

Room: Earl Jellicoe

Chair Person: **Utz Weitzel**

### **Can the information content of share repurchases improve the accuracy of equity premium predictions?**

**Dimitris Andriosopoulos<sup>1</sup>, Dimitris K. Chronopoulos<sup>2</sup>  
and Fotios I. Papadimitriou<sup>3</sup>**

<sup>1</sup>School of Business and Economics, Swansea University, UK

<sup>2</sup>School of Management, University of St Andrews, UK

<sup>3</sup>School of Management, University of Southampton, UK

#### **Abstract**

We adjust the dividend-price ratio for share repurchases and investigate whether predictive power can be improved when constructing forecasts of UK and French equity premia. Regulations in the two largest European stock markets allow us to employ actual repurchase data in our predictive regressions. Hence, we are able to overcome problems associated with markets characterised by less stringent disclosure requirements, where investors might have to rely on proxies for measuring repurchase activity. We find that predictability does not improve either in a statistical or in an economically significant sense once actual share repurchases are considered. Furthermore, we employ a proxy measure of repurchases which can be easily constructed in international markets and demonstrate that its predictive content is not in line with that of the actual repurchase data.

# **European Equity Investing Strategy through the Financial Crisis: the role of Momentum and Trend Following**

**Andrew Clare\*, James Seaton\*, Peter N. Smith† and Stephen Thomas\***

\*Faculty of Finance, Cass Business School, London

†Department of Economics, University of York.

## **Abstract**

A growing body of literature suggests that over widely varying historical eras, across a wide range of asset classes momentum investing, often accompanied by a trend following overlay, provides superior risk-adjusted returns. We examine the effectiveness of applying these methodologies to pan-European equity asset allocation through periods of potentially substantial market dislocation, in particular, with the advent of the single currency and the equity market crashes of the early 2000's and 2008. With the introduction of the Euro there has been much discussion of the benefits of diversification via country based portfolios versus industry sector portfolios. Early studies simply looked at changing return correlations over time. The simple conclusion that increasing country correlations over time drives superior risk-adjusted portfolios towards diversification across sectors has been increasingly challenged. Our approach is different in that we apply momentum and trend following investing strategies and assess whether it is sectoral or country indices which dominate our portfolios through periods of structural changes and extreme volatility. Diversification via sectors is clearly the best strategy in times of equity market stress. In addition, the application of trend following offers a substantial improvement in risk-adjusted performance compared to traditional buy-and-hold portfolios. The terms momentum and trend following have often been used interchangeably although the former is a relative concept and the latter absolute. By combining the two we find that one can achieve the higher return levels associated with momentum portfolios but with much reduced volatility and drawdowns due to trend following. We observe that a flexible asset allocation strategy that allocates capital to the best performing instruments irrespective of asset class enhances this further. Such methodologies offer superior risk adjusted returns even especially through market volatility.

## **Momentum strategies in a group of European countries during the 2008 financial crisis**

Taufiq Choudhry and Yuan Wu  
School of Management, University of Southampton

### **Abstract**

In this paper, we analyse the performance of momentum strategies in a group of European stock markets hit hardest by the 2008 financial crisis—namely, the Greek stock market, Portuguese stock market, and Spanish stock market during the 2008 financial crisis period over the sample period from January 2002 to December 2011. By splitting whole sample time period into pre-financial crisis and post-financial crisis periods, we find compelling empirical evidence showing more pronounced momentum returns over the time periods leading up to the peak of the financial crisis. We reason that the markedly attenuated momentum premia observed during time periods following market downdraft can be elucidated within the framework of feelings as information (Schwarz, 1990). More explicitly, the investors' sentiment turns more pessimistic following market slumps, prompting “detailed-oriented systematic processing” (Schwarz, 1990: page 545) in judgmental process involving extensive practice of cognitive heuristics of System 2 of two cognitive systems (Kahneman and Frederick, 2002) such as statistics heuristics, abstract heuristics (Tiedens and Linton, 2001). The systematic processing procedure crimps the influence of overconfidence, conservatism and underreaction over investors, evoked by intuitive heuristics and in turn deteriorates the momentum premia following market down-side movements. In addition, single-factor model and Fama French 3 factor model are used to decompose the momentum returns found in the study. The empirical results suggest that over the time periods prior to the peak of the financial crisis, the value effect factor and momentum effect factor can explain a very large part of the momentum returns. However, over the sample time period on the heels of the financial crisis, market risk factor takes over and explains most part of the momentum returns. Based on the evidence found in the study over time periods revolving the 2008 financial crisis, we argue that the driving force behind the momentum phenomenon is time-varying.

# **When the going gets tough: Insights into individuals' trading behaviour during, and their likelihood of 'surviving', the global financial crisis**

**Johnnie E. V. Johnson, Peter A. F. Fraser-Mackenzie, Ming-Chien Sung,  
Tiejun Ma and Alexander Dolia**

Centre for Risk Research, School of Management, University of Southampton, UK.

## **Abstract**

If inefficient markets are believed to be efficient this can lead to misallocation of resources and under-regulation. In this light, the focus of the literature examining the global financial crisis of 2008-2009 has failed to focus sufficiently on the degree to which it was caused by a failure of individuals to behave in accordance with the rational expectations model. Indeed, the literature has focussed on causes such as subprime mortgages, bank lending and financial contagion, on the role of central banks and financial regulators, on liquidity management by firms and on the effect on family finances. Far less research has focused on the behaviour of traders, particularly in the rapidly growing retail sector, during the crisis and its effect on their subsequent behaviour. This is an important omission, since the failure to anticipate their irrational actions may well have aggravated the crisis. In fact, Paul Volcker, former Federal Reserve Chairman, claims that 'among the causes of the recent financial crisis was an unjustified faith in rational expectations [and] market efficiencies' (Volcker, 2011, p. 1). Equally, under the rational expectations model, one might expect that this crisis would lead to a significant reduction in the number of noise traders in the market, with positive effects on market efficiency.

We examine these issues by exploring the behaviour of individual traders during the crisis period and explore the extent to which this is associated with their subsequent trading behaviour. To achieve this, we employ individual trader data supplied by a UK-based spread-trading company. As a result, we are able to examine the trading histories of individual spread traders on European (FTSE and DAX) indices and futures both prior to and following the dramatic fall in index prices during September 2008. We employ survival analysis to identify trading discipline characteristics of traders (e.g., holding periods, risk measures, inclination towards the disposition effect etc.) associated with greater 'survivorship' during the crisis (i.e., associated with their tendency to continue to trade after the crisis). Equally, we were able to examine the impact of demographic factors (e.g., age, gender, annual income, equity and savings) on survivorship. We discovered that demographic characteristics, risk attitude and a tendency to be inclined to display the disposition effect (i.e., a greater probability of selling profits compared losses) all impacted survivorship, but often in a manner which would be counter-intuitive to an observer steeped in the rational expectations model. Equally, we found that individuals who adapted their traits throughout the crisis, were more likely to continue to trade following the crisis; but again, the manner in which the 'survivors' adapted would not be predicted by a rational expectations model.

These findings challenge the model of rational expectations, suggesting that those traders who survive crises of this sort may well adopt counter-intuitive behaviours to do so. Second,



our results suggest that these behaviours may aggravate such crises, leading to breakdowns in the ability of the rational expectations model to predict market behaviour during these periods. Third, in highlighting the characteristics of those individuals who ‘survive’ and continue to trade after the crisis our results throw doubt on the view that such crises can lead to better price discovery (resulting from noise traders leaving the market). Fourth, an understanding of the trading and demographic characteristics of those traders who ‘survive’ financial crises can help market makers establish optimal risk management and marketing strategies. Finally, by understanding the trading profile of clients expected to continue trading in the crisis aftermath, we gain a better understanding of the degree and speed to which markets can be expected to return to efficient levels.

# **Fire-sale opportunities or flight to quality? Cross border takeovers in Europe and the crisis.**

**Gerhard Kling<sup>1</sup>, Utz Weitzel<sup>2</sup> and Dirk Gerritsen<sup>3</sup>**

<sup>1</sup> Southampton University, Southampton, UK

<sup>2</sup>Radboud University Nijmegen, IMR, Department of Economics, Nijmegen, The Netherlands

<sup>3</sup> University Utrecht School of Economics, Utrecht, The Netherlands

## **Abstract**

This paper investigates European cross border merger and acquisition (M&A) activity before and after the start of the financial crisis. We find a fundamental, dampening effect of the crisis on M&A activity. The M&A pattern that emerges is strikingly different from the 1997-1998 East Asian financial crisis where 'fire-sale opportunities' increased inbound M&A activity. For Europe the evidence points into the opposite direction of 'flight to quality' where cross border acquirers prefer target countries with lower relative sovereign bond yields in the crisis. We also find indications for capital flight via M&A. A possible explanation for this pattern may be that financial risk does not seem to be fully translated into measurable market risk. In contrast to fire-sale opportunities, where higher risk is compensated by even higher (lower) returns (asset prices), in the current crisis the risk-adjusted returns from M&A into high risk countries may be too low.

## Session 19: **Banking IV**

Time and date: 10.30-12.30, 26 April Friday

Room: Tanners

Chair Person: **Simon Wolfe**

### **Bank bailouts, competition, and the disparate effects for borrower and depositor welfare**

**Cesar Calderon<sup>a</sup> and Klaus Schaeck<sup>b</sup>**

<sup>a</sup> The World Bank

<sup>b</sup> Bangor University

#### **Abstract**

We investigate how government interventions into banking systems such as blanket guarantees, liquidity support, recapitalizations, and nationalizations affect banking competition. This debate is important because the pricing of banking products has implications for borrower and depositor welfare. Exploiting data for 124 countries that witnessed different policy responses to 41 banking crises, and using difference-in-difference estimations, we present the following key results: (i) Government interventions reduce Lerner indices and net interest margins. This effect is robust to a battery of falsification and placebo tests, and the competitive response also cannot be explained by alternative forces. The competition-increasing effect on Lerner indices and net interest margins is also confirmed once the non-random assignment of interventions is accounted for using instrumental variable techniques that exploit exogenous variation in the electoral cycle and in the design of the regulatory architecture across countries. (ii) Consistent with theoretical predictions, the competition-increasing effect of government interventions is greater in more concentrated and less contestable banking sectors, but the effects are mitigated in more transparent banking systems. (iii) The competitive effects are economically substantial, remain in place for at least 5 years, and the interventions also coincide with an increase in zombie banks. Our results therefore offer direct evidence that the mechanism by which government interventions contribute to banks' risk-shifting behavior as reported in recent studies on the bank level runs via competition. (iv) Government interventions disparately affect bank customers' welfare. While liquidity support, recapitalizations, and nationalizations improve borrower welfare by reducing loan rates, deposit rates decline. Our empirical setup allows quantifying these disparate effects.

# **Towards a New Model for Early Warning Signals for Systemic Financial Fragility and Near Crises: An Application to OECD Countries**

**Barbara Casu, Andrew Clare and NashwaSaleh**

All authors are affiliated with Cass Business School, City University London

## **Abstract**

Despite the exorbitant cost of financial crises had highlighted the importance of early warning systems for financial fragility, existing models failed to signal warnings for the 2007-2010 crisis. Using a signal extraction framework and looking at OECD countries over a 27 year period, this paper attempts to identify a number of variables significant in predicting near-crises as a pre-cursor to full-fledged crises. These include growth in pension assets as an indicator for the development of liquidity bubbles, equity market dividend yields as a proxy for corporate balance sheet health, banking sector assets growth and relative size to GDP. We also study the development of asset price bubbles through an equity markets indicator and a house price indicator. Finally we also look at a banking sector funding stability indicator and liquidity indicator on a micro-level. Simultaneously, a dynamic research design improves on previous static set-ups and enhances the model predictive power and applicability to different time periods. Our results indicate that as early as 2004, clear signals were being given that vulnerabilities were building up for a number of countries. EWS design has significant implications for financial stability and financial regulation.

# **Banking branch network, local contestability and consumer welfare during the financial crisis**

**Marta Degl'Innocenti<sup>1</sup>, Claudia Girardone<sup>2</sup>,  
Giuseppe Torluccio<sup>3</sup> and Simon Wolfe<sup>1</sup>**

<sup>1</sup> School of Management, University of Southampton, Highfield Southampton, United Kingdom

<sup>2</sup> Essex Business School, University of Essex, Wivenhoe Park, Colchester, United Kingdom

<sup>3</sup> Department of Management, University of Bologna, Via Capo di Lucca, Italy

## **Abstract**

Focusing on the Italian banking sector over the period 2005-2011, this paper provides novel empirical evidence on how and to what extent the branch network and geographic diversification can affect the competitive viability of banks, even during a period of financial crisis. Moreover, this paper examines whether changes in the competitive conditions of a local market have an impact on the way through which the level of banking output affects the consumer welfare.

# **Too Systemically Important to Fail' in Banking – Evidence from Banking Mergers and Acquisitions**

**Philip Molyneux<sup>a\*</sup>, Klaus Schaeck<sup>a</sup>, Tim MiZhou<sup>b</sup>**

<sup>a</sup>Bangor Business School, Bangor University, Wales, UK LL57 2DG

<sup>b</sup>Sunderland Business School, Sunderland University, England, UK SR6 0DD

## **Abstract**

The recent bailouts of a large number of banks have raised substantial policy concerns regarding institutions that are considered 'Too-systemically-important-to-fail' (TSITF). We exploit a sample of bank mergers and acquisitions (M&As) in nine EU economies between 1997 and 2008 to capture safety net subsidy effects and evaluate their ramifications for systemic risk. We find that safety net benefits derived from M&A activity have a significantly positive association with rescue probability, suggesting moral hazard in banking systems. Also we find no evidence that gaining safety net subsidies leads to TSITF bank's increased interdependency over peer banks.

# **Asymmetric information and the behaviour of bank default risk in a financial crisis**

**Peter Spencer**

University of York, UK

## **Abstract**

Default risk seriously stressed the inter-bank markets during the recent financial crisis and has continued to impede the flow of credit and economic recovery ever since. Asymmetric information is critical in this respect, since it is hard for outsiders to value bank assets, particularly when these are not marketable. In view of problems in measuring Libor and other money market rates, the default probabilities used in this paper are extracted from 1-7 year US bank CDS spreads. They are analysed using a specific effects econometric model based on the deferred filtration approach of Duffie and Lando (2001) which the accounting system gives creditors a lagged signal of net asset value. Other signals, such as the default of similar banks, also inform their estimate of net asset value. Preliminary results suggest that this model combines the advantages of both structural and reduced form approaches to default risk.

## Session 20: Economic Growth and Wealth Effects

Time and date: 10.30-12.30, 26 April Friday

Room: Mill Room

Chair Person: **Yaz Gulnur Muradoglu**

### **The Value of Government Ownership during the Global Financial Crisis**

**Christof Beuselinck<sup>1</sup>, Lihong Cao<sup>2</sup>, Marc Deloof<sup>3</sup> and Xiping Xia<sup>4</sup>**

<sup>1</sup> IESEG School of Management and LEM,

<sup>2</sup> Huazhong University of Science and Technology and University of Antwerp,

<sup>3</sup> Presenting author; University of Antwerp,

<sup>4</sup> University of Science and Technology

#### **Abstract**

This paper examines the value of government ownership in Europe before and during the Global Financial Crisis, taking into account the level of investor protection and country corruption as measures of the risk of expropriation by the government. Using a unique sample of 5,070 listed firms in 29 European countries over the period 2005-2009, we find that government ownership significantly increased firm value and stock returns *during* the crisis. The positive effect of government ownership was driven by firms located in countries with good investor protection and low corruption. Firms with government ownership were also able to invest more during the crisis, indicating that government ownership reduced financing constraints for firms during the crisis.

This study adds to the literature on the role of governments by investigating the value of government ownership during a crisis which was an exogenous shock. The results suggest that government ownership can be beneficial to firms during a crisis period. We find that in 2007-2009, the positive effect of government guarantees in alleviating financial supply shocks outweighed the negative effects of agency costs associated with government ownership. Our results also suggest that government ownership can help overcome crisis shocks only in an environment with low risk of expropriation by the government.

This study provides insights into the debate about the role of governments in public firms. The positive effect of government ownership during crisis period suggests that active government involvement in corporations may indeed help boost the economy during the economic downturn. Furthermore, it highlights the importance of institutional quality, providing additional guidance on the development of institutions.



# **The Recent Financial Crisis and Europe's Economic Growth and Convergence**

**René Cabral and Jorge Jaramillo**

Tecnológico de Monterrey, Campus Monterrey, Escuela de Graduados en Administración Pública y Política Pública, Ave. Rufino Tamayo, Garza García, NL, México

## **Abstract**

This paper reexamines the effects of the recent financial crisis on economic growth and convergence in Europe. Employing a sample of 31 developed countries over the period 1981-2010, we pay particular attention to the effects of the recent financial economic crisis on EMU members and non-members. Using dynamic panel data methods, we observe that by taking part in a the EU, countries GDP per capita grew on average 8.4% faster than on the rest of the developed world. The economic and financial crisis reduce GDP grow across non EU members by 5.7% and by 10.8% across EU members not taking part in the euro zone but only by 4.2% across euro zone members. Third, looking at convergence, we find that the European Union has contributed towards convergence but not the monetary union. Finally, with data up to 2010, we do not find evidence that the pattern of convergence across EU member has changed as a result of the financial crisis.

# **Economic and Financial Growth in Europe. Is Euro Beneficial for all Countries?**

**Kalaitzoglou Iordanis**

Audencia PRES-LUNAM, School of Management, Centre for Financial and Risk  
Management  
8 Route de la Jonelière-BP 31222, 44312, Nantes Cedex 3, France

**Beatrice Durgheu**

Department of Economics, Finance and Accounting  
Coventry Business School, Birmingham

## **Abstract**

European policies have emphasized the development of the open market as the main determinant of a robust financial system. A steady economic growth should ease government access to borrowing and this, upon efficient fiscal policies, should lead to economic growth. In addition, the fixed FOREX rate, namely Euro, should increase mobility of resources and consequently accelerate economic growth. In contrast, it suppresses any monetary action, which might significantly reduce the competitive advantage of developing economies. In this paper the potentially endogenous relationship between economic and financial growth in Europe is investigated, accounting for relative access to government borrowing and the impacts of Euro. In more details a simultaneous system of 3 equations is proposed that investigates, first, the impact of financial growth on economic growth, second, potential endogeneity, and finally, the relative contribution of both to borrowing levels. The model further investigates potential structural effects between countries that have adopted the fixed exchange rate and countries that have decided not to join Eurozone. Other variables have also been included to control for macroeconomic and country specific effects. The system of equations is estimated using GMM, in order to account for heteroskedasticity and autocorrelation of unknown form. The findings highlight that economic and financial growth are indeed endogenously determined, but only in countries that have jointed Euro. Euro is also found to accelerate both economic and financial growth. However, advanced economies enjoy significantly more benefits than developing countries, mainly due to a consistently better access to cheaper external financing. This becomes more profound in the years following the current financial crisis. Consequently, Euro appears to be beneficial, since it enhances national financial systems, which seem to drive economic growth. In Eurozone, this further boosts financial growth and leads to further development. However, this is not robust for developing countries, which cannot have the same access to external financing and can lead to significant deviations in periods of financial instability.

# **Wealth Effects of the Eurozone Crisis: Evidence from European Financial Markets**

**Walter Matthias Kirsten<sup>a,f</sup>, Ali M. Kutan<sup>b,c,d</sup> and Yaz Gulnur Muradoglu<sup>c,e,f</sup>**

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<sup>e</sup>School of Business and Management, Queen Mary, University of London, UK

<sup>f</sup>Behavioural Finance Working Group, UK

## **Abstract**

We conduct an empirical analysis of the wealth impact of the Eurozone crisis on financial markets in Europe. We investigate reactions in stock markets, bond markets, financial sector and foreign exchange market to the crisis related actions of parties involved in the crisis. Our study extends the previous literature that focuses on the impact of IMF-related events and central bank policies on financial markets during financial crises. Our analysis focuses on the current Eurozone crisis and covers many major players, including not only the IMF but also the European Commission, and the European Central Bank, as well as the governments in Europe, Rating Agencies and the public reaction to the crisis in European countries. We find evidence for a split of the Eurozone in debtors and creditors which are hegemonically led by Germany as reflected in bond market reactions. Reactions in financial sector returns indicate creditor nations, especially Germany have an incentive to bailout debtor nations such as Greece, Ireland, Italy, Portugal and Spain, in order to rescue their domestic financial systems. Both stock markets and bond markets prioritise the actions of debtor countries' governments over the so called Troika, (European Commission, ECB, IMF) when it comes to re-establishing confidence in capital markets.



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