

Comments on Sharon Poczter's
'The Long-Term Effects of Bank Recapitalization:
Evidence from an Emerging Market'

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The Issue

- Recapitalization addresses a `short-term' concern:
 - Crisis period triage
 - Fragile bank with potentially viable borrowers
- Raises a long-term one
 - Moral Hazard

This Paper

- Addresses the long-term concern
- Uses interesting, detailed Indonesian data
 - Financial
 - Political

Its Two Key Figures

Figure 1. Time Series of Risk Measure Between Recapitalized and Non-Recapitalized Banks

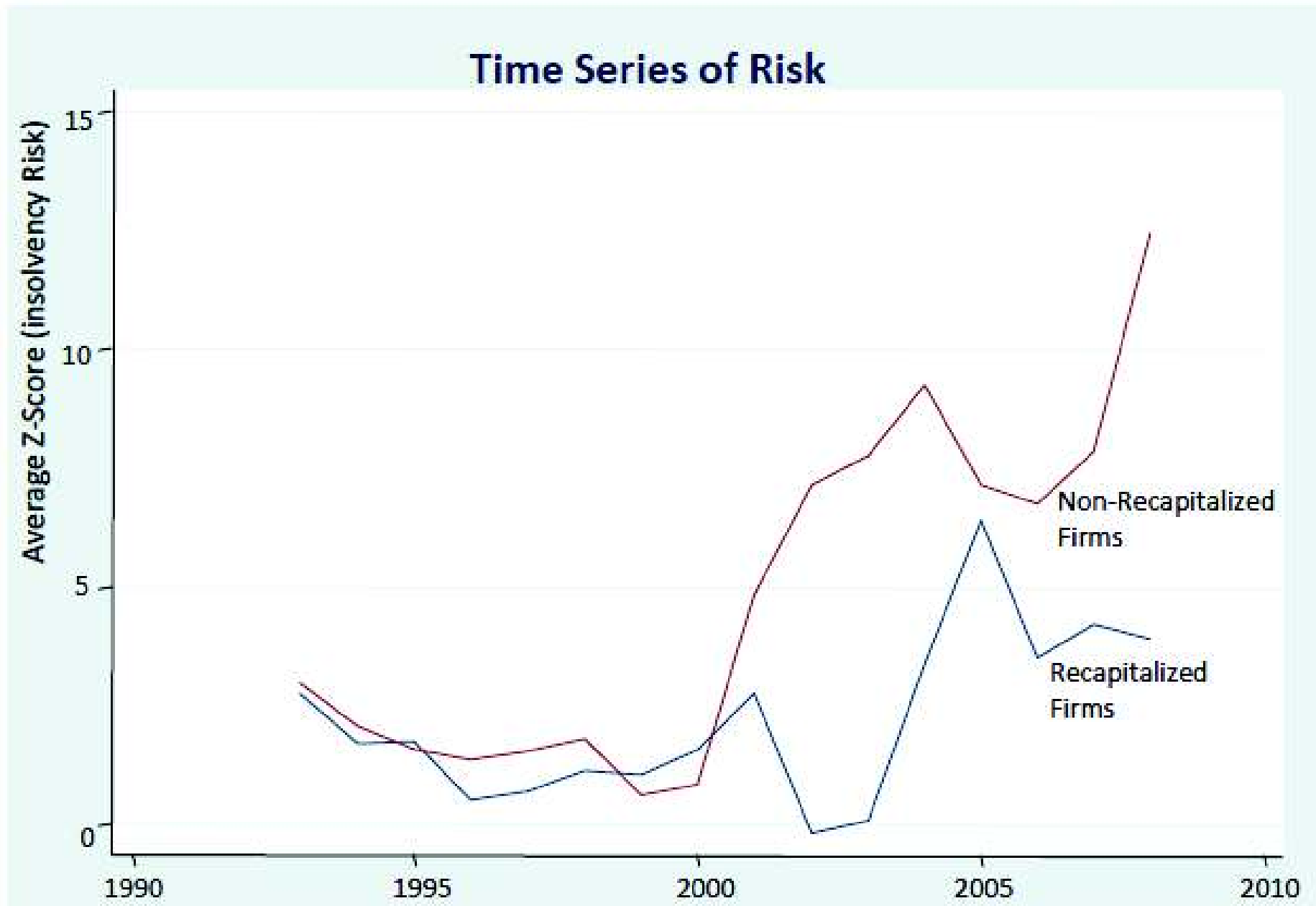
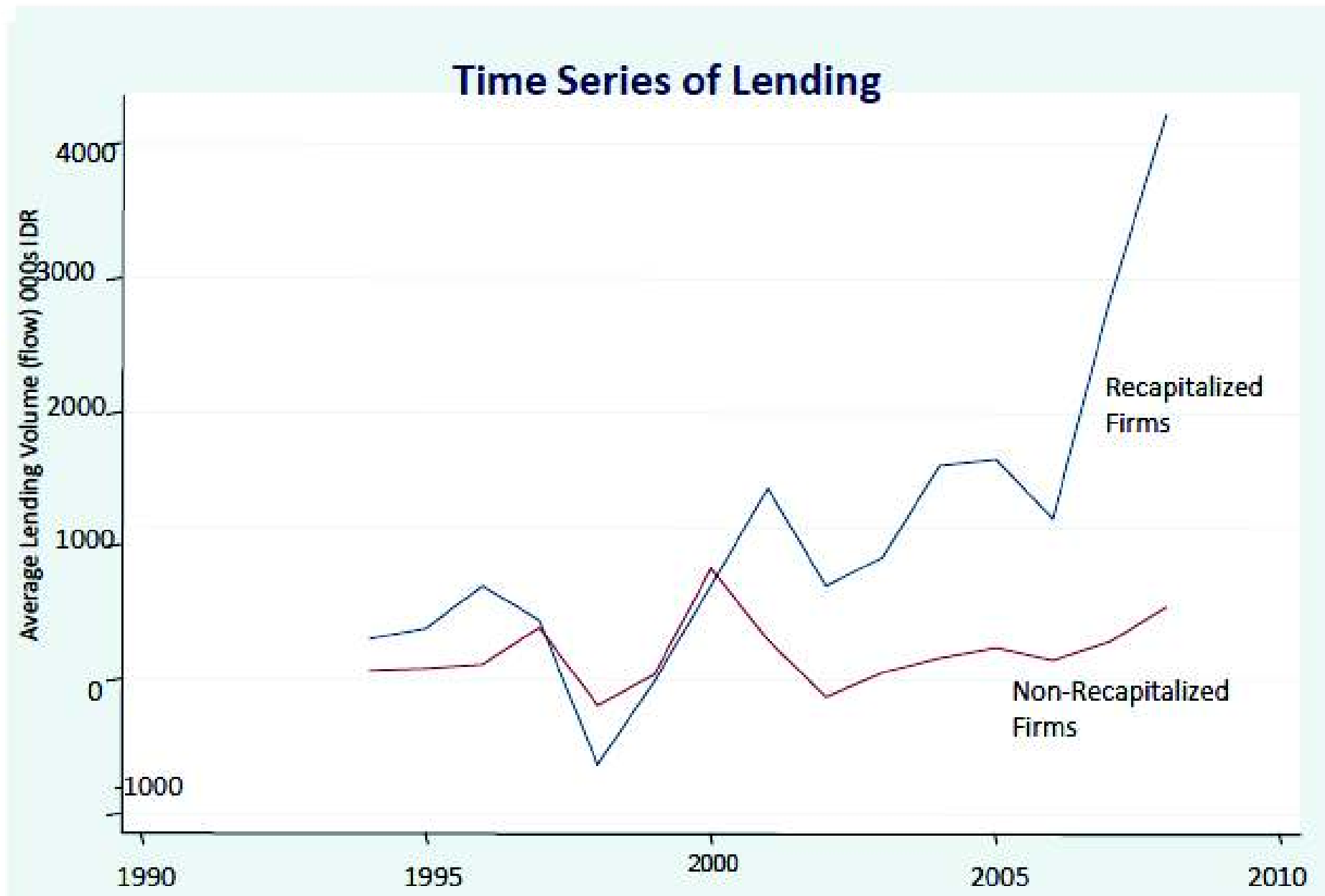


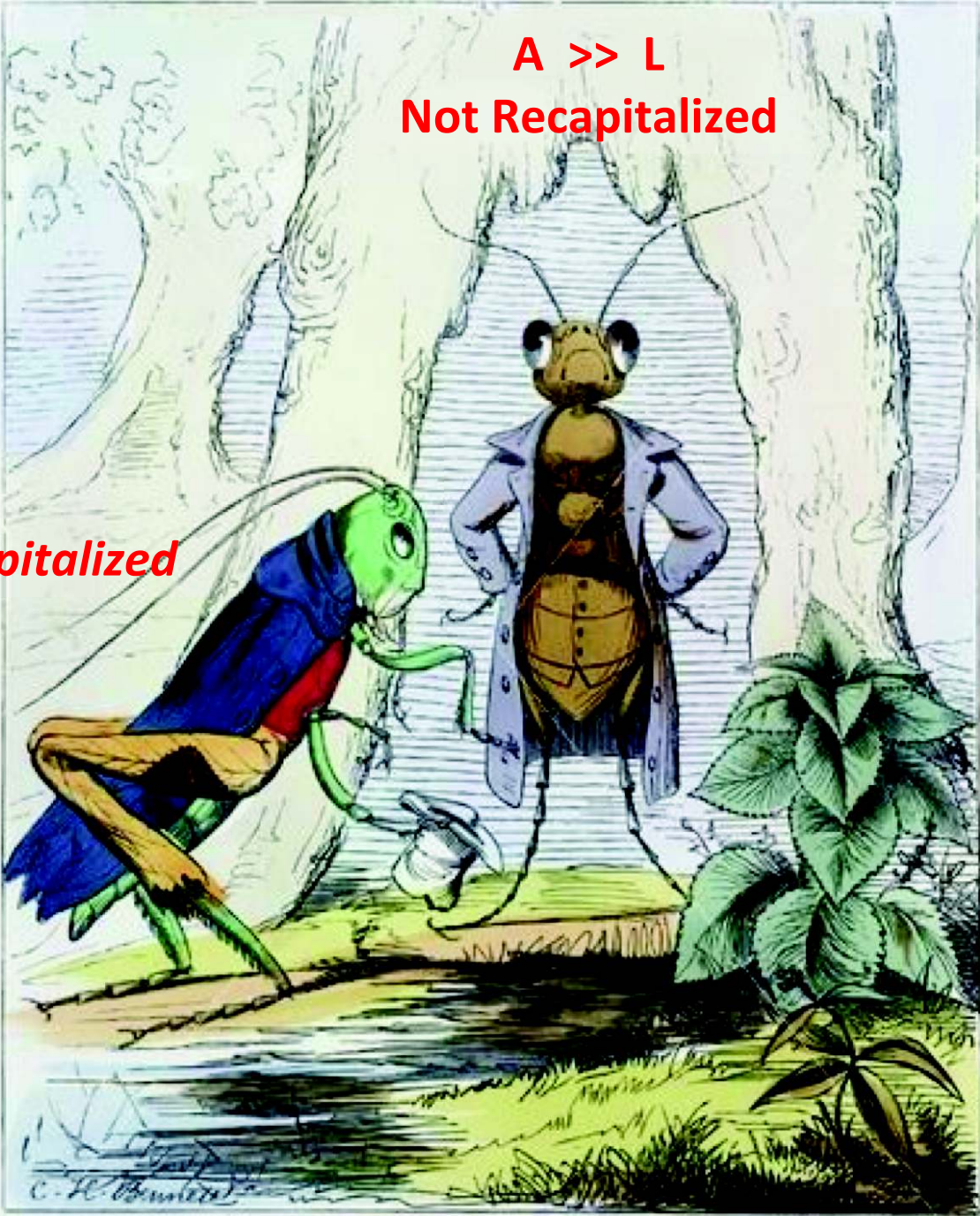
Figure 2. Time Series of Average Lending Volume between Recapitalized and Non-Recapitalized Banks



Interpretation:
moral hazard arising from recapitalization

A >> L
Not Recapitalized

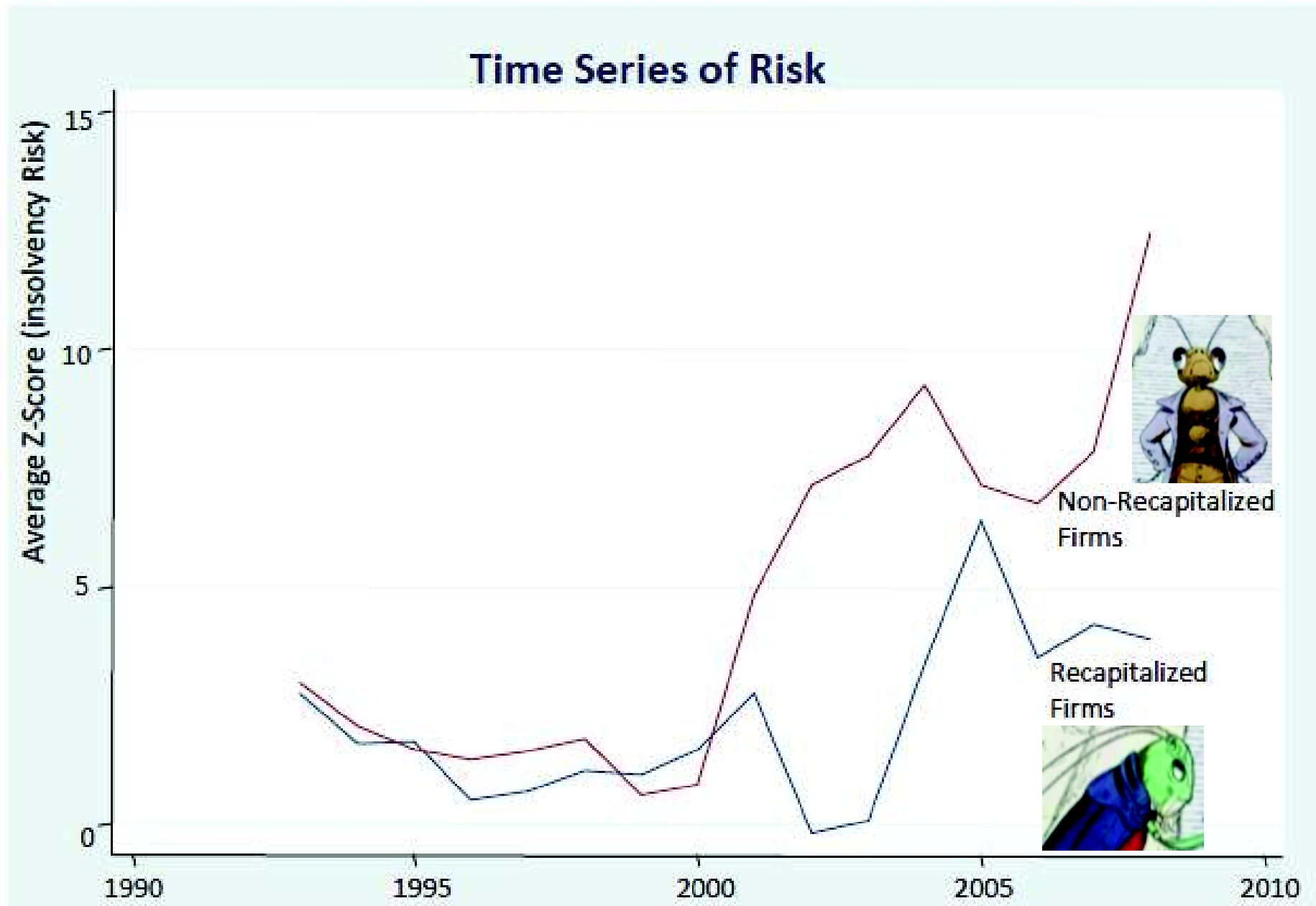
Recapitalized



THE ANT AND THE GRASSHOPPER.

Charles H. Bennett, 1857
(Wikimedia Commons)

Figure 1. Time Series of Risk Measure Between Recapitalized and Non-Recapitalized Banks



Treatment Effect

*Without recapitalization,
a grasshopper would be like an ant.*

Treatment Effect

*Without recapitalization,
a grasshopper would be like an ant.*

*Treatment induces moral hazard in the grasshopper,
while it does the opposite to the ant.*

Three Questions

Question 1

Why would treatment induce moral hazard only in the treated?





Why doesn't the ant learn from the grasshopper?



That is, why wouldn't the riskiness rise for *both* the recapitalized and the non-recapitalized?

Mightn't the ant, too, see a greater likelihood of being bailed out in hard times?



Question 2... Indonesia?

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Distinctive?

Generalizable?

Other emerging Asian Economies?

Japan, US, Europe?

Question 3: Selection

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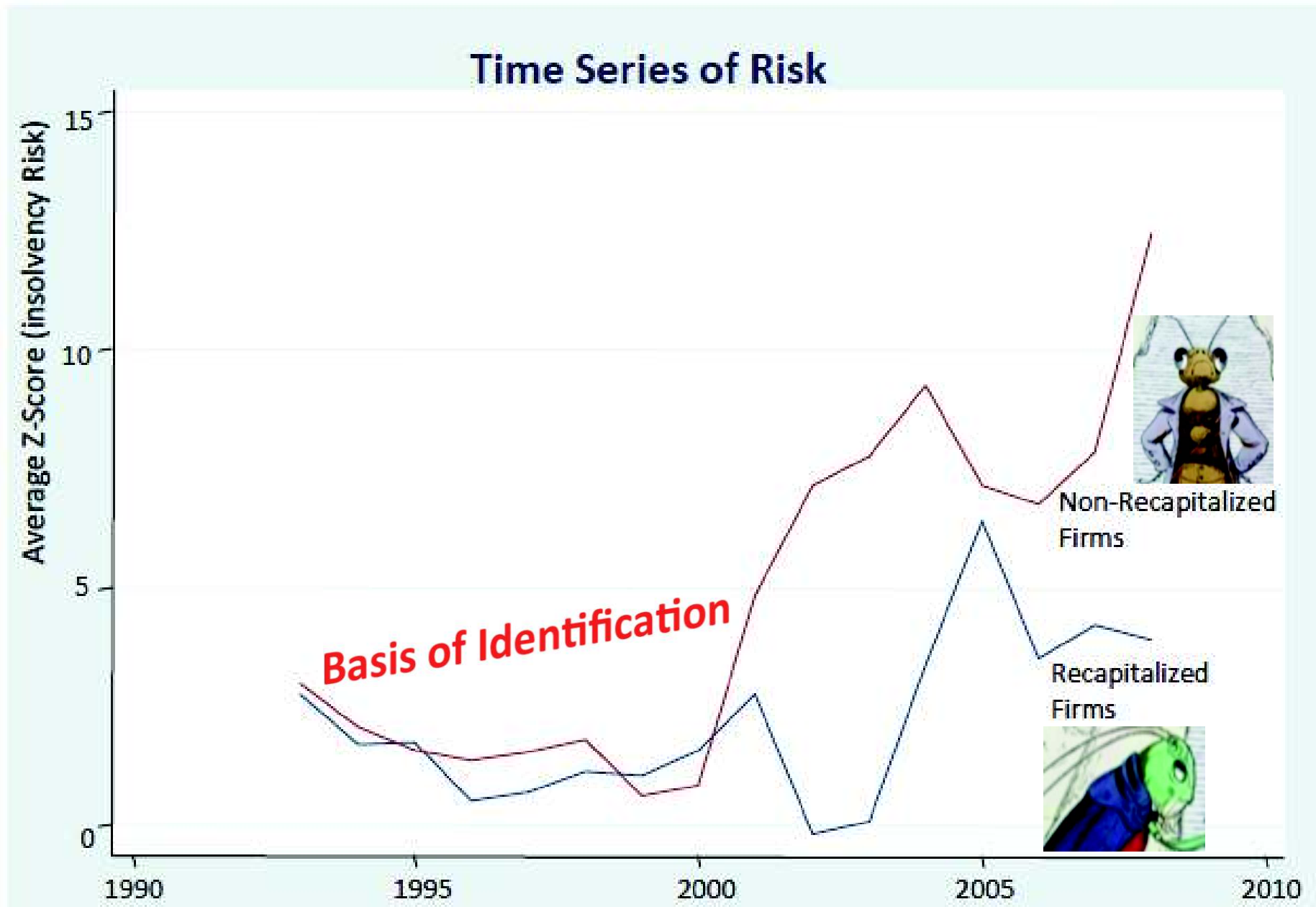


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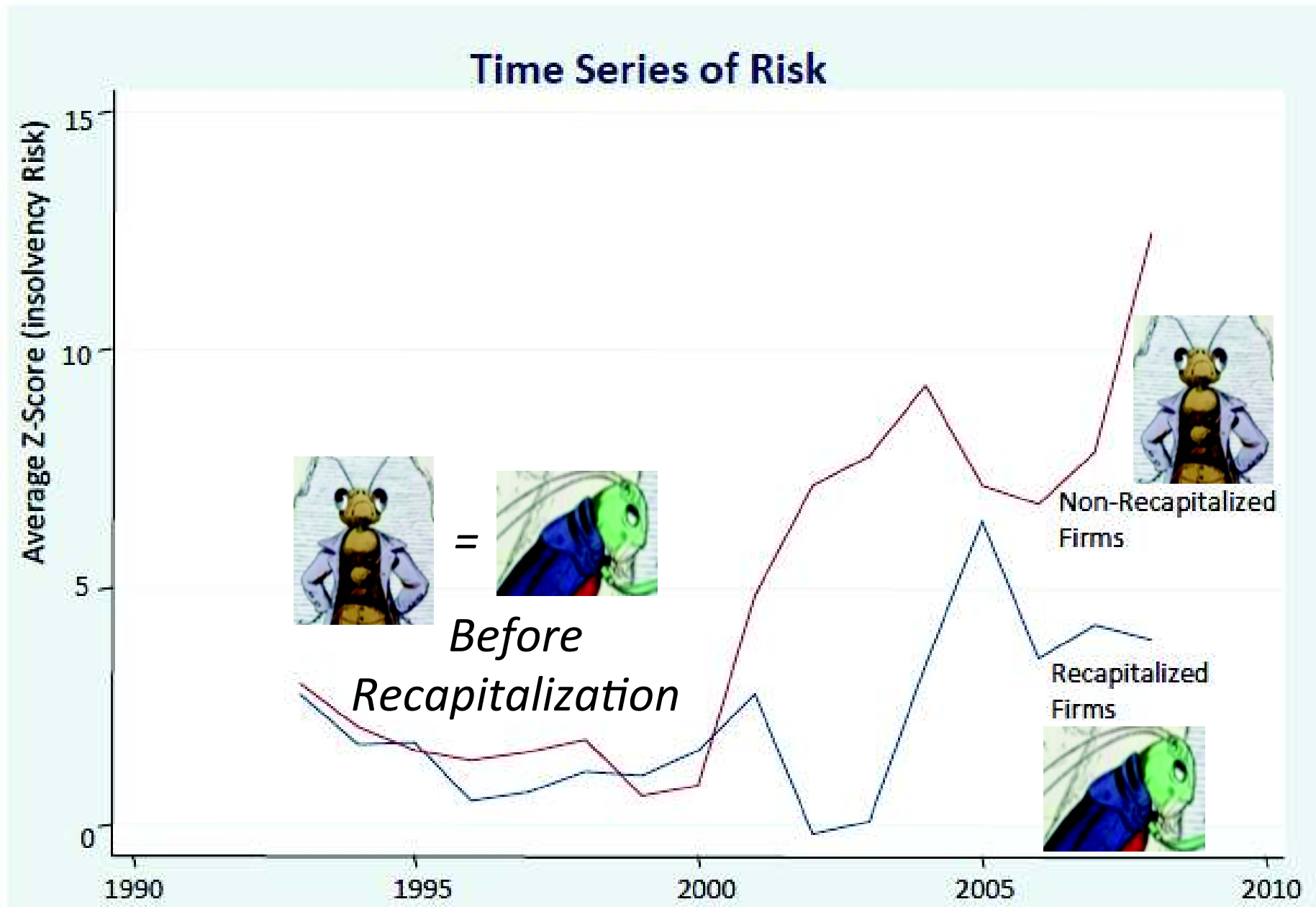
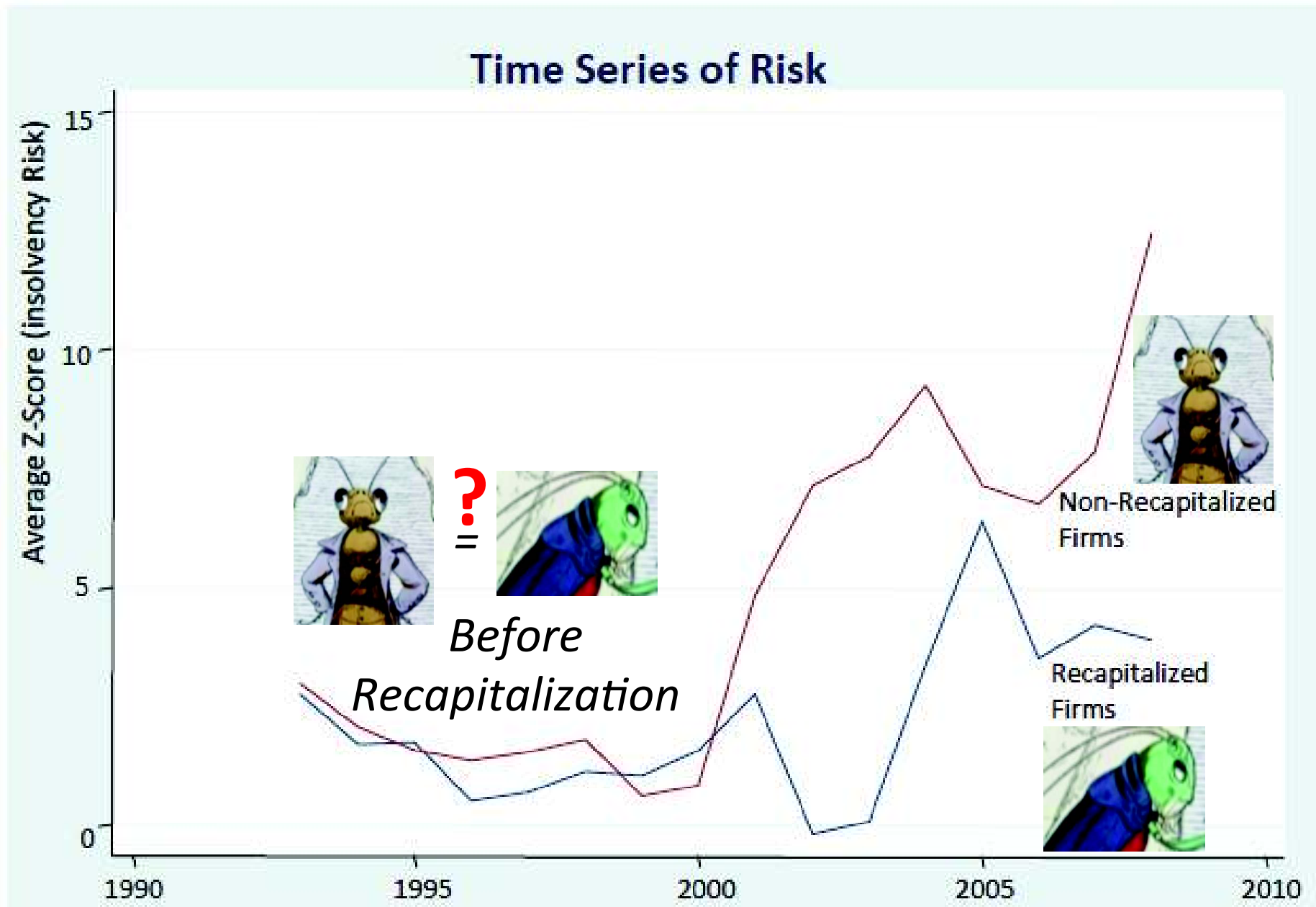
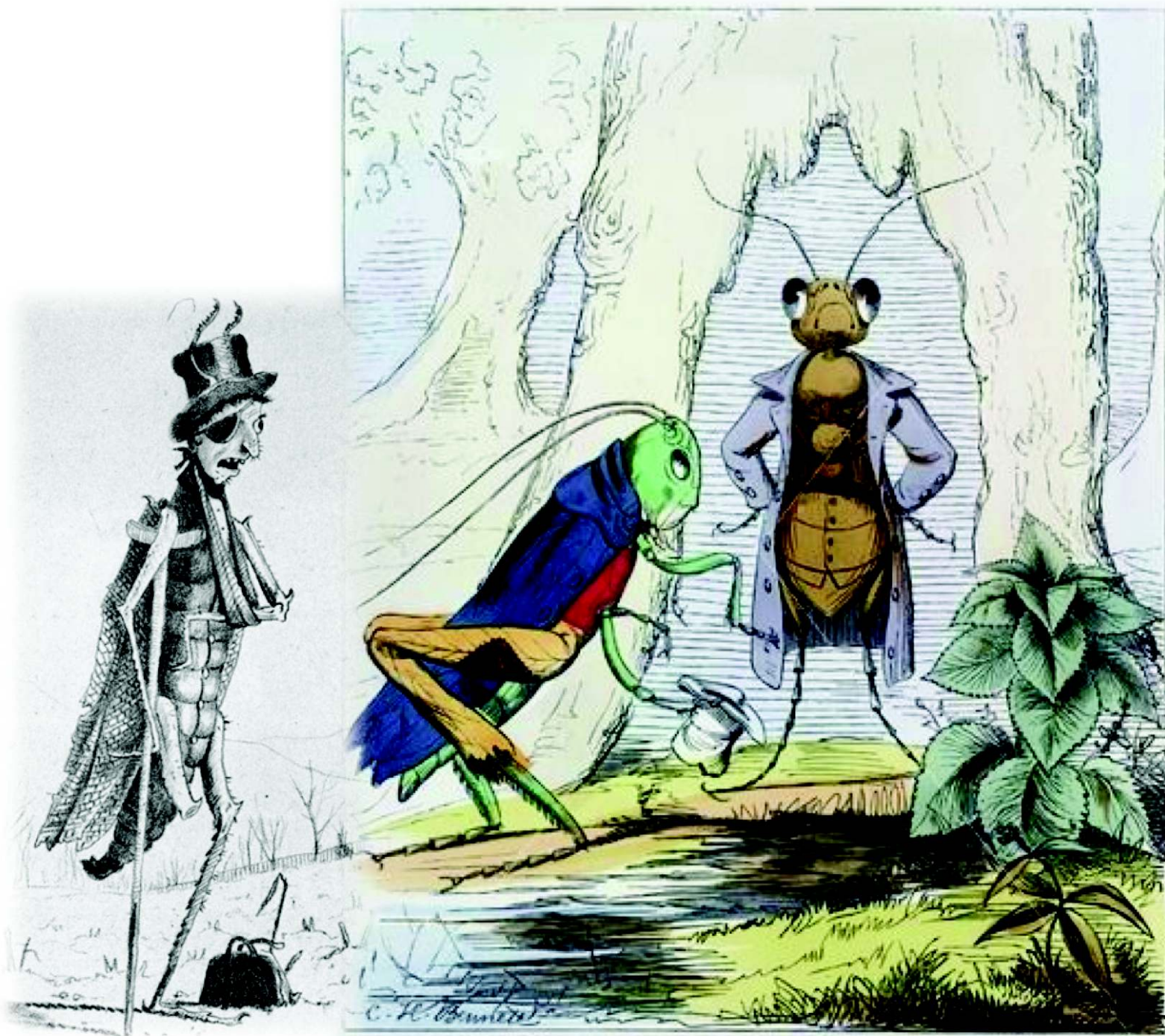


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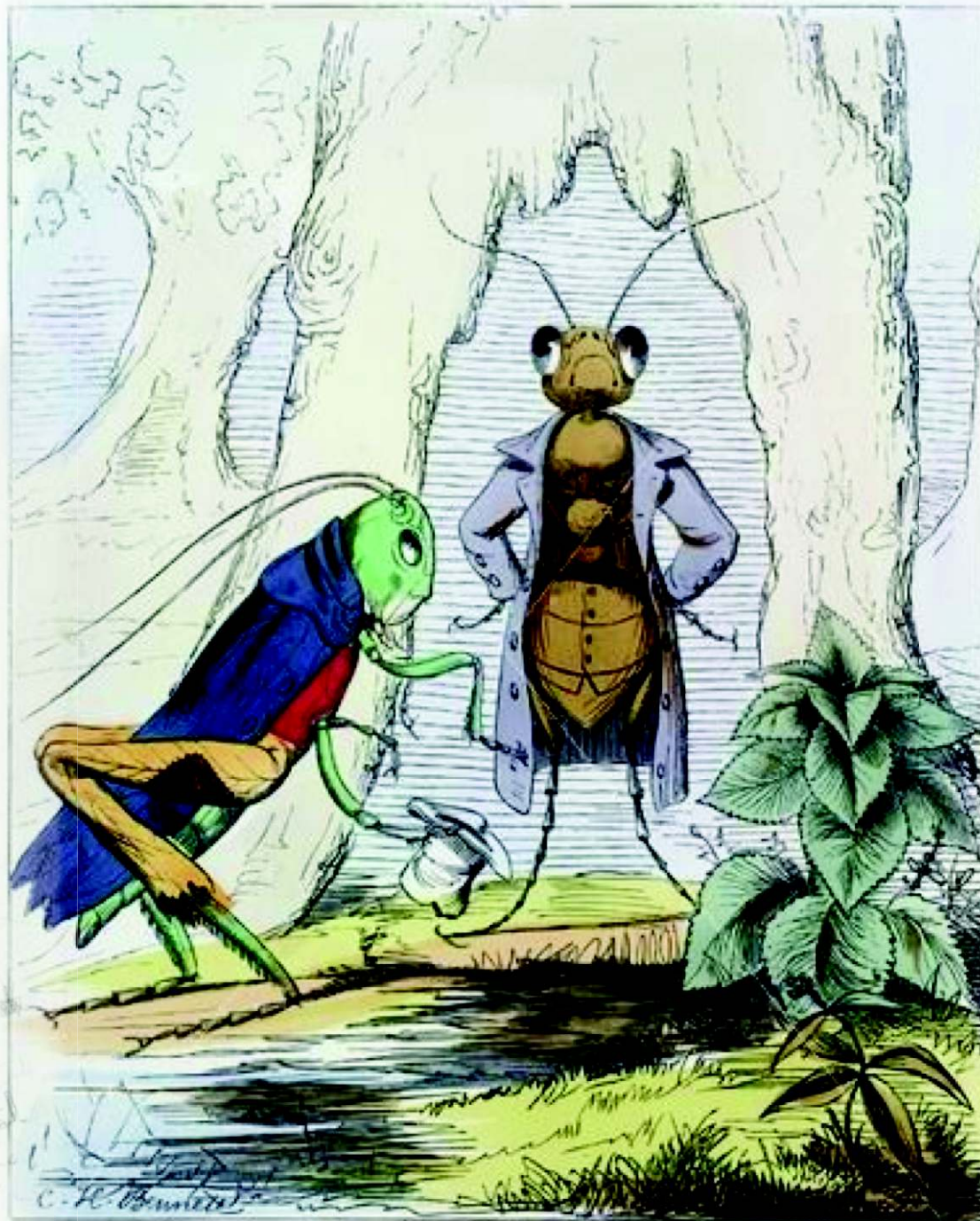
Question 3: What if..... ?



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A << L
Not Recapitalized
Corr(FB, FP) ≠ 0



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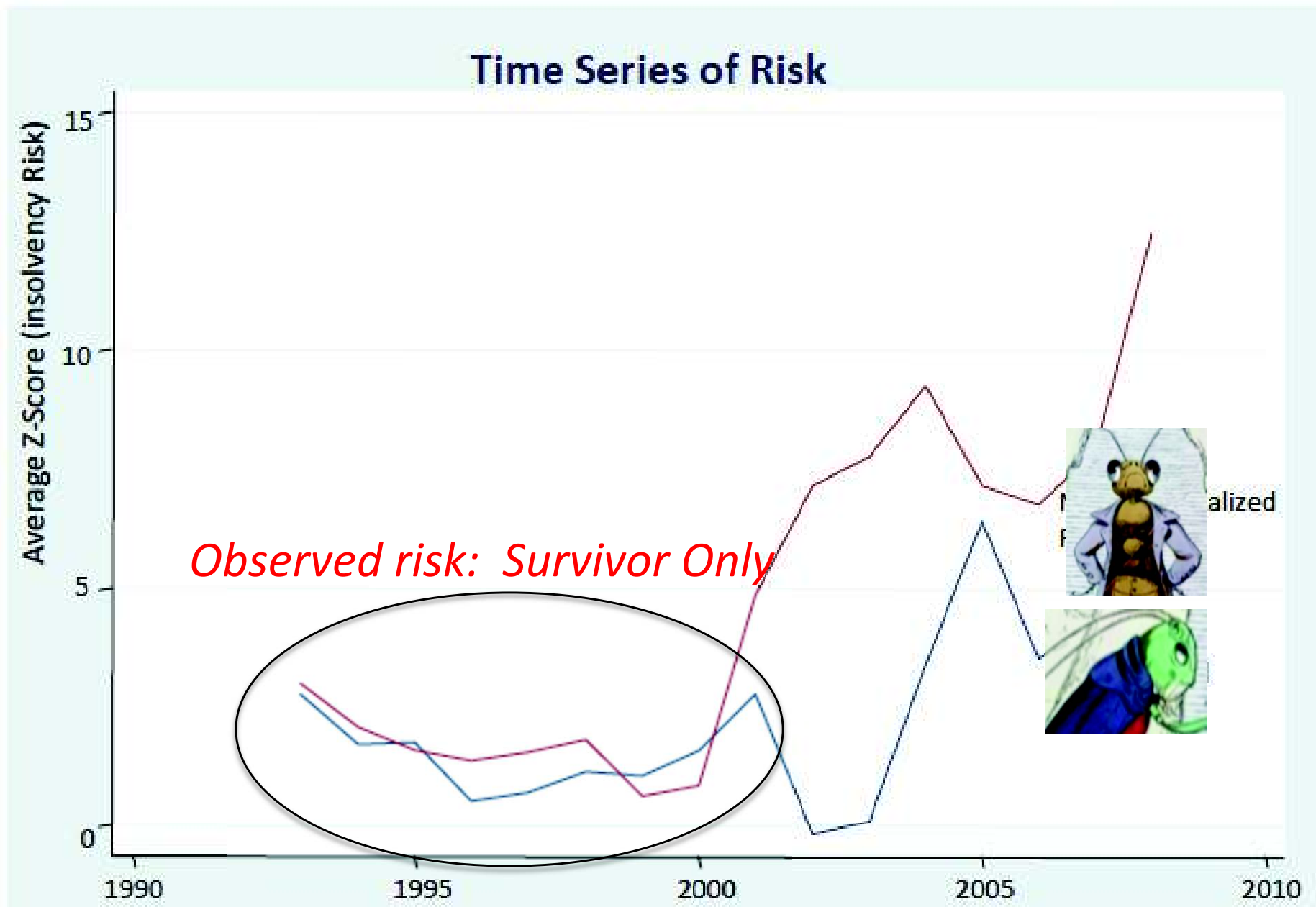


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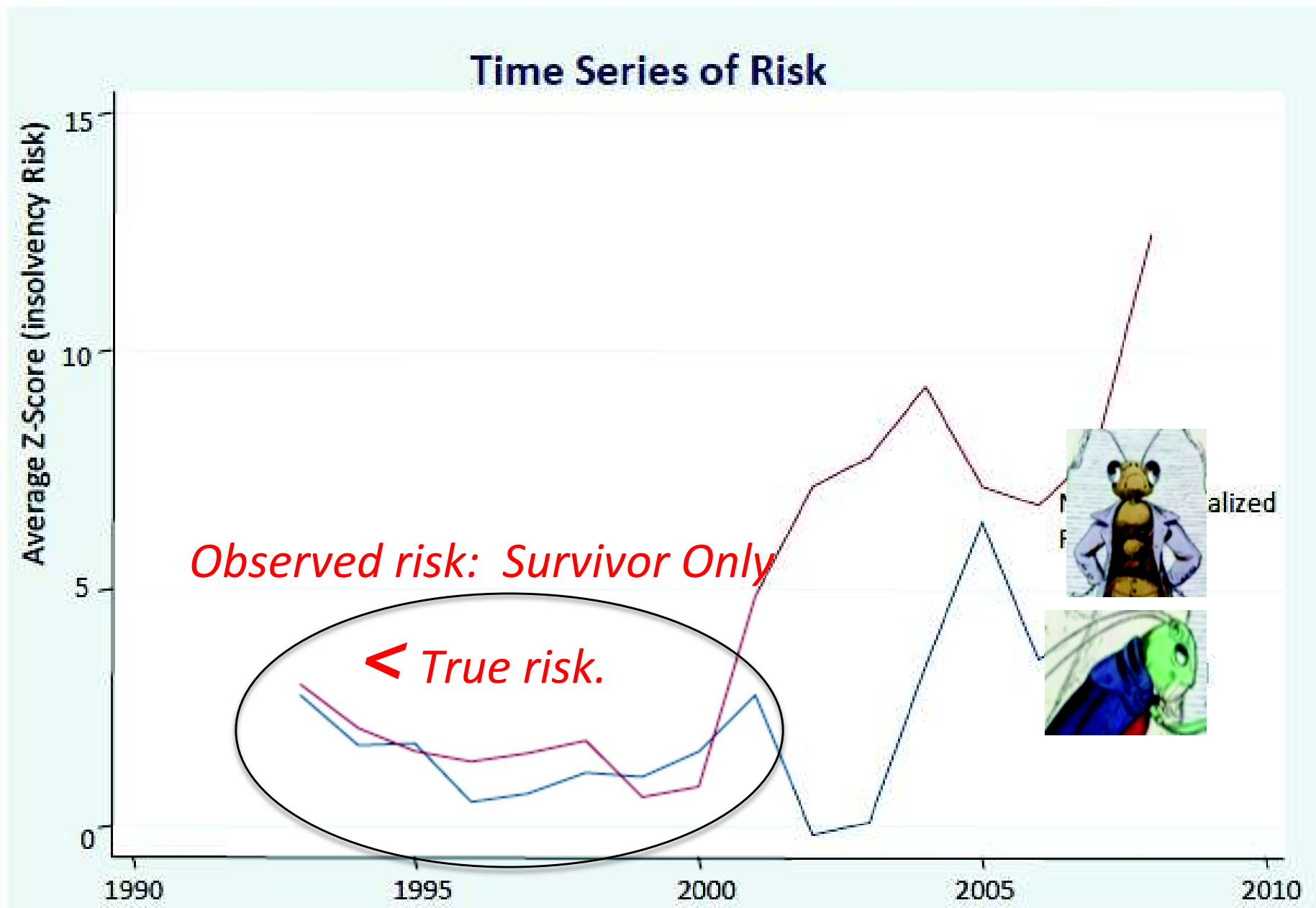
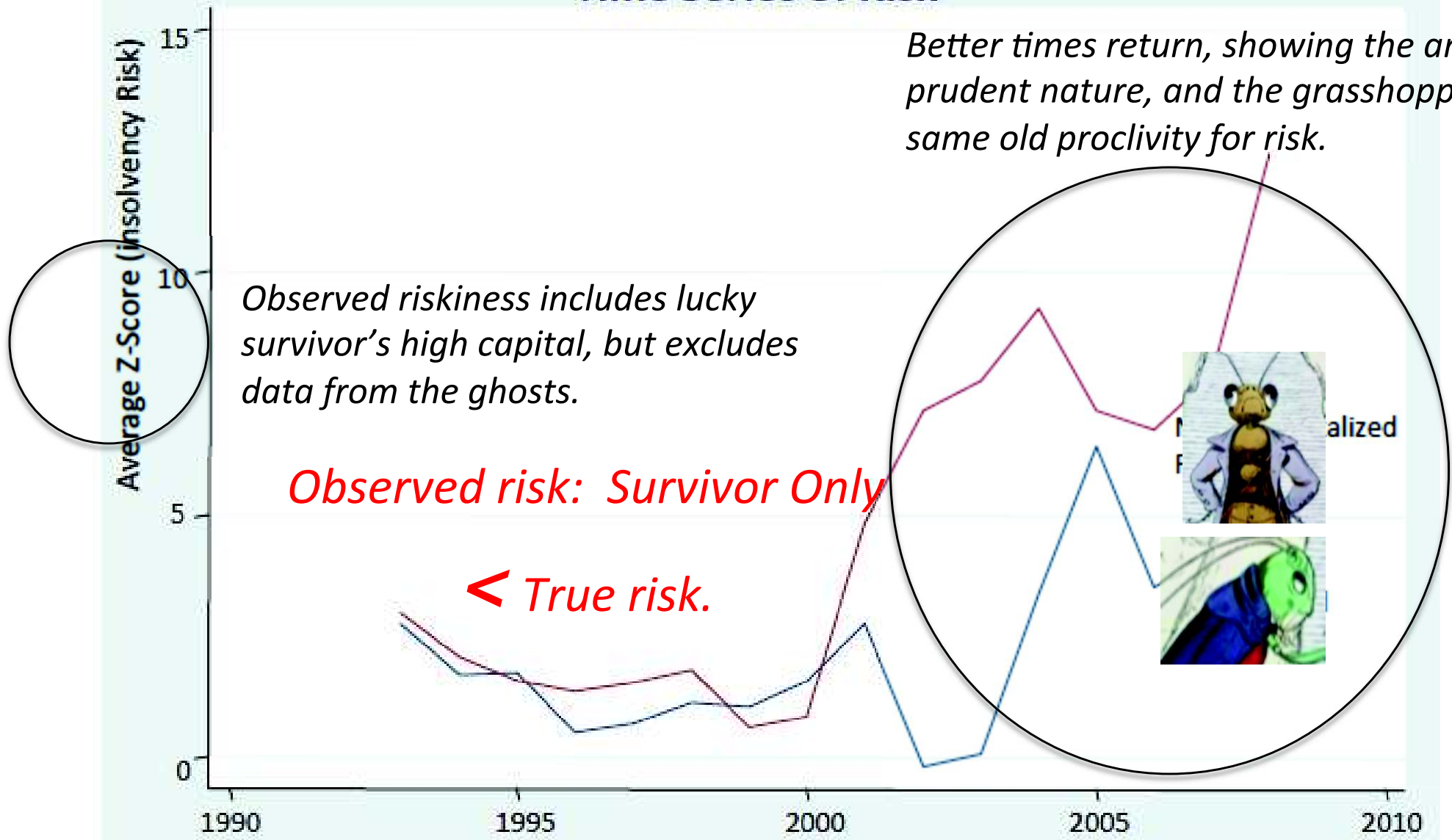


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Time Series of Risk



Average Z-Score (Insolvency Risk)

Observed riskiness includes lucky survivor's high capital, but excludes data from the ghosts.

Observed risk: Survivor Only

True risk.

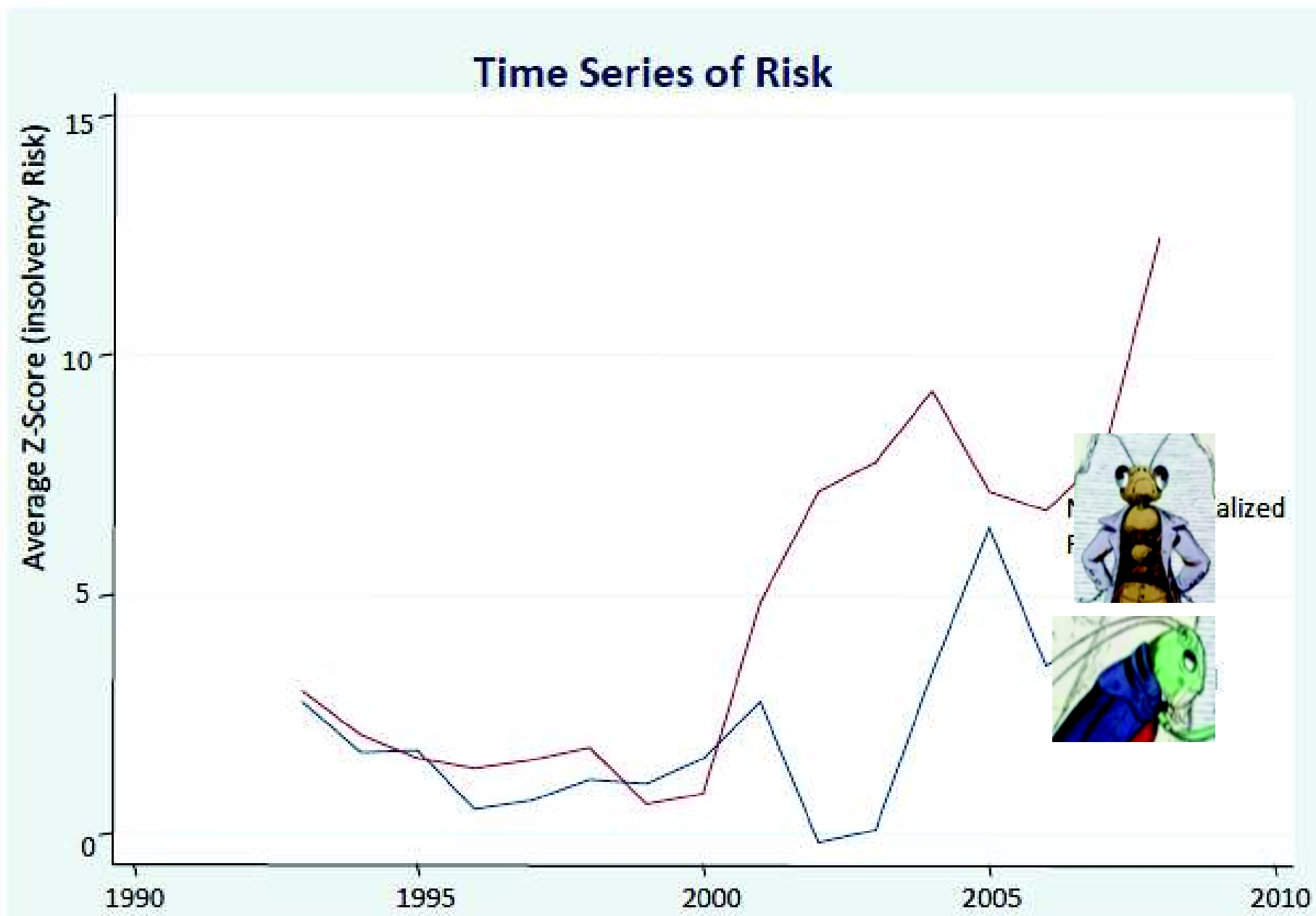
Better times return, showing the ant's prudent nature, and the grasshopper's same old proclivity for risk.



Recapitalized

Non-Recapitalized

Figure 1. Time Series of Risk Measure Between Recapitalized and Non-Recapitalized Banks



Treatment Effect or not?

Without recapitalization, a grasshopper would be like an ant.
(treatment effect)

Or,

An ant is an ant, & a grasshopper is a grasshopper.
(selection artifact)

Treatment Effect or not?

Strength of paper: Data

It would be helpful to see the data for the ghosts.

