Business models and bank performance: A long-term perspective

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*Any views expressed are those of the discussant and do not necessarily reflect those of the ECB.
Contribution

From an economic / policy perspective

• Provides a new look at bank business models by applying rigorous econometrics and factor analysis techniques to an interesting data set (500 banks, 30 European countries, 1998-2013).

From a technical / modelling perspective

• Unified evaluation of existing business model classification methods.
• Factor analysis on business model variables: identifies 2 latent lower-dimensional strategies, generating continuous common factors.
Main Findings

Economic findings

• Highlights limitations of defining business models as discrete clusters. Business models better described as a continuum of strategies.
• Diversification increases profitability but also susceptibility to distress.
• Business models matter a lot for banks’ risk-return profiles – “Retail”-oriented banks have higher profitability and stability.
• Effects of business model are markedly different for different bank types.

Policy-related findings

• Regulators and supervisors should also consider business models (in addition to liquidity and minimum capital requirements).
• Lends support to Basel III additional capital buffers for systemically important banks.
  – Capital ratios more performance impact for larger, wholesale funded, high LR...
General remarks

• Very relevant and timely topic from policy-making perspective
  – Good example of technique at the service of providing practical understanding

• Good application of well-known econometrics technique to gain new depth and angles on this particular topic

• Choice of business model variables:
  – Why use only observed financial ratios and ignore quantities and ratios related to distribution channels, types of clients and products, branches and employees, etc?
  – Sensitivity to choice of variables?

• Naming/interpretation of top 2 factors identified could be better justified, especially “RETAIL” one (“negatively related to size” – but there exist very large retail banks).
  – Why just use top 2 vs top 3 eigenvalues? Does this choice change much?

• Should revisit how the conclusions found compare to existing literature, e.g. role of diversification, different effects for different types of banks
Technical Remarks

• The paper has a clear focus and is well written.

• Use of multidimensional scaling method to compare existing business model classification methods: beware of over-simplifying when interpreting projection from 7 to 2 dimensions.

• Z-score definition different from standard one and maybe problematic

• Assumption: strategy as a long-term notion. Is it changing after the crisis? If yes, what does long-term mean? Could do robustness checks using the time dimension (given time window includes crisis).

• Calculation of NSFR from historical data not straightforward – please explain in more detail how achieved.

• Good point about observing banks at the level at which business model decisions are taken - but could do sensitivity checks of treatment of foreign vs. home subsidiaries.

• Good that robustness analysis sheds light on areas where questions had naturally arisen. Country-year fixed effects could be better justified. Robustness check?
Policy Issues

• Motivations of paper…
  – Seemingly successful business models proved fragile in the crisis (EG ??)
  – Regulation is causing business models to change, and the implications of those changes for profitability should be analysed.
  … could be re-visited after the analysis - how have they been addressed? What are the implications?

• Policy recommendation (regulators and supervisors to pay more attention to bank business model analysis) could be discussed, e.g. :
  – What is already being done in this respect? SREP mentioned but very briefly.
  – Comment further on conclusion that “large size is more stable in the long run but maybe at high societal cost” (section 4.2.1).
  – How should business models be taken into account? Difficulties? Consequences?