How to release capital requirements during a pandemic Evidence from euro area banks

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Abstract

This paper investigates the impact of the capital relief package adopted to support euro area banks at the outbreak of the COVID-19 pandemic. By leveraging confidential supervisory and credit register data, we uncover two main findings. First, capital relief measures support banks' capacity to supply credit to firms. Second, not all measures are equally successful. Banks adjust their credit supply only if the capital relief is permanent or implemented through established processes that foresee long release periods. By contrast, discretionary relief measures are met with limited success, possibly owing to the uncertainty surrounding their capital replenishment path. Moreover, requirement releases are more effective for banks with a low capital headroom over requirements and do not trigger additional risk-taking. These findings provide key insights on how to design effective bank capital requirement releases in crisis time.

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