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

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AbstractThis 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.JEL CodeE61 : Macroeconomics and Monetary Economics→Macroeconomic Policy, Macroeconomic Aspects of Public Finance, and General Outlook→Policy Objectives, Policy Designs and Consistency, Policy CoordinationG01 : Financial Economics→General→Financial CrisesG18 : Financial Economics→General Financial Markets→Government Policy and RegulationG21 : Financial Economics→Financial Institutions and Services→Banks, Depository Institutions, Micro Finance Institutions, Mortgages