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Article
What We Can Learn from the Introduction of Blanket Deposit Guarantees in Germany 2008 about the Benefits of EDIS

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The euro area was severely affected by the global financial crisis. But while many other regions resolved the financial crisis without much ado, the euro area is still suffering from the crisis repercussions ultimately culminating in the sovereign debt crisis, bringing about a double dip in economic growth. This particularity of the euro area is largely due to what is now known as the “doo m loop”: the mutual reinforcement of a domestic banking crisis and a sovereign debt crisis. Expectations of a costly government bailout of individual financial institutions and of the domestic deposit insurance systems raised worries in some member countries about the sovereign’s solvency and led to soaring interest rates on domestic government bonds. The associated drop in the value of domestic sovereign bonds in banks’ portfolios, along with elevated concerns about regulatory forbearance by domestic banking supervisors to avoid costly bailouts, further aggravated the banking crisis, and led to a more severe sovereign debt crisis. This doom loop is particularly acute in the euro area, as the common monetary policy cannot help ease the sovereign debt crisis of individual member countries.

The European Council and the European Commission identified this shortcoming in the construction of the eurozone. In 2014, the European Council and the European Commission agreed on the creation of a Banking Union, which includes two key elements: the Single Resolution Mechanism (SRM) and the Single Supervisory Mechanism (SSM), and the European Deposit Insurance Scheme (EDIS). The SRM and EDIS are measures to foster risk-sharing of banking crises between and within member states. The EDIS implements a common resolution framework for troubled banks that can draw on a fund financed by euro area banks, lessening the need for government bailouts, while EDIS ensures the necessary common deposit insurance scheme. This system is to be funded by risk-based contributions from euro area banks and backed by the European Social Fund. The SSM is intended to establish a level playing field for supervisors and prevent regulatory forbearance, or at least safeguard its consistent application across countries. It ensures that the same rulebook applies when supervising both the large, systemically relevant euro area banks, which are directly monitored by the SSM, and the other euro area banks, which are monitored by the SSM only indirectly.

While the SSM and the SRM took effect in 2014, EDIS has not yet been launched. There are concerns that EDIS could aggravate various forms of moral hazard and risk-shifting, and could introduce unintended cross-subsidies across member states or their respective banking sectors. It is widely established that a deposit insurance scheme undermines market discipline and potentially leads to excessive risk-taking (see, for instance, Calomiris and Jareskis 2016; Lambert et al. 2014). However, in 2000, Art. 94-95/EC imposed minimum requirements on national deposit insurance schemes for all EU member states, indicating that member countries considered the risk-shifting stabilization to be the stabilizing role a deposit insurance scheme plays in banking crises. The risk-sharing implemented through EDIS only increases the credibility of the deposit insurance scheme in countries with a heavily indebted sovereign. To what extent this leads to an unwanted deterioration of market discipline for banks in those countries remains a question.

depositors shift their money between cooperative and domestic banking associations. This introduced a homogenous governance backing of deposits in both savings banks and cooperative banks. This introduced a homogenous government backing of deposits in both savings banks and cooperative banks. As we argue in Facht et al. (2019), this setup lends itself to the study, with a cross-sectional and an intertemporal level. Whether in a period of heightened concerns about bank defaults, depositors shift their money between cooperative and savings banks only because of a heterogeneity of the deposit insurance scheme.

A NOVEL APPROACH TO MEASURING DEPOSITORs’ EXPECTATIONS

To study whether a potential shift of deposits from the quasi-paternalistic cooperative to the supervisory and prevent savings banks is due to increased fears of a bank run by depositors in a particular region, in Fecht et al. (2019) we use a novel empirical indicator to capture those depositors’ expectations at a high frequency. Specifi-
ally, we use Google searches for terms like “deposit insurance” that are available on a weekly basis from Google Trends. An increase in this measure suggests that people are more concerned about losing their money due to a bank run. We then compare this data with statistics from the German Bundesbank’s monetary financial institutions (MFIs) balance sheets (to obtain information at the bank level about German depositors’ outstanding overnight deposits) and to the Bundesbank’s MFI interest rate statistics (for information about interest paid on those deposits). The subsequent analysis focuses only on overnight deposits, since these are immediately transferable, and on the “deposit insurance” search string for the fear indicator constructed from Google Trends.

**ARE INCREASED DEPOSIT FEARS DRIVING DEPOSIT OUTFLOWS FROM PRIVATE BANKS?**

In the first step of the analysis in Fecht et al. (2019), we compare the relative market share in the overnight deposits market of savings banks to cooperative banks, and assess whether a jump in Google searches for “deposit insurance” signals an increase in customers who transfer money from cooperative banks to savings banks. We also control for the fact that gains in market share may be due to a higher interest rate paid by one of the two banking sectors.

Figure 1 shows the ratio of the total volume of overnight deposits at savings banks to the total volume of overnight deposits at cooperative banks (blue line) as well as to the winorized Google searches for “deposit insurance” with a five-month lag (red line). There is a significant correlation between savings banks’ gain in relative market share and an increase in this “fear” indicator. Applying a vector autoregression (VAR) model with the three key variables, we obtain in Fecht et al. (2019) the impulse response functions depicted in Figure 2. It further supports the visual evidence in Figure 1, namely that a spike in Google searches (i.e., an increased level of fear) leads to an increase in the market share of public banks (bottom graph in Figure 2). As is evident from the impulse-response functions, higher anxiety among depositors is also associated with a lower interest rate margin. This could imply that savings banks are lowering their interest rates due to the increased inflow of deposits from anxious investors from cooperative banks. We also show the results for a bivariate Granger causality analysis and reject the null hypothesis that people are more concerned about losing their money due to a bank run. The results support the idea that a spike in Google searches (i.e., an increased level of fear as measured by the searches in each state) leads to a significant decline in the volume of overnight deposits at cooperative banks, whereas the volume of deposits at savings banks remained largely unchanged. After October 5, 2008, a higher level of anxiety among depositors did not lead to any significant in- or outflows to banks in either of the two sectors. Thus, again—but using a different perspective—the introduction of a blanket guarantee allevied the fears of depositors across the banking system.

In addition to this key finding, our results also show that the government guarantee had another significant effect on the banking system: before October 5, 2008, cooperative banks were not able to attract significant additional deposit inflows by increasing the interest rate on overnight deposits, whereas savings banks were successful with the same method. However, the guarantee leveled the playing field in the banking system: after October 2008, deposits at cooperative banks increased significantly when interest rates rose, and the interest rate sensitivity of deposit flows at cooperative banks is not statistically different from that at savings banks.

**CONCLUSION**

Taking the findings from Fecht et al. (2019) together, we can conclude that the announcement of the government backing of deposits across the German banking system in October 2008 stopped the fear-driven withdrawal of deposits from cooperative banks and their reallocation to savings banks, which had been observed prior to that date. This suggests that even in the absence of any renumeration risks, heterogeneity in the backing and credibility of deposit insurance schemes leads to a reallocation of deposits among different banking sectors with potentially destabilizing effects. There is clearly a role for EDIS to play in mitigating this effect.

**REFERENCES**


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![Impulse response functions (IRFs) for the search term ‘Deposit Insurance’](image-url)