Discussion of "Origination and Sale of Loans, and Bank Capital Regulation" by Michal Kowalik and Ernst-Ludwig von Thadden

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[1] The views expressed in this discussion do not necessarily reflect the views of the Federal Reserve Bank of Richmond or the Federal Reserve System.

Their Goal

Effect of capital requirements on credit supply

particularly over a business cycle

The Bank's Decision Problem

$t = 0, 1, 2$

At $t = 0$, decide on deposits and loans L that payoff at $t = 2$

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Assumptions Can't raise equity, investors can't make loans

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Problem: A good bank cannot raise as much capital as it would like by selling loans. Thus, makes less $t = 1$ loans.

- Pooling equilibria - gets the pooled price or no sales
- Separating equilibrium - sells only enough so bad doesn't copy

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Note: Forbearance is good here!

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Data - banks hold (in good times) a buffer over regulatory minimum

But, need to go a level deeper

- What are the costs and benefits of different levels?

This is a big open question.
Lots of theory, but not much quantitative work

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Calem and Rob (*JFI*, 1999)

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Van den Heuvel (*JME*, 2008)

- Estimates the cost of bank capital due to lost liquidity services
- Uses a GE steady state model
- Increase capital 10% costs 0.1 - 0.2% in consumption
- Big - but maybe worth it

Value of Quantitative Work

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Also, relevant for analyzing other types of capital requirements like contingent capital