How Do Government Guarantees Affect Deposit Supply?

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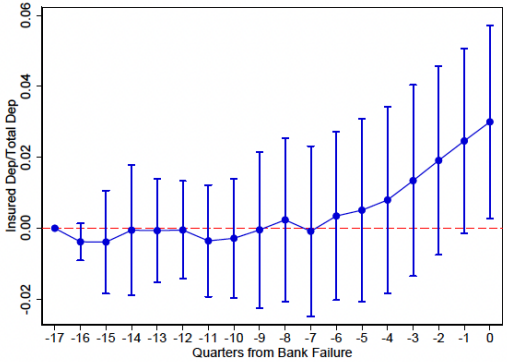
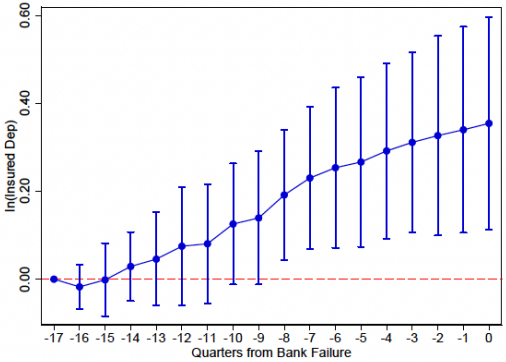
What is this paper about?

- How valuable are deposit guarantees?
- When banks anticipate asset losses, depositors might leave unless they are insured
- Banks try to attract insured deposits if they anticipate losses
- They do it by offering higher insured deposit rates

Banks close to failure increase insured deposits

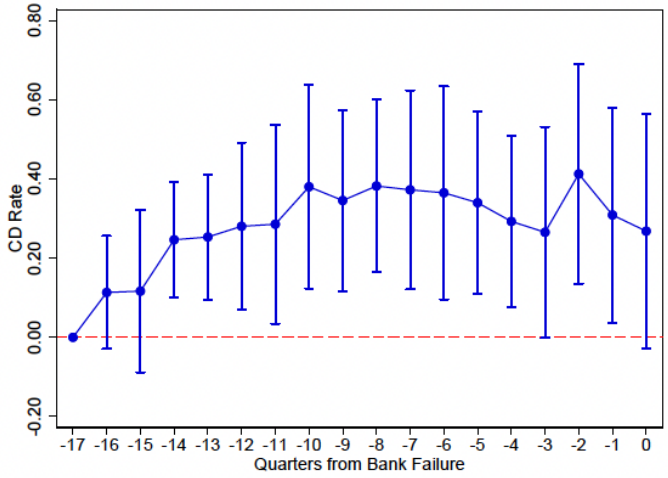


(c) Insured Deposit Fraction



(d) ln(Insured Deposits)

Banks close to failure increase insured deposit rates



Literature

- Drechsler et al (2017): when interest rates rise, banks increase spreads and lose deposits
- Deposit franchise value increases
- Drechsler et al (2025):

$$FV = f(\beta, stickiness)$$

- Uninsured deposits are flightly $\Rightarrow$ higher β $\Rightarrow$ less room for franchise increase

Literature

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- This paper: banks substitute uninsured deposits with insured deposits in bad times

Literature (cont.): Acharya and Mora (2015)

	Large Time		Core	
	(1)	(2)	(3)	(4)
Unused Commitment Ratio$_{t-1}$	0.139	-0.810^{***}	-0.329^{***}	-1.804^{***}
	(0.095)	(0.106)	(0.093)	(0.117)
Unused Commitment Ratio$_{t-1}\times$ Crisis1	0.592^{***}	0.710^{***}	0.033	0.725^{***}
	(0.119)	(0.139)	(0.095)	(0.217)
Bank Fixed Effects	Yes	No	Yes	No
Observations	196,124	196,124	196,151	196,151
R^2	0.74	0.71	0.89	0.76

- Banks pay higher rates
- Even higher for uninsured deposits

Overall asessment

- Important question and solid execution
  - The results are replicable and robust
  - The failing bank event study is convincing
- My comments will focus on mechanisms, interpretations, and extensions

Comment 1: Rate discussion

- From DSSW: both betas and stickiness matter for deposit franchise
- This paper discusses flightiness of the deposits but much less the interest rate risk
- Uninsured betas are high – when banks lose assets in high-interest times, this matters
- Moving to insured deposits reduces "average" beta

- Flightiness is one of the reasons for different betas

Uninsured rates increase even more

	Insured CD Rate		Uninsured CD Rate	
	(1)	(2)	(3)	(4)
L.LLP Ratio	0.018***	0.013***	0.031***	0.031***
	(0.003)	(0.003)	(0.005)	(0.005)
Bank FE	Yes	Yes	Yes	Yes
Time FE	Yes	Yes	Yes	Yes
Controls	No	Yes	No	Yes
Obs.	1,059,056	1,059,056	649,481	649,481
R^2	0.910	0.912	0.754	0.755

- Why is this a case? Does this incentivize banks to switch to a lower-beta type of deposits?
- **Suggestion**: Explore uninsured deposit rates and betas more

Why do banks have uninsured deposits?

- Uninsured deposits are more costly regardless of the state of the world
- In the authors' model, adding uninsured deposits leads to **0 uninsured deposits** in equilibrium
- If banks could, why can't they increase insured rates and lower their average betas?
- Answer: insured and uninsured deposits are not perfectly substitutable
- Insured deposits are mostly retail, uninsured are mostly wholesale

Comment 2: Global vs local

- If banks raise retail deposits by increasing rates, we should see local results

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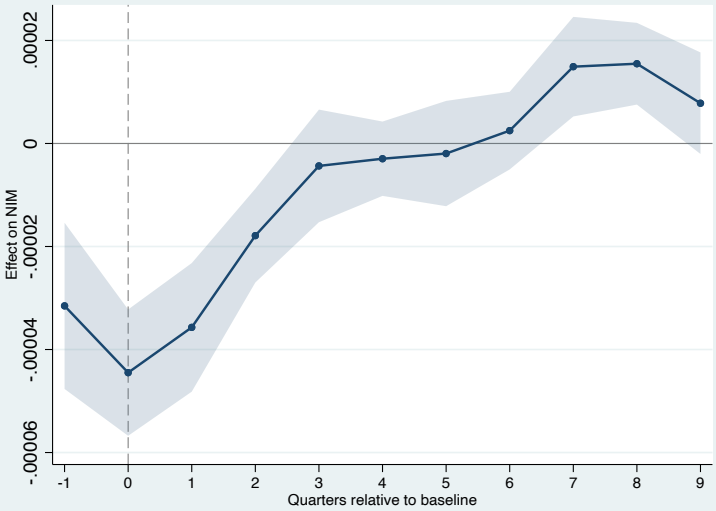
	MM Rate		CD Rate	
	(1)	(2)	(3)	(4)
L.LLP Ratio	-0.020^{***}	-0.021^{***}	-0.006	-0.004
	(0.005)	(0.005)	(0.004)	(0.004)
Bank FE	Yes	Yes	Yes	Yes
State $\times$ Time FE	Yes	Yes	Yes	Yes
Controls	No	Yes	No	Yes
Obs.	303,875	303,875	288,543	288,543
R^2	0.950	0.950	0.767	0.768

- This is quite puzzling and requires explanation
- **Suggestion**: Explore RateWatch and analyze branch-level deposit rates

Comment 3: Does it help to have more insured deposits?

- Acharya and Mora (2015): raising new deposits does not help to fully recover
- **Suggestion:** Respond by analyzing NIMs
- If banks lose part of their franchise by paying more competitive deposit rate, expect decline in NIM
- If banks' average beta improves, NIM can recover

NIM recovers



Comment 4: Deposit channel

- Authors argue their channel is opposed to the deposit channel
  - because conditioning for HHI
- Deposit channel is not only about HHI
  - Market power $\Rightarrow$ deposit betas
  - HHI is just a part of it
- If deposit guarantees $\uparrow$ deposit franchise, then this is deposit channel
- Nothing wrong with this, just a writing comment

Minor comments

- Variation in LLP is quite small but has a big right tail – is the story about banks close to failure?
- Identification discussion focuses on reverse causality but not omitted variables
- Higher NPL can incentivize banks to lower their insured deposit rates
- Long-term share in portfolio weights can impact the preference for time deposits (Supera (2022))
- Discuss economic magnitudes more – similar to Acharya and Mora (2015)
- Discuss why banks that are very close to failure try to rescue themselves
- The model should include uninsured deposits

Conclusion

- Very polished and timely paper
- Reassured us that deposit insurance was a successful policy
- Needs more discussion of deposit betas, local markets, and medium-term consequences

Good luck!