Discussion of

“The Effects of Supervision on Bank Performance: Evidence from Discontinuous Examination Frequencies”

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“The Effects of Supervision on Bank Performance: Evidence from Discontinuous Examination Frequencies”

- Title and framing
- Hypothesis
- Results
- Empirical strategy
- Implications

Title and Framing

- A better title:

  "Do More Frequent Exams Improve Small-Bank Performance? Evidence from Discontinuous Examination Frequencies"

- This is a study of community-bank supervision in the U.S.; it provides no generalizable evidence on the "the effects of supervision on bank performance" in other countries or for large U.S. banks.

- There is a large accounting literature on optimal monitoring/auditing, not cited in paper.

Hypothesis

- The null and alternative hypotheses:

  H_o: Time between exams does not matter for bank performance.

  H_A: More-frequent exams improve bank performance.

- Is it really a one-sided test? Rejection of the null would imply that all banks should be examined continuously (i.e., time between exams = 0).

- Two-sided H_A is better if community-bank exam frequency in the U.S. may be too high or too low.

Results

- Holding all else constant, a more-frequent exam schedule (fewer days between exams) improves bank performance:
  - ROE and NIM
  - Loan-performance measures
  - Capital ratios

- The all-else-constant part is daunting
  - Bank size, location, business mix
  - Charter type and primary supervisor
  - Bank management quality

Empirical Strategy

- Clever use of exam-frequency discontinuities around a moving, fuzzy boundary.

- Consistently conservative approach to drawing inferences from the data; several convincing robustness checks.

Empirical Strategy

- My only nagging concern about the model:

  Have you controlled adequately for the existence of scale economies or other sources of correlation between size and performance in banking?

  - Most banks in the sample are inefficiently small.
  - What if bigger banks are, on average, better performers?
  - Then being bigger could improve performance measures independently of size’s effect on exam frequency, which is at the heart of the identification strategy.
  - This may not be a big deal; I’m just asking.

Implications

- For supervisors: Should we increase exam frequency beyond legislated levels?

- For legislators: How do these results inform social-welfare calculations regarding S&R resources?

- For bankers: Why do they complain so much about exams if it improves their performance?

- For the public: Is the deregulation mantra of the last 30 years wrong—not just in banking but elsewhere?