

Bank Lending Channel and International Capital Flows into a Banking Sector in a Dollarized Economy

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Abstract

In this study, we study sensitivity of bank lending to foreign funding flows by exploiting unique data which allow us to reveal the exact amounts of funds individual Cambodian banks received from abroad. Specifically, we construct dataset from balancesheets of commercial banks on a quarterly basis (2011Q4-2017Q4). Furthermore, our paper develops the empirical model to identify a causality in the impact of foreign funding flows by using the information of bank ownership and foreign countries' economic and monetary conditions as instrument variables. As the result, we empirically find that foreign funding flows are positively associated to bank lending as well as domestic funding flows, and we also find the robust results with sub-sample of largest banks, suggesting that the Cambodian banking sector is significantly dependent on the foreign funding sources. Next, we demonstrate that the foreign funding flows are affected by foreign countries' economic and monetary conditions. Specifically, GDP growth in home countries of the bank's major shareholder negatively affects the foreign funding growths for the Cambodian banks. Furthermore, deposit rates in home countries temporally affect funding inflows in the sense that it has negative effects at first quarter, and positive effects in the following quarters, reflecting that the effect of monetary policy on funding flows is neutral in the long run. Lastly, we find that the causal impact of foreign funding inflows on bank lending in the Cambodian banking sector. Those findings suggest that the Cambodian banking sector is vulnerable to the external shocks.

Keywords: Bank Lending Channel, International Capital Flow, Dollarization