North American Journal of Economics and Finance 32 (2015) 12–28

Contents lists available at ScienceDirect

North American Journal of Economics and Finance

Securitization and credit risk: Empirical evidence from an emerging economy

Helder Ferreira de Mendonça[a,*], Vívian Íris Barcelos[b]

[a] Fluminense Federal University, Department of Economics and National Council for Scientific and Technological Development (CNPq), Brazil
[b] Fluminense Federal University, Department of Economics, Brazil

ARTICLE INFO

Article history:
Received 17 June 2014
Received in revised form 13 January 2015
Accepted 14 January 2015
Available online 28 January 2015

JEL classification:
G14
G21
G28

Keywords:
Securitization assets
Credit risk
Financial system
Brazilian economy

ABSTRACT

This paper presents empirical evidence from the Brazilian experience for the analysis on securitization transactions and credit risk. Based on panel data framework that takes into account 60 financial institutions from October 2002 to September 2012, we observe if there is some effect of the securitization transactions on credit risk and also whether credit risk stimulates securitization. Our findings indicate that securitization transactions imply an increase in the credit risk whereas credit risk is not relevant to explain securitization in Brazil.

1. Introduction

With the objective of increasing liquidity in the financial systems, financial innovations proliferated. Among financial innovations there was a rapid development of credit risk transfer markets. In particular, structured finance allows different classes of assets being regrouped and their risk dispersed among different agents. As identified by Affinito and Tagliaferri (2010), it is possible to identify

* Corresponding author at: Rua Dr. Sodré, 59 – Vila Suíça, Miguel Pereira – Rio de Janeiro, CEP: 26900-000, Brazil. Tel.: +55 24 2484 4143.
E-mail address: helderfm@hotmail.com (H.F. de Mendonça).

http://dx.doi.org/10.1016/j.najef.2015.01.002
1062-9408/

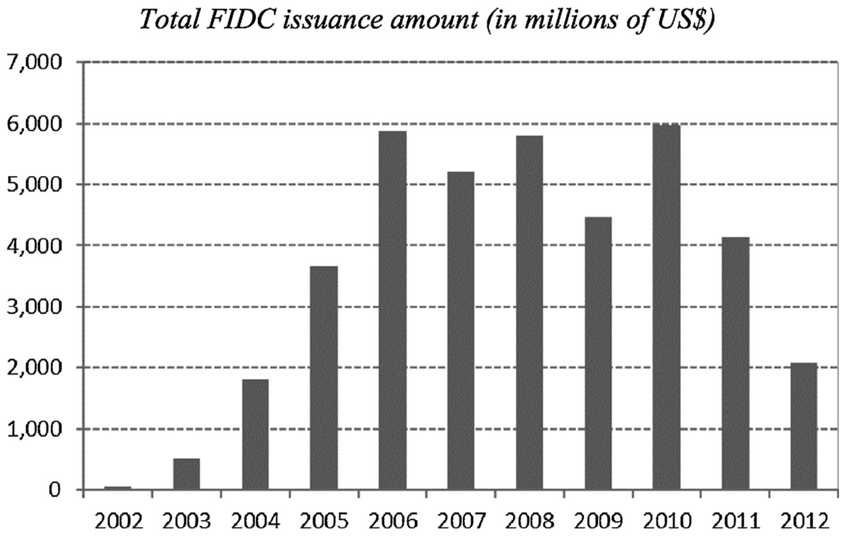

Fig. 1. Total FIDC issurance amount (in millions of US$).
Source: Securities and Exchange Commission of Brazil (CVM).

four main determinants in deciding to securitize bank loans: the need for new sources of funding, the transfer of credit riskiness, the search for new profit opportunities, and the role of capital.

The idea that the development of credit derivatives contributed to the stability of the banking system was well accepted before the subprime crisis (Duffie, 2008). After the subprime crisis the perception that credit derivatives are beneficial for the financial system is doubtful.[1] Some authors such as Uhde and Michalak (2010) found evidence that credit risk transfer operations weaken the stability of the financial system. This result can be connected with the possibility that transfer of credit risk can reduce the monitoring of borrowers by the financial institutions (Keys, Mukherjee, Seru, & Vig, 2010). In contrast, according to Dionne and Harchaoui (2003), in the case of securitization of assets, financial institutions transfer only good quality credit in order to obtain high credit ratings.

In short, there is no clear evidence regarding the effect of securitization transactions on the risk in the financial system. This literature is incipient for emerging economies and, in particular, for Latin American countries. A possible justification for this fact can be a lack of a developed financial system in these countries. However, since 1999, Brazilian economy is marked by a macroeconomic stability which contributes to the development of financial markets (see World Economic Forum, 2011). A good example is that the Central Bank of Brazil, through resolution n. 2907 of 2001, created Credit Rights Investment Funds and opened a new capital market alternative. As a result, the issuance volume of FDIC is not negligible (see Fig. 1) and the domestic market represented 45% of the volume of securitization of Latin America in 2012 (Moody's, 2012). Therefore, analysis on securitization of receivables in Brazil allows one to extract some empirical evidence.

This paper makes a contribution to the empirical literature on securitization transactions and credit risk through empirical evidence from the Brazilian experience. Using Ordinary Least Squares (OLS) and dynamic panel data framework (Difference Generalized Method of Moments – D-GMM and System Generalized Method of Moments – S-GMM) that draws on 60 financial institutions from December 2002 to October 2012, our analysis is divided into two parts. First part of the empirical analysis assesses the effect of the securitization transactions on credit risk. Second part evaluates the determinants of securitization. Special attention is given to checking whether credit risk stimulates securitization

[1] For an analysis regarding if there was a global banking crisis due to financial crisis that started in 2007, see Shehzad and De Haan (2013).