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# The asymmetric effect of international swap lines on banks in emerging markets[☆]

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ABSTRACT

This paper investigates the effect of international swap lines on stock returns using data from banks in emerging markets. The analysis first shows that swap lines by the Swiss National Bank (SNB) had a positive impact on bank stocks in Central and Eastern Europe. It then highlights the importance of individual bank characteristics in identifying the asymmetric effect of swap lines on bank stocks. Bank-level evidence suggests that stock prices of local and less-well capitalized banks as well as banks with high foreign currency exposures and high reliance on short-term funding responded more strongly to SNB swap lines. This new evidence is consistent with the view that swap lines not only enhanced market liquidity but also reduced risks associated with micro-prudential issues.



## 1. Introduction

In response to the global financial crisis, international swap lines between central banks of advanced economies and their counterparts in emerging market economies were introduced as a coordinated policy initiative. Empirical studies by Aizenman and Pasricha (2010), Moessner and Allen (2013), and Baba and Shim (2010) show supportive evidence that these international swap lines (hereafter, swap lines) were coincident with reductions in Covered Interest Parity (CIP) or Credit Default Swap (CDS) spreads. The country-level studies argue that swap lines prevented systemic risk and limited contagion during periods of market stress.

Although empirical studies suggest being able to identify macroprudential effects arising from swap lines, a shortcoming of the literature is its narrow focus on country-level responses to swap lines. Country-level data do not shed light on the channels through which swap lines impact banks, i.e., the beneficiaries of the foreign liquidity provision. The country-level studies assume banks are homogenous.[1] Banks however are heterogeneous in their characteristics and if specific bank characteristics matter then the response to swap lines is not expected to be uniform. In particular, it may arise that banks with high levels of foreign currency exposure benefit more from swap lines than do banks with low levels of foreign currency exposure. Alternative bank characteristics, such as banks with a weak capital structure or with a higher

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[1] For example, Goldberg et al. (2011) and Bruno and Shin (2014) acknowledge that European and Korean banks did not make equal use of liquidity provisions provided by swap lines.

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