Pills

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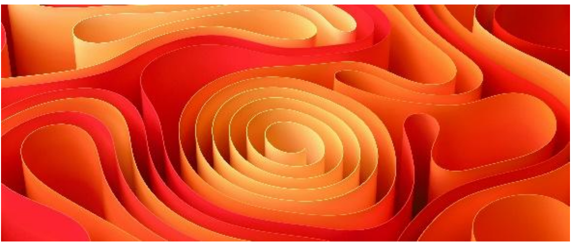

TOPICS:

Liquidity Risk

SOURCE:

Bank for International Settlements

BIS: Liquidity Regulation and Bank Funding Costs

- This paper analyses **how Basel III liquidity regulation** - specifically the Liquidity Coverage Ratio (LCR) - **affects banks' wholesale funding costs**. Using detailed U.S. money market fund (MMF) lending data from 2011–2015, the authors show that stricter liquidity requirements significantly reduced banks' borrowing costs.
- The LCR requires banks to hold enough High-Quality Liquid Assets (HQLA) to survive 30 days of stressed cash outflows. The paper argues that **stronger liquidity buffers make banks safer and therefore lower the risk premium** demanded by uninsured wholesale creditors.
- To identify the effects of regulation, **the study compares banks with different pre-regulation** "LCR gaps," meaning differences in how far banks were from meeting the new requirements before implementation in 2013. Banks with larger gaps increased their liquid asset holdings more substantially after the reform.
- The results show that **banks more exposed to the LCR experienced larger declines in wholesale funding costs**, with average reductions of around 2.5 basis points. The decline was particularly strong for longer-maturity instruments, consistent with the view that liquidity regulation reduces rollover and refinancing risk. Banks also shifted their funding structure toward longer-term liabilities.
- The paper concludes that **liquidity regulation not only improves financial stability but can also offset some compliance costs** by lowering banks' funding expenses.