Banking without Deposits: Evidence from Shadow Bank Call Reports

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We ask how much leverage banks would choose in the absence of safety nets tied to insured deposits. Using uniquely assembled data on capital structure decisions of shadow banks – intermediaries that provide banking services but are not funded by insured deposits – we document five facts. (1) Shadow banks use twice as much equity capital as equivalent banks but are substantially more leveraged than non-financial firms. (2) Leverage across shadow banks is substantially more dispersed than leverage across banks. (3) Like banks, shadow banks finance themselves primarily with short-term debt and originate long-term loans. (4) Shadow bank capitalization decreases substantially with size. Bank capitalization hardly changes with size. Uninsured leverage, defined as uninsured debt funding to assets, increases with size for both banks and shadow banks. (5) Average interest rates on uninsured debt decline with size for banks and shadow

banks. Shadow banks pay substantially higher rates than banks on debt across the size distribution. As external validity we find that modern shadow bank capital structure choices across the size distribution resemble those of pre-deposit-insurance banks both in

the U.S. and Germany, suggesting that the differences in capital structure of modern banks and shadow banks are at least partly due to banks' ability to access insured deposits. We rationalize these facts within a calibrated quantitative equilibrium model of intermediation. Using shadow bank data allows us to calibrate to moments which are otherwise inferred from model assumptions. We find that safety nets are responsible for lowering bank capitalization by at least 25%. The effect of deposit related safety nets is largest (almost double) for small banks and is negligible for the largest banks. The main contributor to high leverage of large banks is their ability to produce money-like deposits, whereas for smaller banks it is the access to safety nets embedded in the insured deposit funding. The aggregate consequences of the absence of safety nets provided by insured deposits are limited, because of reallocation from smaller banks to large banks and to shadow banks that can accomplish a lot of lending with substantially smaller leverage.

Acknowledgements and Disclosures

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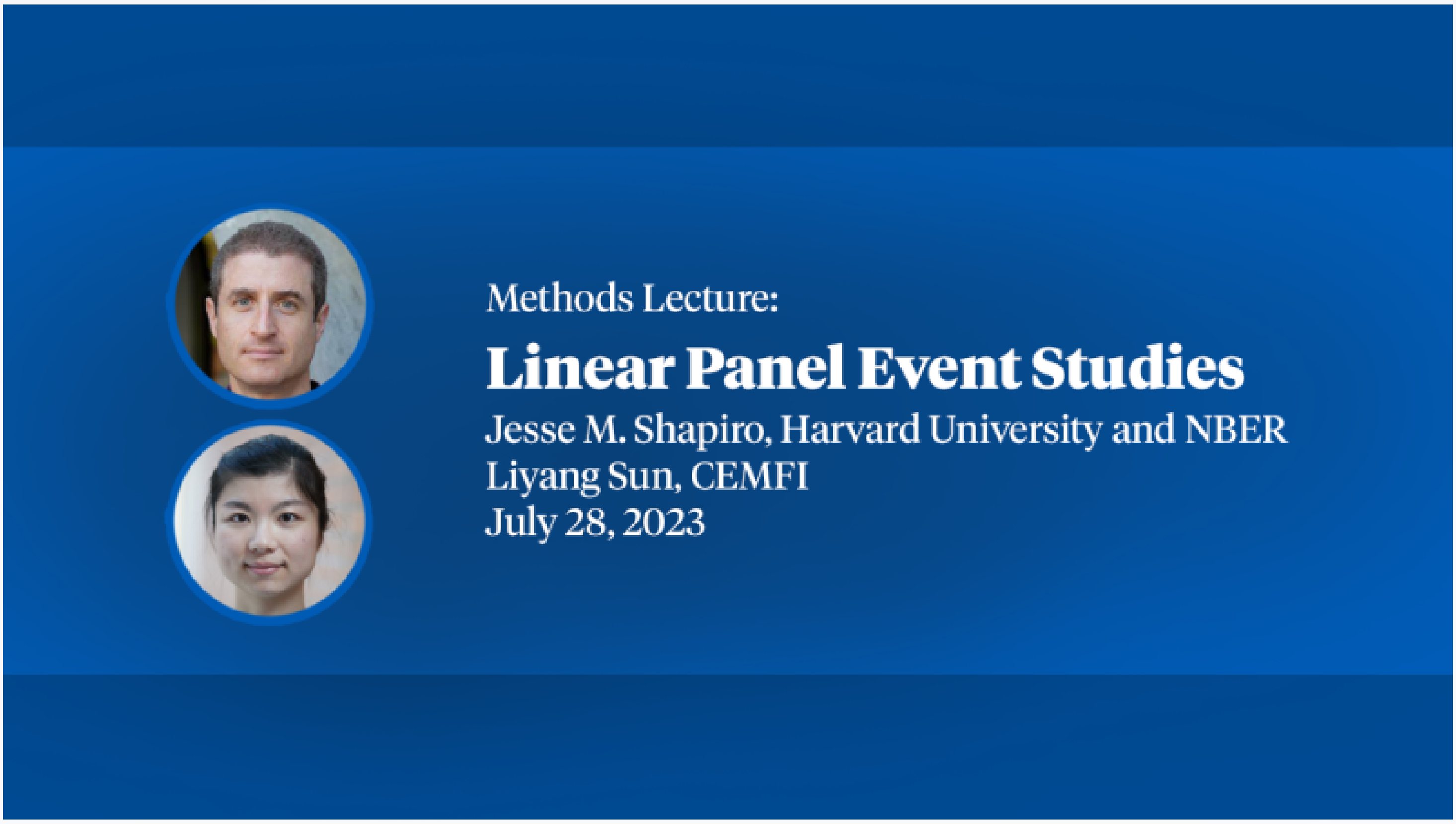

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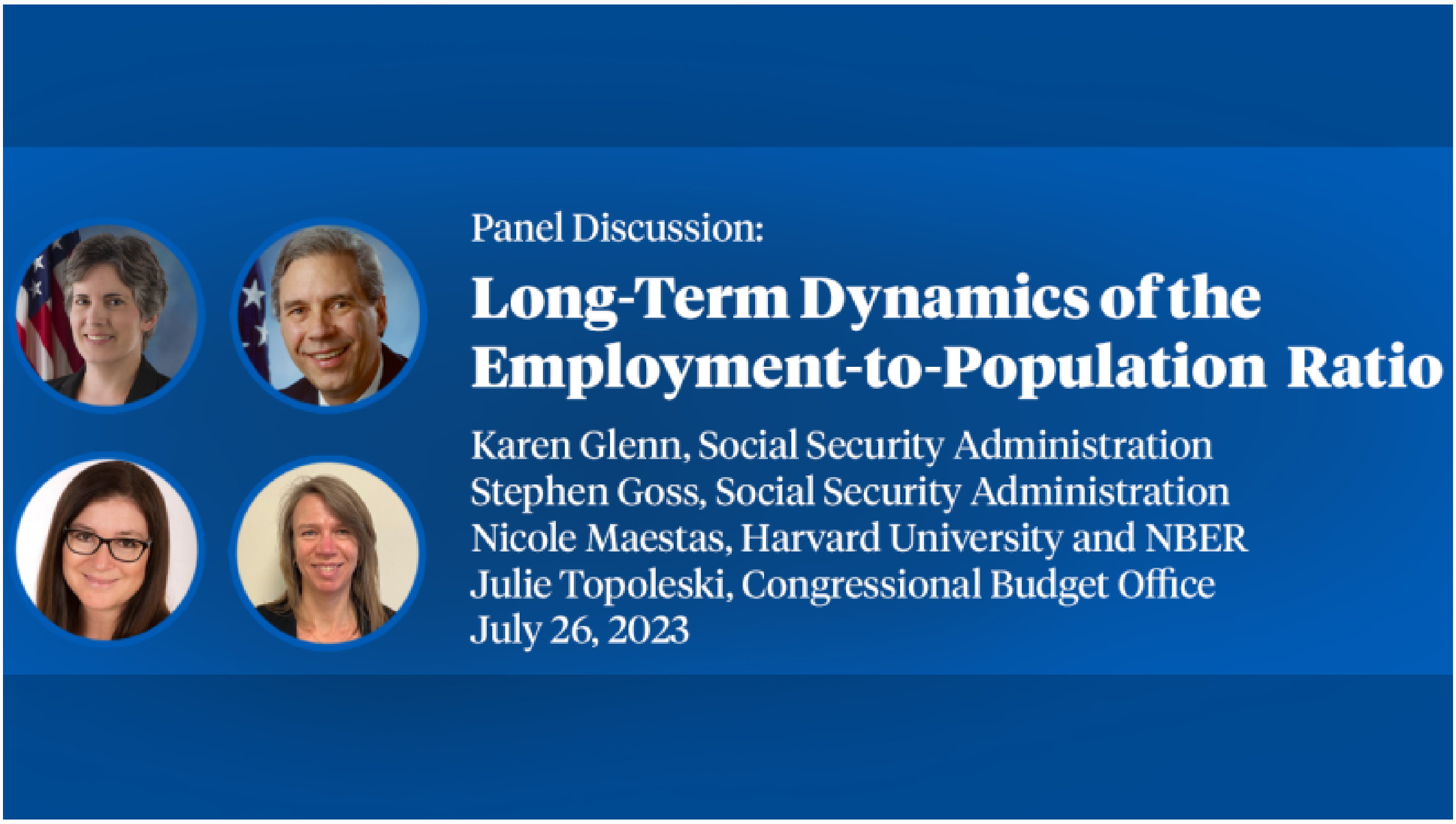

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