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Countercyclical capital buffers: credit-to-GDP ratio versus credit growth

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Abstract

This article provides a comparative analysis of the performance of the credit growth variable compared to the credit-to-GDP ratio as an early warning indicator of banking crises. We find that both variables correctly detect expansive credit growth leading to financial stability problems. However, the timing of the early warning indicators is closer in keeping with cycle changes when the credit growth variable is used. The results obtained are important to design prudential policies aimed at preventively monitoring and fostering banking sector stability and, particularly to manage the countercyclical capital buffer envisaged in the Basel III package.

Keywords:

- financial stability
- credit procyclicality
- countercyclical capital buffers
- Basel III

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Notes

¹ Drehmann and Gambacorta ([2012](#)) simulate the effects of this countercyclical capital buffer in the bank credit supply.

² This article sets out the results for α , typical value used for annual data. On the other hand, we have tested the resilience of the results for alternative values of α taking into consideration the research of Drehmann et al. ([2010](#)), Borio and Drehmann ([2009](#)), Maravall and Del Río ([2007](#)), Ravn and Uhlig ([2002](#)) and Gourinchas et al. ([2001](#)). Thus, for all the verified α values ($\alpha \in [0, 1]$), results obtained are consistent with those presented.

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