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The Drivers of Foreign Bank Lending in Central and Eastern Europe: The Roles of Parent, Subsidiary and Host Market Traits[1]

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Abstract: We analyze the relative roles of subsidiary and parent banking group traits in driving foreign banks' lending patterns in the Central and Eastern European (CEE) region before and during the crisis. We use a bank-level dataset on Western European banking groups and their CEE subsidiaries over the 2002-2013 period. We find that lower capital-to-asset ratios and higher non-performing loans (NPL) ratios at either the subsidiary or the parent bank level significantly lowered subsidiary lending growth before and during the crisis. The onset of the crisis not only lowered subsidiary lending growth in the CEE countries, but also has altered the relationship between balance sheet conditions and lending growth. However, we also find strong evidence that this crisis effect is significantly less pronounced for subsidiaries participating in the Vienna Initiative. Our results' policy implications include purging banks of NPLs, enhanced regulatory coordination and the inclusion of parent bank traits in countercyclical capital buffer calculations.

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