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Michael Diemer*

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Abstract

In the aftermath of the recent financial crisis, several countries implemented a bank levy. This paper studies the impact of different types of bank levies on the risk-taking behaviour of banks competing in the market for secured or unsecured debt à la Hotelling. We differentiate between three types of bank levies: a levy on secured liabilities, a levy on unsecured liabilities and a levy on risk-weighted assets. Banks collect funds and invest in either a prudent or a gambling asset. We find that a levy on secured and unsecured liabilities can prevent banks from investing in the gambling asset. A levy on risk-weighted assets also induces banks to behave more prudent. Such a levy is even more effective than a levy on liabilities if banks are well capitalized. Finally, a guarantee on debt makes a bank levy more effective.

Keywords: Bank levy, competition, moral hazard, transparency

JEL classification: D82, G21, G28

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