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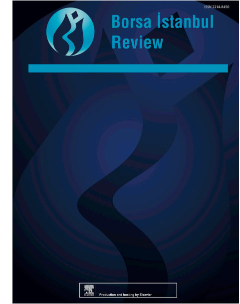

Deposit Insurance and the Banking Industry Stability in ASEAN: Evidence from a Dynamic Panel Investigation

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Abstract

The banking industry is the main agent of financial development in an economy, due to its critical function of circulating money from a surplus to a deficit. The aim of this paper is to investigate the influence of deposit insurance policy on the stability of the banking industry. Stability is measured by the ratio of retail deposit to total asset and the ratio of loan/total asset to cover both positive and negative influence, and deposit insurance policy is assessed in various stages. The survey uses a data panel of 127 commercial banks from 2000 to 2013 in ASEAN consisting of Indonesia, Malaysia, Singapore, the Philippines, Thailand and Vietnam. Through dynamic panel data investigation, the results attained show that the implementation of deposit insurance policy negatively influences the ratio of retail deposit to total asset while positively influencing the ratio of loan/total asset. This is an important finding, as it implies that the deposit insurance policy causes the banking manager to take higher risks to increase their return, rather than the deposit insurance policy which will increase the confidence level of depositors and finally increase the total deposit. This result is very important for the regulators to evaluate the deposit insurance policy and anticipate any negative circumstances which will be incurred.

JEL: *G21, E58*
Keywords: Deposit Insurance, Banking Stability and GMM

I. Introduction

Financial crises during 1997 and 2008 provided valuable lessons for the banking industry and banking regulators in ASEAN region about the safety of retail depositor's money and trustworthiness of financial market problems. This problem brings about systemic risk when the regulator cannot properly control the market and the financial crisis become deeper. To avoid systemic risk, since the end of twentieth century, banking regulators have proposed a deposit insurance program, implemented from 2000-2005, wherein the banking sector insures deposits from customers. The program is not new for banking industry in United States, as it had already been in use in the early years of 1800s as mentioned by Calomiris and White (1994).

Academics, practitioners and regulators have been discussing this program for as long as it has existed, with the concentration of their discussion focusing on the benefits and costs of deposit insurance. Despite the U.S banking system having employed deposit insure for

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