Bank size and market value:The role of direct monitoring and delegation costs

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PII: S0378-4266(18)30116-X
DOI: 10.1016/j.jbankfin.2018.05.016
Reference: JBF 5358

To appear in: *Journal of Banking and Finance*

Received date: 17 September 2017
Revised date: 13 April 2018
Accepted date: 23 May 2018

Please cite this article as: Panagiotis Avramidis , Christos Cabolis , Konstantinos Serfes , Bank size and market value:The role of direct monitoring and delegation costs, *Journal of Banking and Finance* (2018), doi: 10.1016/j.jbankfin.2018.05.016

Bank size and market value:The role of direct monitoring and delegation costs[1]

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Abstract

Recent studies have presented evidence of scale economies for large banks, providing a rationale for some very large banks seen worldwide. In this study, we focus on the negative side of bank size which relates to monitoring costs. In particular, we show that the relationship between size and bank's market to book value of assets is contained by the cost of the manager to directly monitor the borrowers and by the (delegation) cost of the owner to monitor the bank manager. Using a sample of US bank holding companies from 2001 to 2015, we provide evidence that the relationship between size and bank's market to book value of assets is inverse U-shaped and that monitoring costs offset the benefits from economies of scale.

KEYWORDS: Bank Size, Market Value, Asymmetric Information, Monitoring
JEL classification: G21, G32, L25

[1] We would like to thank Mitchell Berlin, Manthos Dellis, Iftekar Hasan, Robert M. Hunt, Beverley Lennox, Philip Molyneux, Fotis Pasiouras, George Pennacchi, Aris Stouraitis, Nickolaos Travlos, Pavlos Vlachos and the seminar participants at EFMA 2016, IMAEF 2016 and the HKBU International Corporate Governance Conference 2016 for helpful comments and suggestions.
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