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Title: The Quest for Banking Stability in the Euro Area: The Role of Government Interventions

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The Quest for Banking Stability in the Euro Area: The Role of Government Interventions

Highlights

i) Government interventions in the European banking sector deteriorate sovereign credit risk.

ii) Riskier sovereign debt depresses the collateral value of loans and leads to bank retrenchment.

iii) A regime-dependent relation between the banking sector and sovereign credit risk is revealed.

iv) A positive and regime-dependent relation between implied volatility and CDS spreads is identified.

v) A negative and regime-dependent relation between stock returns and CDS spreads is obtained.