Empirical evidence on "Systemic as a Herd": The case of Japanese Regional Banks

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Abstract

We examine a sample of Japanese regional banks and explore whether exposure to market risk factors affects systemic risk through a banks' portfolio composition or revenue source, using Adrian and Brunnermeier's (2016) CoVaR to proxy for systemic risk. We find evidence of "systemic as a herd" behavior among Japanese regional banks, as portfolio and revenue components associated with market activities exert positive and significant impacts on systemic risk by generating higher comovement among banks, even though they reduce standalone bank risk through portfolio diversification. Further, the marginal effect of an increase in a given banks' market-related components on systemic risk is larger when the share of the corresponding components is already high among other banks. Our results have important implications from the macro-prudential perspective.