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"Loan Portfolio and Stock Price Correlations in the Banking System of Japan"

Abstracts:

We analyse loan portfolio correlations (from the credit market) and stock return correlations (from the stock market) in the banking system of Japan. We observe that in the different markets, the correlations can have different structures and temporal dynamics.

In addition, our results show that although there is a certain degree of persistency, the interactions among banks in each market also evolve over time. Typically, when the dominance of a group of banks in one period vanishes, banks in another group will become the main actors in the backbone of cross-correlations in the next period.

Furthermore, we find that the correlations in each market are mainly driven by a global common factor and a couple of "groups" factors. After filtering out the effects of the global common factor, we further explore the determinants of non-systematic correlations by utilizing the characteristics and the balance sheet information of banks. We find that this bank specific information can only partially explain the residual correlations.