Bank sectoral concentration and (systemic) risk: Evidence from a worldwide sample of banks*

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Abstract

We propose a new stock return-based methodology to measure banks' sectoral specialization, sectoral herding, and financial sector exposure. Using these measures for a broad cross-section of banks and countries over the period 2002 to 2012, this paper is the first to empirically gauge both the short- and long run relationship between banks' sectoral concentration and banks' performance and stability. We find that (i) sectoral concentration has only a weak (or even no) impact on banks' valuation; (ii) bank volatility and systemic risk exposure decrease with banks' sectoral specialization and banks' sectoral herding, and increase with banks' financial sector exposure; (iii) these effects are significantly stronger in the long run than in the short-run; and (iv) there exists important time and cross-country variation in these relationships.

Keywords: bank concentration, sectoral specialization, herding, bank risk, systemic stability, factor model

JEL classification: G01, G21, G28, L5

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