# An International Forensic Perspective of the Determinants of Banks' CDS spreads

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**Abstract**

*In this paper, we provide a forensic perspective of the determinants of banks' CDS spreads. Using data for 118 banks of 30 countries over the period 2004-2011, we find that banks' default risk typically reflects: (i) the quality of the banks' balance sheet; (ii) liquidity of banks' assets; (iii) how profitable banks' operations are; (iv) the banks' leverage ratios; and (v) how stringent/lenient regulatory capital ratios are. Considering a series of indicators of the financial structure of the banking system, our results reveal that: (i) higher concentration of the banking sector, stronger presence of foreign banks and a deterioration of the health of the banking sector lead to higher banks' CDS spreads; and (ii) the availability of alternative means of finance does not significantly influence banks' default risk. We also show that periods of high inflation, low GDP growth and stock market crashes are prone to an intensification of tensions in the banking system, but financial reforms (especially, in the field of banking supervision and privatizations) can mitigate them. Moreover, the timing, the duration and the composition of fiscal consolidation programs have a significant impact on banks' CDS spreads, and, in particular, expenditure-driven consolidation episodes are associated with a rise in banks' default risk. Finally, we highlight that although the financial crisis of 2008-2009 was a global event, higher quality of economic and legal institutions (and, therefore, in the regulatory framework) could have dampened the rise in bank' CDS spreads.*

Keywords: Bank CDS, leverage, capital requirements, liquidity, macroeconomic-, political- and institutional-factors, financial reforms, financial structure, fiscal consolidation.
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