

# Bank Organization, Market Structure and Risk Taking: Theory and Evidence from U.S. Commercial Banks

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## Abstract

This paper examines (1) the change in commercial banks' risk taking as states in the United States removed restrictions on bank branching within state borders and (2) the channels through which the removal of these restrictions affects bank risk taking. I find that, after the liberalization of branching restrictions, banks that do not expand their branch network into other markets decrease risk taking, while expanding banks do not change risk taking. Existing theories, which focus on the importance of market structure on risk taking, are not able to explain this pattern. Therefore I provide a theoretical framework, building on theories from organizational economics, which can account for this by showing that non-expanding banks have a comparative advantage in lending to informationally difficult borrowers, which induces them to lower risk taking as competitors expand. Empirical evidence supports this channel and highlights the importance of borrower information, since non-expanding banks decrease risk taking more as competitors expand if they operate in a county with more informationally difficult borrowers.

**Keywords:** Bank Risk, Market Structure, Organization, Regulation

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