Why Did Bank Lending Rates Diverge From Policy Rates After The Financial Crisis?

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**Paper Abstract:** The global finance crisis prompted central banks in many countries to cut short-term policy rates to near zero levels. Yet, lending rates did not fall as much as the decline in policy rates would have suggested. We argue that comparing lending rates to policy rates is misleading: banks do not obtain all their funds at policy rates, and after the crisis, costs of funding rose substantially. Comparing lending rates with a weighted average cost of funds suggests that banks did not substantially change their rate setting behaviour after the financial crisis: interest rate pass-through relationships across eleven countries in Europe appear to have remained stable.