



Common Themes?

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1. John and Kadiyala: How distress is resolved affects debt capacity and debt structure: Changes in bankruptcy codes are used to identify a bankruptcy law effect.
2. Korte: Failure resolution policies have real effects. Swift and certain resolution is promotes real growth. Cross country differences in resolution rules are used to identify the real effects of resolution policies
3. Chu: Do book value based capital requirement lead to cherry picking? Bank liquidity and capital ratios are used to identify cherry picking an fire sales

Debt Restructure and Bankruptcy Law

- Question: How do changes in bankruptcy laws affect leverage and the structure of debt claims?
- Empirical approach: “Quasi” diff in diff using changes in bankruptcy laws in 11 to identify the effect of bankruptcy laws on leverage and use of bank debt

Theory

- The rules of the game in bankruptcy determine the reservation prices associated with private debt restructuring (what you get in bankruptcy less the cost of delay).
- The limit on renegotiable bank loans is the value of collateral less the dead weight costs of collateral transfer.
- The value of tax shields can be increased by the use of additional subordinated “non-negotiable” public claims.
- However, hold out, information and free rider problems may lead to inefficient liquidations and dead weight costs of distress... leading to less debt capacity (inefficient liquidation).

Hypotheses

- Bankruptcy rules that strengthen creditor rights in bankruptcy increase firm debt capacity.
 - Greater creditor rights decrease loss given default
- Bankruptcy rules that make private work out easier increase debt capacity and increase bank lending capacity.
 - DIP financing
 - Pre-packs
 - Exclusivity rules
 - Cram downs
 - Super Majority rules (minimize holdout problems)

Comments

- Not clear that there is a distinction between creditor rights and renegotiation incentives. Creditor rights correspond to secured creditor rights that directly affect unsecured creditors incentives grant concessions
- Quote from Anguist: 11 countries...a China effect?
- Quasi “Diff in Diff” no firm fixed effects

Catharsis In the Financial Sector

- Basic idea: Soft resolution policies promote bad (zombie) lending (risky negative NPV projects) which hampers economic growth. Offsetting this may be ex-post efficiency gains.
- Catharsis indicator:
Failed bank assets resolved/Bank assets that should be resolved

Comments

- First order importance? Effect is likely to vary with economic conditions and state of the banking sector. 1.8% to 2.3% difference in growth rates seems like a large impact. Does strong economic growth lead to more cathartic policies?
- Order of magnitude difference in “Catharsis effect” when firm and year fixed effect are added.
- If “Catharsis is important why is bank undercapitalization positively related to growth?

Asset Fire Sales or Cherry Picking

- Basic idea: Liquidity needs may create needs for quick sales thus fire sale discounts. Book value based capital requirements may lead to selling winners and holding losers.
- Are commercial property sales prices/Time on the market related to the selling banks liquidity and capital needs.
- Empirical challenge: Finding good controls for property quality.
 - The fact that REO properties sell at lower prices isn't surprising... the borrower could sell the property to repay the loan and income from the property could service the loan.