The Effects of Informational Frictions on Credit Reallocation (*O. Darmouni*)

Some Borrowers are More Equal than Others: Bank Funding Shocks and Credit Reallocation (*De Jonghe, Dewachter, Mulier, Ongena, and Schepens*)

Information Sharing and Lender Scope: Evidence from the U.S. Commercial Lending Market (*Liberti, Sturgess, and Sutherland*)

Discussion by Giovanni Dell'Ariccia (*IMF* and *CEPR*)

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Background: Information asymmetries and lending

- **Lender-borrower (standard Stiglitz-Weiss framework)**
  - Hidden quality/action (Moral hazard/Adverse selection)
  - Backward bending credit supply curve: **Credit Rationing**
  - No direct implication for competition

- **Lender-lender (Broker, Sharpe, Dell'Ariccia-Marquez)**
  - Learning by lending: Relationship banking
  - Cherry-picking causes additional AS.: **Barriers to entry**
  - Lending margins depend on informational advantage
  - Competition might have paradoxical effects

The papers in this session (all very good)

- **All three papers deal with lender-lender informational asymmetries**
- **Different identification strategies**
  - First two papers use “liquidity” shocks to identify effects of information asymmetries on credit
  - Third paper focuses on what happens when banks choose to share private information
- **Same basic focus**
  - Look at the consequences of changes in adverse selection
- **Overall, they support theoretical predictions**
  - Although second paper a bit of a stretch

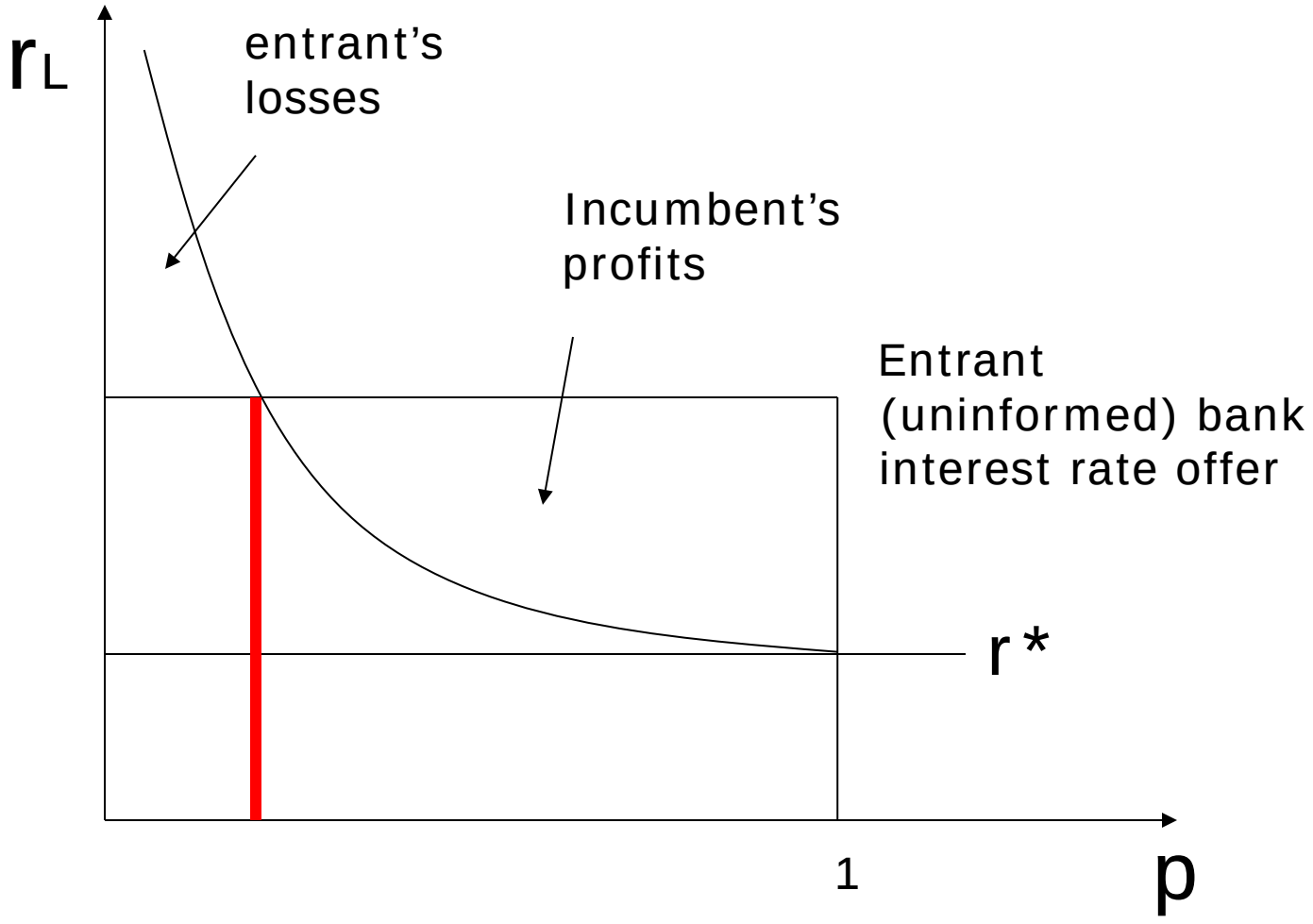
Competition under adverse selection

- Heterogeneous borrowers: prob. of success p
- Break-even if interest rate $r_L = r^*/p$
- Informed bank will match offers for worthy borrowers
- Without exogenous separations, uninformed bank can only make losses
- **Two main implications**:

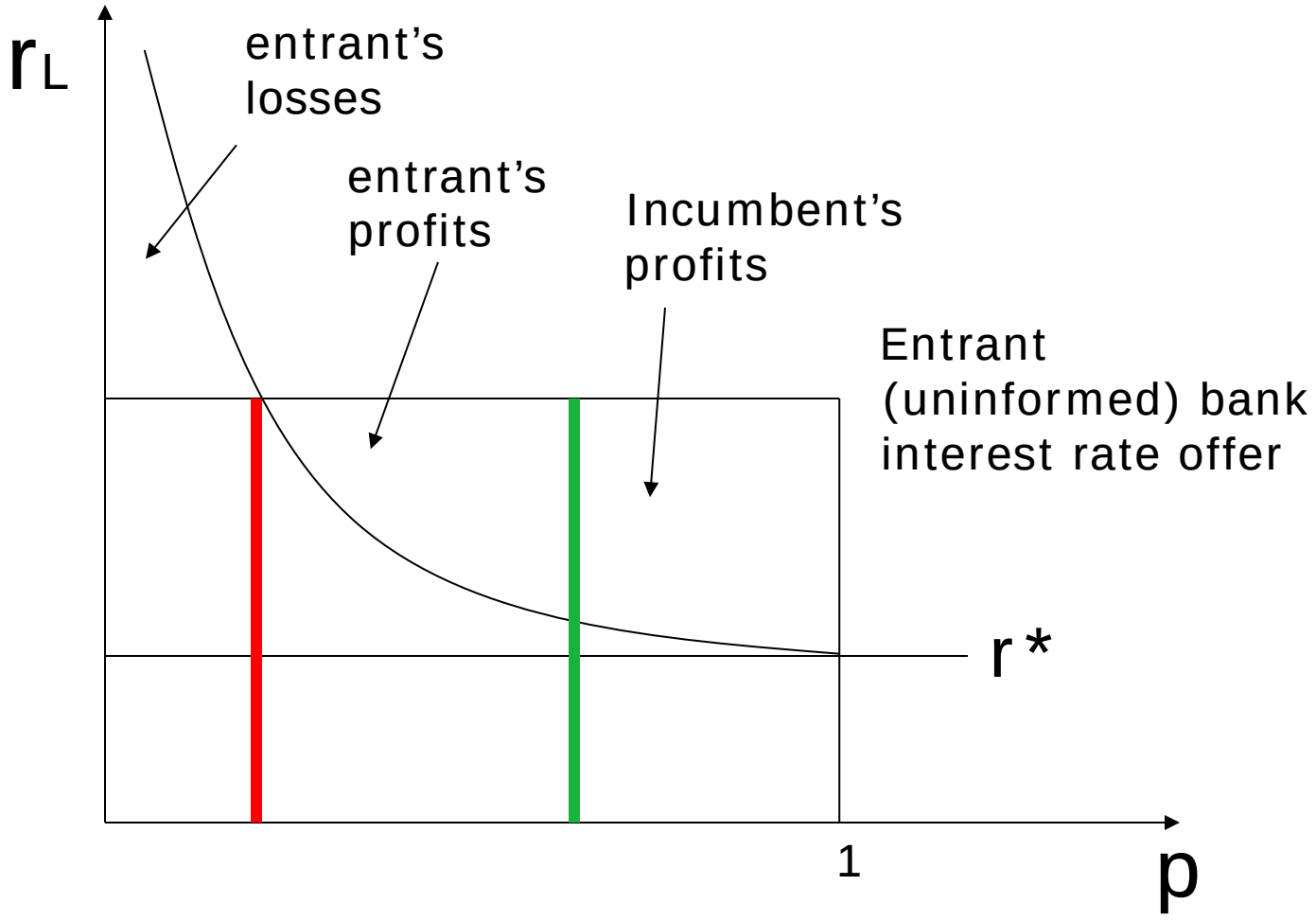
  1) *Informed bank makes more money on more opaque and better borrowers*

  2) *Larger exogenous separations reduce AS, lower barrier to entry*

A bank's lemon problem



Exogenous shock



Info frictions and credit reallocation (O. Darmouni)

- **Essentially a direct test of AS stemming from lender-lender informational asymmetries**
  - Adverse selection makes it difficult for borrowers to switch lenders
  - But when a lender cuts borrowers lose for exogenous reasons, adverse selection more limited
- **Focus on lending relationships around Lehman bankruptcy**
  - Borrowers with a pre-existing relationship with “more exposed” lenders found it relatively easier to establish new lending relationships.
  - Careful strategy to make sure this is not a Stiglitz-Weiss type effect
  - Syndicated loan data
- **Policy implication: *Help the borrowers not the banks***
  - Support for the most hit lenders may actually increase AS to the detriment of aggregate credit

Comments

- **Paper executed very carefully**
  - Lots of robustness tests
  - Results convincing
  - Reasonable economic magnitudes
- **Some concerns with exposure measure and data**
  - Some lenders may have more transparent borrowers, more churning, and these borrowers find it easier to get credit elsewhere
  - But alternative exposure measures (real estate, correlation with MBS, co-lending with Lehman) deliver similar results (perhaps rely on those)
  - Syndicated loan data most likely deliver smaller effect than other loans
- **Policy implications**
  - How much this depends on parameters?
  - Different result if you fully restore lender's health?
  - MH problems with direct subsidies

Some Borrowers are More Equal than Others (De Jonghe et al.)

- **How did Belgian banks adjust their portfolio after Lehman?**

- **Negative funding shock exogenous to portfolio allocation**

- **Banks retrench on:**
  - Sectors in which they have higher presence (market share)
  - Sectors with large share in their portfolio (specialization)
  - Safer firms (more collateral, lower debt)
  - Not necessarily firms with whom they had previous relationships

Comments

- **Another paper executed very carefully**
  - Very detail borrower-lender specific data
  - They can control for both firm and bank characteristics
  - Beyond syndicated loans
- **Concerns**
  - Does this really support information asymmetry across lenders view?
  - One has to stretch models a bit. More sectoral expertise than relationship banking
  - Retrench on sectors on which (by revealed preferences) a bank has comparative advantage
- **Policy implications**
  - Diversification does not help in crisis
  - But if a bank were fully concentrated on one sector it would be forced to cut there

Info sharing and lender specialization (Liberti/Sturgess/Sutherland)

- **Examine how information sharing affects lender specialization**
  - Data from voluntary sharing scheme (PayNet) on equipment finance
  - Nice. It allows to examine role of collateral expertise (see first paper)
- **After joining PayNet:**
  - Lenders expand geographically and by industrial sector
  - Increase portfolio diversification and reduce delinquency
  - Enter new collateral markets (related types, and types used by their borrowers)
  - **Results mostly driven by small lenders**
- **Info asymmetries imply mkt power and profits for incumbents. Then, why voluntarily share?**
  - Small banks: more to gain than to lose
  - Large banks? Expand into small-borrower/relationship lending
  - Borrowers: more relationships and greater access to credit

Comments

- **Another paper executed carefully**
  - Explore info asymmetries by looking at what happens when they are (partially) removed
  - Results support view that information can be a barrier to entry/expansion
  - Information on collateral markets new angle
- **Concerns**
  - Decision to join PayNet may be non random. Authors very careful with interpretation of results
  - Ideally, one would use lender characteristics, but lenders are anonymous (any way around this?)
- **Policy implications**
  - Information sharing increases diversification and credit for small lenders
  - Aggregate net effect less clear
  - Also what is the effect on profitability?
  - Support credit bureaus?