Self-fulfilling Credit Cycles

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Discussion by Patrick A. Pintus

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• As such this fact challenges the current literature that largely focuses on collateralized credit
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Natural interpretation: unsecured credit relies on borrower’s “reputation”
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- Simple model exhibits three steady states:
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  - a “middle” one with *inefficient* capital allocation
- When reputation is too low, credit constraint tightens: this results in capital misallocation
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- Intuition is crystal clear: dynamic complementarity

- If tomorrow’s credit limit expected to tighten, larger incentives to renege on debt that tightens today’s credit limit
Large-Firm Bias?

- Authors acknowledge that Compustat has a large-firm bias: public companies
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- Would be great to look at data samples with larger firm coverage (French data?)
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- Paper provides a neat model of unsecured credit: quid of extension to labor misallocation?
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- Idea is: slightly lower credit means no quantity first-order effect on welfare and lower interest rate
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- Difference with Azariadis-Kaas-Wen: non-monotonic map
- Azariadis-Kaas-Wen show that sunspot-driven credit cycles do not necessarily rest on such intuition when the credit market allows capital reallocation (they have a monotonic map)
- In addition, their richer model predicts that unsecured credit is volatile and correlate with business output as in US data