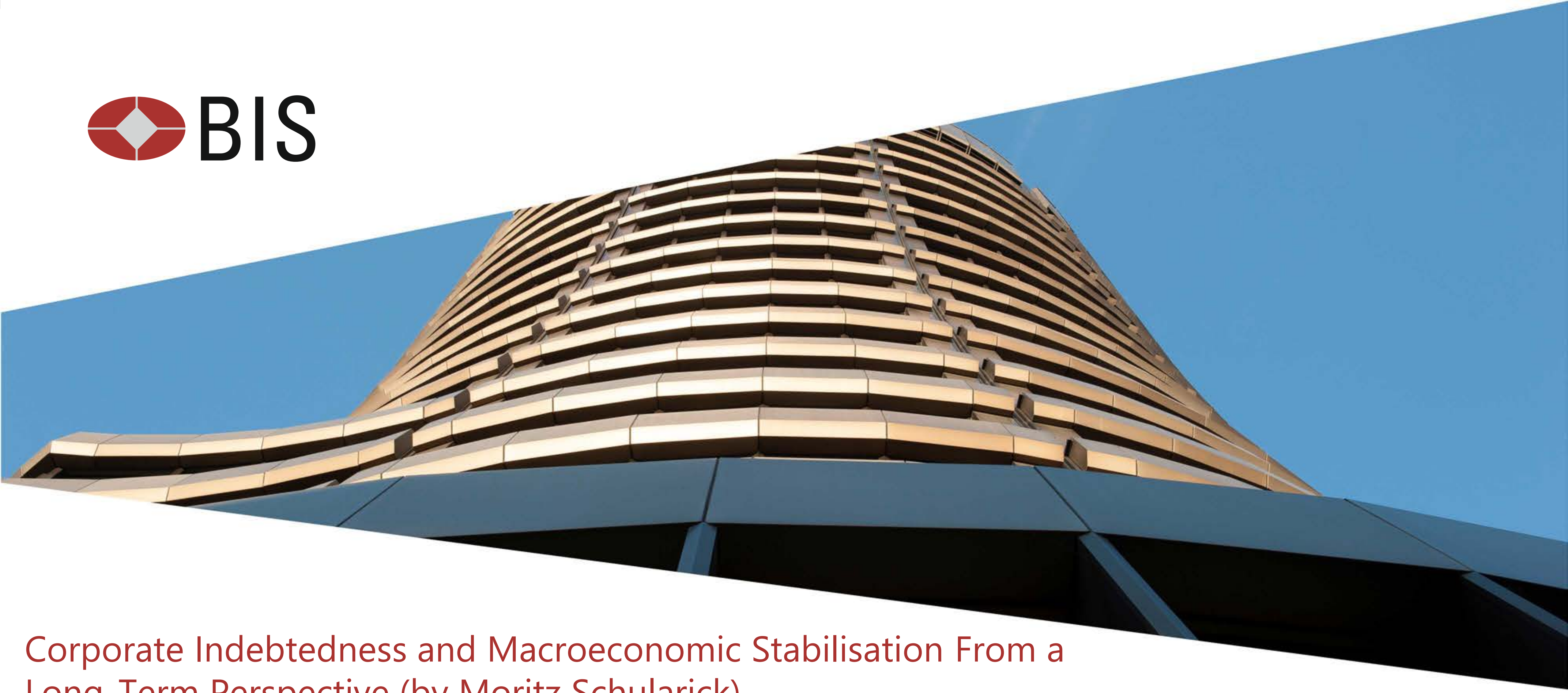
BIS



Corporate Indebtedness and Macroeconomic Stabilisation From a Long-Term Perspective (by Moritz Schularick)

ECB Forum on Monetary Policy, 28-29 September 2021 (online event)

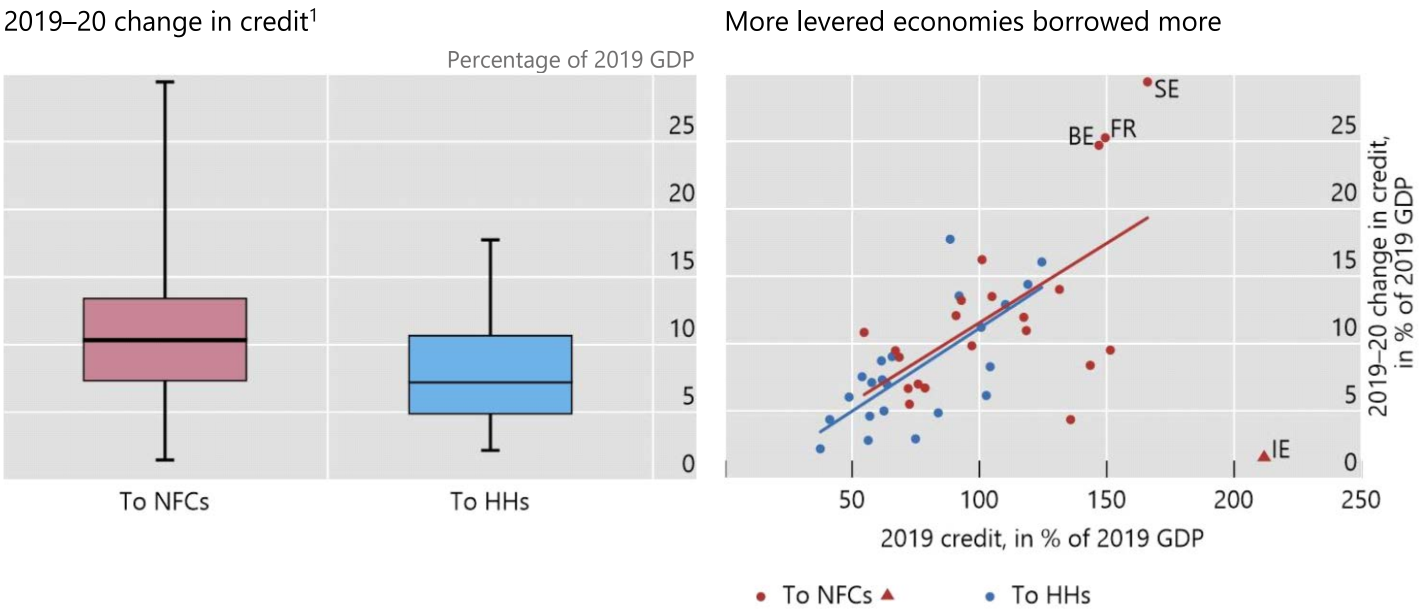
Discussion by Egon Zakrajšek*

*The views expressed are my own and do not necessarily reflect the views of the Bank for International Settlements.

Introduction

- Corporate debt levels have risen substantially before the pandemic.
- Pandemic has led to a further significant increase in corporate debt.
- How concerned should you be?

Corporate and household indebtedness during the pandemic



The sample includes AT, AU, BE, CA, CH, DE, DK, EA, ES, FI, FR, GB, GR, IE, IT, JP, NL, NO, NZ, PT, SE and US.

[1] The box plots show the minimum, the 25th percentile, the median, the 75th percentile and the maximum.

Sources: BIS; author's calculations.

Not too much, according to Moritz … Why?

- 150 years of macro-financial history for 17 advanced economies:
  - Unlike household debt booms, corporate debt booms do not influence post-peak GDP dynamics.
    - corporate debt booms are not followed by deeper recessions or weaker and more sluggish recoveries (Jordà, Kornejew, Schularick & Taylor 2021).

- With some important caveats:
  - Composition of corporate debt matters:
    - credit build-up in non-tradable goods sector is worrisome (Mueller & Verner, 2021)
  - Insolvency regimes must be efficient:
    - inefficient insolvency regimes prevent a quick restructuring of firms' balance sheets
  - Bank-centric financial systems tend to be more vulnerable (Greenspan, 1991; Gambacorta et al 2014):
    - banks' extend-and-pretend policies can lead to "zombie lending"

My discussion …

- Interesting, thought-provoking and timely paper.
  - Important enhancement of the JST *Macrohistory* data base – thank you!

- **Comment I**: "*History never repeats itself, but it often rhymes.*" <Mark Twain>

- **Comment II**: Fluctuations in credit quantities provide an incomplete account of credit cycles.

- **My view**: Current corporate debt build-up presents a material downside risk to economic outlook.

Comment I: How informative can history be about the Covid-19 fallout?

- Nature of the Covid-19 shock was unprecedented:
  - Strong supply-side dimensions due to economic/social restrictions.
    - initial shock confined to sectors linked to movements of people (i.e., air travel, tourism)
    - ultimately propagated to other sectors and global supply chains
  - Monetary and fiscal responses were unprecedented and ongoing.
  - Support programs were of broad scope and limited conditionality.

- Need an approach that captures firm-level heterogeneity (e.g., industry, size, financial condition …).

An important French case study

- In March 2020, the French parliament established an independent committee (chaired by B. Cœuré) to evaluate and monitor the financial support available to French companies during the Covid-19 crisis:
  - Firm-level information on take-up of credit-support schemes matched with balance sheet data.
  - Analysis based on 3.5 million French firms (employing 16.1 million people) that had recourse to the various credit-support schemes during the first two waves of the pandemic.

- Findings relevant to today's discussion:
  - Intensity take-up rate (support/turnover) was highest for financially weakest firms.
  - Share of the amount paid out to small businesses was higher than their share of employment.
  - Pre-crisis "zombies" did not make a disproportionate use of the credit-support schemes.

- Much more analysis – across different countries – is needed to ascertain the likely impact of corporate debt build-up on post-Covid macroeconomic dynamics.

Comment II: an integrated view of credit cycles

- Post-GFC research on credit cycles:
  - At low frequencies (i.e., 3-5 years), rapid credit growth presages economic downturns.

    (Schularick & Taylor, 2012; Jordà, Schularick & Taylor, 2013; Mian, Sufi & Verner, 2017)
  - "Sentiment" in credit markets also carries negative information about future economic growth, above and beyond that contained in credit aggregates.

    (López-Salido, Stein & Zakrajšek, 2017; Kirti, 2020)

- **Credit market sentiment**: variation over time in expected returns to bearing credit risk
  - Expected returns to bearing credit risk are "too low" ➔ credit is priced too aggressively

    (i.e., narrow credit spreads; a lot of high-yield bond issuance; easy lending standards)
  - Ex post, when investors are predictably disappointed ➔ abrupt and large revaluation of credit-related assets ➔ sharp pullback in the supply of credit ➔ recession

    (Bordalo, Gennaioli & Shleifer 2018; Greenwood, Hanson & Jin, 2019)

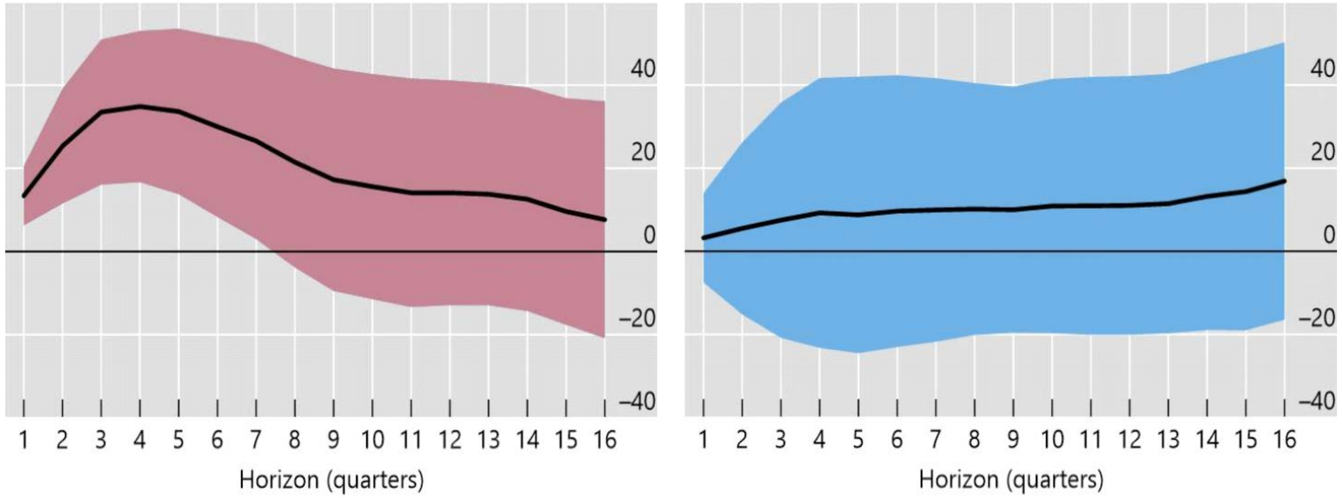
Do corporate credit booms lead to a reversal in credit market sentiment?

- Excess bond premium (EBP):
  - corporate bond credit spread net of default risk
  - natural interpretation as a measure of credit market sentiment
- Sharp and sudden reversal in sentiment for highly leveraged economies could be problematic.

Response of the excess bond premium

In basis points

Two standard deviation increase in Δ_5 [NFC/GDP]$_t$ — Two standard deviation increase in Δ_5 [HH/GDP]$_t$



/ 95% confidence interval

Sources: BIS; Board of Governors of the Federal Reserve System; author's calculations.