NANYANG TECHNOLOGICAL UNIVERSITY SINGAPORE

Discussion of

Loan Syndication Structures and Price Collusion

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Summary of Paper

- Developed a measure of lending expertise based on industry similarity in loan portfolios of lenders.
  - Close (distant) syndicates are those with high (low) levels of industry similarity in expertise among members.
- Hypothesize that lead arrangers trade-off benefits of a close syndicate (improved information production) versus costs of close syndicate (increased competition).

Overall

- Interesting paper with important implications
- Asked interesting questions
  - How to deal with your competitors? Collaborate with them or compete directly with them?
  - “Keep your friends close and your enemies closer” – Sun Tzu and Al Pacino in Godfather
  - Loan syndication is an ideal setting to study this question

#1: Clarification on institutional details

- When is the pricing of the loan determined? Is it in the first stage when banks bid to be the lead arranger or the second stage when the lead arranger invites other banks to join the syndicate and loan pricing is determined based on the book-running?
  - If it is the former, the loan pricing would be determined prior to the forming of the syndicate. Would syndicate similarity be determined by the loan pricing rather than loan pricing be a function of syndicate similarity?

#2: Participant banks' willingness to join

- The paper assumes that the lead-arranger determines the syndicate members but the syndicate is a result of both the lead-arranger's actions as well as syndicate members' willingness to join the syndicate.
  - Presumably, syndicate members would only be willing to join if the costs of monitoring is lower than the benefits.
  - In this case, we would see members who are experts in the borrower's industry more willing to join a syndicate with larger loan commitments. Or where the borrower is easier to evaluate.

    ➔ We would then see smaller, more concentrated syndicates which are highly similar in expertise.

#3: Hypothesis

- The assumption is that syndicates where participant lenders are highly similar “have lower production costs to produce borrower-specific information.”
  - Why? If all members are highly similar but they are lending to an unfamiliar borrower (outside their expertise), would there still be lower production costs?
  - Perhaps draw on diversity literature?
    - Highly similar syndicates may improve efficiency of decision making because of better coordination/ communication but may have worse access to information especially in complex situations.
    - Would load syndication structure differ depending on type of borrowers or loan complexity?

	Syndicate Distance		
	Close	Mid	Distant
	(1)	(2)	(3)
Borrower characteristics:			
Public borrower indicator	0.359	0.406	0.306
Debt rating indicator	0.627	0.667	0.521
Investment-grade rating indicator	0.325	0.373	0.252
# of previous syndicated loans	4.907	5.383	3.502
First borrower loan indicator	0.299	0.281	0.418
Sales at closing ($mm)	3,893	4,921	3,025

- If closer syndicates are better at producing information, we should observe those borrowers with higher monitoring needs to be associated with closer syndicates.
- The pricing hypothesis are all based on the assumption that close syndicates are better at producing information.

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    - Highly similar syndicates may improve efficiency of decision making because of better coordination/ communication but may have worse access to information especially in complex situations.
- What about free-rider issues?
  - The lead-arranger and perhaps the co-agents monitor, should we expect the other participant banks to also monitor and participate in information production? If not, would the similarity of other participant banks to the lead arranger matter?
- What about the costs of having similar syndicates? More should be discussed about the costs, otherwise, why would highly dissimilar syndicates exist?
  - Exclude competitors? Should be included in theoretical framework section

#4: Lending Expertise

- Developed a measure of lending expertise based on industry similarity in loan portfolio in the prior twelve months
  - Banks who lend to same industries are more similar

$$distance_{s,k,t} = \frac{1}{\sqrt{2}}\sqrt{\sum_{j=1}^{J}(w_{s,j,t} - w_{k,j,t})^2}$$

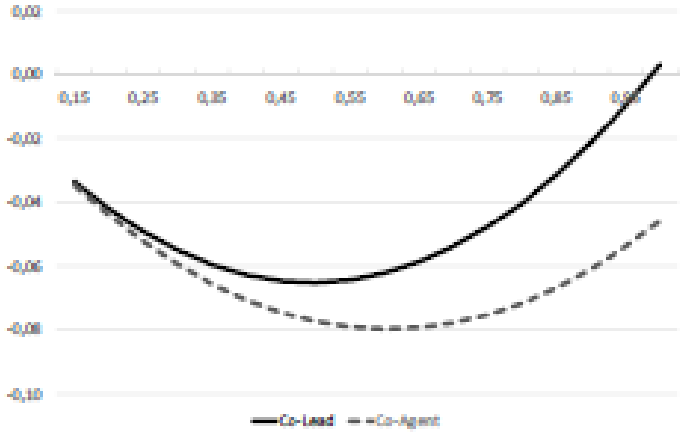
- More discussion on the industry expertise measure would be useful
  - Are these weights stable? Is the distance between two banks stable?
  - The biggest lead arrangers are banks such as BOA, JP Morgan Chase, Wells Fargo – probably have (equal?) expertise in all industries. How meaningful then is a distance measure when measured vis-à-vis these big lenders?
- Implicit assumption is that banks who are more similar in terms of their borrowers' industry are direct competitors.

#5: Two-dimensional lending expertise measure

- Banks compete not only in terms of the industry they lend to but also regionally.
- Would it make sense to construct a two-dimensional lending expertise measure based on industry and regional expertise?
- A regional expertise measure would be useful.
  - Might even be able to use the Interstate Banking and Branching Efficiency Act (IBBEA) in 1994 that legalizes interstate branching as a natural experiment or use the pre-IBBEA loan portfolio as an instrument for current expertise.

#6: Who gets the more senior roles?

- Average number of lead arranger is 1.55.
- Who determines the number of lead-arranger? Do they co-bid on the loans in the first stage?
- Interesting that the more distant banks are likely to be appointed co-leads
  - Paper argues that this is consistent with the lead arranger avoiding competition for future loans from the borrower.
  - Is this sustainable in a repeated game framework? Are you creating more competitors instead?



(a) Distance from Lead Arranger and Syndicate Membership: Co-Lead and Co-Agents

#7: Syndicate size versus Syndicate similarity

- Close syndicates tend to be smaller (Table 3).
  - Which one is of first order impact?
  - Do lead-arranger decide on the size first or the similarity in expertise first?
  - Would the results on loan pricing apply if we change lending expertise to syndicate size?

Other Quibbles

- Do banks re-contract with each other repeatedly over multiple deals?
  - Are these banks close in expertise?
- Do you delete the loans with only 1 lender?
- Are there any bias introduced when you restrict the sample to large lead arrangers?

In summary

- Enjoyed reading the paper.
- Learnt a lot from it.
- All the best for the paper!