

Personal Web

Beyond Financial Intermediation: Common Lender Monitoring as a Substitute for Supply Contract Covenants

Ting Dai, CFA CPA

Department of Accounting, Hong Kong University of Science and Technology



香港科技大學
THE HONG KONG
UNIVERSITY OF SCIENCE
AND TECHNOLOGY

Research Question and Findings

RQ: Whether the common lender's monitoring can substitute the covenants between their clients in the same supply chain?

Findings: Common Lender Effect

- Less supply contracts covenants ↓
- Longer trade credit and More likely to cite customers' patents ↑
- Effect Varies with hold-up risks and communication challenges △

Highlight the critical role of banks **Beyond** traditional functions:

- Reducing contracting frictions
- Enhancing supply chain efficiency

Main Result: The Common Lender Effect

Less supply contracts covenants ↓

Dep. Var =	Sales Audit Cov.		Product Quality Cov.	
Common Lender	-0.090** (-2.44)	-0.103** (-2.32)	-0.147** (-2.56)	-0.166** (-2.51)
Customer Standalone Banked	No	Yes	No	Yes
Supplier Standalone Banked	No	Yes	No	Yes
Controls, FEs	Yes	Yes	Yes	Yes
N	1,157	1,157	1,157	1,157
Adj. R ²	0.24	0.24	0.31	0.31

*Contract, Supplier, Customer Chars controlled; Year, Paired Industry, Paired State FEs included

Mechanisms: Through the supplier's loan capital covenants monitoring

Dep. Var =	Sales Audit Cov.		Product Quality Cov.	
Avg C-Cov×Common Lender	-0.100* (-1.78)		-0.305*** (-3.21)	
Avg P-Cov×Common Lender		-0.023 (-0.50)		-0.049 (-0.94)
Common Lender	-0.044 (-1.05)	-0.053 (-1.01)	-0.113** (-2.20)	-0.141** (-2.30)
Controls, FEs	Yes	Yes	Yes	Yes
N	1,157	1,157	1,157	1,157
Adj. R ²	0.16	0.16	0.30	0.29

*Contract, Supplier, Customer Chars controlled; Year, Paired Industry FEs included

Cross-Sectional Tests and Benefits

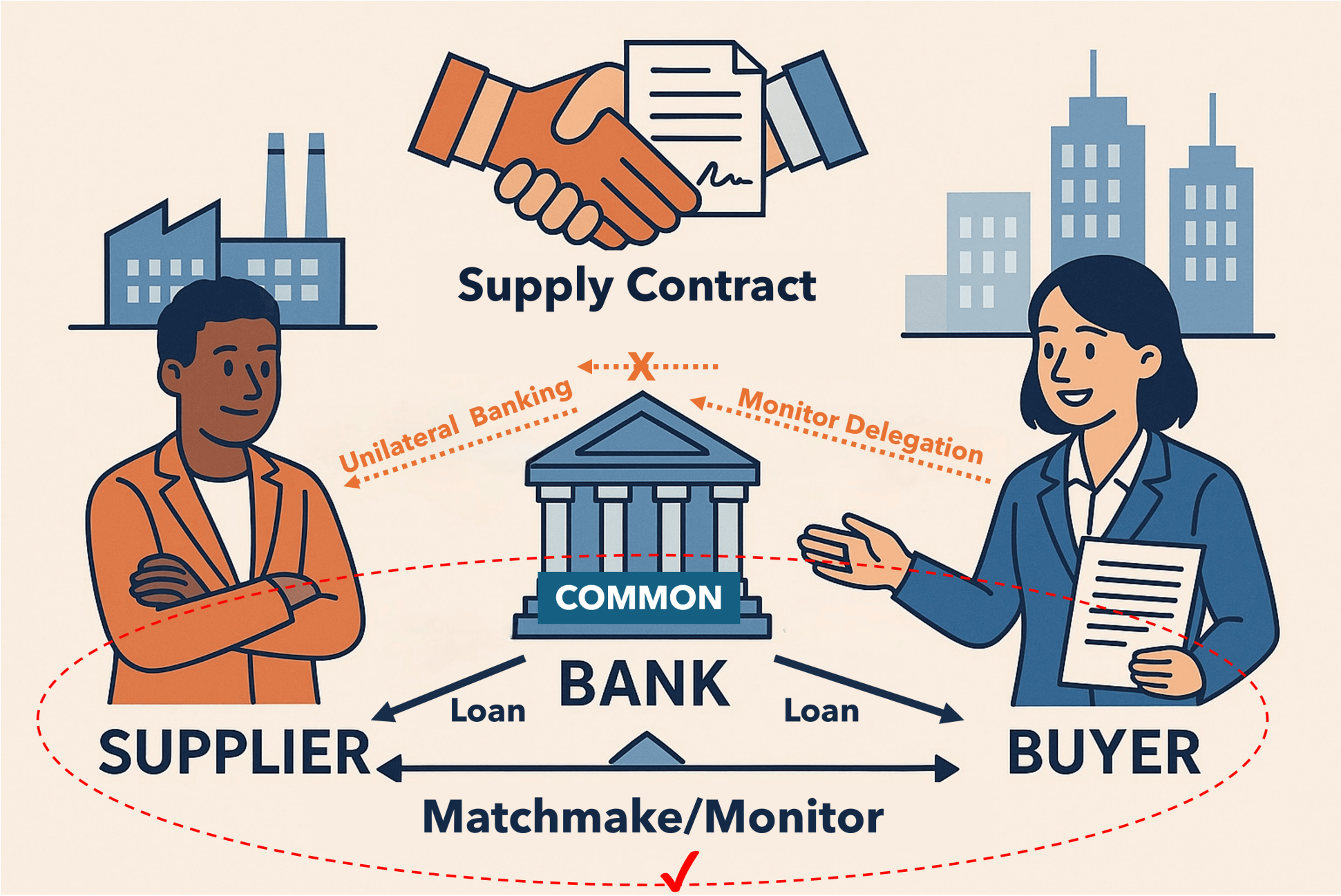
- Significantly stronger when facing severe hold-up risks
- Enhance trust when communications are impaired.
- Longer Trade Credit and More Cross Citations ↑

Panel A: Contract Sample			Trade Credit	
Supsample:	Supply	Origination	Whole Sample	
Common Lender	18.323*** (4.57)	12.726*** (3.16)	5.352 (1.43)	
Controls,FEs	Yes	Yes	Yes	
N	312	344	588	
Adj. R ²	0.83	0.55	0.58	
Panel B: Pair-Year Sample			Cross Cite _{t+1}	Cross Cite _{t+2}
Common Lender		0.163*** (3.49)	0.160** (3.27)	
Controls, FEs		Yes	Yes	
N		311,984	311,984	
Pseudo R ²		0.43	0.44	

*Panel A: Contract, Supplier, Customer Chars controlled; Year, Paired Firm FEs included; Panel B: Contract, Supplier, Customer Chars controlled; Year, Supplier Firm FEs included

Motivations

- Monitoring supply contracts can be **Costly**.
- Common Lender:
 - (1) a monitoring **Specialist** to both ends of the supply chain
 - (2) has an incentive to protect the **Value** of the **Whole** supply chain.
 - (3) aim to be a **Value-added** service provider.

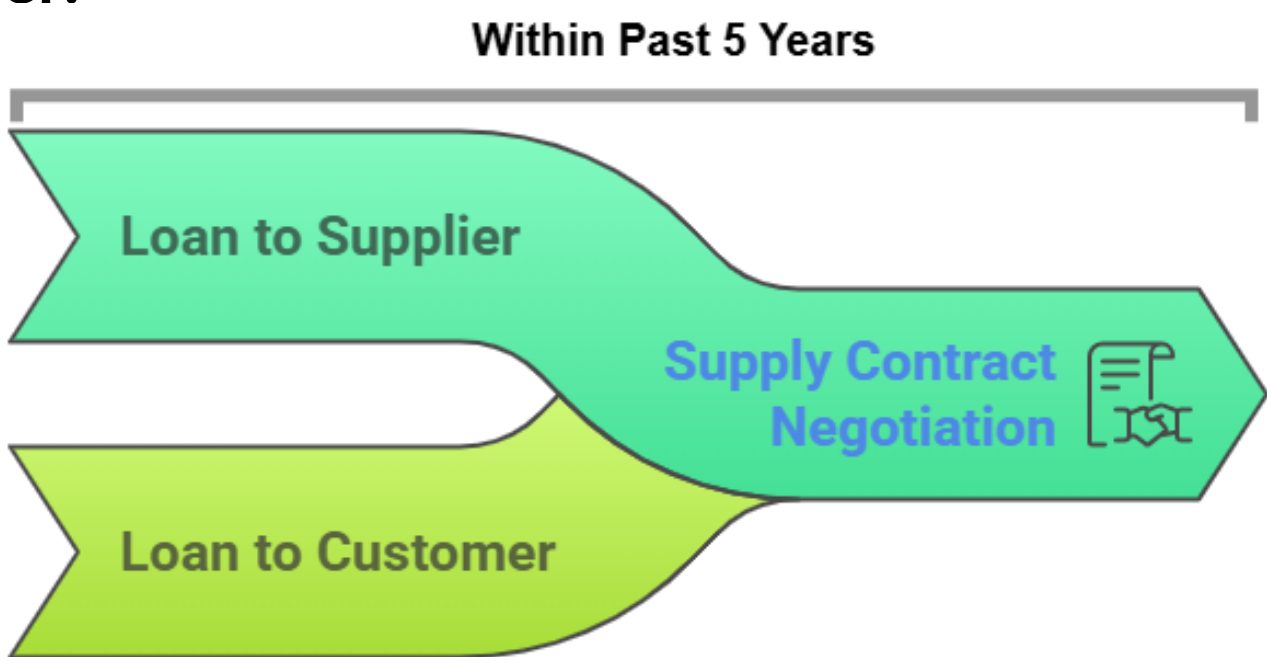


- Supply contracts from firms' 10-K, 10-Q, 8-K, and S-Form
- Factset, Compustat, PatentView

Two types of covenants:

- Sales audit covenant → Financial reporting accuracy
- Product quality covenant → Product quality assurance

Common Lender:



Endogeneity Concerns

- Restrict sample on relationships formed after common lender establishment, SDC data
- Survival analysis, FactSet Data
- Quasi-exogenous variation from financial institution mergers

Dep. Var =	End Relationship		
Panel A: Survival Test	OLS	COX	Weibull
Common Lender	-0.005** (-2.33)	-0.055*** (-5.65)	-0.105*** (-8.22)
Controls	Yes	Yes	Yes
Year Effects	Yes	No	No
N	311,984	311,984	311,984
Panel B: Bank M&A	(1)	(2)	
Treat × Post	-0.077** (-2.72)	-0.116*** (-3.91)	
Controls, FEs	Yes	Yes	
N	5,704	5,704	
Adj. R ²	0.20	0.21	

Panel B col (1) include Year, Supplier, Customer, Event FEs, col (2) include Year, Supplier × Event, Customer × Event FEs