“Motivating Banks to Lend? Credit Spillover Effects of the Main Street Lending Program”

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Main Street Lending Program

- **Fed SPV purchases from banks loans to mid-sized businesses**
  - April to November 2020
  - Loans standardized: LIBOR+300bp; repayment schedule
  - Banks retain >5% of the exposure

- **Take-up $16bln out of $600 available**
  - Bank registration rate 11.7%, about ½ of which granted loans
  - 6.5% of <$1 billion size banks, 63.8% of >$50 billion size banks
- **Why limited participation?**
  - Burdensome registration
  - Loans too expensive
- **But possibly liquidity backstop effects**

Estimation and Results

$$Loan\ outcome_{ijt} = \alpha + \beta MSLP_i\ bank \times Post_t + \gamma' Bank\ characteristics_{it} +$$

$$+ \delta' Bank\ characteristics_{it} \times Post_t + \zeta_{jt} + \eta_i + \theta_{ij} + \epsilon_{ijt},$$

- **Participating banks, compared to other banks:**
  - More likely to originate and renew C&I loans
  - Less likely to tighten lending standards
  - Larger loans and tighter spreads

- **MSLP-registered banks 30-32% more likely to renew loans and 22-27% more likely to originate loans than non-MSLP banks**
- Note: Understand that don’t compare MSLP and non-MSLP loans

Channels

- **Easing of current/future balance sheet constraints vs. risk-aversion**
  - “Risk-aversion” = dealing with the risk of balance sheet constraints

- **SLOOS: Whether bank has tightened lending standards because of capital, liquidity, or risk tolerance**
  - **MSLP affects “risk tolerance” but not capital or liquidity**

- **Additional tests**
  - Stronger effects for banks with high RMI of Ellul and Yerramilli, 2013
  - No stronger effects for constrained banks compared to unconstrained banks

Identification

- **Selection of banks into MSLP is non-random**
  - Participating banks are larger, with less capital, more specialized in C&I lending
  - Control for all observables, what about the unobservables
- **IV: plausibly exogenous variation in the costs of MSLP participation**
  - Predict banks' decision to enroll in the program, but not their lending behavior during the pandemic (other than through their effect on participation)
  - Narrative: Burden of participating depends on bank familiarity with posting collateral

- D1 banks that did not participate in MSLP because registration too burdensome
- D2,3 banks that had pledged either loans (+) or securities (–) collateral pre-pandemic

Identification

- **D1: Banks that did not participate in MSLP because registration too burdensome**
  - Do SLOs distinguish costs vs. benefits?
  - ***Relatively*** burdensome ***because*** don't expect to use? But then no different from use?
  - What's the comparator : banks that don't participate ***or*** that have low burden of participation

- **D2,3: Banks had pledged either loans (+) or securities (–) pre-pandemic**
- May affect bank lending during the pandemic directly
  - Banks that more frequently post collateral **must be different**
  - More likely to support firms during bad times = "relationship banking" (Boot-Thakor-Udell, 1997)
  - **Post loan collateral AND lend more in downturns**
  - NB: bank X firm FE – controls for size and/or pre-existing lending, not relationships

- **Solution?**
  - Placebo tests, but 2008 (or 2016 slowdown) instead of 2018-19 (Fahlenbrach-Prilmeier-Stulz, 2012 "This time if the same")
  - Whether pre-existing bank lending terms were close to MSLP criteria

Questions

- Other programs:
  - SBA's paycheck protection program
  - Fed's Corporate Credit Facilities (CCF)
- What about QE? See how banks differentially exposed
- Determinants of MSLP participation: which were they?

	(1) MSLP bank	(2) Non-MSLP bank	(3) p-value
			A. Balance she
	sample means		
Total assets (USD bn)	63.50	16.66	0.003
Loans/Assets	72.2%	68.9%	0.043
C&I Loans/Loans	30.0%	21.2%	0.000
CET1 capital ratio	12.1%	14.4%	0.008
Excess CET1 capital cushion	5.0%	7.3%	0.008
Core deposits/Liabilities	48.3%	50.2%	0.162
Credit line drawdowns (2019:Q4 vs 2020:Q1)	0.3%	0.1%	0.168
Credit line drawdowns (2020:Q1 vs 2020:Q2)	-1.0%	-0.8%	0.065
Loan loss reserves	1.6%	1.5%	0.513

Economic Costs

- The study focuses on the program's benefits – but what about costs
- Direct costs → Data on loan impairments?
- Moral hazard → How did MSLP affect bank capital and liquidity choices (changes on capital and liquidity as outcomes)
- Important for policy going forward