Zombie Lending and Policy Traps

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Stanford GSB & NBER & CEPR

Why have post-financial crisis policies failed to deliver growth?

Contribution

Key model features

Results

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- Model matching qualitative facts on zombie lending
  $\Rightarrow$ reg. forbearance effects on economy
- Formalizes idea of too much reg. forbearance for economy

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- heterog. banks (exg. capital) & firms (exg. risk & productivity)
- entry and exit of firms (good and bad) (creative destruction)
- given exog. capital, banks choose b/w safe assets or two firm types
- policy instruments: R^f and share of guaranteed loan repayment

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- Optimal policy depends on shock size

Comment 1: Explanation of slow recovery

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  - Debt overhang $\rightarrow$ low investment (e.g., DeMarzo and He 2021)
  - Crouzet and Tourre (2021) use DeMarzo and He model to quantify short-run vs. long run trade-off of government support via credit for corporations during pandemic
  - Similar in spirit to this paper just w/o banks & w/ debt overhang mechanism

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- Model could also be used to test & size narrative

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How much of slow recovery is driven by forebearance induced zombie firm

- As opposed debt overhang?
- Get a sense of model's implied magnitudes
  - What fraction of zombie firms does the model imply?
  - What shock size is large?
  - What bank capital size is considered low vs. high?

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Key considerations

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- Size of bank dependent sector (differs in EU vs US)
- Size of loans to productive sector (C& I) in bank assets
- How large is the zombie firm externality on good firms?
- Incentives for "good" firms to seek funding elsewhere? E.g., private equity, shadow banks

Conclusion

- Very interesting paper with important policy message
- Key open question
  What is the strength of this bank-centric mechanism in explaining the slow recovery?

Smaller comments for authors

- The write up can be sharpened: Examples
  - Abstract not clear
  - Question isn't clear after diving into the paper
  - Some associate "unconventional" policy with bond purchases etc not reg. forbearance
  - Argument missing why you need a model.
- Clarify contribution: Empirically the effects have been described & even quantified. Theoretically, some overlap with other work.
  - Literature on unconventional policy
    (1) Gertler and Karadi (2011)
    (2) Curdia and Woodford (2009)
    (3) Joyce, Miles, Scott, Vayanos (2012)
  - Recent theoretical literature on zombie lending
    (1) Faria e Castro et al paper cited has also (at least the version I saw) a theoretical part
    (2) My paper with Bigio, Majerovitz & Vieyra delivers some of your results (different focus/model)
  - Other explanations of slow recovery (e.g., Crouzet and Tourre)