Discussion: Credit Allocation When Private Banks Distribute Government Loans

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The views expressed are solely my own and do not necessarily represent the opinions of the Banco Central do Brasil.
This paper

• Study bank lending when private banks distribute earmarked market characterized by government-funded loans

• Main findings
  – Banks are more likely to extend earmarked loans to larger firms and firms with existing relationships
  – A cross-selling strategy whereby banks increase the price of free-market loans for riskier borrowers that obtain earmarked credit
Comments

• The percentage and quality of collaterals earmarked loans is usually very high, and this may affect some insights of the paper, concerning risks of the borrowers and so on
  – E.g. riskier firms borrowing from a top-three bank have higher chance to of obtaining an earmarked loan simultaneously with a working capital loan and this is interpreted as finding as evidence of product cross-selling

• Many insights of the paper concern large banks.
  – It is not completely clear if these large banks are the top 3 or top 5
Suggestions

• Improve the comments on earmarked loans
  • E.g. Earmarked loans are considered a *premium credit* by the lender and by the borrower (cheap funding) and this may explain why banks are more likely to extend earmarked loans firms with existing relationships

• Compare the results with credit unions
  • they lend proportionally a lot earmarked credit, specially in some regions of Brazil

• As a robustness check, use the client risk rate available in the Brazilian credit registry
Overall

• Very good paper and relevant question