

Report Type

Mid Term Award Report

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Project Title

Real Effects of Deregulating the Scope of Financial Intermediation

Project Abstract

The first project quantifies the reduction in agency costs and the efficiency gains of universal banks by considering the boundaries of syndication. I focus on the size of syndicates depending on the scope of the participating banks, and hypothesise that such syndicates will be smaller in size in the presence of universal, rather than commercial or investment, banks. The second project looks at the relationship between corporate disclosure and bank-level information production, in particular by considering the debtor's decision to patent when financing innovation.

Activities and Achievement

First project from proposal:

Does Bank Scope Improve Monitoring Incentives in Syndicated Lending?  
(with Daniel Neuhann, University of Pennsylvania)

Non-technical summary:

Over the past two decades, loan shares retained by lead arrangers in lending syndicates have been on a steep decline in the United States. As smaller lead shares indicate reduced financial incentives to monitor borrowers, this has been interpreted as an alarming fact of declining monitoring efficiency. However, this development needs to be interpreted also against the background of financial deregulation. Starting in the 1990s, the scope of banks has been deregulated through the stepwise repeal of the Glass-Steagall Act. In this paper, we provide a theoretical rationale for why banks of wide scope, because they are exposed to their borrowers not just through the loan but also through other products (such as underwriting services), require smaller lead shares for safeguarding the same degree of monitoring. We confirm these predictions empirically by exploiting the repeal of the Glass-Steagall Act. Our findings suggest that the observed increases in syndicated-loan volumes and simultaneous decreases in lead shares over the last two decades are not associated with losses in monitoring efficiency.

Second project from proposal:

Banks' Information Production and Corporate Disclosure  
(with Alminas Žaldokas, Hong Kong University of Science and Technology)

Non-technical summary:

Banks of wide scope, such as universal banks, have more means of generating information about their borrowers, operationalized through cross-selling. It is often assumed that this leads to a positive shock to the quality of the lender's information about the borrower. In order to empirically estimate this value of information, we relate universal banks' information production in lending relationships to firms' disclosure decisions. An important disclosure decision is the release of patents in conjunction with R&D and innovation. A benefit of patents is, besides competitive reasons, that they are a credible signal of the firm's otherwise hard-to-observe

innovation. We show that when banks can gather more information about their borrowers in lending relationships for financing innovation, firms are less likely to patent. In this manner, we establish a substitution relationship between banks' information production and corporate disclosure for the case of innovation.

#### Dissemination

Project 1 will be submitted to a top finance journal after MT 2015. Project 2 will generate a working paper by MT 2015.

Policy makers will gain a more holistic perspective on the evaluation of the optimal scope of banks, by considering the real effects on borrower firms in particular and financial contracting technology in general.

#### Outputs

First project from proposal:

Does Bank Scope Improve Monitoring Incentives in Syndicated Lending?  
(with Daniel Neuhann, University of Pennsylvania)

Link to most recent draft:

<http://farzadsaidi.com/papers/Scope.pdf>

Conference presentations in 2014/15:

Jackson Hole Finance Conference, London Business School Summer Finance Symposium, ESMT Berlin.

Scheduled seminars:

Annual Cambridge-Princeton Conference, University of Zurich.

Second project from proposal:

Banks' Information Production and Corporate Disclosure  
(with Alminas Žaldokas, Hong Kong University of Science and Technology)

Scheduled seminars:

Stockholm School of Economics, INSEAD.

#### Major Difficulties and Any Other Issues

None.

#### Web Links

Paper 1: <http://www.farzadsaidi.com/papers/Scope.pdf>

#### Additional Information

#### Declaration

This award has not yet produced any relevant outputs, but details of any future publications will be submitted to the CERF database as soon as they become available.