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Information Asymmetry, the Cost of Debt, and Credit Events: Evidence from Quasi-Random Analyst Disappearances

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Abstract

We hypothesize that greater information asymmetry causes greater losses to debtholders. To test this, we identify exogenous increases in information asymmetry using the loss of an analyst that results from broker closures and broker mergers. We find that the loss of an analyst causes the cost of debt to increase by 25 basis points for treatment firms compared to control firms, and the rate of credit events (e.g., defaults) is roughly 100-150% higher. These results are driven by firms that are more sensitive to changes in information (e.g., less analyst coverage). The evidence is broadly consistent with both financing and monitoring channels, although only a financing channel explains the impact of the loss of an analyst on firms' cost of debt.

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Keywords: Information asymmetry; Cost of debt; Default; Bankruptcy; Natural experiment; Matching estimators; Difference-in-differences; Equity research analysts; Creditors

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