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## Creditor Control and Product-Market Competition

Matthew T. Billett , Burcu Esmer , Miaomiao Yu

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Matthew T. Billett\*, Burcu Esmer\*\*, and Miaomiao Yu\*\*\*

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## Abstract

We explore how rival firms respond when firms in their industry violate debt covenants. We find that rival firms increase advertising expense, and that this increase is proportional to the size of industry violators' pre-existing market share. Rival firm product-market share also increases in the industry market share of violators, and this relation is more pronounced when products are more substitutable. Rival firm operating performance also increases in proportion to the industry market share of violators. Overall, these findings suggest that the increased creditor control associated with covenant violations has a significant influence on rival firms and product-market competition.

Keywords: Debt covenants, Covenant violations, Creditor control, Product market competition  
JEL Classification: G21, G30, M30

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