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Bank loans and borrower value during the global financial crisis: Empirical evidence from France☆

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ABSTRACT

We investigate the impact of bank loan announcements on borrower value during the recent boom and bust cycle of the 2000 s using a sample of 253 large loans to French borrowers. We find a significant and negative stock market reaction to bank loan announcements during the Global Financial Crisis. Hence, although we document significant changes in bank behavior during the crisis with conservative contractual and organizational modifications, we cannot provide empirical support for the certification value of bank loans during a period of increased informational asymmetries. We propose several explanations based on borrowers' financial constraints and lenders' identity. Nevertheless, bank loan announcements for larger firms receiving large loans funded by international pools of lenders contributed to borrower value even during the crisis.

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1. Introduction

The ongoing economic and financial turmoil that started in 2007 has (again) put financial institutions at the center of harsh debate and massive criticism, in particular with respect to their role

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in fueling and propagating the crisis as well as in provoking a credit crunch. Indeed, according to Dell'Ariccia et al. (2008) and Purnanandam (2011), banks had gradually relaxed their screening and monitoring standards before the crisis, especially in the US sub-prime mortgage market. Then, they sharply curtailed new credit and forced firms to reduce their investments, hence propagating the financial crisis to the real economy (Duchin et al., 2010; Ivashina and Scharfstein, 2010; Santos, 2011).

These findings are somewhat disturbing because according to the seminal contributions by Diamond (1984, 1991) and Fama (1985), financial intermediaries are considered to be efficient in screening and monitoring borrowers and play a specific role in managing the problems resulting from imperfect information on firms. As banks are believed to produce valuable private information regarding a borrower's risk profile and quality, bank loan announcements should convey valuable information to the market about the borrower's financial situation. The empirical evidence tends to support the view that bank loans are thus "special" according to several authors, who find positive and significant abnormal returns for borrowers' stocks around the date of a bank loan announcement (Focarelli et al., 2008; James, 1987; Lummer and McConnell, 1989; Preece and Mullineaux, 1996).

The bank loan signaling and certification role should be crucial particularly during episodes of boom and bust, such as the most recent one starting in the aftermath of the Internet bubble followed by the financial turmoil of 2007–2008. Indeed, De Haas and Van Horen (2010) show that banks tighten their screening and monitoring during a financial crisis when information asymmetries are exacerbated. Thus, the value of bank loan signaling and certification should be even more important during periods of financial turmoil, leading eventually to larger positive stock market reactions following a bank loan announcement.

However, more recent empirical evidence seems to question the "specialness" of bank loans. Billett et al. (2006) find that bank loans are not "special" at all when abnormal returns are estimated over a longer period, while Fields et al. (2006) suggest that the diminishing market reaction to bank loan announcements is consistent with the dramatic change in the financial market. Furthermore, Armitage (1995) finds very little stock market response to loan announcements in the UK, while Gasbarro et al. (2004) find significantly negative share price responses to term loan announcements. The results of event studies performed on samples from emerging markets' borrowers show negative abnormal returns for bank loan announcements (Bailey et al., 2011; Godlewski et al., 2011; Huang et al., 2012).

These issues are even more important in regard to the largest market for external corporate financing in terms of bank debt: the syndicated lending market.[1] Its development provides a representative proxy for the boom and bust cycle (see Fig. 1) with 2 trillion USD and 3000 issues in 2002, then 4.5 trillion USD and 9000 issues in 2007 and 4 trillion USD and 6500 issues in 2011. If we establish a parallel between loan syndication and securitization,[2] we can wonder whether such techniques have reduced the incentives of lenders to perform their screening duties properly, as shown by Mian and Sufi (2009) and Keys et al. (2010) in the case of loan securitization. Also, due to the particular structure of syndicated loans, the issues related to informational frictions are more complicated and severe in such a setting. The private information available to some lenders may create an adverse selection problem, while the moral hazard problem may arise when the participant banks delegate some monitoring tasks to the lead bank.

This market provides an excellent laboratory in which to investigate our main research question: are bank loans (still) "special," especially during a crisis? We aim here to revisit the issue of bank loan "specialness," i.e. the certification value of bank lending, with a particular focus on the recent boom and bust cycle. To do so, we perform an empirical investigation into stock market reactions to bank loan announcements during the 2000–2009 period using event study methodology. We perform an empirical test of the loan, bank syndicate, and borrower characteristics influencing stock market reactions. We investigate whether the stock market perception differs over the boom and bust period and to which loan, syndicate, and borrower characteristics this perception is the most sensitive. We

[1] A syndicated loan is granted by a pool of banks composed of lead and participant banks that provide funding to a borrower under a single agreement.

[2] A securitization does not change the contract between the borrower and the original lender. Instead, a new contract is created by the lender and a third party to sell the cash flow from the underlying loan. In a syndicated loan, all the lenders are and remain part of one loan contract with the borrower.

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