

Breaching the Chinese Wall: Cross-Market Information Flow Following Financial Institution Mergers

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- ▶ **Setting:** Mergers between lenders (DealScan) and institutional equity investors (13F)
 - ▶ Private information on **dual-held** firms
- ▶ **Method:** Difference-in-differences around legal closing
 - ▶ **ID I:** Same institution, treated (dual-held) vs other holdings
 - ▶ **ID II:** Same stock, informed vs uninformed institutions

Main findings

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- ▶ **Key takeaway**: Loan-side private information leaks into equity trading once the two desks are under one roof

Comments

- ▶ The paper belongs to a mature literature on dual ownership
 - ▶ **Haselmann et al. (2022)** use trade-by-trade data to show that banks that also have equity positions in firms are able to exploit their private information to improve trading results
- ▶ This paper contributes by documenting a **causal link** between private information and trading returns
- ▶ Contribution hinges on the quality of the empirical design
- ▶ Suggestions to improve the empirical design

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 - ▶ **Suggestion:** use returns over $q + 1$, after the position change is known
- ▶ Possible to look at the precise timing of the change in holdings?

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- ▶ Timing of deal is plausibly exogenous, but **who merges with whom** may not be
 - ▶ Acquirers may pick targets *because of* shared clients
- ▶ It doesn't negate the differential effect of private information on dual-held firms but the selection concern that superior investors may choose dual holding still remains

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Merger $\rightarrow$ cheaper credit for relationship firms $\rightarrow$ firm value $\uparrow$

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- ▶ **Suggestions:**
 - ▶ Exclude firms that take new loans from the merged parent or see any changes in interest rates
 - ▶ Goal is to **hold everything else constant** and just focus on better access to information

Comment 4a: Evidence on the information channel

- To provide evidence on the mechanism, the paper uses the following triple-diff strategy

$$R_{jq}^f = \alpha + \underbrace{\beta_1}_{\text{key}} Treat_j^f \times Post_q^f \times PI_j^f + \beta_2 Treat_j^f \times Post_q^f + \beta_3 Post_q^f \times PI_j^f \\ + \beta_4 Post_q^f + \gamma Controls_{q-1}^f + \lambda FE_{jq}^f + \epsilon_{jq}^f$$

where PI_j^f is a dummy variable that equals 1 for firms that provide routine financial information (and forecasts) to lenders

- Is PI_j^f exogenous? If bigger firms or firms with larger loans are able to provide such information, PI_j^f would be positively correlated with R_{jq}^f

Comment 4b: Evidence on the information channel

- ▶ Can you exploit the **timing** and **novelty** of private information and link it to trades using trade-level data?
- ▶ Private information reaches lenders at known dates: monthly statements, compliance certificates, amendments and waivers (Ivashina and Sun, 2011)
- ▶ If private information is the channel, trades should **precede** the public release of that information
- ▶ Do position changes following the private information arrival predict *future* returns?
- ▶ Trade-level data for a subsample would help a lot because timing is key

Comment 5: Evidence on information exchange across desks

- ▶ It would be useful to provide some evidence on *how* private information is shared between the lending and trading desks
- ▶ The paper discusses some channels such as “platform/ data unification (deal rooms, monitoring dashboards, borrower pipelines)” and “unified risk oversight”
- ▶ Possible to quantify any of these dimensions?
- ▶ Evidence would be useful to understand whether there is **unintended** information leakage or **active** information exchange
- ▶ The covenant evidence points towards active information sharing but the discussion seems to suggest both channels could be at play
- ▶ Important to understand this difference for policy implications

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- ▶ Can a 1% equity holder change disclosure policy by 11%? What is the channel of influence?

Comment 7: Focus

- ▶ The paper does a lot: returns, covenants, loan pricing, disclosure, sentiment, ... (31 tables)
- ▶ Some results rest on **very small samples**
 - ▶ Covenant and loan-pricing results: 94 treated loans
- ▶ **Suggestion:** Focus on nailing the core result
 1. Which **information** is traded on, and **when**
 2. A **return measure** that is clearly predictive
 3. Evidence on information exchange
 4. Rule out alternative explanations

Conclusion

- ▶ Good attempt to identify the causal impact of private information access on trading returns
- ▶ Paper can be improved by
 - ▶ using timing of private information to predict trades and future returns
 - ▶ providing more detailed evidence on the exchange of information between trading and lending desks
 - ▶ ruling out alternative explanations
- ▶ All the best!