Discussion of Firm Financial Conditions and the Transmission of Monetary Policy

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What role do financial factors play in monetary transmission?

Empirical approach:

- Local projections with firm-level bond data combined with balance sheet characteristics and high frequency monetary policy shocks
- **Firm-level excess bond premium**
  - The component of the bond's credit spread that is unexplained by firm's default risk

Main findings

Empirical results:

Expansionary monetary policy shocks decrease credit spreads

- happens more for *high-EBP* bonds than for low-EBP bonds.

Expansionary monetary policy shocks increase investment

- happens more for *low-EBP* firms than for high-EBP ones

Main findings

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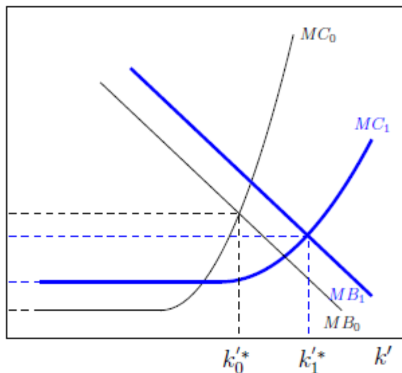
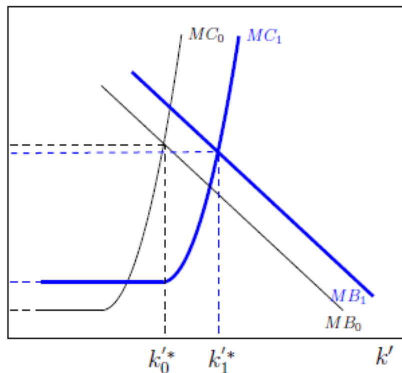
Interpret results with heterogenous firm model

- where financial intermediary frictions make EBP depend on firm's marginal benefit curve
- lower EBPs for firms with flatter marginal benefit curves (reflecting higher resilience of investment prospects)

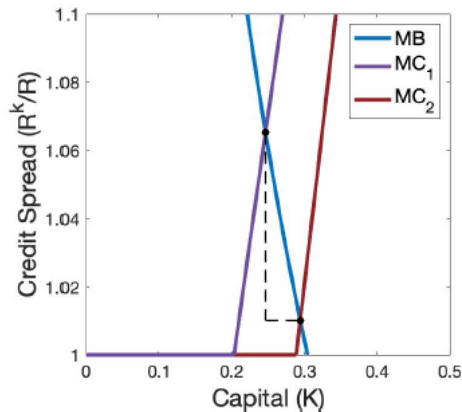
Existing literature focuses on heterogeneity in firm's marginal cost curve

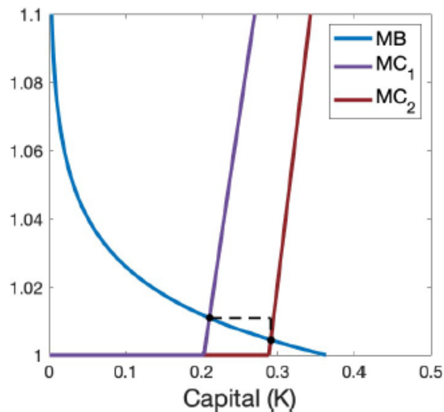
Example: Ottonello-Winberry (2020)





This paper instead emphasizes heterogeneity in firm's marginal benefit curve





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Analysis is extremely thorough and careful. I'm convinced! So only minor/nitpicky suggestions:

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Interact monetary shock with controls

- For firm-level results: all of them simultaneously
- For aggregate results: interact monetary shock with controls (especially uncertainty)

Is there any change in monetary transmission since the financial crisis?

- Do conventional monetary shocks transmit similarly to unconventional ones?

Try Romer & Romer monetary shocks:

- Will enable including early 1970s to mid 1980s in the sample

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Alternative explanation is heterogeneity in size of intermediary frictions

- Should we expect this to be different based on source of funding for firms?
- For example, can check if firms that borrow from bond market vs banks have systematically different EBP

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- Could it be capturing second moments?

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My hypothesis: Suppose firms with high EBP also face higher uncertainty.

- Then paper's empirical results can also be explained by uncertainty at the firm-level

1. firms facing higher EBP/uncertainty dampen their investment response to monetary policy shocks
2. EBP/uncertainty goes up in recessions

Would be interesting to see if uncertainty is being priced into firm-level credit spreads

Suggestions for future work

1. How does EBP itself respond to monetary policy?
   - Is credit spread response to monetary policy driven by default risk or EBP?
2. Does EBP play similar role in transmission of monetary policy to stock prices?

Conclusion

- Very interesting paper!
- Empirical work is thorough and careful.
- Leading theoretical models of monetary transmission focus solely on marginal cost. We should think carefully about marginal benefit side as well
- Nice simple indicator for policymakers to understand how efficacy of their policies can vary over time.

Might be helpful to understand more about what EBP is capturing