New online fintech competitors have entered the small business lending space, filling a gap in small-dollar loans. More than 70 percent of small businesses seek loans in amounts under $250,000 and more than 60 percent want loans under $100,000. Gaps in regulation of the alternative small business lending market create issues of oversight and concerns about predatory lending. The paper first describes the current market for small business lending, including the new disruptors, and presents strategic alternatives for existing banks to partner with fintech entrants and compete in the new environment. The authors then describe the current regulatory environment with its large number of agencies, each with overlapping authority and mandates, and provide a set of recommendations for regulatory activity that will protect borrowers and investors in this space. These recommendations address concerns about systemic risk while trying to avoid dampening innovation that is filling the gap in small business access to credit.

New tech-heavy financial firms are helping millennials invest, but with a twist. They are swapping out investment advisers for financial robots, and passing along the savings. Luis Viceira explains the rise of "fintech" in a new case study.

It is clear that risk-taking by financial institutions is one of the main causes of financial crises and severe recessions. Yet we know relatively little about what gives rise to such risk-taking in the first place. This paper presents evidence that a focus on short-term stock prices induces publicly-traded banks to increase risk relative to privately-held banks. The findings provide support for the view that compensation schemes should require management to hold stock for longer periods to mitigate their incentives to pump up short-term earnings and the short-term stock price.

Why would a country default on its sovereign debt when the government could instead inflate it away? The authors argue that a government is more inclined to default than inflate when the currency mismatch of the corporate sector implies large adverse balance sheet effects from a currency depreciation. To make this argument they construct a dataset on the currency composition of emerging market external borrowing. Results show that the corporate sector relies on external foreign currency debt even as sovereigns have swiftly moved toward borrowing in their own currency.

Top executives who are inclined to reduce personal taxes might also benefit shareholders in their companies, concludes research by Gerardo Pérez Cavazos and Andreya M. Silva.  
   
 Open for comment; 0 Comments posted.

Cash flow is a major concern for small businesses, which, on average, hold only 27 days’ reserve. Karen Mills looks at how "fintech" and government policies can pull companies off the cash flow edge.  
   
 Open for comment; 2 Comments posted.

This paper explains the relation between sovereign debt portfolios and government bond risks across countries. It demonstrates how the interaction of lender risk aversion and monetary credibility can explain why countries with positive bond-stock betas have the lowest local currency debt share. The framework gives rise to testable predictions on inflation, inflation cyclicality, sovereign debt portfolios, and proxies of effective monetary policy credibility, which the authors verify in the data. Overall, the study contributes to and builds upon the literature of government debt asset pricing.

This study surveys 885 institutional VCs at 681 firms asking how they make decisions across eight areas: deal sourcing; investment selection; valuation; deal structure; post-investment value-added; exits; internal VC firm issues; and external VC firm issues.

Recent empirical research in finance and economics has revived the idea that investor sentiment drives credit booms and busts. To explore the drivers of sentiment in credit markets, the authors model the two-way feedback between credit market sentiment and credit market outcomes. In their model the propagation of credit cycles is driven by the interplay between expectations and the refinancing nature of credit markets.

The European Union recently hit Apple with a $14.5 billion tax bill, but that’s hardly the first or worst financial challenge the technology giant has faced. Mihir Desai explains the financial wiring behind the inventors of the iPhone.  
   
 Open for comment; 2 Comments posted.

Venture capital is a relatively small financial institution receiving a large amount of theoretical, empirical, policy, and media interest—perhaps because venture capital encompasses the extremes of corporate finance challenges: uncertainty, information asymmetry, and asset intangibility—and yet has been successful at growing many leading companies. This paper looks at the availability of information about venture capital. While it is it is difficult to paint in definitive terms the level of investment activity and fund performance, the quality of information available has increased in recent years and will likely continue to do so going forward.

A key function of many financial intermediaries is liquidity transformation: creating liquid claims backed by illiquid assets. To date it has been difficult to measure liquidity transformation for asset managers. The study proposes a novel measure of liquidity transformation: funds’ cash management strategies. The study validates the measure and shows that liquidity transformation by asset managers is highly dependent on the traditional and shadow banking sectors.

Coming off the dot-com bust, Thomas R. Eisenmann was confident enough in his internet vision that he wrote a book about what would happen next. For the most part, he was wrong. He offers lessons learned for navigating the boom-bust cycle.  
   
 Open for comment; 1 Comment posted.

Shareholder proposals on environmental, social, and governance (ESG) topics have more than doubled in the last two decades. Testing the effect that ESG proposals have on firms’ subsequent ESG performance and market valuation, the authors find a considerable portion (42 percent) of ESG proposals to be financially beneficial and associated with subsequent increases in environmental and social performance, too. Managers need to identify significant sustainability issues, based on their industry, wisely because errors could be value-destroying as the authors show declines in financial value for the rest of the sample (58 percent).

In the aftermath of the financial crisis of 2007-2008, the United States Federal Reserve took an unprecedented decision to lower short-term nominal interest rates to zero, a policy commonly known as zero lower bound policy. This study shows that the policy adversely affected an important part of the shadow banking system, money market funds, whose returns are linked to the Fed funds rate. During times of unusually low interest rates, fund managers tended to increase their portfolios’ risk. The policy also triggered a reduction in capital supply to financial firms and large corporations and increased the financial markets’ exposure to costly runs and defaults.

This study at the intersection of macroeconomics and banking explores the optimal regulation of banks. Studying and quantifying the effects of capital requirements in a model that features regulated (commercial) and unregulated (shadow) banks, the authors find that a higher capital requirement makes regulated banks safer, but does not affect the riskiness of shadow banks. The net benefit of such a policy would depend on the level of fragility of the unregulated banks.

For several decades, one of the most important questions in international macroeconomics has been “why do governments repay their debts?” This study provides evidence that a sovereign default significantly reduces the value of domestic firms. Foreign-owned firms, exporters, banks, and large firms are particularly hurt more by increases in the probability of sovereign default.

In quarterly earnings calls with investors and analysts, some retail managers may underplay how their companies are actually performing, according to recent research by Kenneth Froot and colleagues.  
   
 Open for comment; 0 Comments posted.

LOYAL3 allows consumers to make small stock purchases of companies they love. In this Cold Call podcast, Luis M. Viceira discusses LOYAL3's move into IPOs and the idea that shareholders make better customers.  
   
 Open for comment; 0 Comments posted.

In a first-ever look at the internal economics driving private equity partnerships, Victoria Ivashina and Josh Lerner find that founding partners who take an unequal share of the pie can ruin their firms.  
   
 Open for comment; 6 Comments posted.