

Dynamic Disclosures and the Secondary Market for Loan Sales

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Abstract

This paper predicts that prospective loan sales by banks create a positive option value for borrowing firms from deferring disclosures to a later period. When banks incur positive transaction costs in selling their loan assets, we show that borrowing firms' initial firm and equity values can actually decrease when: (i) firms have multiple opportunities to disclose relative to when they can disclose only once; and (ii) banks engage in any positive level of monitoring relative to no monitoring at all. Further, even absent transaction costs, we predict that the likelihood of banks' informationally motivated loan sales increases in each one of: firms' leverage, firms' forward-looking preference, the likelihood of banks not experiencing a liquidity shock, and the posterior default probability conditional on public news. We also show that the probability of borrowers' disclosures can decrease in the intensity of bank monitoring and firms' leverage.