Discussion of "Bank market power and credit allocation"

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Plan

1.1 Overview

Bank market power creates distortions

- Financial stability (risks of bank failure, deposit runs)
- Policy transmission (monetary, tax)
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- DOJ's 2023 Merger Guidelines (Banking Addendum)
- Dodd–Frank Act (2010) consumer-facing provisions
- Open Banking / Data Access CFPB §1033 rule (2024)

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} Supply

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} Demand

Regulations target different sources of bank power

- How does each source affect commercial lending?

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Follow-up of Brugués and De Simone, 2024 (R&R JPE, congrats!)

- Ecuador's banking structure reflects limited competition
  - Incomplete pass-through of a loan tax reform in Ecuador, consistent with a joint-maximization behavior of banks
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Main results:

- Changes in loan use, and the welfare of moving to competition
  - Heterogeneous effects by firm size and age
- Positive effect of more loan use on firm productivity
- Positive effects of moving to competition on aggregate efficiency

2. What about the demand side?

1. How large are the distortions from the demand-side?
   - Demand side accounts for 70% of markups (market power)
   - Understanding demand-side may be more relevant than supply-side

	Panel C: Markups	
Markup - Not Accounting for Conduct	2.43	2.30
Markup - Accounting for Conduct	6.38	4.79
Markup - Move to Bertrand-Nash	4.56	2.43
% Share of Markup due to Conduct	25.46	19.18
% Share of Markup due to Preferences	70.27	72.62
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   - Firms face limited outside options, switching costs, and info frictions
   - Bank market power can moderate the welfare losses caused by asymmetric information (Crawford et al. 2018)

3.1 Instrumental Variable

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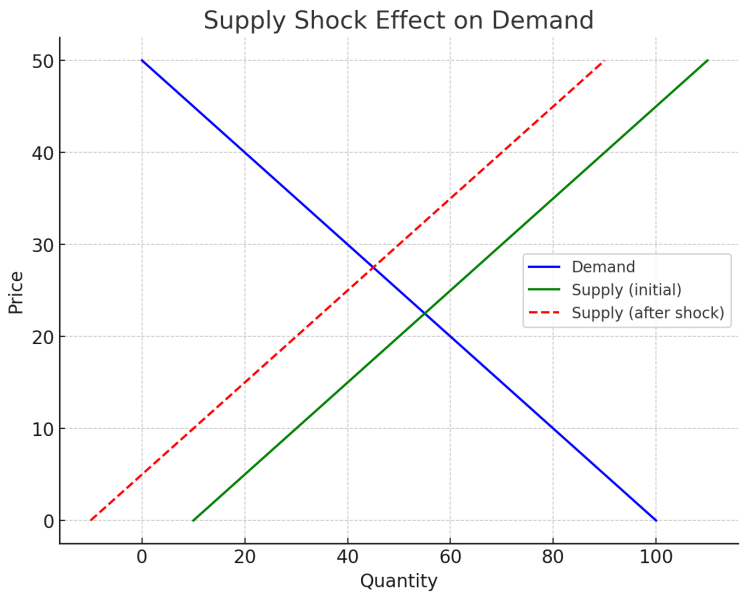

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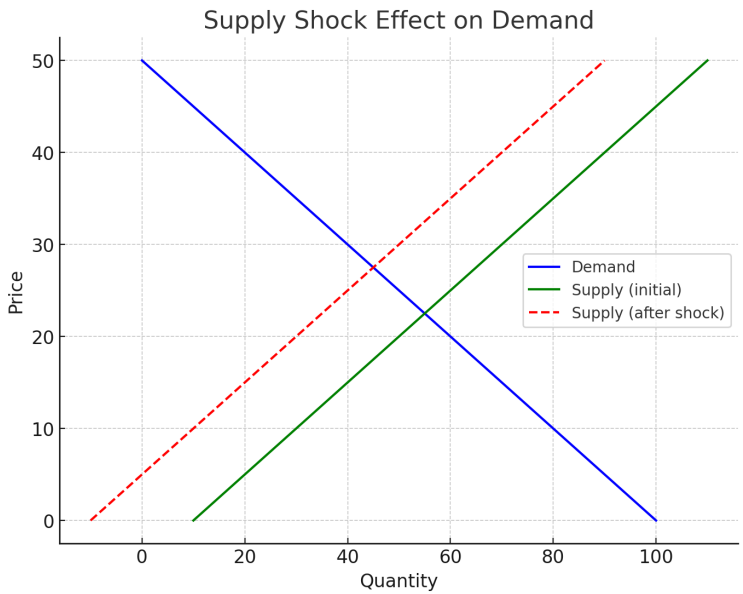

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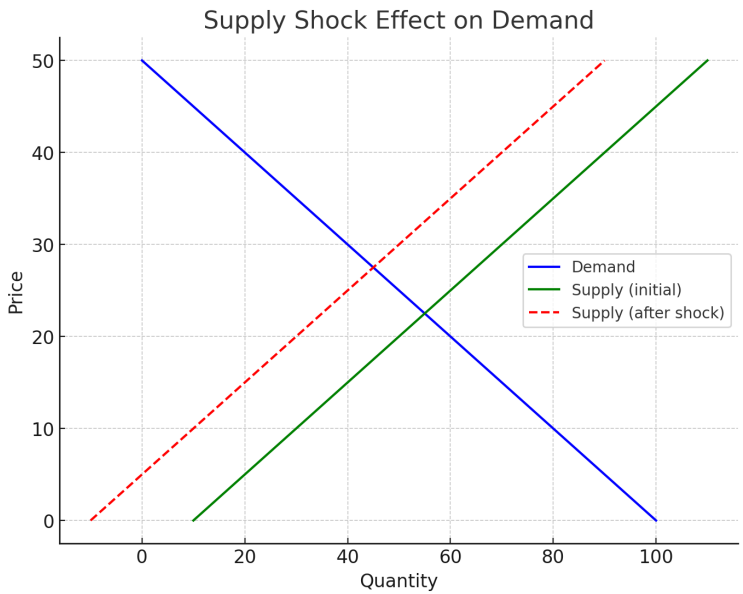

- **Identification:** Instruments should capture bank-level marginal cost variation that is orthogonal to individual demand
- **Proposed instruments:** Average prices of matched banks in other provinces
  - Commercial credit, mortgages, micro-lending
  - Delinquencies in non-commercial credit products

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- **Suggestions**
  - Placebo test: use non-matched banks in other provinces
  - Young's test for IV (Young, 2022)
  - Report information about compliers (relevant for external validity)

4.1 Control function

Control function approach: Residuals of the FS are included in the SS

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- In CF, if $cov(x, e) \neq 0$, $\hat{u}$ controls for endogeneity
- 2SLS not valid if instruments do not satisfy the exclusion restriction
- If the exclusion restriction holds, why not just use IV?
  - α should be interpreted in terms of $\hat{x}$ instead of x
  - It loses "natural" interpretation

5.1 Additional comments

1. **Two-step causality:**

$$\begin{aligned} r &= \rho Z + u \\ ln(credit) &= \alpha r + e \\ TFP &= \beta ln(credit) + v \end{aligned} \tag{4}$$

   - Need not only $cov(\hat{r}, e) = 0$, but also $cov(ln(\hat{credit}), v) = 0$
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Overall: Interesting paper, natural extension of B&DS, 2024

Best of Luck with the Next Draft!