Debt Contract Enforcement and Product Innovation

Tanya Jain, Rahul Singh, Chetan Subramaniam

Discussant: Renuka Sane

12th Emerging Markets Conference, Mumbai

14 December 2021

Summarising the paper

- Does efficient debt enforcement lead to product growth?
- Evaluate if this was because of the credit channel

- Compare within-firm changes in product scope for firms in DRT states to firms in non DRT states
- Study the differential effect of DRT based on a firms tangible assets

- Firms increase product scope
- The effect is more pronounced in high tangible asset firms
- This is largely because of the easing of *financial constraints*
- There is an improvement in firm performance; improvement in TFP

Unpacking product scope #1

- Measurement of product scope is central.
- The paper needs to build on what is known about product scope in India.
- Goldberg et al. (2010)
  - Use CMIE Prowess data from 1989 to 2003
  - Multiproduct firms are strong performers: firms are larger, more productive, and more likely to export
  - More likely to be “high tangible asset” firms
  - Product shedding was not happening in India
  - No evidence of creative destruction
- Chakraborty and Henry (2018)
  - Causal link between increase in imports from China and product scope of Indian firms
  - Study product scope between 1992-2001 and 2002-2007 through a Bartik-type estimation method
  - Find that a 10 percentage point increase in India’s Chinese share of imports in the domestic market reduces the product scope of firms by 1.7-4.4%

Unpacking Product Scope #2

Dosi, Mathew and Pugilese (2020)

- Firms that decide to diversify are substantially different from those that do not.
- Non-diversifying (single-product) firms are such because they lack the need or the capabilities to diversify
- The coherence of the product basket of the firm does not affect firm growth, however a coherent basket directly increase profitability, in particular in specific sectors
- Useful to see the correlation between high tangibility and multi-product firms
- Useful to correlate the product scope in this paper to the standard metrics of measuring product scope.

Unpacking Product Scope #2

Dosi, Mathew and Pugilese (2020)

- Firms that decide to diversify are substantially different from those that do not.
- Non-diversifying (single-product) firms are such because they lack the need or the capabilities to diversify
- The coherence of the product basket of the firm does not affect firm growth, however a coherent basket directly increase profitability, in particular in specific sectors
- Useful to see the correlation between high tangibility and multi-product firms
- Useful to correlate the product scope in this paper to the standard metrics of measuring product scope.

Efficiency of DRTs?

- Insufficient number of DRTs and presiding officers.
- Inconsistent procedures followed by different DRTs
- Significant delay in proceedings (the recommended time is six months, whereas proceedings actually last for two years or more)
- 43,000 cases involving Rs.1.43 lakh crore pending with 33 DRTs across the country. Source: Financial Express, August 13, 2013
- A really credit constrained economy: the promise of a DRT makes credit flows happen.
- But it was soon followed by SARFAESI, then the CDRs, then IBC - each because the previous scheme was not good enough.
- What does one really make of the DRT reform? That banks were naive to believe that enforcement would change?
- When it became evident that DRTs are not upto the mark, did some of these credit flows get reversed?

Efficiency of DRTs?

- Insufficient number of DRTs and presiding officers.
- Inconsistent procedures followed by different DRTs
- Significant delay in proceedings (the recommended time is six months, whereas proceedings actually last for two years or more)
- 43,000 cases involving Rs.1.43 lakh crore pending with 33 DRTs across the country. Source: Financial Express, August 13, 2013
- A really credit constrained economy: the promise of a DRT makes credit flows happen.
- But it was soon followed by SARFAESI, then the CDRs, then IBC - each because the previous scheme was not good enough.
- What does one really make of the DRT reform? That banks were naive to believe that enforcement would change?
- When it became evident that DRTs are not upto the mark, did some of these credit flows get reversed?

Efficiency of DRTs?

- Insufficient number of DRTs and presiding officers.
- Inconsistent procedures followed by different DRTs
- Significant delay in proceedings (the recommended time is six months, whereas proceedings actually last for two years or more)
- 43,000 cases involving Rs.1.43 lakh crore pending with 33 DRTs across the country. Source: Financial Express, August 13, 2013
- A really credit constrained economy: the promise of a DRT makes credit flows happen.
- But it was soon followed by SARFAESI, then the CDRs, then IBC - each because the previous scheme was not good enough.
- What does one really make of the DRT reform? That banks were naive to believe that enforcement would change?
- When it became evident that DRTs are not upto the mark, did some of these credit flows get reversed?

Long-term impact

- Here is a different story
- This was a period of boom in India.
- DRTs helped - high tangible firms got more loans than low tangible firms.
- If not for the optimism, this wouldn't have happened.
- What if you did better credit enforcement in a slump?
- Would you see the same result?