Product Network Connectivity and Information for Loan Pricing*

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Abstract

A theory predicts that loan pricing is less sensitive to public information, such as a credit score provided by an credit information vendor, if the lender obtains more accurate private information about the credit quality of borrowers. We find that loan pricing is less sensitive to public information when a borrower is more connected with other borrowers of the lender through a supply network by using a unique database of inter-firm relationships and bank-firm relationships. This effect is significant statistically and economically even after controlling for the bank-firm relationship characteristics and other firm and relationship characteristics. This finding provides evidence that banks make use of private information through their borrowers' network in their loan pricing.

Keywords: inter-firm network, loan pricing, soft information, information production.
JEL classification: G21, L14

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