Discussion of the paper

Cyclicality of leverage: A study of Indian firms

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Overview of the paper

- Analyses the effect of business cycle fluctuations on firms financing choices, in particular book and market leverage

- Uses a large sample of non-financial firms, both listed and unlisted, covering a long period of fifteen years from 2001-2015.

- Finds that e book leverage varies in a pro-cyclical manner for both listed and unlisted firms but

- Finds no cyclical behavior in market leverage

- Contributes to the literature on corporate capital structure dynamics

Comments – Theoretical

- Will Nice to have a theory of capital structure choice
  - Optimum capital structure varies between firms
  - Different firms are at different stages of their optimum capital structure
  - Firms try to achieve their optimum capital structure over time and their movement varies according to their current state
  - Financial constraints make firms react differently to business cycles
  - Financing constraints prevent firms from achieving their optimal capital structure but these constraints ease over time
  - Economy wide shocks to put firms into temporary disequilibrium but the optimal capital structure is maintained – look at short run and long run leverage
  - The optimal capital structure itself changes due to structural changes in the economy - look at old and newly born firms
  - Signaling theory – commitment through debt look at low and high growth firms separately - look at high growth and low growth firms

Comments - Empirical

- Does capital structure affect both the start as well as the length of economic cycles?
  - a simultaneous equations model is more appropriate

- Dynamic effects suggest that a simple one period lag estimation may not be enough due to auto correlated errors (partial adjustments)
  - a GMM type estimation method may be helpful for single equations

- Coding of the recession dummy – will be better to have a continuous variable measured as deviation of actual output from long run output
  - possible to identify the state of the economy in the cycle

- Identifying financially constrained firms: interplay of supply and demand – can use capital structure of firms in developed countries

Bringing in the emerging economy angle

- Do business group and non-business group firms behave differently in their capital structure choice as well as their response to business cycle conditions?

  - the relation between ownership structure and capital structure: business groups firms have higher leverage to have control on many firms for a fixed amount of equity

  - the response of business group firms to business cycles differ due to existence of internal capital markets

  - strategic borrowing - who are the lenders to firms? public banks versus private banks
    do firms with higher leverage borrow mostly from public banks

- A promising paper and with some additional work I hope to see this published in a very good journal

THANK YOU