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Liquidity Backstop, Corporate Borrowings, and Real Effects

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Abstract

This research investigates the real effects of public liquidity provision. Using the Commercial Paper Funding Facility's (CPFF) eligibility criteria for non-financial commercial paper issuers as the identification strategy, we show that firms with access to the CPFF were able to mitigate the financing disruptions caused by the Lehman Brothers bankruptcy and the ensuing dysfunctional credit market. CPFF directly reduces risk of eligible firms, which in turn improved their financing and short-term profitability. We find liquidity spillover effects from CPFF-eligible firms to their customers through the increased use of trade credit, which propagates the real effects throughout the economy.

Keywords: public liquidity, commercial paper, financial crisis, government intervention

JEL Classification: G18, G21, G28, G32, G38

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