Discussion of

Firm Dynamics and Aggregate Volatility with Endogenously Segemented Credit Markets

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by

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| Research Question: |
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| Does the macroeconomic transmission of aggregate shocks depend on the characteristics of the financial sector? |
| Answer: |
| Yes. |
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Better Research Question:

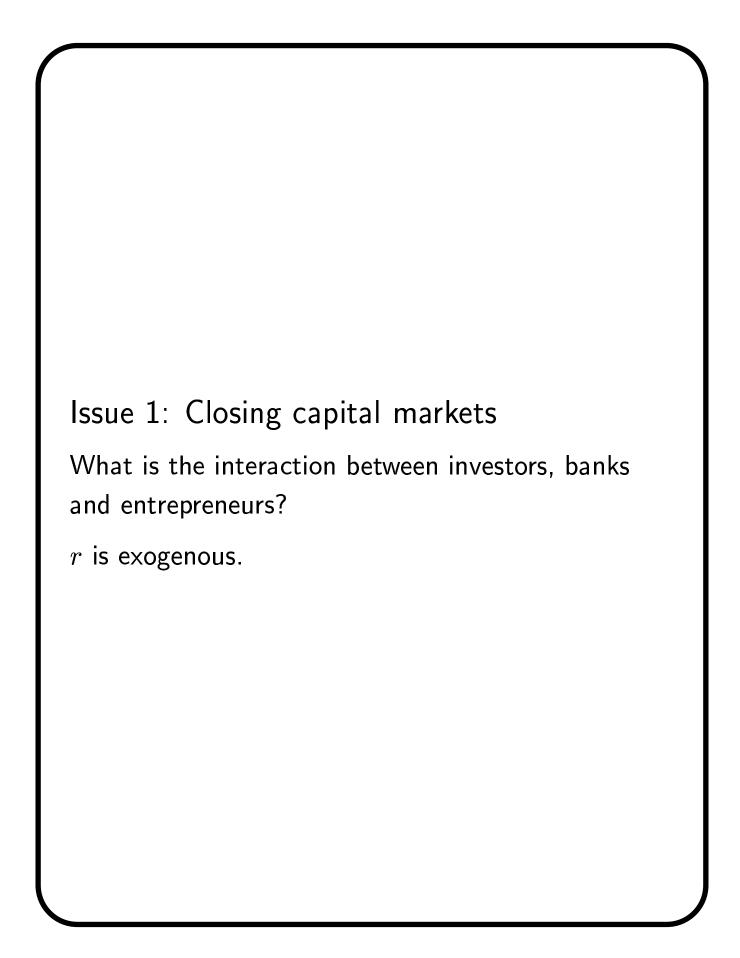
 How much do bank capital requirements matter in a dynamic general equilibrium model with optimal bond and bank credit contracts, capital, goods and labor markets, and firms heterogeneous by capital and investment return?

Answer:

Quite a lot.

Essential points

- Banks are more efficient than bond market, but more expensive.
 - → more bank lending leads to less volatility;
- Firms are borrowing constraint, especially small ones:
 - → go to banks and pay spread,
 - → suffer most when capital requirements are binding;
- Entrepeneurship is very risky
 - → strong need for risk sharing;
- Penalty for repudiation is mild
 - → entrepreneurs can still extract surplus.

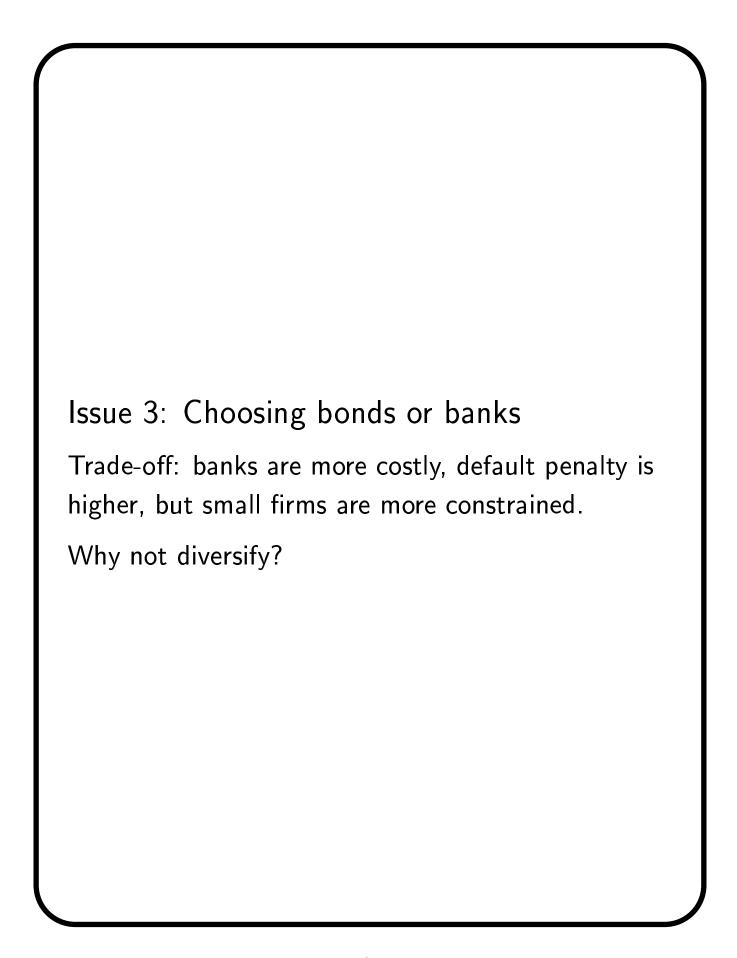


Issue 2: The financing of banks is important Capital requirements are met for each contract individually.

Not clear where funds come from.

r is exogenous.

No occupational choice.



| Diff | icult extensions |
|-------------------|--|
| \longrightarrow | uccessful bond subscriptions converted to loans. make capital requirements binding. crowd small firms out even more. |
| Prop | er penalties for default. |
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