Monetary Policy Without Borrowing: Capacity Constraints and Lumpy Investment (joint with Boragan Aruoba, Andres Fernandez, and Will Lu)

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Abstract

Understanding monetary transmission requires understanding which firms respond to interest-rate changes. We study how limited access to debt shapes firm-level transmission of monetary policy. Using monthly administrative records for all Chilean firms that file VAT returns, matched to a comprehensive credit registry, we combine firm outcomes with monetary policy surprises. We document substantial pass-through from surprises to the interest rates firms pay on new loans. We then show that the effects on investment are sizable and persistent but concentrated among firms with active debt, while firms without debt have responses that are statistically indistinguishable from zero at short horizons in the baseline specification. We interpret these facts with a heterogeneous-firm model with lumpy capacity expansion and limited external finance. In the model, firms without debt access must save and then invest in discrete jumps, can operate with marginal products of capital far above the cost of funds plus depreciation, and do not adjust investment on impact when rates change. Once firms can borrow, they scale up and operate near the point where the marginal product of capital equals the cost of funds plus depreciation, making investment immediately responsive.