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The Internal Capital Markets of Business Groups: Evidence from Intra-Group Loans

David Buchuk, Borja Larrain, Francisco Muñoz, and Francisco Urzúa I.

Abstract

We study business groups' internal capital markets using a unique data set on intra-group lending in Chile (1990–2009). In line with groups' financing advantage, firms that borrow internally have higher investment, leverage, and return on equity (ROE) than other firms. At the margin, controlling shareholders have higher cash-flow rights in borrowing firms than in lending firms. However, there is no robust evidence of minority shareholders losing out from intra-group loans as tunneling predicts. Our evidence is consistent with the idea that strict regulation and disclosure requirements for intra-group loans, which are features of the Chilean market, reduce the risk of expropriation in pyramids.

JEL classification: G32

Keywords: Business groups; Pyramids; Internal capital markets; Intra-group loans; Cash-flow rights.

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