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Corporate Innovation, Default Risk, and Bond Pricing[†]

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ABSTRACT

We propose firm-level innovation performance to be an important determinant of corporate creditworthiness and examine such a relation from the perspective of bond investors. We find that firms' default probabilities are negatively related to the quantity, impact, originality, and generality of their patent portfolios. Moreover, bonds issued by more innovative firms have lower issuance premiums and lower realized excess returns. Our findings are further supported by instrumental regressions that use monetary and time costs of innovation, and by difference-in-differences tests based on exogenous shocks from state-level R&D tax credits.

JEL classification: G12; O32

Keywords: Innovation; Patent; Default risk; Bond premium; Bond return

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