Threat of Entry and Debt Maturity: Evidence from Airlines

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Abstract

I explore the effect of the threat posed by low-cost competitors on debt structure in the airline industry. I use the route network expansion of low-cost airlines to identify routes where the probability of future entry increases dramatically. I find that when a large portion of their market is threatened, incumbents significantly increase debt maturity before entry occurs. Overall, the main findings suggest that airlines respond to entry threats trading off the benefits of short-term financing for lower rollover risk. The results are consistent with models in which firms set their optimal debt structure in the presence of costly rollover failure.

Keywords: Competition, debt maturity, rollover risk, threat of entry

JEL classification: G31, G32, D22, D43, L93

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