

Abstract

Law and Project Finance

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We investigate Project Finance as a private response to inefficiencies created by weak legal protection of outside investors. In the context of large investment projects, we offer a new illustration that law matters by demonstrating that Project Finance provides a contractual and organizational substitute for investor protection laws. Project Finance accomplishes this by making cash flows verifiable, thereby enhancing debt capacity. Comparing the incidence of bank loans for Project Finance with regular corporate loans for large investments ("Corporate Debt Finance"), we show that Project Finance is more likely in countries with weaker laws against insider stealing and weaker creditor rights in bankruptcy. In addition, the effect of investor protection on Project Finance is disproportionately more in industries with higher free cash flows. We employ cross-country tests as well as time-series, difference-in-difference tests that exploit country-level changes in legal rules.

Profile of Dr. Krishnamurthy Subramanian

Krishnamurthy Subramanian is an Assistant Professor of Finance at the Indian School of Business. Prior to joining the ISB, Professor Subramanian was a Finance faculty at Goizueta Business School, Emory University, USA. Professor Subramanian obtained his PhD in Finance from Booth School of Business, University of Chicago under the advice of Prof. Raghuram Rajan and Prof. Luigi Zingales and was declared the Kauffman Foundation Dissertation fellow for this Ph.D. dissertation. He is the recipient of a number of awards, including the Best research paper award at the Corporate Finance Conferences at University of Michigan and Indian School of Business as well as the Best Teaching Awards at the Executive MBA programmes of Chicago Booth in both its Asian and European campuses in consecutive years. As the batch topper during his PGDM at Indian Institute of Management, Calcutta, he was nominated to the Honor roll of the institute. He has also been awarded grants by the President's Commission on Race and Community, the Kauffman Foundation and Georgia Research Alliance for his research on Corporate Governance and Innovation. Prof. Subramanian is an Electrical Engineer by training from the Indian Institute of Technology, Kanpur.