Relationship Lending and the Transmission of Monetary Policy*

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Abstract

This paper demonstrates that relationship lending can have important implications for the transmission of monetary policy. I first construct a credit channel model that accommodates long-term credit relationships as an equilibrium outcome and then analyze how these relationships affect aggregate output. The results indicate that credit frictions still transmit monetary shocks but the extent to which they do so is influenced by the institutional parameters that give rise to relationship lending. In particular, economies poised to foster longer-term credit relationships – due, for example, to better regulatory environments – are also poised for a smoother output response to monetary shocks. In future work, I will aim to quantify the proportion of cross-country transmission differences that can be explained by relationship lending.

JEL Classifications: D83, E37, E44

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