Paying to Brag? A Structural Model of Cheap Talk in Online CrowdLending

Weining Bao
weining.bao@uconn.edu, School of Business, University of Connecticut

Jian Ni
jni@jhu.edu, Carey Business School, Johns Hopkins University

October 2019

Abstract

Online crowdlending platforms often allow initiators to provide various (often unverified) information about the focal projects. On one hand, these unverified descriptions of initiators’ characteristics and project prospects may help backers evaluate the underlying projects, while on the other hand could result in cheap talk by the initiators that reduces the credibility of the information about the underlying projects. We study cheap talk in online crowdlending platforms that could potentially undermine the crowdlending efforts. We utilize detailed transaction data of an online crowdlending platform and use text-mining tools to analyze the raw text in over 11,000 project descriptions. Our reduced-form analysis shows that cheap talk, on average, does not improve the crowdlending outcome. However, the effect of cheap talk on crowdlending is heterogeneous over projects. We find that cheap talk helps low credit rating initiators in crowdlending, and this positive effect depreciates as the initiators’ credit ratings improve. We then develop and estimate a structural model of cheap talk in online crowdlending, conduct counterfactual experiments and discuss the related managerial implications for platforms and initiators.