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## Asset-Measurement Uncertainty and Credit-Term Structure

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*Working paper*

In this paper, we test whether credit investors' uncertainty about a company's asset values affects short-term credit spreads and the underlying credit term-structure. There are three main reasons why we think that the time period studied in this paper provides a powerful setting to test this hypothesis.

First, the growth of a liquid credit default swap market provides a rich cross-section and time-series of clean and reliable data on credit term-structure. Second, regulators began requiring firms to improve disclosures for difficult-to-sell financial assets. Third, the spike in financial market volatility 2007 allowed for more powerful tests to discriminate between potential determinants of short-horizon credit spreads.

Our results suggest that the credit term-structure is flatter at the short end for firms with higher asset measurement uncertainty as captured by larger magnitudes of difficult-to-sell Level 2 and Level 3 assets, which are assets with values based partly on internal estimates, relative to total assets. Our findings are robust to a variety of control variables and sensitivity analyses and are consistent with our predictions, which are guided by a theory that Darrell Duffie and David Lando first published in 2001.

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