The effect of Bank Recapitalization Policy on Corporate Investment

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Common challenges in Asia and Europe
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Main question and results

Does recapitalization of banks lead to higher firm investment? Quantitative assessment
Mechanism: higher bank capital $\rightarrow$ higher willness to lend $\rightarrow$ more borrowing firms $\rightarrow$ more investment

- Japan 1998-1999
- Two recapitalisations (March 1998) (March 1999) : 2 percent of GDP
- Without recapitalisation of March 98 aggregate investment would be 1.3 pct lower
- If recapitalisation of March 99 would have been done in March 98: aggregate investment would be 8.3 pct higher

Micro level investment

Firm loan demand will depend on

- availability of cash flow
- profitability of new investment (TFP shocks, capital)
- cost finance (level of indebtedness)
- price investment goods

Bank loan supply will depend on

- bankruptcy risk of individual firms
- availability of collateral
- Basel I ratio

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- combines micro-mechanism of lending-borrowing-investment
- Allows to analyze the effect of recapitalization

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- exist cost default

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select sample: manufacturing firms quoted on the Tokyo Stock Exchange

- large firms
- access to other finance (bond and equity)

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- Estimated effects are probably lower bound? Effect on SME's should be larger

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- Why so high interest rates? Difference between credit rationing and high interest rates.

Overall conclusion

- paper on an important issue: Does bank recapitalisation promote investment? Yes
- quantitatively important.
- leads to a better understanding of micro-mechanism of bank recapitalisation that eventually needs to be incorporated in macro-models
- high data needs to estimate: matched firm-bank data
- 2 pct of GDP is a lot of money. Is bank recapitalisation its best use?