Bank Soundness and Bank Lending to New Firms during the Global Financial Crisis

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Abstract

This paper examines how the soundness of financial institutions affects bank lending to new firms during the 2008 financial crisis by using a unique firm–bank match-level dataset of 1,467 unlisted small and medium-sized enterprises incorporated in Japan. We employ a within-firm estimator that can perfectly control for unobserved firms' demand for credit through firm$*$time fixed effects. The major findings of this paper are the following four points. First, sound financial institutions are less likely to provide financing to new firms. Second, our results suggest that sound financial institutions are less likely to provide loans to new firms during the 2008 financial crisis. Third, financial institutions are less likely to provide financing to new firms during such crisis compared to those with the same soundness during non-crisis periods. Finally, such lending relationships to new firms that are established during the financial crisis by sound financial institutions are more likely to be continued than such lending by unsound financial institutions.

JEL classification: G01; G21; L26; M13

Keywords: Bank soundness; Bank lending; New firms; Financial crisis; Lending supply; Lending demand

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