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Do Financial Shocks Have Negative Effects on Small Businesses? New Evidence from Japan for the Late 1990s

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Abstract

The banking literature suggests that the low performance of the banking sector can spread to real economic activities, especially small businesses. Many previous studies insist that the Japanese experience of the 1990s supports this argument. However, many studies of small businesses are often insufficient since they depend on aggregate data, even though small businesses are likely to face difficult constraints in their activities when financial problems are severe. In this study, we use firm-level data on small businesses and investigate whether bank-dependent small businesses face severe constraints on their activities, which lowers performance. Our results differ from the findings of previous work in this area. First, we show that per the widely used TANKAN statistics, the focus of many existing studies, is misleading and that a majority of respondents in this survey (at least 71%) report no worsening in the lending attitude of financial institutions in the so-called credit crunch period of 1998-1999 (or even in the 2000-2001 period). Second, using detailed firm level panel data from the Credit Risk Database, we find no significant reductions in the loans for the majority of small businesses. Third, while we do find evidence that bank-dependent firms increased reliance on internal funds during the period of the credit crunch (1998-2001), we find no evidence that this negatively impacted firm performance (as reflected in firm growth and profitability measures).

Keywords: credit crunch; financial shock; small business

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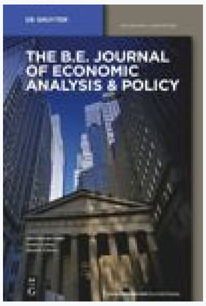

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