



All Content

Images

Search journals, books, images, and



Search ▾

Browse ▾

[About](#) [Support](#)

Tools ▾

JOURNAL ARTICLE

The Response of Corporate Financing and Investment to Changes in the Supply of Credit

Michael Lemmon and Michael R. Roberts

The Journal of Financial and Quantitative Analysis

Vol. 45, No. 3 (JUNE 2010), pp. 555-587 (33 pages)

Published By: Cambridge University Press



<https://www.jstor.org/stable/40930468>

[Cite](#)

This is a preview. [Log in through your library.](#)

[Cookies Settings](#)

ITHAKA websites, which ITHAKA manages from its location in the United States, use cookies for different purposes, such as to ensure web site function, display non-targeted ads, provide social media features, and track usage, engaging with third party service providers such as Google Analytics. Some cookies are essential and always active and you may allow others, such as the Google Analytics cookies, as may be needed to use certain functions on the website, by accepting all or managing "Cookie Settings". For more information, please see our [Cookie Policy](#).

Accept Cookies

The Response of Corporate Financing and Investment to Changes in the Supply of Credit

Michael Lemmon and Michael R. Roberts*

Abstract

We examine how shocks to the supply of credit impact corporate financing and investment using the collapse of Drexel Burnham Lambert, Inc.; the passage of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989; and regulatory changes in the insurance industry as an exogenous contraction in the supply of below-investment-grade credit after 1989. A difference-in-differences empirical strategy reveals that substitution to bank debt and alternative sources of capital (e.g., equity, cash balances, and trade credit) was limited, leading to an almost one-for-one decline in net investment with the decline in net debt issuances. Despite this sharp change in behavior, corporate leverage ratios remained relatively stable, a result of the contemporaneous decline in debt issuances and investment. Overall, our findings highlight how even large firms with access to public credit markets are susceptible to fluctuations in the supply of capital.

I. Introduction

Fluctuations in the supply of financial capital flowing to different sectors of the market can be extreme.¹ Coupled with the presence of financing frictions,

*Lemmon, finml1@business.utah.edu, Eccles School of Business, University of Utah, 1645 E. Campus Center Dr., Rm. 109, Salt Lake City, UT 84112; Roberts, mrobert@wharton.upenn.edu, Wharton School, University of Pennsylvania, 3620 Locust Walk, Ste. 2300, Philadelphia, PA 19104. We are especially grateful for helpful comments from an anonymous referee, Paul Malatesta (the editor), and Mitchell Petersen. We also thank Andy Abel, Marshall Blume, David Chapman, Darrell Duffie, Itay Goldstein, Joao Gomes, Wei Jiang, Arvind Krishnamurthy, Augustin Landier, David Matsa, Andrew Metrick, Toby Moskowitz, Stewart Myers, Vinay Nair, Josh Rauh, Andreea Roman, Nick Souleles, Phil Strahan, Amir Sufi, Petra Todd, Greg Udell, Toni Whited, Julie Xu, and Rebecca Zarutskie; seminar participants at Boston College, Massachusetts Institute of Technology, Northwestern University, Norwegian School of Management (BI), Stanford University, University of

ITHAKA websites, which ITHAKA manages from its location in the United States, use cookies for different purposes, such as to ensure web site function, display non-targeted ads, provide social media features, and track usage, engaging with third party service providers such as Google Analytics. Some cookies are essential and always active and you may allow others, such as the Google Analytics cookies, as may be needed to use certain functions on the website, by accepting all or managing “Cookie Settings”. For more information, please see our [Cookie Policy](#).

[Cookies Settings](#)

[Accept Cookies](#)

Abstract

We examine how shocks to the supply of credit impact corporate financing and investment using the collapse of Drexel Burnham Lambert, Inc.; the passage of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989; and regulatory changes in the insurance industry as an exogenous contraction i...

Journal Information

The Journal of Financial and Quantitative Analysis (JFQA) is published bimonthly in February, April, June, August, October, and December by the Michael G. Foster School of Business at the University of Washington in cooperation with the Arizona State University W. P. Carey School of Business and Universit...

Publisher Information

Cambridge University Press (www.cambridge.org) is the publishing division of the University of Cambridge, one of the world's leading research institutions and winner of 81 Nobel Prizes. Cambridge University Press is committed by its charter to disseminate knowledge as widely as possible across the globe. It publishes...

Rights & Usage

This item is part of a JSTOR Collection.

For terms and use, please refer to our [Terms and Conditions](#)

The Journal of Financial and Quantitative Analysis © 2010 [University of Washington School of Business Administration](#)

[Request Permissions](#)

ITHAKA websites, which ITHAKA manages from its location in the United States, use cookies for different purposes, such as to ensure web site function, display non-targeted ads, provide social media features, and track usage, engaging with third party service providers such as Google Analytics. Some cookies are essential and always active and you may allow others, such as the Google Analytics cookies, as may be needed to use certain functions on the website, by accepting all or managing "Cookie Settings". For more information, please see our [Cookie Policy](#).

[Cookies Settings](#)

Accept Cookies

[Collections](#)

[LibGuides](#)

[Publisher](#)

[Research Basics](#)

[Advanced Search](#)

[Images](#)

[Data for Research](#)

[About JSTOR](#)

[JSTOR Labs](#)

[Mission and History](#)

[JSTOR Daily](#)

[What's in JSTOR](#)

[Careers](#)

[Get JSTOR](#)

[Contact Us](#)

[News](#)

[Webinars](#)

[For Librarians](#)

[For Publishers](#)



JSTOR is part of [ITHAKA](#), a not-for-profit organization helping the academic community use digital technologies to preserve the scholarly record and to advance research and teaching in sustainable ways.

©2000–2023 ITHAKA. All Rights Reserved. JSTOR®, the JSTOR logo, JPASS®, Artstor®, Reveal Digital™ and ITHAKA® are registered trademarks of ITHAKA.

[Terms & Conditions of Use](#)

[Privacy Policy](#) [Accessibility](#)

[Cookie Policy](#) [Cookie Settings](#)

[Cookies Settings](#)

ITHAKA websites, which ITHAKA manages from its location in the United States, use cookies for different purposes, such as to ensure web site function, display non-targeted ads, provide social media features, and track usage, engaging with third party service providers such as Google Analytics. Some cookies are essential and always active and you may allow others, such as the Google Analytics cookies, as may be needed to use certain functions on the website, by accepting all or managing “Cookie Settings”. For more information, please see our [Cookie Policy](#).

[Accept Cookies](#)