





< Working Papers

Financing Constraints and Corporate Investment

Steven Fazzari, R. Glenn Hubbard & Bruce C. Petersen







WORKING PAPER 2387

DOI 10.3386/w2387

ISSUE DATE September 1987

Most empirical models of investment rely on the assumption that firms are able to respond to prices set in centralized securities markets (through the "cost of capital" or "q"). An alternative approach emphasizes the importance of cash flow as a determinant of investment spending, because of a "financing hierarchy," in which internal finance has important cost advantages over external finance. We build on recent research concerning imperfections in markets for equity and debt. This work suggests that some firms do not have sufficient access to external capital markets to enable them to respond to changes in the cost of capital, asset prices, or tax-based investment incentives. To the extent that firms are constrained in their ability to raise funds externally, investment spending may be sensitive to the availability of internal finance. That is, investment may display "excess sensitivity" to movements in cash flow. In this paper, we work within the q theory of investment, and examine the importance of a financing hierarchy created by capitalmarket imperfections. Using panel data on individual manufacturing firms, we compare the investment behavior of rapidly growing firms that exhaust all of their internal finance with that of mature firms paying dividends. We find that q values remain very high for significant periods of time for firms paying no dividends, relative to those for mature firms. We also find that investment is more sensitive to cash flow for the group of firms that our model implies is most likely to face external finance constraints. These results are consistent with the augmented model we propose, which takes into account different financing regimes for different groups of firms. Some extensions and implications for

public policy are discussed at the end.

Download a PDF

Information on access

Acknowledgements and Disclosures	~
Download Citation	~

Published Versions

Fazzari, Steven M., R. Glenn Hubbard, and Bruce C. Petersen. "Financing Constraints and Corporate Investment." From Brookings Papers on Economic Activity, Vol. 1, pp. 141-195, (1988). citation courtesy of RePEC

Related

PROGRAMS

Monetary Economics Public Economics

More from NBER

In addition to working papers, the NBER disseminates affiliates' latest findings through a range of free periodicals — the NBER Reporter, the NBER Digest, the Bulletin on Retirement and Disability, the Bulletin on Health, and the Bulletin on Entrepreneurship — as well as online conference reports, video lectures, and interviews.



<u>2023, 15th Annual Feldstein Lecture, Mario Draghi, "The Next Flight of the Bumblebee: The Path to Common Fiscal Policy in the Eurozone"</u>

LECTURE

Dr. Mario Draghi, who served as President of the European Central Bank and Prime Minister of Italy, presented the 2023...



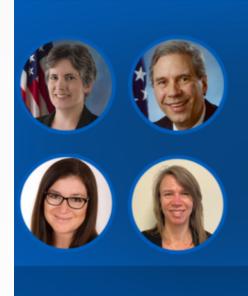
Methods Lecture: Linear Panel Event Studies Jesse M. Shapiro, Harvard University and NBER Liyang Sun, CEMFI

2023 Methods Lectures, Jesse Shapiro and Liyang (Sophie) Sun, "Linear Panel Event Studies"

July 28, 2023

LECTURE

Overview: Linear panel event studies are increasingly used to estimate and plot causal effects of changes in policies...



Panel Discussion:

Long-Term Dynamics of the Employment-to-Population Ratio

Karen Glenn, Social Security Administration Stephen Goss, Social Security Administration Nicole Maestas, Harvard University and NBER Julie Topoleski, Congressional Budget Office July 26, 2023

<u>2023, SI Economics of Social Security, Panel Discussion, "Long-Term Dynamics of the Employment-to-Population Ratio"</u>

Supported by the Alfred P. Sloan Foundation, the National Science Foundation, and the Lynde and Harry Bradley...

National Bureau of Economic Research

Contact Us
1050 Massachusetts Avenue
Cambridge, MA 02138
617-868-3900
info@nber.org
webaccessibility@nber.org

HOMEPAGE

Accessibility Policy
Diversity Policy
Privacy Policy

FOLLOW









© 2024 NATIONAL BUREAU OF ECONOMIC RESEARCH. ALL RIGHTS RESERVED.