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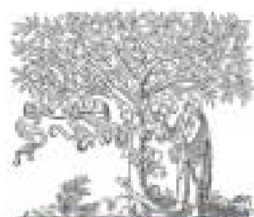

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Bank loan supply shocks and leverage adjustment

Masayo Shikimi

Nagasaki University, Japan

A R T I C L E I N F O

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A B S T R A C T

We investigate the effect of bank loan supply shocks on firms' leverage adjustment. We show that the impact of bank shocks is larger for firms with greater dependence on financially troubled banks. We measure firms' pre-crisis loan dependence on troubled banks by using matched firm–bank loan data. Using the boom-bust cycle from 1987 to 2014 in Japan as a quasi-experiment, we find that financially constrained firms adjust their leverage slower during credit-crunch periods than during other periods. During credit-crunch periods following banking crisis, firms associated with failing banks or with banks that have a limited capacity to supply loans show a slower adjustment than other firms. Bank shocks have significant effects on small firms' adjustment but not on that of large firms. These results are robust when we consider demand-side effects and perform other robustness tests. Our results imply that bank shocks have a persistent effect on borrowers' leverage.