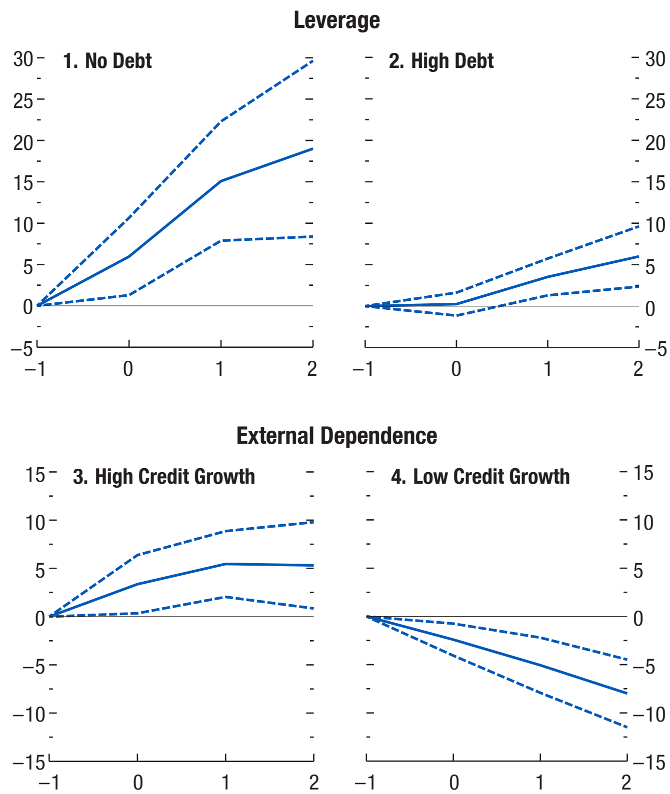
Figure 3.9. Direct Effects of Product Market Reforms on Incumbent Firms' Investment: The Role of Financial Conditions

(Percent; years on x-axis)

The effect of product market reforms on investment tends to be weaker for firms with high debt and for firms that depend heavily on external financing during periods of tight credit conditions.



Source: IMF staff estimates.
Note: $t = 0$ is the year of the shock. Solid lines denote the response to a major reform in product market regulation, and dashed lines denote 90 percent confidence bands. External dependence is defined as the difference between capital expenditure and cash flows as a share of capital expenditure. This measure is then averaged across firms over time and across countries within each industry. Only data from the United Kingdom and United States are used for the calculation of this measure. This definition is based on Rajan and Zingales 1998. Under high and low credit growth, respectively, panels 3 and 4 show the difference in the investment response to reform between firms in sectors that depend strongly on external financing and firms in sectors that depend weakly on external financing.