Article Link
http://www.economist.com/blogs/freeexchange/2011/12/post-crisis-economy

Cautious capitalism

IPA Research Affiliate Antoinette Schoar, who has conducted several studies in SMEs, was cited in an *Economist* article exploring whether the continuing economic recession has changed attitudes toward firm investment and financial decisions.

Excerpt:

> Past research has shown that exogenous shocks, such as recessions, can modify firm-level behaviour. This view is at odds with traditional theories which posit that firms base their financing decisions on sound economic analysis. But a firm is not a rational actor. It is shaped by its managers whose beliefs are coloured by past and present events. For instance, managers who lived through the Great Depression were scarred by the collapse in capital markets and preferred to rely on internal financing even when it was cheaper to borrow externally.
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> Interestingly, a firm's aversion to capital markets can persist for decades after a recession. A recent paper by **Antoinette Schoar** and Luo Zuo, from MIT's Sloan School of Management, concludes that managers who begin their career during a recession have a conservative management style when compared with their non-recession peers. The authors find that early career experiences are important and can influence firm-level decisions even decades later, when the â€œrecession managerâ€ becomes a CEO. The companies headed by these managers are reluctant to access public markets, have lower capital budgets and pay higher effective tax. If the pattern from previous downturns holds, then we can expect the next generation of business leaders to eschew capital markets in favour of self-sufficiency. Firms will invest less in capital-intensive projects and in research and development (R&D) to tightly control finances.

Check out the full article here.

December 07, 2011