

Impaired Credit Dynamism and the Innovation Slowdown

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Abstract

Distortions in credit allocation can slow technological progress by sustaining unproductive firms and generating congestion that crowds out innovation from otherwise healthy firms. We study this mechanism using Japan's banking crisis of the 1990s, linking firm-level borrowing data to the universe of patent applications with more than fifteen years of historical citation outcomes. Innovation declines more in technology fields facing greater credit distortion, with effects substantially larger for forward citations than for patent counts. Firm-level evidence reveals persistently low innovation by zombie firms and reduced innovation by healthy firms operating in zombie-intensive industries, consistent with congestion effects.