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Phoenix rising: Legal reforms and changes in valuations in Finland during the economic crisis

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Abstract

Finland experienced an extremely severe economic depression in the early 1990s. As a part of the government's crisis management policies, significant new legislation was passed that increased supervisory powers of financial market regulators and reformed bankruptcy procedures significantly decreasing the protection of creditors. We show that the introduction of these new laws resulted in positive abnormal stock returns. The new laws also lead to increases in firms' Tobin's q, especially for more levered firms. In contrast to previous studies, our results also suggest that public supervision of financial markets fosters rather than hampers financial market development.

JEL classification: G34; K22

Keywords: Corporate governance; Bankruptcy; Financial supervision; Investor protection; Corporate valuations; Political economy; Crisis management

1. Introduction

Finland went through an economic depression in the early 1990s that was unprecedented in its severity for a highly developed modern economy.[1] An integral part of this depression was a

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[1] From 1990 to 1993 the GDP per capita declined by 14% and the unemployment shot up from 3% of labor force up to 20% (see Honkapohja and Koskela, 1999, for further details).

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