

Accepted Manuscript

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PII: S0378-4266(14)00161-7

DOI: <http://dx.doi.org/10.1016/j.jbankfin.2014.04.028>

Reference: JBF 4445

To appear in: *Journal of Banking & Finance*

Received Date: 28 May 2013

Accepted Date: 29 April 2014



Please cite this article as: Enikolopov, R., Petrova, M., Stepanov, S., Firm Value in Crisis: Effects of Firm-Level Transparency and Country-Level Institutions, *Journal of Banking & Finance* (2014), doi: <http://dx.doi.org/10.1016/j.jbankfin.2014.04.028>

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Firm Value in Crisis: Effects of Firm-Level Transparency and Country-Level Institutions*

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February 2014

Abstract

Recent empirical research suggests that country-level and firm-level governance institutions are substitutes with respect to their effect on firm value. In this paper we demonstrate that during a crisis these institutions may actually become complements. Specifically, we find that the decline in companies' valuation during the financial crisis of 2007-2009 was more sensitive to firm-level transparency in countries with stronger investor protection. We propose a theoretical model that reconciles our findings with the results in the literature. In our model, during "normal times" strong firm-level governance is crucial to attract outside financing in countries with weak investor protection, but is less important in countries with good investor protection. During a crisis, however, investment opportunities decline even in countries with strong investor protection, and, as a result, *relative* importance of firm-level governance increases in such places.

*Our special thanks go to Irek Akhunianov and Alexei Goriaev for their invaluable contribution at the initial stage of this project. We thank Danil Borilo for excellent research assistance. We are grateful to Oleg Shvyrkov from Standard & Poor's for sharing the data. We thank Art Durnev, Sergei Guriev, Oleg Rytchkov, two anonymous referee and the editor as well as seminar participants at Fox Business School, New Economic School, and European Economic Association meeting for helpful discussions. All errors are our own.

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