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

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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.

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