Bank Concentration, Private Credit Development, and Firm Turnover: Evidence from EU.

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Abstract
Firm entry and exit is at the core of the Schumpeterian process of creative destruction, which affects productivity and growth through reallocation of resources and innovation. The literature shows that among the determinants of barriers to firm turnover there are financial factors, which might prevent the creation of new business activities or expansion of existing businesses, thus acting as barriers to entry and growth. This paper analyzes the effect of bank concentration and private credit development (banking market size) on firm entry and exit. Firm turnover is influenced by the banking sector through the firms' need of external finance. If banking system is not efficient in allocating funds to the private sector, firms will face higher barriers to access to credit. Younger firms would be especially credit-constrained because they usually have a limited or no credit history at all, or because banks prefer to limit real sector competition in order to preserve the market shares of their older clients (incumbent firms). If incumbent firms do not have to face higher competition, they are less likely to improve their production processes in order to keep their market shares and, thus, are less likely to quit the market . We use industry level data for 15 European countries for the period 2001-2005, and we apply the Rajan-Zingales (1998) methodology. The empirical evidence shows that there is the effect of bank concentration on firm turnover is conditional on the level of private credit development. In particular, bank concentration has negative effects on firm turnover when domestic the size of banking market is sufficiently large (i.e. only in EU-15 countries). This suggests that bank concentration in itself is not a barrier to firm turnover and has different real effects in EU-15 and New Member States.