Capital Reallocation and Capital Investment

by: David Rodziewicz and Nicholas Sly

May 28, 2019

Rising merger and acquisition activity complements investment growth by allowing firms to build their productive capacity.

Corporate debt levels have grown substantially during the 10-year recovery from the global financial crisis. This debt might be expected to finance investments that support firm expansion, as the U.S. economy has experienced strong growth over the last 10 years. However, much of the corporate debt has been used to reallocate capital through mergers and acquisitions rather than to fund investment activity. Perhaps as a result, some market watchers have expressed concerns that corporations are crowding out, rather than complementing, new investment.

David Rodziewicz and Nicholas Sly show that rising merger and acquisition activity does not fully crowd out new capital investment, as both sales of existing capital between firms and investment in new capital tend to rise and fall together. Moreover, they find that this relationship holds both in the aggregate and within most U.S. industries. Their results suggest that rising merger and acquisition activity complements investment growth by allowing firms to strategically position themselves and build their productive capacity.

Publication information: 2nd Quarter 2019
DOI: 10.18651/ER/2q19RodziewiczSly
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