Dynamic analysis of expectations on firms' external financing behavior
A behavioral perspective

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Semester: Spring 2020
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Abstract

We analyze the role of expectations on firms external financing decisions on the example of European SMEs via the ECB’s SAFE dataset. From a theoretical perspective we combine standard cost optimization approaches with behavioral economics aspects. To conduct our analysis, we use the powerful and complex multinomial logit methodology. The empirical evidence reveals, that firms’ cost optimization behavior is driven by expectations, based on former experience and fundamental systemic changes, and biased by animal spirits. Our results stress the importance of an integrated central bank policy, considering all transmission channels of external finance and implementing a comprehensive communication strategy. Furthermore, our analysis reveals the importance of a full financial education for managers in SMEs. Finally, our results are important to further understand the dynamics of external financing behavior, which becomes especially important in the context of economic crises, like the actual Covid-19 Pandemic.