“Zero-Zero” Loan Policy and Moral Hazard (Summary)

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This study examines whether the special credit-guaranteed loans known as the“zero-zero” loan policy, implemented by the Japanese government during COVID-19, caused moral hazard problems in lending behavior. This policy had looser borrowing conditions than regular loans, and provided a 100% credit guarantee and interest payment support to firms that were severely affected by COVID-19. On the other hand, for private banks, these loans carried no default risk due to the 100% credit guarantee. This may have led to the moral hazard problem because private banks lost the incentive to select good borrowers. Furthermore, by supporting interest payments, private banks were able to earn interest income immediately after the loan began. The lending interest rate for the “zero-zero” loan was not set freely by private banks for each borrower, but each prefectural government set the standard for setting the interest rate independently of the will of the private banks, and the private banks decided the interest rate based on that standard. Consequently, private banks might have prioritized immediate interest revenue, and as a result, moral hazard problem may have occurred, especially in prefectures with higher interest rates, since private banks in these areas were more likely to lose their incentive to select borrowers carefully. This study examines whether these two types of the moral hazard problems occurred.

This study uses a unique dataset that combines firm-level corporate financial data and survey results. The corporate financial data is provided by Tokyo Shoko Research

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(TSR), a major Japanese rating agency, to the Center for Research and Education in Policy Evaluation (CREPE) at the University of Tokyo. The questionnaire survey used in this study is an excerpt from a survey conducted jointly by TSR on the use of the "zero-zero" loan policy and the subsequent situation of firms. Using this original dataset, we analyze the relationship between the application for, acceptance of, and amount of the "zero-zero" loan and firms' business characteristics and loan interest rates, respectively.

The results of this empirical analysis suggested that the "zero-zero" loan policy was likely to cause the two types of moral hazard problems described above. Specially, the analysis revealed that private banks were more likely to approve loans to firms with high default risk prior to COVID-19 and provide larger loans to these firms. Additionally, private banks were more likely to accept and provide larger loans to firms with higher loan interest rates. This study contributes to the evaluation of the "zero-zero" loan policy under COVID-19. It also contributes to the arguments about the pros and cons of credit-guaranteed loans in that it reveals a negative aspect of credit-guaranteed loans by highlighting the occurrence of the moral hazard problem in lending behavior.