

## Year of the Zombie

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[The American Dialect Society](#), which determines the word of the year every year, has voted “[bailout](#)” as the word of the year for 2008. If 2008 was the year of the bailout, 2009 may well become the year of the zombie, because bailouts of troubled banks and firms create zombie banks and zombie firms, which should exit the markets but manage to stay with help from creditors and the government. In [a paper that appeared in the \*American Economic Review\*](#), I showed (with Ricardo Caballero and Anil Kashyap) how the zombie firms in Japan hurt healthy firms in the same industry, discouraged new entrants, and stifled growth.

The bailouts often create zombie firms by allowing inefficient firms to stay around longer than they should. The mechanism to create zombies in the U.S. is different from Japan, where banks supported these dead firms so that they can stay around. In the U.S., the government seems willing to help troubled firms directly. Starting with the financial industry and auto industry, many companies have been asking for and have been receiving bailouts. The number of industries that ask bailouts will continue to grow. Even [the adult entertainment industry](#) asked a bailout. The waves of bailouts are not limited to the U.S. For example, many governments in the world are rushing to [rescue their DRAM manufacturers](#). (In the DRAM industry, Micron, the only U.S. manufacturer, is not planning to ask bailout. They may suffer from competition with zombies in other countries.)

Although the mechanisms of zombie creation are different, the consequences are the same. Zombie firms compete with healthy firms for funding, human capital, and/or demand for the products, and reduce the potential profits for healthy firms. This discourages healthy firms from expanding and prevents new companies from entering the industry. Our paper uses the data from Japan and finds that healthy firms reduce their investment and employment growth disproportionately when the proportion of zombies in the industry increases. We argue that the zombie problem was an important factor behind the long stagnation of the Japanese economy in the 1990s and the early 2000s. When bailouts are spread to many industries, American zombies will prolong the current recession in the U.S.

[The Bailout Game](#), an online game by [Blue Earth Interactive](#), is a pretty interesting game that reminds us how many financial institutions and companies have already been rescued in the name of preventing the economic meltdown. The game is, however, incomplete. None of those bailed out companies come back as zombies. At least that does not happen when I played the game.