

## **Does economic policy uncertainty aggravate financial constraints?**

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### **ABSTRACT**

This paper examines the impact of economic policy uncertainty on economic growth due to its effects on firms' investment decisions, which subsequently justify firms' financial constraints. Using a sample of Chinese listed firms, the study documents that economic policy uncertainty reduce firms' financial constraints. The reduction in financial constraints stems mainly from the decrease in investments which increases the firm's cash holding. Additional tests reveal that the reduction in firms' financial constraints is pronounced more among non-politically connected firms compared to their counterparts. Further tests reveal that a reduction in a firms' financial constraints is of a short-term nature. In the long run, economic policy uncertainty increase firms' financial constraints. The study recommends that changes in policies must be done carefully to avoid turbulence and friction in firms' investment decisions.