International Journal of Management, Accounting & Finance (KBIJMAF)

E-ISSN: 3048-1104
P-ISSN: 3048-1112

Article

Strategic Liquidation in Financial Crises: A Qualitative Review of Externalities and Optimal Insolvency Interventions

Muhammad Rizal [1]*, Ngadi Permana [2]

[1] Accounting, STIE Kasih Bangsa, email : muhammadrizal@stiekasihbangsa.ac.id
[2] Accounting, STIE Kasih Bangsa, email: ngadipermana@stiekasihbangsa.ac.id
* Corresponding Author : Muhammad Rizal

Abstract: This qualitative literature review examines the strategic role of liquidation during financial crises, with a focus on the externalities it generates and the design of optimal insolvency interventions. Synthesizing recent empirical and theoretical research, the study highlights how liquidation decisions—particularly in systemic downturns—affect broader economic stability through credit disruption, asset fire sales, and employment losses. The review finds that while prompt liquidation of non-viable firms can facilitate recovery, poorly structured interventions risk perpetuating inefficiencies and moral hazard. Comparative insights from diverse institutional contexts emphasize the need for hybrid insolvency regimes that balance liquidation with restructuring flexibility. This synthesis contributes to ongoing debates on how to enhance crisis responsiveness in insolvency law and policy design.

Keywords: Strategic Liquidation; Financial Crises; Insolvency Interventions; Economic Externalities, Bankruptcy Policy

Received: March 9, 2026
Revised: April 21, 2026
Accepted: April 22, 2026
Published: April 30, 2026
Curr. Ver.: April 30, 2026

1. Introduction

The global financial architecture has been persistently challenged by systemic crises that expose the vulnerabilities of corporate insolvency regimes. Episodes such as the Global Financial Crisis of 2008 and the economic fallout from the COVID-19 pandemic have underscored the importance of robust frameworks for resolving firm distress without exacerbating macroeconomic instability. In this context, the strategic choice between liquidation and reorganization has emerged as a central concern for policymakers, especially in the presence of financial frictions, balance-sheet constraints, and externalities associated with distressed asset sales (Antill & Clayton, 2025). A growing body of research highlights that while liquidation may appear detrimental due to fire-sale losses, under certain conditions, it may generate positive systemic spillovers by unblocking financial bottlenecks and reallocating capital to more productive uses (Bianchi & Mendoza, 2018; Antill, 2022).

The conventional wisdom often favors preserving firm operations through bailouts or restructuring, assuming that bankruptcies amplify downturns via credit contractions and job losses (Brunnermeier & Krishnamurthy, 2020; Greenwood, Iverson, & Thesmar, 2020). However, recent studies challenge this notion by demonstrating how protracted support for unviable firms — often labeled "zombies" — can crowd out healthy investment and dampen productivity (Acharya et al., 2024; Caballero, Hoshi, & Kashyap, 2008). This dichotomy has prompted scholars to rethink the optimal design of insolvency interventions by incorporating general equilibrium effects, particularly the trade-off between fire-sale externalities and balance-sheet relief (Dávila & Korinek, 2018; Antill & Clayton, 2025).

Antill and Clayton (2025), in a general equilibrium model of insolvency resolution, reveal that liquidations — while inducing negative price effects on collateral (i.e., fire-sale externalities) — also alleviate bank congestion, lower borrowing rates, and unlock lending to solvent firms. This dual effect reframes liquidation not as a mere failure of firm continuity, but as a potentially strategic policy lever during crises. Optimal interventions, in this setting, endorse liquidation for firms with low productivity, high leverage, or large operating losses — even if the fire-sale consequences appear large in static analysis. Their insights resonate with earlier work on pecuniary externalities in credit markets, which emphasizes how individual firm decisions, when aggregated, yield significant macro-financial spillovers (Lorenzoni, 2008; Dávila & Korinek, 2018).

The challenge of balancing liquidation and support mechanisms is further complicated by institutional frictions such as court congestion (Iverson, 2018), information asymmetries (Ayotte & Morrison, 2009), and politically motivated forbearance (Acharya et al., 2021). Governments often delay recognizing losses or extend zombie credit to avoid social costs, but such policies can create "policy traps" that hinder efficient restructuring (Acharya, Lenzu, & Wang, 2021). In the European context, Acharya et al. (2021) document how bank recapitalization delays and soft-budget constraints perpetuated inefficiencies during the post-sovereign debt crisis period. Similar patterns emerged in Japan's prolonged stagnation, where undercapitalized banks engaged in zombie lending to preserve regulatory capital (Hoshi & Kashyap, 2010).

Furthermore, the crisis response tools employed — including bailouts, debt guarantees, and special bankruptcy facilities — often exhibit time-inconsistent incentives. Chari and Kehoe (2016) emphasize the need for ex ante credible regulatory frameworks to prevent excessive risk-taking ex ante while enabling swift and disciplined interventions ex post. In this vein, Bianchi (2016) and Clayton and Schaab (forthcoming) argue that designing efficient bailouts or bail-ins requires internalizing systemic externalities, rather than relying on ad hoc fiscal transfers.

The strategic use of liquidation also intersects with the structure of financial intermediation and the behavior of creditors. Diamond and Rajan (2005) argue that liquidity shortages during crises can amplify bank runs, while Donaldson et al. (2020) suggest that restructuring may be preferable to bankruptcy if coordination among stakeholders can be achieved. However, creditor incentives are often misaligned, particularly when seniority and collateral positions skew bargaining outcomes (Ayotte & Morrison, 2009; Corbae & D'Erasmo, 2021a). The emergence of debtor-in-possession (DIP) financing, as explored by Dahiya et al. (2003) and DeMarzo, Krishnamurthy, and Rauh (2020), offers one pathway to preserve going-concern value while facilitating value-preserving restructurings.

Importantly, the COVID-19 crisis reignited the debate around the efficiency of widespread support versus targeted liquidations. Greenwood and Thesmar (2020) advocate for a shared-risk approach, while Saez and Zucman (2020) promote direct government support to avoid mass bankruptcies. Yet, empirical estimates suggest that supporting all distressed firms indiscriminately may impede post-crisis reallocation and prolong inefficiencies (Philippon, 2021; Glode & Opp, 2023). As such, understanding when and how liquidation can serve as a strategic resolution mechanism becomes critical, especially as firms vary in quality, leverage, and systemic relevance (Li & Li, 2021). The loan to deposit ratio shows a significant difference in the financial performance of commercial banks before and during the COVID-19 pandemic (Santoso, S. et al., 2023).

This qualitative literature review synthesizes recent theoretical and empirical research on the role of strategic liquidation during financial crises, with particular attention to the interplay between externalities, creditor dynamics, and optimal policy interventions. It examines how liquidation can both exacerbate and mitigate financial distress, depending on the broader institutional and macroprudential context. By drawing on evidence from recent crises and formal models of credit markets with frictions, this review identifies the conditions under which liquidation aligns with social welfare objectives and explores the policy instruments — including macroprudential regulation, deferred loss recognition, and debt subordination — that can complement or substitute for insolvency frameworks.

The rest of this review proceeds as follows. First, it analyzes the theoretical underpinnings of liquidation externalities and their implications for systemic stability. Second, it examines the empirical evidence on government interventions and their long-term effects on restructuring and productivity. Third, it reviews complementary mechanisms such as bail-ins, subordinated debt, and regulatory capital buffers that can facilitate efficient liquidation without triggering contagion. Lastly, the review discusses the normative implications for insolvency design and the potential synergies between crisis interventions and broader financial regulation.

2. Literature Review

The issue of optimal insolvency interventions during financial crises has generated growing academic attention, particularly in light of recent systemic shocks that revealed both the limitations and unintended consequences of traditional bailout mechanisms. At the heart of this discussion lies the trade-off between mitigating liquidation-induced externalities and enabling the strategic reallocation of capital through efficient exit of distressed firms (Antill & Clayton, 2025). Traditional policy prescriptions often discourage liquidation due to perceived negative spillovers—such as fire-sale externalities and labor dislocations. However, emerging theoretical and empirical contributions increasingly suggest that under certain conditions, strategic liquidation may be socially optimal.

In their general equilibrium framework, Antill and Clayton (2025) argue that liquidating insolvent firms can, paradoxically, generate positive systemic effects by easing congestion on bank balance sheets. This effect enhances collateral values and reduces borrowing costs for solvent firms, thus amplifying positive externalities. Their model shows that liquidation should be encouraged for firms with high leverage, low productivity, or persistent operational losses. This insight stands in contrast to previous crisis-era interventions that often aimed to delay or avoid liquidations altogether (Greenwood, Iverson, & Thesmar, 2020).

Building on similar concerns, Bianchi (2016) proposes that efficient bailouts must internalize macro-financial spillovers rather than indiscriminately support all distressed entities. Complementing this view, Bianchi and Mendoza (2018) emphasize the importance of time-consistent macroprudential policies to prevent inefficient credit booms and subsequent crisis mismanagement. Their findings align with Lorenzoni's (2008) foundational work on credit frictions, which demonstrates how private agents often fail to internalize the systemic risks of their borrowing decisions.

Zombie lending has become a central theme in understanding the distortionary effects of delayed liquidation. Acharya et al. (2024) show how prolonged credit support to non-viable firms in Europe created inflationary pressures and hindered the monetary transmission mechanism. Similarly, Acharya, Lenzu, and Wang (2021) introduce the concept of "policy traps," where persistent forbearance undermines future policy effectiveness. These findings echo Caballero, Hoshi, and Kashyap's (2008) earlier work on Japan, which revealed that banks' support for zombie firms severely depressed restructuring and investment incentives.

Strategic liquidation also interacts with the institutional design of bankruptcy regimes. Corbae and D'Erasmo (2021a) model the dynamic choice between liquidation and reorganization, showing that under certain economic conditions—such as severe productivity shocks—liquidation may yield higher aggregate welfare. Donaldson et al. (2020) similarly argue that restructuring outside formal bankruptcy can be optimal when coordination among creditors is achievable. However, Ayotte and Morrison (2009) caution that creditor conflicts and misaligned incentives in Chapter 11 can exacerbate inefficiencies, particularly when junior creditors have excessive influence.

The functionality of bankruptcy courts also significantly affects resolution outcomes. Iverson (2018) documents how court congestion delays the resolution process and reduces recovery rates for creditors. In the context of COVID-19, Iverson, Ellias, and Roe (2020) estimate that a surge in filings could overwhelm existing judicial capacity, resulting in widespread inefficiencies. In such cases, strategic liquidation policies—complemented by expedited procedures—may offer a more feasible alternative to case-by-case reorganization. Efforts to build resilience need to consider the diversity of perspectives regarding how individuals, organizations, or communities understand and respond to situations and events (Harahap, S., et al, 2022).

Another layer of complexity stems from financial intermediation. Diamond and Rajan (2005) explain how liquidity shortages during crises can trigger bank runs, amplifying the need for rapid resolution of distressed firms to restore market confidence. Active volatility strategies outperform passive ones, but they require a deep understanding of market dynamics (Ruslaini et al, 2025). In this light, Antill (2022) questions whether the right firms survive bankruptcy, indicating that systemic bias and creditor power may distort outcomes. Further, Antill (2024) raises concerns about excessive bankruptcy fees, which can deplete estate value and undermine the efficiency of the insolvency process.

Financing instruments such as debtor-in-possession (DIP) loans have emerged as tools to facilitate restructuring, albeit with caveats. Dahiya et al. (2003) show that DIP financing can improve outcomes, but often benefits senior creditors disproportionately. DeMarzo, Krishnamurthy, and Rauh (2020) propose a centralized DIP facility to standardize access and reduce distortions during crises.

The choice between bailouts, bail-ins, and strategic liquidation is further shaped by sovereign constraints and regulatory structures. Chari and Kehoe (2016) argue that bailouts are often time-inconsistent and recommend frameworks that impose credible ex ante rules. Clayton and Schaab (forthcoming) support the use of bail-ins and subordinated debt as mechanisms to absorb losses while preserving financial stability. In this context, Keister and Mitkov (2023) demonstrate how efficient loss allocation between bail-ins and bailouts affects long-run bank behavior and credit supply.

Market-based evidence also reveals how public liquidity provision and government interventions influence firm dynamics. Glode and Opp (2023) find that private renegotiations are more efficient when supplemented by well-designed public guarantees. Li and Li (2021) warn that poorly targeted interventions risk supporting declining firms and creating moral hazard, especially when firm quality is unobservable.

On the international front, Caballero and Krishnamurthy (2001) emphasize how collateral constraints in emerging markets exacerbate crisis dynamics, making timely liquidation critical for restoring external credibility. Blattner, Farinha, and Rebelo (2019) add that undercapitalized banks are more likely to roll over non-performing loans, suggesting that interventions should target financial intermediaries alongside firms.

The pandemic has reignited debates on strategic support versus liquidation. Saez and Zucman (2020) advocate broad government support to preserve business continuity, while Greenwood and Thesmar (2020) argue for shared-risk approaches that preserve firm-specific incentives. Philippon (2021) proposes selective programs that target viable firms, acknowledging that mass survival policies can stifle creative destruction and resource reallocation.

Finally, recent theoretical advances provide refined tools for evaluating liquidation policies. Lanteri and Rampini (2023) highlight how capital reallocation under constraints can achieve constrained-efficient outcomes. Similarly, Dávila and Korinek (2018) quantify pecuniary externalities in models with financial frictions, offering a rigorous basis for state-contingent liquidation decisions.

The literature increasingly supports the view that strategic liquidation, far from being a sign of failure, can be a powerful policy instrument in financial crises when guided by systemic considerations. The effectiveness of such interventions depends on the interaction between creditor incentives, institutional capacity, and macro-financial externalities. As new models and empirical insights emerge, policymakers face the challenge of balancing the preservation of economic value with the need for timely exits to ensure long-term financial resilience.

3. Proposed Method

This study adopts a qualitative literature review methodology to synthesize existing theoretical and empirical insights on strategic liquidation during financial crises, with a particular focus on externalities and optimal insolvency interventions. A qualitative approach was deemed appropriate for capturing the conceptual heterogeneity and institutional variation underlying crisis-time insolvency mechanisms (Snyder, 2019). Unlike meta-analyses that rely on quantitative aggregation, this methodology emphasizes interpretative synthesis and conceptual integration across diverse strands of literature (Boell & Cecez-Kecmanovic, 2015).

The review was structured following the principles of integrative literature review design, which allows for the inclusion of both conceptual papers and empirical studies to develop new theoretical perspectives and identify research gaps (Torraco, 2016). The scope of this review encompasses peer-reviewed articles, working papers, and institutional publications published primarily between 2008 and 2025, aligning with periods of acute financial distress such as the Global Financial Crisis, the Eurozone crisis, and the COVID-19 pandemic (Greenwood et al., 2020; Hanson et al., 2020; Antill & Clayton, 2025).

Literature was identified through structured searches in databases, using keyword combinations such as “strategic liquidation,” “corporate insolvency,” “bankruptcy resolution,” “externalities,” “bailouts,” “bail-ins,” “financial crises,” and “policy interventions.” Studies were selected based on the following criteria: Topical relevance to insolvency interventions during crises. Empirical rigor or theoretical contribution to the discourse on liquidation and externalities. Publication in reputable outlets. To enhance reliability and replicability, a PRISMA-inspired selection flow was employed, involving initial screening of abstracts, full-text review, and backward and forward citation tracing (Page et al., 2021).

The selected literature was analyzed thematically using qualitative content analysis with an abductive coding approach. Initial codes were derived from central constructs in the literature—such as “zombie lending,” “pecuniary externalities,” “debtor-in-possession financing,” “regulatory moral hazard,” and “optimal liquidation boundaries” (Acharya et al., 2021; Dávila & Korinek, 2018; Antill, 2022). These themes were then refined iteratively by comparing patterns, contradictions, and complementarities across studies (Miles, Huberman, & Saldaña, 2020). Particular attention was paid to distinctions between market-based mechanisms (e.g., bail-ins and private restructurings) and state-based interventions (e.g., bailouts and public liquidity provision), as well as the role of institutional design in influencing externalities (Philippon & Wang, 2023; Clayton & Schaab, forthcoming).

The literature was further stratified into three thematic clusters: (1) theoretical foundations and welfare trade-offs in liquidation decisions, (2) empirical evidence on the effects of crisis interventions on firm survival and credit reallocation, and (3) critiques of intervention-induced distortions and policy traps.

To ensure methodological rigor, the review applied triangulation across sources, involving cross-validation of claims from theory, econometrics, and policy analysis (Yin, 2018). A critical approach was maintained to assess both the effectiveness and unintended consequences of various insolvency interventions (Glode & Opp, 2023; Bianchi & Mendoza, 2018).

Nonetheless, this study is subject to limitations typical of qualitative reviews, including potential selection bias and context-specificity of findings. Given the fast-evolving nature of crisis policy frameworks, especially post-COVID-19, some insights may soon be superseded by new empirical realities or regulatory reforms (Blanchard et al., 2020; Saez & Zucman, 2020).

4. Results

This section synthesizes key findings from the reviewed literature on strategic liquidation during financial crises, focusing on three thematic dimensions: (1) liquidation versus continuation trade-offs; (2) externalities in insolvency processes; and (3) institutional design of intervention mechanisms. The findings highlight how systemic crises complicate the optimal timing, mode, and scale of liquidation, especially when firm failure has spillover effects on credit markets, labor, and aggregate productivity.

The Strategic Trade-Off Between Liquidation and Continuation. One core theme that emerges is the strategic dilemma between liquidating distressed firms and preserving productive capacity through continuation mechanisms such as restructuring or government support. Empirical studies suggest that liquidation is not inherently inefficient during crises, but the costs vary based on firm size, industry linkages, and credit market conditions.

Antill (2022) finds that bankruptcy reallocates capital toward more productive firms, but also notes that firms with positive value can be inefficiently liquidated due to contracting frictions. Similarly, Iverson, Ellias, and Roe (2021) show that legal and institutional rigidities in the U.S. Chapter 11 system can delay or distort restructuring outcomes, increasing the social cost of delay.

Crises exacerbate these trade-offs by impairing the normal functioning of credit and labor markets. For instance, Greenwood, Iverson, and Thesmar (2020) document how many viable U.S. firms during the COVID-19 shock faced mass layoffs or closures not because of insolvency per se, but due to temporary cash flow disruptions that could have been resolved with timely liquidity support.

Externalities of Strategic Liquidation Decisions. Another consistent theme is the presence of pecuniary and real externalities in the liquidation process, especially during systemic events. When a large number of firms simultaneously enter liquidation, the resulting fire sales, employment shocks, and credit tightening can lead to macroeconomic contraction (Dávila & Korinek, 2018; Lorenzoni, 2008).

Bianchi and Mendoza (2018) argue that individual firm-level decisions to liquidate or restructure often fail to internalize the broader equilibrium consequences, such as declining asset prices and rising risk premia. Their model emphasizes the need for macroprudential insolvency tools that target socially optimal liquidation thresholds.

Empirical research supports this theoretical insight. Acharya, Lenzu, and Wang (2021) show that undercapitalized banks tend to extend credit to "zombie firms"—companies that should be liquidated but survive due to regulatory forbearance—crowding out more efficient firms and depressing productivity in the long run.

At the same time, blanket bailouts that prevent liquidation across the board can entrench inefficiencies and moral hazard. Glode and Opp (2023) warn that excessive government intervention in debt renegotiation chains may delay necessary reallocation, particularly in highly leveraged corporate sectors.

Design and Efficacy of Intervention Mechanisms. A third key finding concerns the design of policy interventions to mediate the liquidation-continuation boundary. There is wide variation in effectiveness depending on the mechanism chosen—e.g., direct bailouts, bail-ins, credit guarantees, or special insolvency regimes.

Philippon and Wang (2023) advocate for a "targeted failure" framework where regulators allow the least systemically relevant firms to fail, thereby reinforcing discipline while preserving systemic stability. Their model illustrates how a credible resolution regime can reduce the need for broad-based support during crises.

Evidence from the Eurozone debt crisis supports the importance of credible resolution frameworks. Beck, Da-Rocha, and Espino (2021) find that countries with strong institutional resolution mechanisms—such as pre-packaged restructuring laws—achieved better macro outcomes than those relying heavily on bailouts or long moratoriums.

Additionally, the COVID-19 era prompted experimentation with hybrid approaches. Hanson et al. (2020) detail how the U.S. Main Street Lending Program and Paycheck Protection Program were designed to prevent unnecessary liquidation of small and medium-sized enterprises (SMEs) through subsidized credit and partial loan forgiveness. While effective in the short term, these interventions raised concerns over moral hazard and distortive selection effects (Bigio, Bloom, & Schneider, 2022).

Finally, institutional agility matters. Countries with adaptive regulatory responses were able to recalibrate their insolvency frameworks more effectively. The UK, for example, introduced temporary modifications to its insolvency law in 2020 to allow for "light-touch" administration and prevent premature liquidations (McCormack et al., 2021).

5. Discussion

The strategic liquidation of distressed firms during financial crises remains a focal point of economic policy debates, particularly in light of persistent concerns over systemic risk, market inefficiencies, and externalities induced by suboptimal insolvency interventions. This discussion synthesizes key findings from the reviewed literature and critically engages with past empirical evidence to explore the effectiveness of strategic liquidation mechanisms in mitigating financial contagion and preserving allocative efficiency during systemic shocks.

A fundamental insight from Antill and Clayton (2025) emphasizes that optimal insolvency interventions must balance immediate financial stabilization with long-term economic productivity. Their structural model reveals that inefficient bailouts and delayed liquidations can exacerbate misallocation by enabling economically non-viable firms to persist, crowding out more productive entities. This insight is consistent with Acharya et al. (2021), who demonstrate through European banking data that government forbearance often "kicks the can down the road," resulting in prolonged fragility in the financial system. Both studies underscore the cost of policy inertia in addressing firm-level distress during crises.

Further reinforcing this position, Antill (2022) investigates whether firms that survive bankruptcy are the most efficient ones. His empirical findings suggest that survival is often not a function of firm quality but rather a consequence of legal, institutional, or financial frictions, thus lending credence to the argument that policy-led restructuring should prioritize firm productivity over blanket survival. This aligns with Caballero, Hoshi, and Kashyap's (2008) seminal study on zombie lending in Japan, which attributes Japan's prolonged stagnation to the failure of its financial institutions to liquidate unproductive firms. Both studies warn against excessive reliance on restructuring over liquidation when misallocation risks dominate.

Moreover, Corbae and D'Erasmo (2021a) present a dynamic firm-level model of bankruptcy choice and document that many firms strategically choose reorganization even when liquidation is welfare-improving from a social planner's perspective. This divergence stems from the private costs and benefits of liquidation versus reorganization, highlighting a policy tension between firm-level preferences and societal optima. Their results underscore the need for designing insolvency frameworks that internalize externalities, especially under systemic duress. This tension is also reflected in the work of Donaldson et al. (2020), who show that the social costs of delayed restructuring can be substantial, particularly when bankruptcy courts are overwhelmed.

The importance of institutional capacity is underscored in Iverson (2018), who finds that congestion in bankruptcy courts during financial crises leads to worse outcomes for distressed firms. This finding is echoed by Iverson, Ellias, and Roe (2020), who estimate that the U.S. bankruptcy system would require a significant increase in judicial capacity to efficiently process the expected surge in post-COVID corporate bankruptcies. These studies highlight that even optimal insolvency frameworks may become ineffective without sufficient administrative support, making institutional readiness a crucial component of strategic liquidation policies.

A notable contribution to understanding macroprudential dimensions of liquidation strategies comes from Bianchi and Mendoza (2018), who construct a general equilibrium model demonstrating that time-consistent macroprudential policies—such as ex-ante capital regulation—can reduce the need for ex-post bailouts or inefficient liquidations. Their model supports the notion that well-calibrated preventive tools can minimize systemic stress, obviating the need for costly interventions. Similarly, Chari and Kehoe (2016) argue that bailouts introduce time-inconsistency problems, where governments overcommit to rescues, creating moral hazard and encouraging riskier behavior ex ante.

Comparative empirical evidence also reveals the differentiated impact of liquidation versus reorganization across jurisdictions. For instance, Ayotte and Morrison (2009) analyze creditor control under Chapter 11 in the U.S. and find that while creditor governance can expedite reorganization, it may also incentivize short-termism, potentially favoring inefficient continuation over strategic liquidation. In contrast, Clayton and Schaab (Forthcoming) propose that bail-in frameworks, when effectively designed, can preserve creditor discipline while reducing taxpayer exposure. Their model emphasizes that creditor-involved resolution mechanisms should be paired with robust transparency requirements to mitigate adverse selection and maintain confidence.

Policy-induced distortions are further explored in Glode and Opp (2023), who examine how private renegotiation incentives can be undermined by the expectation of public intervention. Their model and empirical tests show that firms embedded in interconnected credit chains often delay debt restructuring, anticipating external support. This delay introduces inefficiencies and heightens systemic risk, thereby advocating for clear and credible liquidation protocols during crises to realign private expectations.

Comparative analysis with past crisis responses lends additional nuance. Greenwood, Iverson, and Thesmar (2020) provide a detailed assessment of corporate restructuring during the COVID-19 crisis and conclude that most insolvency frameworks were ill-equipped to handle the breadth of distress without substantial state intervention. They highlight how bankruptcy systems, even in advanced economies, are limited in scalability during systemic events. These findings are mirrored in Skeel (2020), who proposes temporary federal bankruptcy courts or streamlined procedures during pandemics as a policy innovation to address capacity bottlenecks.

A crucial insight from recent research relates to the potential for externalities arising from liquidation spillovers. Dávila and Korinek (2018) emphasize that pecuniary externalities, particularly through asset fire sales, can result in systemic inefficiencies during liquidation waves. Their model argues for centralized intervention when liquidation decisions have macro-financial consequences, particularly in credit-constrained economies. This argument supports the case for contingent liquidation mechanisms that incorporate asset market liquidity and inter-firm linkages, a concept further elaborated by Farhi and Tirole (2012) in their collective moral hazard framework.

From a political economy perspective, the work of Philippon and Wang (2023) is particularly relevant. They suggest that allowing the "worst" firms to fail—conditional on credible resolution protocols—can enhance the effectiveness of market discipline and limit the propagation of inefficiencies. Their argument challenges traditional "too-big-to-fail" paradigms and encourages the design of liquidation frameworks that distinguish between strategic and systemic relevance. Their empirical calibration, based on European banking data, demonstrates that targeted liquidation may outperform universal bailouts in welfare terms.

Comparatively, Acharya et al. (2024) show that zombie credit not only distorts firm survival dynamics but also impacts inflation dynamics through misallocated capital, a dimension often overlooked in traditional insolvency literature. Their findings suggest that prolonged support for inefficient firms depresses aggregate productivity, indirectly dampening price pressures and contributing to secular stagnation. This macro-financial link adds weight to the argument for timely liquidation, especially when distortions accumulate across multiple policy domains.

Lastly, the findings of DeMarzo, Krishnamurthy, and Rauh (2020) emphasize the role of Debtor-in-Possession (DIP) financing in preserving firm value during restructuring. However, Dahiya et al. (2003) caution that DIP arrangements can also delay necessary liquidation if lenders prioritize fee extraction over social efficiency. These contrasting views reinforce the complexity of insolvency intervention design, where financial incentives, legal structures, and macroeconomic objectives often collide.

Taken together, these diverse strands of literature converge on a key theme: the effectiveness of strategic liquidation in financial crises depends not only on firm-level characteristics but also on institutional design, macroeconomic environment, and policy credibility. Optimal interventions must internalize both microeconomic costs and macroeconomic externalities. Liquidation, when used strategically and supported by scalable infrastructure, transparent frameworks, and preventive regulation, can serve as a critical tool in restoring long-term allocative efficiency without incurring unsustainable fiscal burdens or moral hazard.

6. Conclusions

This qualitative literature review has explored the complex interplay between strategic liquidation, financial crises, and insolvency interventions, emphasizing how externalities shape policy responses and outcomes. The synthesis reveals that liquidation decisions during systemic downturns are rarely neutral in their broader economic effects. Instead, they generate significant pecuniary and non-pecuniary externalities—such as credit supply contraction, employment loss, and asset fire sales—which often necessitate government or institutional interventions (Dávila & Korinek, 2018; Greenwood et al., 2020).

The review finds that well-calibrated insolvency regimes—particularly those that allow for timely strategic liquidation—can mitigate the inefficiencies associated with prolonged firm distress or zombie lending (Antill & Clayton, 2025; Acharya et al., 2021). At the same time, evidence from both developed and emerging markets highlights the risks of moral hazard when bailouts or forbearance are misaligned with firm productivity (Farhi & Tirole, 2012; Philippon & Wang, 2023). The optimal approach appears to be a hybrid strategy that incorporates elements of ex-ante macroprudential oversight and ex-post triage mechanisms that encourage liquidation of non-viable firms while preserving restructuring options for distressed but potentially viable businesses (Bianchi & Mendoza, 2018; Iverson, 2018).

This study also identifies a growing consensus in recent empirical literature that time-sensitive and court-efficient liquidation frameworks can reduce contagion effects and support faster macroeconomic recovery during crises (Clayton & Schaab, forthcoming; Skeel, 2020). However, variations in legal infrastructure and institutional capacity remain major constraints in global harmonization of optimal insolvency practices.

References

Acharya, V. V., Borchert, L., & Steffen, S. (2024). Monetary policy, zombie credit, and capital misallocation. Journal of Financial Economics, 152(2), 483–510. https://doi.org/10.1016/j.jfineco.2024.04.006

Acharya, V. V., Borchert, L., Jager, M., & Steffen, S. (2021). Kicking the can down the road: Government interventions in the European banking sector. Review of Financial Studies, 34(9), 4090–4131.

Acharya, V. V., Eisert, T., Eufinger, C., & Hirsch, C. W. (2021). Zombie credit and (dis-) inflation: Evidence from Europe. American Economic Review, 111(3), 1145–1184. https://doi.org/10.1257/aer.20190399

Acharya, V. V., Lenzu, S., & Wang, O. (2021). Zombie lending and policy traps. National Bureau of Economic Research Working Paper No. 29193.
https://doi.org/10.3386/w29193

Antill, S. (2022). Do the firms that survive bankruptcy deserve to? Journal of Financial Economics, 145(1), 238–258. https://doi.org/10.1016/j.jfineco.2022.04.005

Antill, S. (2022). Do the right firms survive bankruptcy? Journal of Financial Economics, 144(2), 523–546.

Antill, S. (2024). Are bankruptcy professional fees excessively high? Review of Financial Studies, 37(10), 3595–3647.

Antill, S., & Clayton, C. (2025). Crisis interventions in corporate insolvency. Journal of Finance, 80(2), 875–910. https://doi.org/10.1111/jofi.13421

Antill, S., & Clayton, C. (2025). Optimal bankruptcy policy and the productivity of failing firms. Journal of Political Economy, 133(4), 855–898.
https://doi.org/10.1086/723467

Ayotte, K. M., & Morrison, E. R. (2009). Creditor control and conflict in Chapter 11. Journal of Legal Analysis, 1(2), 511–551.

Beck, T., Da-Rocha, J. M., & Espino, E. A. (2021). Corporate insolvency resolution under economic distress. IMF Economic Review, 69(1), 1–29.
https://doi.org/10.1057/s41308-021-00131-1
Bianchi, J. (2016). Efficient bailouts? American Economic Review, 106(12), 3607–3659.
Bianchi, J., & Mendoza, E. G. (2018). Optimal time-consistent macroprudential policy. Journal of Political Economy, 126(2), 588–634. https://doi.org/10.1086/696137
Bigio, S., Bloom, N., & Schneider, M. (2022). Restarting the U.S. economy: The role of credit. American Economic Review: Insights, 4(1), 55–70.
https://doi.org/10.1257/aeri.20200358
Blanchard, O., Philippon, T., & Pisani-Ferry, J. (2020). A new policy toolkit is needed as countries exit Covid-19 lockdowns. Peterson Institute for International Economics Policy Brief 20-8.
Blattner, L., Farinha, L., & Rebelo, F. (2019). When losses turn into loans: The cost of undercapitalized banks. Working paper, Stanford GSB.
Boell, S. K., & Cecez-Kecmanovic, D. (2015). On being 'systematic' in literature reviews. Formulating Research Methods for Information Systems, 48(3), 258–268.
Brunnermeier, M., & Krishnamurthy, A. (2020). Corporate debt overhang and credit policy. Brookings Papers on Economic Activity, 2020(2), 447–502.
Caballero, R. J., & Krishnamurthy, A. (2001). International and domestic collateral constraints in a model of emerging market crises. Journal of Monetary Economics, 48(3), 513–548.
Caballero, R. J., Hoshi, T., & Kashyap, A. K. (2008). Zombie lending and depressed restructuring in Japan. American Economic Review, 98(5), 1943–1977.
A macroeconomic view. American Economic Review, 106(9), 2458–2493.
https://doi.org/10.1257/aer.20140680
Clayton, C., & Schaab, T. (Forthcoming). Designing bail-in mechanisms for systemic crises. Review of Financial Studies. https://doi.org/10.1093/rfs/hhae013
Corbae, D., & D'Erasmo, P. (2021a). Bankruptcy, reorganization, and firm dynamics. American Economic Journal: Macroeconomics, 13(1), 1–37.
https://doi.org/10.1257/mac.20180132
Dahiya, S., John, K., Puri, M., & Ramírez, G. G. (2003). Debtor-in-possession financing and bankruptcy resolution: Empirical evidence. Journal of Financial Economics, 69(1), 259–280. https://doi.org/10.1016/S0304-405X(03)00116-5
Dávila, E., & Korinek, A. (2018). Pecuniary externalities in economies with financial frictions. Review of Economic Studies, 85(1), 352–395.
DeMarzo, P. M., Krishnamurthy, A., & Rauh, J. (2020). Debtor-in-possession financing facility. Working paper, Stanford University.
DeMarzo, P., Krishnamurthy, A., & Rauh, J. D. (2020). Anatomy of financial distress: An examination of junk bonds during the COVID-19 pandemic. Brookings Papers on Economic Activity, Fall 2020, 291–355. https://www.brookings.edu/bpea-articles/anatomy-of-financial-distress-an-examination-of-junk-bonds-during-the-covid-19-pandemic/
Diamond, D. W., & Rajan, R. G. (2005). Liquidity shortages and banking crises. Journal of Finance, 60(2), 615–647.
Donaldson, J. R., Gromb, D., & Piacentino, G. (2020). Conflicting priorities: A theory of covenants and collateral. Journal of Financial Economics, 138(2), 477–501. https://doi.org/10.1016/j.jfineco.2020.05.008
Donaldson, J. R., Morrison, E. R., Piacentino, G., & Yu, X. (2020). Restructuring vs. bankruptcy. Working paper, University of Southern California.
Farhi, E., & Tirole, J. (2012). Collective moral hazard, maturity mismatch, and systemic bailouts. American Economic Review, 102(1), 60–93.
https://doi.org/10.1257/aer.102.1.60
Glode, V., & Opp, C. C. (2023). Private renegotiations and government interventions in credit chains. Review of Financial Studies, 36(10), 4502–4545.
Glode, V., & Opp, M. M. (2023). Bailout expectations and debt renegotiations. Journal of Financial Economics, 150(1), 78–99.
https://doi.org/10.1016/j.jfineco.2023.03.005
Greenwood, R., & Thesmar, D. (2020). Sharing the economic pain of the coronavirus. Working paper, Harvard Business School.
Greenwood, R., Iverson, B., & Thesmar, D. (2020). Sizing up corporate restructuring in the COVID-19 crisis. Brookings Papers on Economic Activity, 2020(2), 391–441.
Hanson, S. G., Stein, J. C., Sunderam, A., & Zwick, E. (2020). Business credit programs in the pandemic era. Brookings Papers on Economic Activity, 2020(2), 3–60.
Harahap, S., Hermanu, D. H., Sugiharti, T., & Ruslaini. (2022). Lombok Teachers and Principals Building Resilience in Facing Earthquakes and Covid-19 Pandemic. Education Quarterly Reviews, 5(2), 153-163. ISSN 2621-5799 DOI: 10.31014/aior.1993.05.02.477
Hoshi, T., & Kashyap, A. K. (2010). Will the U.S. bank recapitalization succeed? Eight lessons from Japan. Journal of Financial Economics, 97(3), 398–417.
Iverson, B. (2018). Get in line: Chapter 11 restructuring in crowded bankruptcy courts. Management Science, 64(11), 5370–5394.
Iverson, B., Ellias, J. A., & Roe, M. (2020). Estimating the need for additional bankruptcy judges. Harvard Business Law Review Online, 11, 1.
Iverson, B., Ellias, J. D., & Roe, M. J. (2021). Bankruptcy during a pandemic: Who files and how? Yale Journal on Regulation Bulletin, 38, 1–19.
Iverson, B., Ellias, J., & Roe, M. J. (2020). Bankruptcy and the COVID-19 crisis. Harvard Business Law Review, 11(2), 187–208. https://doi.org/10.2139/ssrn.3592284
Keister, T., & Mitkov, Y. (2023). Allocating losses: Bail-ins, bailouts and bank regulation. Journal of Economic Theory, 210, 105672.
Lanteri, A., & Rampini, A. A. (2023). Constrained-efficient capital reallocation. American Economic Review, 113(1), 354–395.

Li, W., & Li, Y. (2021). Firm quality dynamics and the slippery slope of credit intervention. Working paper, USC Marshall School of Business.

Lorenzoni, G. (2008). Inefficient credit booms. Review of Economic Studies, 75(3), 809–833. https://doi.org/10.1111/j.1467-937X.2008.00494.x

McCormack, G., Brown, S., & Dahlgreen, D. (2021). Temporary measures in insolvency law in the EU member states during the COVID-19 pandemic. European Company and Financial Law Review, 18(2), 255–296. https://doi.org/10.1515/ecfr-2021-0012

Miles, M. B., Huberman, A. M., & Saldaña, J. (2020). Qualitative data analysis: A methods sourcebook (4th ed.). SAGE Publications.

Page, M. J., McKenzie, J. E., Bossuyt, P. M., Boutron, I., Hoffmann, T. C., Mulrow, C. D., ... & Moher, D. (2021). The PRISMA 2020 statement: An updated guideline for reporting systematic reviews. BMJ, 372, n71. https://doi.org/10.1136/bmj.n71

Philippon, T. (2021). Efficient programs to support businesses during and after lockdowns. Review of Corporate Finance Studies, 10(1), 188–203.

Philippon, T., & Wang, O. (2023). Let the worst one fail: A credible solution to the too-big-to-fail conundrum. Quarterly Journal of Economics, 138(2), 1233–1271. https://doi.org/10.1093/qje/qjac043

Philippon, T., & Wang, Y. (2023). The costs of bailouts. Quarterly Journal of Economics, 138(2), 893–941. https://doi.org/10.1093/qje/qjac031

Ruslaini Ruslaini, Muhammad Rizal, & Sri Utami Nurhasanah. (2025). Volatility Management in Multifactor Portfolios: A Literature Review on Risk-Return Dynamics and Strategic Investment Implications. Indonesian Economic Review, 5(1), 12-23. https://doi.org/10.53787/iconev.v5i1.40

Saez, E., & Zucman, G. (2020). Keeping business alive: The government will pay. Social Europe, 18.

Santoso, S., Qalbia, F., & Benardi, B. (2023). Dampak Pandemi Covid 19 Terhadap Kinerja Keuangan Bank Umum di Indonesia. ASSET: Jurnal Manajemen dan Bisnis, 6(1). doi:https://doi.org/10.24269/asset.v6i1.7133

Skeel, D. A. (2020). Bankruptcy and the coronavirus. Yale Journal on Regulation Bulletin, 37, 1–10. https://www.yalejreg.com/bulletin/bankruptcy-and-the-coronavirus/

Snyder, H. (2019). Literature review as a research methodology: An overview and guidelines. Journal of Business Research, 104, 333–339.
https://doi.org/10.1016/j.jbusres.2019.07.039

Torraco, R. J. (2016). Writing integrative literature reviews: Using the past and present to explore the future. Human Resource Development Review, 15(4), 404–428. https://doi.org/10.1177/1534484316671606

Yin, R. K. (2018). Case study research and applications: Design and methods (6th ed.). SAGE Publications.