From the 2008 Crisis to Today: Large Firms are Still Cautious

Economic Studies

TEPAV Policy Note

September 2010

From the 2008 Crisis to Today: Large Firms are Still Cautious

2008 global crisis had a profound effect on corporate sector in Turkey and caused a significant contraction in the balance sheets of firms. As of the last quarter of 2009, the said contraction started to be replaced by recovery. However, debates go on in both world markets and in Turkey that the mentioned recovery is not reflected in investment and that firms are still cautious since they are yet unable to foresee the future.

This policy note examines the level of recovery across large firms in Turkey after the crisis, current state and the position these firms take in the current state in comparison with the favorable conditions before the eruption of the global crisis with a view to identify how the corporate sector in Turkey has been affected by the crisis and how firms perceive the future outlook. First, the note makes an assessment of existing conditions by analyzing the quarterly balance sheets of 120 firms operating in the manufacturing sector and quoted in IMKB (Istanbul Stock Exchange) for the period between the first quarter of 2007 and the first quarter of 2010. After that, the note reviews the indicators for the perception and expectations of firms for the year 2011.

I. Recovery from the 2008 crisis has began in the corporate sector

Although the global crisis has led to a major destruction in balance sheets of firms, a considerable recovery in balance sheets is observed as of the last quarter of 2009. In this context, sales revenues and profitability of 120 firms quoted in the IMKB are scrutinized[1]. According to this, the following points applying for the corporate sector, particularly large firms, strike attention[2]:

Downwards movement in sales revenues during the crisis began to be reversed

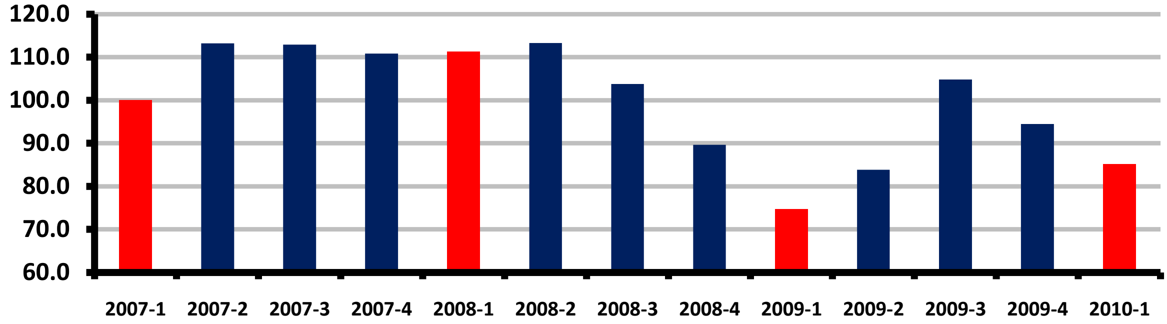
It is seen that the net sales revenue of firms started to fall rapidly as of the second half of 2008. The trough was hit in the second half of 2009. Given the seasonal effects on balance sheet items such as sales, data was compared with the same quarter in the year before. In this respect, it is observed that net sales revenues which continued to drop until the second quarter of 2009 along with the impact of the crisis started to surge year-on-year after the said quarter. However, it is important to note that

[1] Firms that were not operable throughout the period between the last quarter of 2006 and second quarter of 2010, firms that operated in the field of petro chemistry, firms that employed less than ten people, firms that holds considerably large assets in comparison with the number of employees and firms that have considerably large assets that will change the sample results were not included in the analysis. The sample relying on the data from 120 countries represent a balanced panel.

[2] The sample, taking into account both the number of employees and the size of balance sheet, represent large firms.

despite this surge, net sales revenue realized by the first half of 2010 is still lower than the amount in the first quarter of 2008 (Figure 1).

Figure 1: Real Net Sales (2007-2010*)

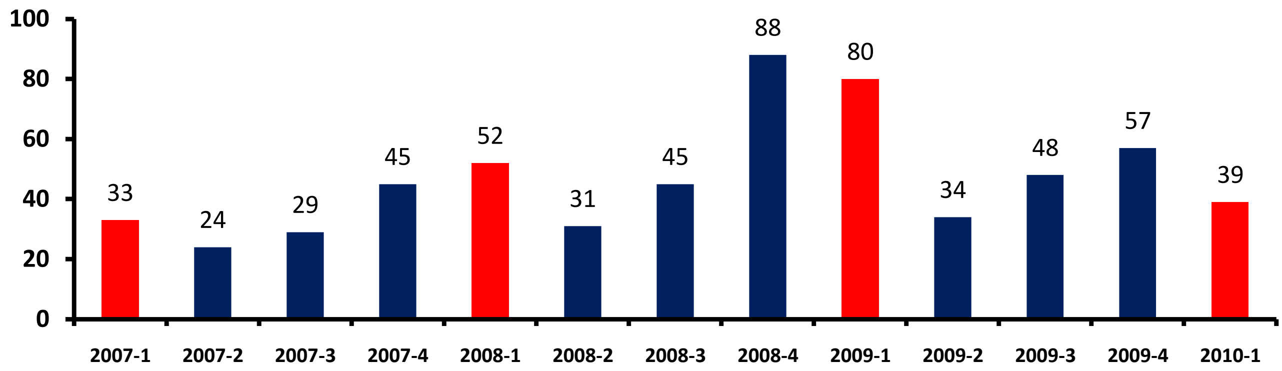


*Net sales revenues represent only the relevant quarter. Series are indexed to the first quarter of 2007 (100).

Number of firms making losses decreases, overall profitability rises

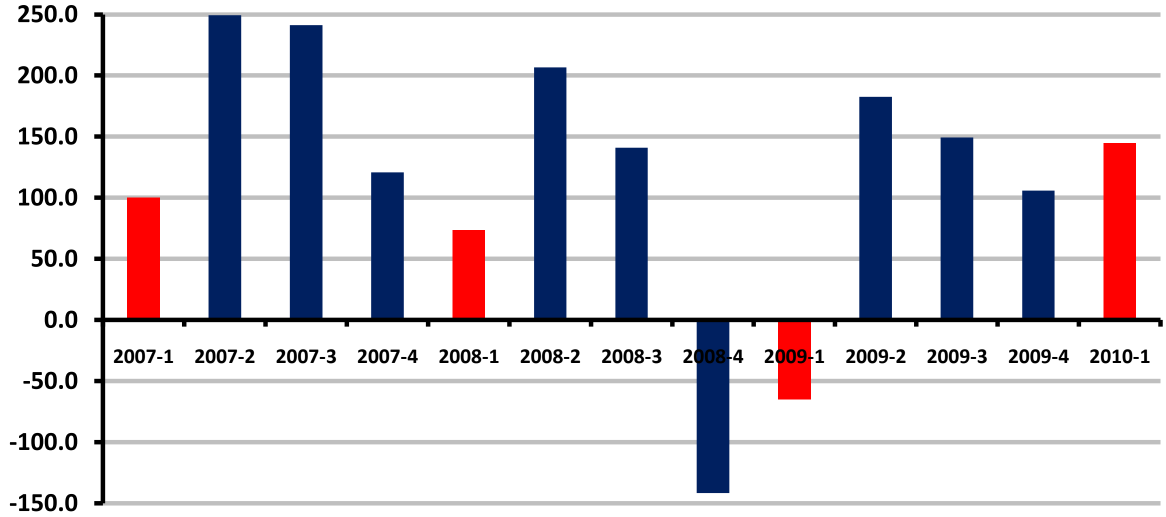
A similar trend can be observed also with respect to the profitability of analyzed firms. Across the selected 120 firms, number of those making losses increased as of the last quarter of 2008, reaching 80 by the first quarter of 2009. From that quarter onwards, however, number of firms making losses diminishes (Figure 2). The developments over the first quarter of 2010 can be assessed in two different lines. Assuming that seasonal effects applied, it is seen that fewer firms faced losses in the first quarter of 2010 compared to the first quarter of 2009. Even if it is assumed that seasonality did not work, number of firms making losses by the first quarter of 2010 appears to be less than that for the fourth quarter of 2009. Therefore it is possible to conclude that firms start to recover as of the first quarter of 2010. Profits (losses) of firms for relevant financial years also demonstrate a trend similar to the overall outlook (Figure 3). It is analyzed that firms made negative profits in the last quarter of 2008 and that the loss was compensated for only as of the second quarter of 2009. By the first quarter of 2010, overall profit of firms exceeded that achieved in the first quarter of 2007.

Figure 2: Number of firms Making Losses (out of the sample of 120 firms * (2007 -2010)



*Calculations for relevant quarters are based on three-month figures. For example, the quarter 20083 covers the period between July 2008 and September 2008.

Figure 3: Realized Total Profit-Loss *



*: Series are indexed to the first quarter of 2007, where 2007Q4 is 100.

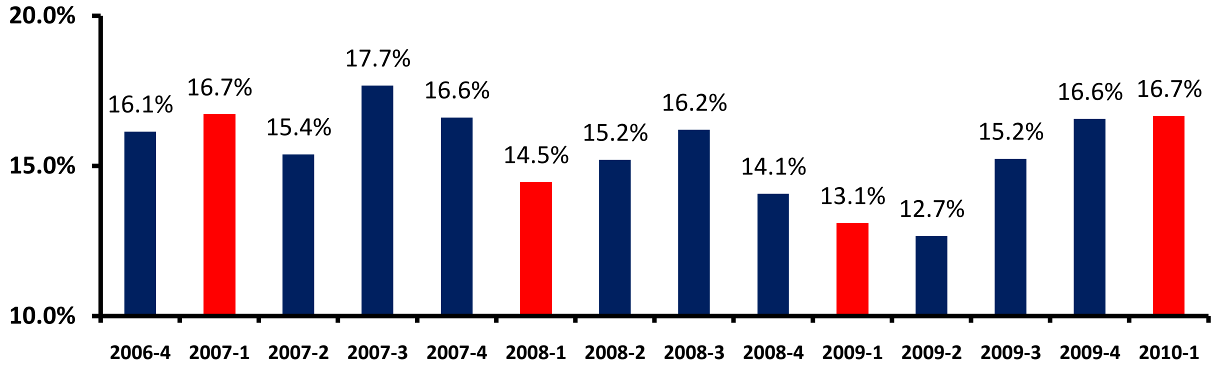
II. Large firms remain cautious

Following the eruption of the crisis, firms used their working capital whereas a recovery in the level of working capital was observed along with the surge in profitability and net sales. Nonetheless, in spite of the improvement in profitability and sales as well as in working capital, firms do not appear to demonstrate a substantial investment attack. Firms' preference in the recent period to deplete inventories and remain liquid; recovery in private investments being weaker than that in consumption, the reduction in imports of investment goods and firms' reluctance in borrowing from financial markets imply that the corporate sector suspended investment and production decisions waiting for the reestablishment of confidence in the economy. This phenomenon is elaborated further below:

Though working capital re-achieved the pre-crisis levels, the underlying factor appears to be operational items

The impact of the crisis in working capital crystallized as of the third quarter of 2008. It is detected that firms melted down their working capital until the last quarter of 2009, after which a surge in the level of working capitals is observed[3] (Figure 4). By the last quarter of 2009 firms display a favorable outlook with regard to working capital levels. This outlook perpetuates also in the first quarter of 2010; the ratio of working capital to total assets stands way below that in the year before also achieving the level in the same period in 2008.

Figure 4: Ratio of Working Capital to Total Assets (2006-2010, %)



The factor underlying the rise in the level of working capital is mainly firms' tendency to hold liquidity[4]. It is identified that similar to the tendency pertaining to working capital, firms reduced the level of liquidity along with the crisis and increased it starting from the first quarter of 2009 (Figure 6 and Annex: Figure 1). By the first quarter of 2010, the share of liquidity in total assets of firms stands 3.6 points below the pre-crisis level (Annex: Figure 1). It is estimated that this rise mainly stems from the fact that in the face of the crisis firms acted cautiously, refrained from taking any position and stood on the safe side keeping liquidity[5].

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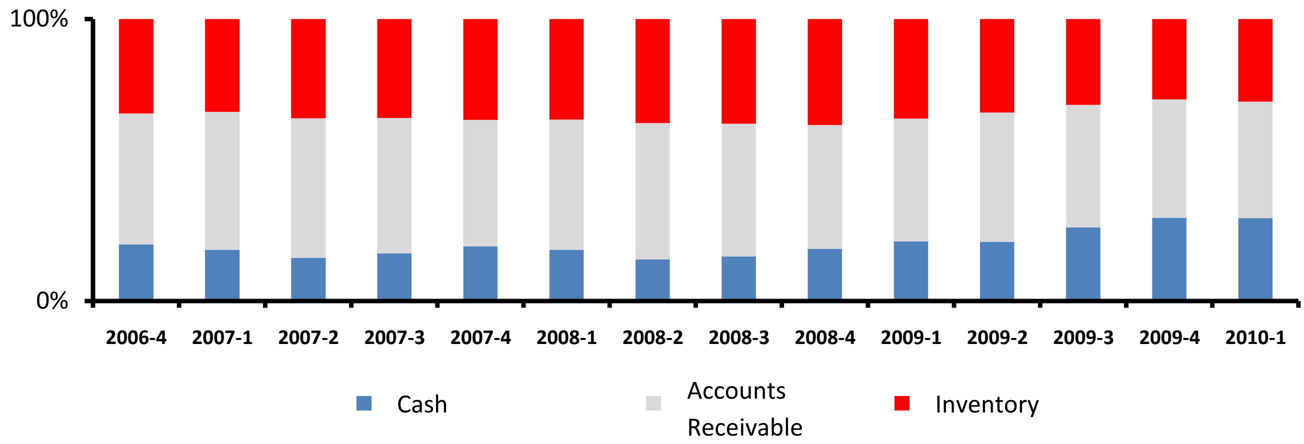
[3] Since the level of total assets of firms did not change considerably between 2007 and 2009, the ratios used were proportioned to total assets. Working capital is defined as the difference between liquid assets and short term foreign funds.

[4] The changes in the ratio of the level of the components of working capital, i.e. cash, inventories, and accounts receivable, to total assets is given in annexed figures.

[5] This phenomenon perpetuates also in world markets, particularly in the US corporate sector. Since 2007, US firms have increased liquid assets by 27% in total and currently keep US$1.84 trillion liquid assets.

Figure 5: Composition of Working Capital (2006-2010)

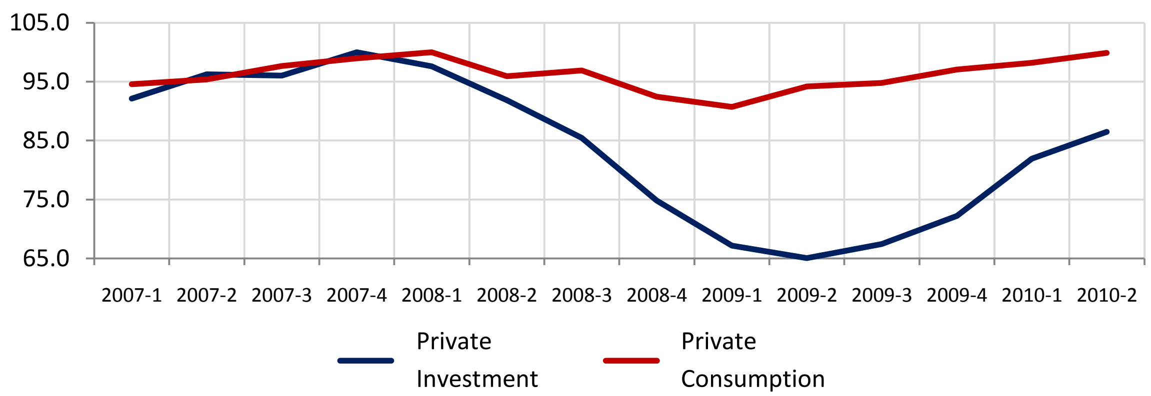


Another striking point is that corporate sector reduced the level of inventories along with the crisis (Figure 5 and Annex: Figure 2). Although it is quite natural that the corporate sector diminished the level of production and depleted inventories in the face of the crisis, the process of recovery is expected to have a positive impact on level of production and inventories. Inventories have increased by 0.51 percent year-on-year in the last quarter of 2008, whereas firms depleted inventories in the following periods (Annex: Figure 2).

Private consumption recovered, investments still stand way below the peak level

Concerning the movements in private consumption and private investment, it can be concluded that the trough of the private investments is quite below that of private consumption. In tandem with this, it is seen that private consumption achieved the pre-crisis level while private investment could not (Figure 6). Even though it is a commonly accepted phenomenon that in times of crisis private consumption does not deteriorate as much as private investment due to factors including compulsory consumption and flight from quality, the recent changes in investment good imports prove that private investments yet are far from recovery.

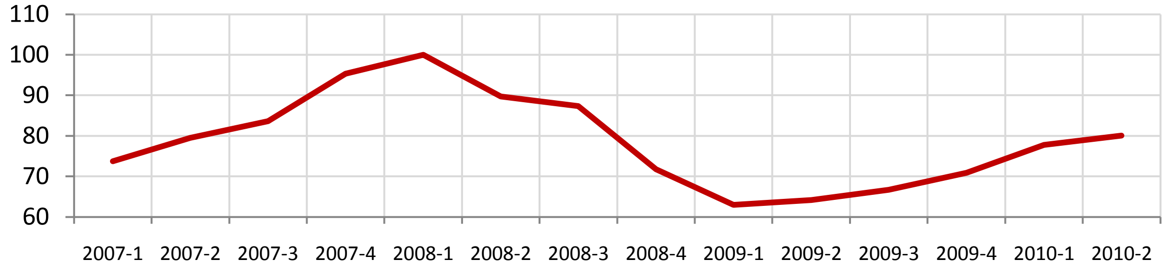
Figure 6: Private Consumption and Private Investment (2007-2010, Index*)



*: Series are net of seasonal effects and indexed to the pre-crisis peak level at 100.

It is known that in Turkey rise in investments is closely associated with the rise in capital goods. In this respect, it is possible to assert that level of investment good imports is a lead indicator for level of investments. In this context, as the impact of the crisis started to be felt, imports of investment goods started to fall by the first quarter of 2008 and showed no sign of recovery by 2010. Level of investment goods imports net of seasonal effects remain quite below the peak level before the crisis (Figure 7)[6].

Figure 7: Import of Investment Goods (2007 -2010, Net of Seasonal Effects, Index*)

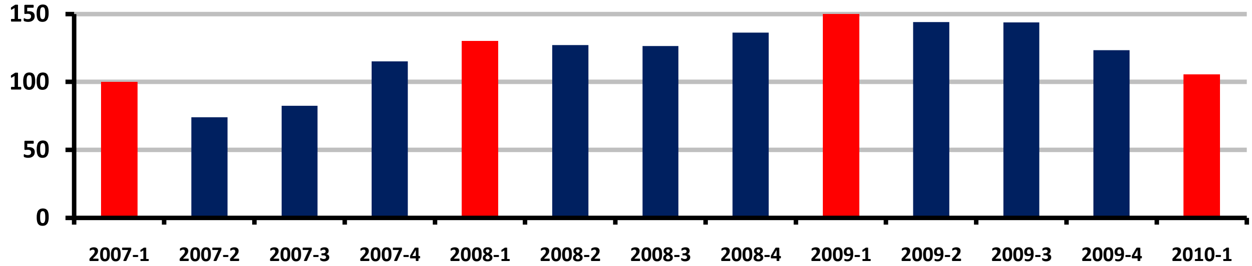


*: The series is indexed to the peak of the series before the crisis, where the peak is 100.

Despite the recovery, corporate sector still demands lower level of financial loans

Poor investment performance in a milieu where interest rates are sufficiently low evokes the question whether large firms, the locomotive of investment, receive financial loans. When the realized financial and commercial loans of firms are examined for the crisis period, it is realized that large forms used more financial loan along with the emergence of the crisis but reduced the use of loans by the last quarter of 2009 (Figure 8). Usage of commercial loans tends to drop along with the crisis and to rise after the crisis though the pre-crisis level is not yet achieved (Figure 9). The drops in the usage of commercial loans reflect the loss of confidence across firms and the reestablishment of confidence. Nonetheless, change in financial debts to rise reflects firms' 'wait and see' policy and reluctance to take risks.

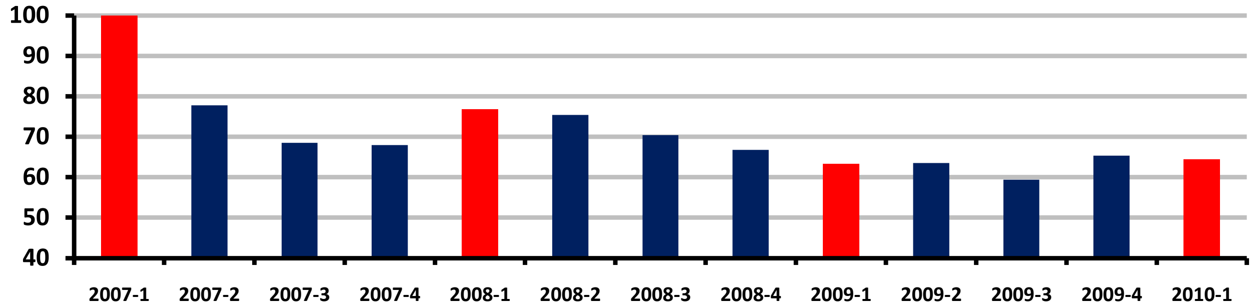
Figure 8: Financial Loans (2006-2010*)



*: The series are indexed to the first quarter of 2007, where 2007Q1 corresponds to 100.

[6] Sub-items of investment goods imports reveal that non-vehicle as well as vehicle imports stand far below the pre-crisis levels, net of seasonal effects.

Figure 9: Commercial Loans (2006-2010*)



*: The series are indexed to the first quarter of 2007, where 2007Q1 corresponds to 100.

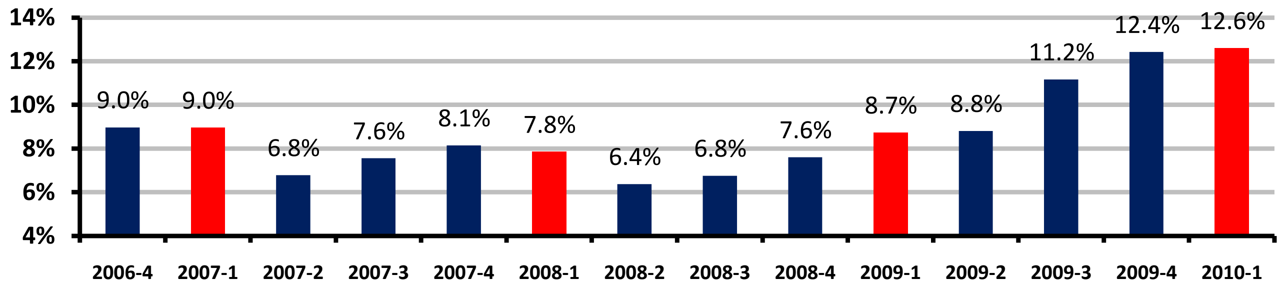
Conclusion:

This policy note analyzed how the corporate sector in Turkey was affected by the crisis and whether a recovery was observed across large firms. Results of the research can be summarized as follows:

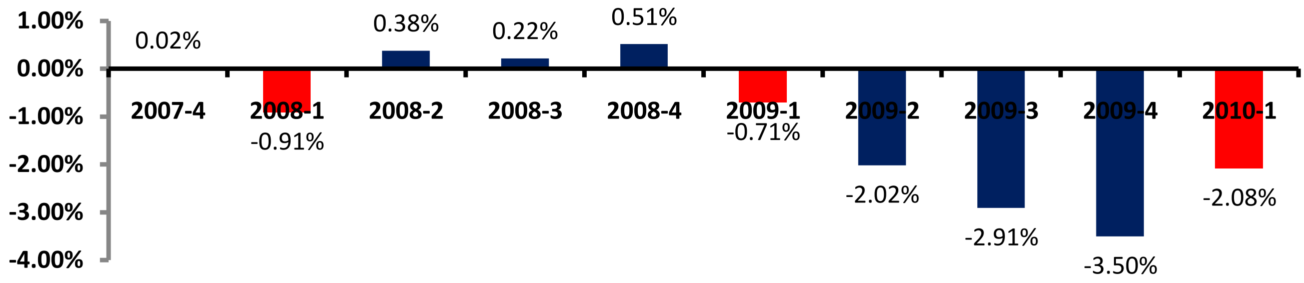
- In the light of the analysis, it is possible to conclude that along with the second quarter of 2008 relatively large firms witnessed the negative effects of the crisis in terms of the falls in profitability and sales revenues, faced drops in working capitals and accumulated inventories at the first instance. With the second half of 2009, firms tended to deplete inventories and raised sales entering a phase of recovery.
- Second, though the recovery has begun for large firms, import of investment goods and private investments still remain low, firms stay liquid and drop their financial debts backing the argument that firms refrain from making new investments and see an uncertain blurry future. Even though firms' holding large amounts of liquidity can be assessed as an opportunity for the next period, the prolongation of this process could prove harmful for the economy.
- When evaluating these results indicating the recovery and caution of the firms, it should also be kept in mind that this reflects only one side of the coin, namely the conditions for large firms. Therefore, it is of critical importance to analyze the impacts of the crisis on small firms.
- Large firms which remain cautious as well as relatively small firms which are expected to be affected more deeply and adversely by the crisis need the removal of uncertainties.

Annex:

Annexed Figure.1: Ratio of Liquid Assets to Total Assets (2006-2010, %)



Annexed Figure.2: Year-on-year Change in the Ratio of Inventories to Total Assets (%)



Annexed Figure.3: Ratio of Accounts Receivable to Total Assets (2006-2010, %)