

ROLE OF ACCESS TO FINANCE IN IMPROVING THE INVESTMENT CLIMATE

Hasan Ersel

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The Role of Investment Climate and Incentives

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DETERMINANTS OF INVESTEMENT

- Expected profitability
- Availability of the technology
- Managerial capability
- Locational factors
- ***Finance constraint...***

HOW FIRMS FINANCE THEIR INVESTMENTS? [1]

I. Asset substitution (Financing without changing the size of the balance sheet)

- 1) Using existing liquid assets (such as government securities portfolio, deposits with banks)
- 2) Changing the composition of its fixed assets (such as selling old equipment or land)

HOW FIRMS FINANCE THEIR INVESTMENTS? [1]

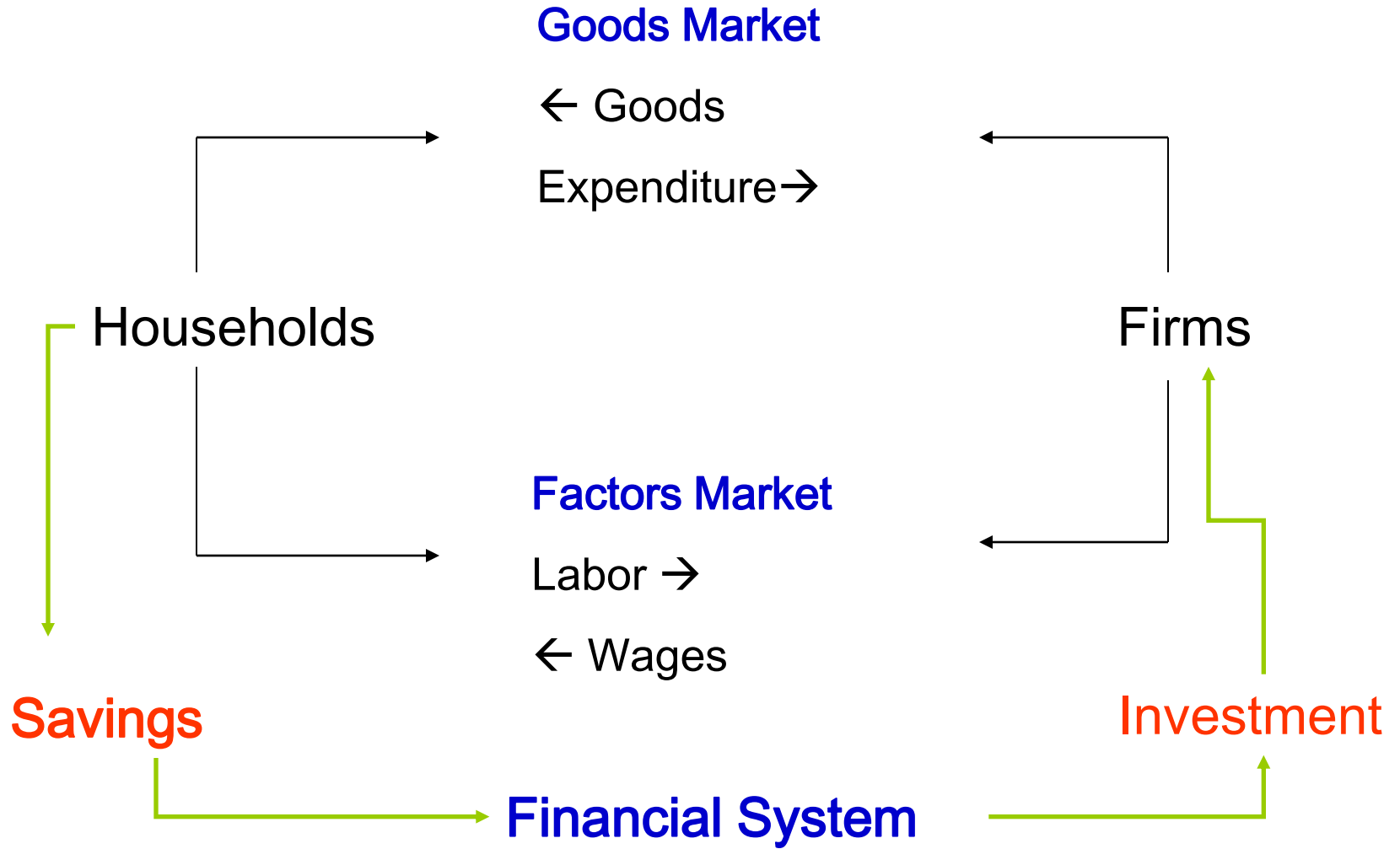
II. Balance Sheet Expansion

- 1) Injection of capital by existing shareholders
- 2) *Increasing equity through initial public offerings (IPOs).***
- 3) Borrowing from stake holders (trade credits, borrowing from shareholders)
- 4) *Borrowing from banks: Bank Credit***
- 5) *Borrowing through securities markets: Selling bonds to public***

ACCESS TO FINANCE

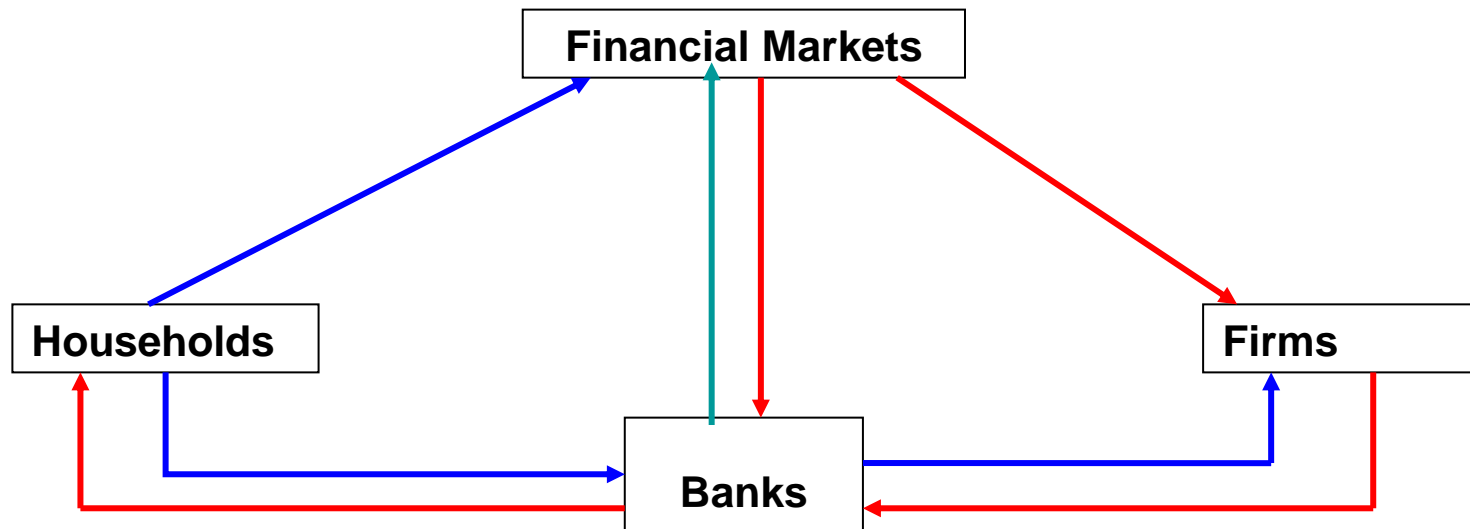
- Firms are, to varying degrees, constrained in all of these forms of finance.
- Existing shareholders financial contributions may not be adequate when the investment projects is sizeable.
- Therefore the financial system's ability to channel financial resources to firms becomes important.

THE ROLE OF THE FINANCIAL SYSTEM



STRUCTURE OF THE FINANCIAL SYSTEM

DIRECT FINANCE



INDIRECT FINANCE

FINANCIAL SYTEM DEVELOPMENT AND THE REAL ECONOMY

- The financial system is not the only way at which firms get access to finance
- A well-functioning financial system, however, enables firms to access finance in a more efficient way.
- Such a system may decrease transaction costs for firms (as well as savers)
- Under competition such an efficiency gain can be expected to translate into lower financing costs.

TURKEY: SOME OBSERVATIONS

- The Turkish financial sector is not a well developed one.
- Bank assets to the GDP ratio in Turkey was only 84% by the end of 2009. Which is well below the figures for financially advanced countries.
- Corporate bond market is almost non existent
- Access to finance through equity finance is limited to relatively large companies.

SOURCE OF FINANCE FOR INVESTMENT IN TURKEY

- Turkish firms rely considerably on internally generated funds in financing their investment (around 50%)
- Bank credit is the second largest source of finance for investment, but it lags behind the first with a considerable margin.
- The rest of the financing needs of firms are obtained from various sources, each individually being insignificant.

FINANCIAL SYSTEM BEHAVIOR

- Note that, the financial sector is small (or even underdeveloped) and imperfectly competitive in most developing countries.
- Financial system may discriminate against corporate sector. It may choose to extend loans to consumers and hold government securities.
- Financial system may also choose to serve a small portion of the firms, such as large ones or those connected with international production chains.
- Therefore the problem is not merely to increase financial savings and establish a financial system.
- What is needed is a financial system which is capable to satisfy the financing needs of the corporate sector as a whole.

ACCESS TO FINANCE: HOW IT CAN BE IMPROVED

- Increase loanable-funds to private sector by reducing public sector borrowing requirements.
- Promote long term saving schemes, such as pension funds, life insurance etc.
- Enforce strict accounting standards and the transparency of the corporate sector.
- Strengthen credit information especially for SMAs.
- Improve legal framework for the functionality of the collateral.
- Enhance the capacity the efficacy of the judiciary system in dealing with financial issues.

Thank You For Your
Attention