

Chapter 1 : Financial Structure and Economic Development : Firm, Industry, and Country Evidence

Demirgüç-Kunt, Feyen, and Levine () discuss the related Global Financial Development Database, which encompasses all the statistics from the Financial Development and Structure dataset, plus several additional series.

Beyond that limit, expanded bank lending or market-based financing no longer adds to real growth. But when it comes to moderating business cycle fluctuations, banks and markets differ considerably in their effects. In normal downturns, healthy banks help to cushion the shock but, when recessions have coincided with financial crises, we find that the impact on GDP has been three times as severe for bank-oriented economies as it has for market-oriented ones. G10, G21, O16, O Banks perform intermediation mostly on their balance sheets. They take in savings typically as deposits and provide funding primarily in the form of loans, often through close relationships with borrowers. Banks can overcome problems arising from asymmetric information and contract enforcement using the knowledge they accumulate through relationships; markets do so by means of contract covenants and the courts. All financial systems combine bank-based and market-based intermediation. But financial structure - the particular blend of the two intermediation channels - varies across countries. In this article, we discuss some of the determinants of financial structure, and how that structure might affect economic growth. The latter question is much debated. Some studies find that both financial intermediaries and markets are important for economic growth Boyd and Smith , Levine and Zervos Others conclude that financial structure per se does not matter: We focus on three issues. We find that financial structure evolves alongside the changing profile of the economy. The second is the link between financial structure and economic growth. We find that banks and markets foster economic growth in a complementary way, but also that there comes a point of negative returns: The third issue relates to the role banks and markets play in moderating business cycle fluctuations. We find that the shock-absorbing function of bank-oriented systems is inhibited when the downturn coincides with a financial crisis. The rest of the article consists of four sections. The first presents the facts and discusses the mix between bank- and market-based intermediation across a range of countries. The second explores the varying linkage between financial structure and economic growth. The third empirically tests the roles banks and markets play in moderating business cycle fluctuations. The concluding section summarises the main results. As a result, empirical analysis of this topic relies on indicators that approximate different aspects of the two intermediation channels Beck et al , Levine Even then, data availability and comparability over time and across countries are an issue. It plots the ratio of bank credit to the sum of bank credit plus total equity and bond market capitalisation as a proxy for the relative importance of banks and markets. The higher this ratio, the more a given financial system relies on banks and, consequently, the less it does on markets. Two broad patterns stand out. First, financial structure differs considerably between countries. Second, financial structure is not static. Market-based intermediation has gained ground over the past two decades. To see this, note that roughly three quarters of the blue diamonds, which represent the ratio for the s, lie above the bars, which represent the ratio for the s. A closer look shows that the bulk of this shift reflects changes in emerging market economies. Financial structure and country characteristics What drives cross-country variability in financial structure? What is the influence of real sector characteristics, such as the level of economic development or the sectoral composition of economic activity? And what is the role of institutional factors such as the legal framework? We discuss these issues by drawing on the literature and on cross-country sectoral information. Generally, market-based financial intermediation tends to increase as per capita GDP rises. One is that the financial literacy of households and firms improves with economic development, lifting demand for services linked to market-traded securities Allen and Gale , Boyd and Smith For instance, insurance companies, pension funds and mutual funds account for a larger share of GDP in richer countries. Another factor may be that more highly developed countries have stronger institutions. In particular, market-based finance benefits from better enforcement of property rights through a stronger legal and judicial framework see discussion below. But differences in financial structure also reflect the sectoral composition of output. Some productive sectors are more likely to rely on bank loans as a source of external funds. By their nature, different lines of business are more suited to different types of

intermediation. Sectors with tangible and transferable capital such as agriculture , as well as those where output is easier to pledge as collateral such as construction , are more amenable to bank debt finance. By contrast, sectors that rely heavily on human capital eg professional services , or those where output is hard to collateralise, will tend to rely more on equity or bonds. Empirical analysis based on a cross section of EU countries confirms this overall pattern see box for details. Firm size also has a bearing on the funding mix. Small firms typically depend on bank finance because of the fixed costs involved in tapping capital markets, not least those associated with the corresponding governance mechanisms. Graph 2 shows the negative correlation between bank dependence and firm size at the sectoral level. The downward slope means that sectors dominated by smaller firms are more bank-dependent. Investors are more likely to part with their money if they feel sure of being able to claim it back. Research on the interactions between law and finance has highlighted a number of regularities. Minority shareholders have more tools, such as the exercise of their voting rights, to protect their interests from actions by management or large shareholders. For their part, creditors find it easier to avoid an automatic stay on assets and enjoy greater priority when their claims are secured and they face managements that have less freedom to seek court protection. By contrast, banks, through their repeated interaction with clients and through their closer screening and monitoring of borrowers, can compensate for the more limited protection offered by French civil law frameworks. Firms in common law countries tend to rely more on traded equity and have a more diffuse shareholder base than firms in countries that follow the French civil law tradition magenta and blue bars in Graph 3. As shown by the yellow bars in Graph 3 , common law countries tend to have more developed financial systems than countries with legal systems based on French civil law.

Banks, markets and economic growth What is the relationship between financial structure and economic growth? The literature suggests that both bank- and market-based intermediation are positively linked with output growth. This suggests that the services provided by financial markets become comparatively more important as countries grow. In a similar vein, Cecchetti and Kharroubi examine how the size of the financial system affects productivity growth. They conclude that, at low levels, a larger financial system goes hand in hand with higher productivity growth. But there comes a point where larger financial activity is associated with lower growth. Law and Singh find a similar effect in the relationship between GDP growth and the size of the financial sector. Is there a link between the sectoral composition of an economy and its financial structure? We construct an index of the importance of bank funding relative to other forms of financing equity and bonds using information from the BACH database on the funding of non-financial firms. This database covers 17 sectors in nine European countries. The index is defined as: Both the numerator and denominator are averages over the period , weighing yearly figures by sectoral gross value added. Unfortunately, it is not possible to disentangle control stakes from other equity financing raised on the market. As a result, the denominator includes total equity, together with bonds and bank loans, but excludes trade credit and provisions. Graph A shows the average bank funding ratio for three different groups of countries: Regression analysis can help identify how far specific sectors tend to depend more on bank loans than others do. A simple model for the bank funding index is specified as: Table A reports the regression results. Finally, once differences in sectoral composition are taken into account, there are no significant differences in the results across groups of countries within the sample. The coefficients on the sectoral dummies provide additional interesting results. Innovative sectors, such as "Professional, scientific and technical activities" sector M and "Information and communication" sector J , rely less on bank funding, while sectors where firms are typically smaller, such as "Accommodation and food service activities" sector I and "Administrative and support service activities" sector N , rely on it more. We revisit these issues using a panel of 41 advanced and emerging market economies during the period We augment the statistical model of Beck and Levine , which estimates the effect of stock market and banking sector development on economic growth, by allowing for this impact to change with the level of financial deepening. Our benchmark statistical model follows Beck and Levine , Table 4: The key variables are the two indicators of financial structure: $B_{i,t}$, defined as the logarithm of the ratio of bank credit to GDP; and $M_{i,t}$, which indicates the logarithm of the turnover ratio, ie the ratio of the value of total shares traded to average market capitalisation. In contrast to other findings in the literature, a higher ratio of bank credit to GDP does not go hand in hand with higher economic

growth. This difference might reflect the fact that these findings are based on earlier data samples or on a somewhat different set of countries that includes a lower proportion of advanced economies. We next modify the equation by allowing non-linear quadratic terms for both bank credit and the turnover ratio. In particular, we have: The results of the non-linear specification in the second column of Table 1 indicate that increases in both bank and market activity are associated with higher growth, but only up to a certain point. Both indicators are statistically significant, suggesting that banks and financial markets provide different services and are complementary. The limits of financial deepening on growth are more clearly depicted in Graph 4. Growth benefits from a higher ratio of bank credit to GDP until the logarithm of the ratio reaches 3. The corresponding peak for the logarithm of turnover ratio is 4. We also report on the horizontal axis the average values of the two ratios bank credit and turnover over the period for the advanced and emerging market economies in our data. Emerging market economies have, as a group, an average ratio of bank credit to GDP that is approximately equal to the value that corresponds to the peak of the relationship with growth 3. Taken at face value, these estimates suggest that in EMEs further market deepening would boost GDP growth while any gains from further development of the banking sector would be limited. Both indicators at 4.

Chapter 2 : Financial Development and Structure | Data Catalog

Empirical model. The view of new structuralism anticipates that banks are the main institutions in the financial system during the early stages of economic development, while in advanced stages the financial system has a market-based structure.

Chapter 3 : Financial, Capital Structures impact Owner Lender Risks Profits

For most companies, financial structure and capital structure change by small amounts more or less continuously. They change because the values of several structural components may be relatively fluid from period to period: short-term liabilities, long-term liabilities, and even retained earnings, for instance.

Chapter 4 : Financial structure and growth

FINANCIAL STRUCTURE AND DEVELOPMENT AS A SUBJECT FOR INTERNATIONAL COMPARATIVE STUDY RAYMOND W. GOLDSMITH National Bureau of Economic Research It is the purpose of this memorandum:1 first, to argue that comparative.

Chapter 5 : Financial structure and economic development in Africa : some evidence (Book,) [calendrierde

Financial Structure and Economic Database (Beck et al.,) DEVELOP A dummy variable that takes the value of 1 if the country is a financially developed economy, and 0 otherwise. A country has.

Chapter 6 : Financial Structure and Development: R W Goldsmith: calendrierdelascience.com: Books

Abstract The authors explore the relationship between financial structure - the degree to which a financial system is market- or bank-based - and economic development.

Chapter 7 : Financial Structure and Economic Development : A Reassessment

August A country's level of financial development and the legal environment in which financial intermediaries and markets operate critically influence economic development.

Chapter 8 : Financial Structure Database

Financial structure and country characteristics What drives cross-country variability in financial structure? What is the influence of real sector characteristics, such as the level of economic development or the sectoral composition of economic activity?

Chapter 9 : Goldsmith, R. W., (), Financial Structure and Development. New Haven: Yale University Press.

financial development is important for economic development, but financial structure, per se, will not add much to our understanding of the process of economic development. 4.