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STOCK FINANCING AS AN ALTERNATIVE FINANCING TECHNIQUE AND ITS APPLICABILITY IN TURKEY

Abstract:

Banks are important institutions that finance economies by collecting deposits and lending those deposits as creditors. Today, most of the businesses that need funding sources primarily apply to the banks for receiving loan. Loans provided by banks are classified according to the nature of the loans and the cost of each varies according to their attributes. The important thing is for businesses using the most appropriate loan with the least cost.
The concept of "stock financing" which is often heard recently emerges as an alternative financing technique. Here the main aim is minimizing the cost of seeking new funds and trying to find new funds at the financial value of current inventories of business. In this respect in the study the applicability of stock financing techniques, appearing very attractive for business, in Turkey are discussed.

Keywords:

Inventory Management, Stock Financing, Banking, Loan

JEL Classification: G21, G32

1. Introduction

The main objective of the company is maximizing the net present value of the firm by managing the assets in the way of contributing the visions of the company instead of getting most profit. In this respect, determining the appropriate funding sources and optimum resource allocation have great importance for firms (Seyhan, 2010, p. 4). Equity financing and debt financing are the types of resource allocation.

Equity financing is the funding source method gained from retained earnings created within the firm or issuance of shares provided externally. Short, medium, long term loans from banks are the most preferred form of funding through borrowing for firms (Önuçak, 2009, p. 17). In the study, it is mentioned first that debt financing that is bank loans which is used mostly by firms, then information is given about stock management and the current situation in Turkey is evaluated.

2. Bank Loans

Today, companies provide funding sources from various ways such as bank loans, bonds, commercial paper issuance, commercial loans, leasing and derivative instruments. The most readily available and most commonly used sources of borrowing are bank loans (Önuçak, 2009, p. 20).

Banks collects money from various ways and lends this money to loanee under the rules within determined credit limits or by using their reputation, banks make a commitment in customers' favor. Then, they collect receivable at due date and lends to other loanees (Parasız, 2005, p.220).

Bank loans are also defined as the limits or opportunities like providing assurance or guarantee or credit against security or unsecured credit to legal persons as a result of some examination of loanee by considering its own resources and rules also bank laws (Parasız, 2005, p. 219).

In concept of credit, there are three main elements as time, trust and risk (Nezih, 1999, p. 9). In order to get back lent money and the prestige provided to customer, time is considered as one of these elements. Extension of the terms means increased uncertainty so this increases risk. Because cash, goods, bail or credit given in any case have to be taken after given time, there must be also trust element. Here risk means the sum of all potential threats that can be occur in the fulfillment of the commitment which is the subject of guarantee and for the receiving the lent money (Oyakbank, 2005, p.2).

The reasons why firms use credits are as follows (Yıldırım, 2007, p.37):

- The quick growing rate of the firms. Thus, the companies' receivables, inventories, currents and values will increase then they will need to finance the company.
- Making loss or insufficient profit. Making loss leads to decrease in net working capital.

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- Funding the investment in fixed asset with short term funds.
- Seasonal mobility. Financing needs of the firms' increases when their operations are in recession and the needs of funding decreases when inventories are sold and receivables are collected.
- Speculative purposes (speculation)
- Payment of a current debt.
- Fulfillment of capital commitment. If the firm has joined to another firm's capital, fulfillment of the obligations towards a partnership.
- Financing to purchase desired assets.

These are the reasons why firms demand for loans also credit managers and economic analyst want to find the answer of some questions while examining loanee (Rose, 1991, p. 208):

- Does loaner have credit worthiness?
- Does the requested loan appropriate to bank's credit policy and the bank's protection measures?
- Does the customer have solvency or does the repayment of the loan possible?

It can be understood from these questions about evaluating loanee carefully, safe collateralization, appropriate pricing and regional analysis are the important points for risk mitigation in terms of banks (Uyar, 2003, p.23).

3. Stock Financing

Stocks are the most important current assets of the companies that can be the security for the short term loans of the banks. Banks that accept the stocks as assurance, guarantee with the concept of "bank loans in exchange stock guarantee" know that in case repayment of the loans is impossible, it is possible to liquidate the stocks by selling them with their market value or book value. Therefore, not any kind of stock gives guarantee. Stocks must be easily sold, easily stored and their prices should be stable (Gürsoy, 2012, p. 384,385).

Here is the important thing is where the inventories will be kept and who will supervise them. The first method applied in this regard, the stocks in the firms' warehouse is pledged to the bank. In this case, borrower can sell the stocks whenever he want but the sale proceeds must be banked with its accrued interest. The second method is delivering the stocks to reliable third parties. Another method is the inventory control is under the bank and when the stocks are sold, credit can be easily repaid to bank. Generally for this types of loans the interest rate is higher when compared with unsecured loans. Also insurance costs and storage costs belong to the borrower firm (Gürsoy, 2012, p. 384-385).

Because the costs and the interest rates is higher in the "bank loan in exchange stock assurance" method most firms do not prefer this method, another method similar to this method is stock financing. As a result of information obtained from the bank used this stock financing system in Turkey, this method is a new collateral model to be allocated to automotive dealers in the context of direct debiting system (DDS) of banks with a certain credit limits. With this method it is aimed that for payments of automotive dealers to be made to parent company, provision of cost-effective and easy availability of credit in exchange for the stock of vehicles.

The general functioning of stock financing system is as follows:

- Dealer makes an order for vehicles to parent company.
- Bank sends the costs of vehicles to accounts of parent company within the DDS limits of dealers.
- Parent company sends technical documentation of vehicles to bank.
- Dealer pay off a loan within its term.

Stock financing has significant advantages in terms of banks, parent company and dealers. The advantages for the banks can be summarized as follows:

- Expansion of product range.
- New customer acquisition.
- Deepening the relations with existing customers and providing continuity.
- Structured and low risky lending facility.
- Ensuring the increased working productivity.

The advantages for parent company are as follows:

- Minimizing the risk of receivables
- Accelerating the cash flows
- Monitoring and reporting facility on the system
- Increasing the sales by ensuring easiness to dealers who need funding sources

And the system provides advantages in terms of dealers:

- Meeting the working capital needs with structured and the practical credit facilities
- Accelerating cash flows
- Providing monitoring, reporting and loan demand opportunity on the system.

4. The Applicability of Stock Financing System in Turkey

In general automotive industry is defined as the sector reaching the raw materials and sub industry automotive products to customers and generating the large volume of business and employment in the marketing, dealer, service, fuel, finance and insurance sectors that contributes the automotive industry operations. Thus, this industry has an important role in the development of society.

However, this sector that has an important role in the national economy is one of the most affected sectors by the crisis in Turkey. Especially, during the crisis period dealers strive to survive with the selling pressure and they encounter financing problem just because extension of stock status. An automotive dealership has summed up the problem they faced during the crisis as: “When we take the car from manufacturer firm, we have to sell in approximately 21 days. Manufacturer supports this time in exchange for the guarantee letter. However, when prolonged period of time, we finance the stocks with the loan borrowed by banks. In the past time limit was enough but today our term of sale period almost doubled so our need of funding sources has increased" (www.yonetimhaber.com).

Stock Financing Technique is the alternative financing technique for this industry which is either very important industry for economic development or affected from economic situation very much. In Turkey, there are regulations just for automotive industry and some examples for this technique are as: first, Garanti Bank specially developed this stock financing technique for Mercedes. Therefore, when inventory turnover rate has decreased, this method provide cost-effective way of credit in the electronic environment in exchange for vehicles in their stocks for Turkish dealers in the payments of vehicles of Mercedes- Benz. According to the bank, with this method Mercedes will minimize the risk of receivables and decrease operational responsibilities and in terms of dealers their needs of working capital will decrease. With this application, Garanti Bank was awarded "Best Practice and Innovation" in 2009 in International Treasury Today Adam Smith Award in the category of working capital management.

Another example for this method is the agreement between Turkish Economy Bank (TEB) and Toyota. According to this agreement, a contract regulating the transactions between Toyota Parent Company and TEB has been signed. The dealers who want to benefit from stock financing will be customers and a number of documents specified by bank and general loan agreement are signed. The unlicensed vehicles received from parent company are hold in pledge by banks. These vehicles are considered as warrant and dealers can use loan. Also in Turkey, Akbank and ING Bank have some applications related to stock financing.

4. Conclusion

Since providing funding sources is not so easy and is expensive in today's conditions, it is fact that the biggest obstacle for businesses to carry out their activities is inadequacy of financing management. Especially the biggest problem for borrowing loan is inadequacy of guarantee. Such a situation businesses are directed to alternative financing methods. Since the beginnings of 2000's, stock financing method is one of these alternative financing techniques.

An inventory which will be the subject of stock financing must have these features. It must not be obsolete, must preserves price stability and be the non-perishable goods.

For this reason in Turkey, this method is only applicable for automotive industry. With this stock financing technique which is very important for automotive industry, dealers can use loans from banks for the goods which have not sold to customers yet.

Although it seems as there is no problem to apply this method in Turkey, since application of this method is limited just with automotive industry it shows that stock financing method remains barren. However if this method is tried to apply in other industries like durable consumer goods, it contributes both the development of the industry and also economic condition of the country. Thus, in Turkey it is necessary that searching the industries in which stock financing technique is applicable, conducting more studies about this method and correcting the short comings of the method.

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