

FINANCING OVERSEAS : A LOGICAL ALTERNATIVE

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Introduction

The integration and associated globalization of the capital market has opened up a vast array of new sources and forms of corporate financing. In general, today's corporate treasurers of large domestic as well as multinational corporations can access foreign capital markets as easily as their own home markets. International means of raising capital include stocks, bonds, parallel loans between corporations, credit swaps between banks and corporations, and loans from host governments and development banks, among others.

All in all, though, Korean corporations have limited means to finance overseas. The main methods for financing overseas are public loans, commercial loans, international leasing, stock and bond issuing, and foreign spot market financing. However, these types of financing are regulated by the government. On July 7,

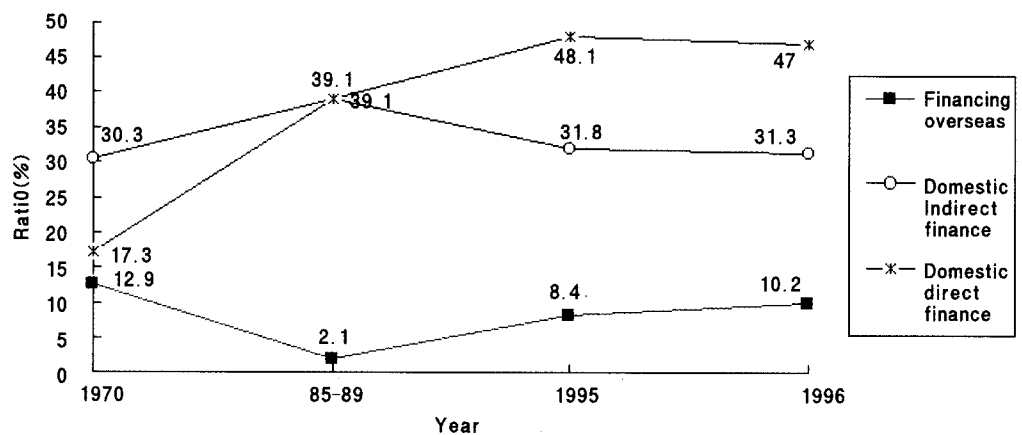
1997, the Federation of Korean Industries (FKI) said that it had asked the Government not to interfere in the individual financial restructuring of each corporation. It also asked the government to cultivate a "responsible management system" in domestic financial institution, to energize the stock market, to allow different loan interest rates reflecting firm's creditworthiness, and to change the overlapping credit guarantee system.

Three months have passed since the domestic banks reached an agreement to protect financially-ailing conglomerates (for example, Jinro), but only now have they seemingly reached a conclusion on its actual implementation. Some economists have negative views on this, insisting that the artificial anti-bankruptcy device runs directly counter to free market principles. Regardless of what problems this anti-bankruptcy device may have, the basic task lying before corporations is how to revise their financial structures of their own accord.

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〈Figure 1〉 Korean Corporations' Financing Structure



This antibankruptcy device is not enough to solve corporate financial difficulties completely. Therefore, financing overseas can be considered as one of many methods to improve one's corporate financial condition.

Korean Corporations' Financing Overseas

As already mentioned above, Korean corporations have limited methods of financing overseas, which is controlled by the government. Even though corporations were trying to recover their financial health, they could not borrow overseas freely.

There is an interesting report related to government intervention in the economy. The World Bank's annual World Development report, released in June 1997, has one central point: that an effective state is essential for a prosperous economy. For half a century the state has been the dominant force in most of the world's poorer countries. Governments have owned factories, run banks, built protectionist barriers, allocated foreign exchange and woven

great webs of regulatory red tape-mainly with disastrous results. Bloated budget deficits, high inflation, stagnant growth and rampant corruption were the hallmarks of incompetent bureaucrats trying to usurp the market. The counter-trend of recent years has been to reduce the role of government. Market-based reform-budget balancing, privatization, trade liberalization and so forth seems to be the fastest way to discipline profligate and overweening states. The role of government in a market-oriented economy should be decreased to a minimal level. Deregulation of financing overseas will be good for corporations that needs a low cost of borrowing.

Fortunately, a government official recently announced that "Korean firms, which currently have to obtain prior approval in issuing overseas securities, will be only required that they report to related officials after the issuance." In addition, the strict qualifications on overseas bond issuance, such as paid-in capital, net profits and good credit ratings, will be sharply eased or totally abolished. In 1996, Korean corporations used overseas financing for only 10.2% of their

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<Table-1> Corporate Financing in Japan, Germany, the United Kingdom and the United States¹ in 1993

	Japan	Germany	U.K. ²	(Percent of total) U.S.
		All non-financial corporation		
Depreciation charges	61.2	84.4	35.2	64.4
Retained earnings	0.2	-4.0	17.2	18.9
Internal sources	61.4	80.4	52.4	83.2
Equity issues	7.6	1.5	18.7	2.1
Bond issues	3.9	n.a.	16.2	14.7
Bank borrowing	37.1	18.1	4.8	-4.1
Other sources ³	-10.0	n.a.	7.9	4.0
Total	100	100	100	100

Notes: 1. Based on balance sheets and income statements of representative samples of companies
 2. 1990 figures
 3. Including borrowing from affiliate companies, trade credit and accounts payable

Sources: Calculated from OECD Financial Statistics, Non-financial enterprise financial statements, 1994

total borrowing. The percentage of financing abroad seems to be too low and should be increased. Let us compare this with other corporations in developed countries.

Corporate Finance in Developed Countries

The patterns of corporate finance in four developed countries have been portrayed in Tables 1 and 2. Table 1 shows the sources of financing for representative samples of firms in the non-financial sectors of the four countries. What is immediately apparent is that most investment is financed with internally generated funds, in the form of depreciation allowances and retained earnings. This implies that external finance is costly because of information asymmetries of various sorts.

Table 2 gives data on the capital structure of non-financial corporations in the four countries and shows the contribution of equity and various types of debt in total liabilities (equity plus debt). Here the differences seem to be more marked and the major role played by Japanese and German banks in lending to non-financial corporations is clearly revealed. Conversely, in both Germany and Japan, equity is low compared with the positions in the U.S. and the

U.K., while bonds and short-term securities are a relatively insignificant source of funding capital holdings.

Conclusion

Capital financing decisions by firms obviously reflect a wide variety of historical/institutional/economic factors, and it would be wrong to attribute all of the differences to one or two factors. Investment by corporations in developed countries is mainly financed with internally generated funds, in the form of depreciation allowances and retained earnings. This implies that external finance is costly because of information asymmetries of various sorts. However, it is inevitable for Korean corporations to finance abroad since there is always over-demand in the Korean financial market. Therefore, regulations on financing abroad should be loosened so that Korean corporations can find financing at low cost.

The globalization of capital market has opened up wide variety of new sources of corporate financing. Korean corporations should be able to access foreign capital markets easily and borrow low-cost funds, with the ultimate aim of enhancing their international competitiveness. **VIP**

"It is inevitable for Korean corporations to finance abroad since there is always over-demand in the Korean financial market."

〈Table-2〉 Capital Structure of Non-financial Corporations in Japan, Germany, United Kingdom and United States, 1991

	Japan	Germany	U.K.	U.S.
Equity	20.1	26.3	48.4	53.4
Bonds	4.5	2.4	n.a.	15.7
Short-term securities	n.a.	-	n.a.	1.3
Bank loans	38.1	42.9	12.1	7.5
Other loans	2.5	2.8	n.a.	6.1
Trade debt	28.9	n.a.	8.7	9.2
Other	5.9	25.6	30.8	6.8

Sources: OECD Non-financial Enterprise Financial Statements, 1991