

## summary

### **Financial sector development in Egypt And its effect on Corporate finance.**

A recent and expanded literature established the importance of financial development for economic growth, through mobilizing savings, allocating capital and transforming risks. The diversity of this sector, (banks, securities market and a range of other types of intermediary and ancillary financial firms) also contribute to balance financial development for the firms. Therefore policymakers around the world through last two decades made financial strengthening to build deeper and sophisticate financial system. Most of the developing countries started to apply financial reform and became more liberalize, to be able to integrate with international financial system.

Egyptian Financial sector, suffered from several financial repression policies throughout the 1960s and even after the (opening up) period after 1974 until the end of eighties. These policies affected the function of this sector to mobilize savings and channel them into productive activities. Since 1990 Egypt has been started an economic reform program. The program is designed to transform the Egyptian economy to one dominated by the private sector through macroeconomic structural adjustment and financial stability

Therefore the last decade, the Egyptian financial sector has witnessed several changes affected not only its size, activity, and efficiency but also its structure. During this period, the stock market and other financial institutions have gained relative importance.

The main target of this paper is examine the effect of financial sector development on the firm financial decision, to determine if the firms' reliance on internal funds for investment or decreased with financial reform and liberalization of the financial sector. Reaching to this target we must , firstly, reviewing the main government policies towards financial markets in the last two decades through the financial reform program and its liberalization policies. Secondly describing the developments in Egyptian financial markets to investigate the changes and progress in the banking sector and in various types of capital Markets (bond, stock, pension and insurance markets) during the same period. This is done by evaluating changes in financial markets size, activity, and efficiency. Finally examine the effect of these changes at firm level

**Methodology:** The paper will use the most common financial indicators which reflect changes in financial market size, activity, and efficiency . Econometric approach will be used to estimates and tests the effect of these changes at firm level, the sample consisted of 20 firms that are listed in the stock market and for which quarterly balance sheet and financial statement data for the period 1996-2002 are available and complete. We will use both the OLS- WLS (Weghited least squares) methodology, we will apply the panel structure of our data to take advantage of this method and overcome the lack of data due to the short period.

The paper was arranged as follows:

section one is the introduction, section tow discusses the macroeconomic development of financial sector. First reviewing financial policies over the last two

decades, in the second part of this section we will examine the changes and progress in the banking sector and in various types of capital markets (bond, stock, and insurance markets) during the same period. This is done by evaluating changes in financial markets size, activity, and efficiency to determine the effect of these reform on the financial sector.

Section three discusses the effect of the financial structure change at the firm level. in the first part of this section we provide a brief survey of the literature about the main categories of sources to finance the investment according to the theories of corporate finance, and the most recent applied literature which investigate the effect of the financial sector development on the firm investment decision. The second Part is the empirical evidence, will examine how financial development at macro level, has affected the investment sources of the firm, we would like to test whether as the result of the financial sector development in 1990s firms are less dependent on their internal resources and balance sheet composition. so we will also examine the effects of the changes in the banking sector ,stock market on the investment decision of the firm. Finally, the results and conclusion.

The paper was concluded to the following:

Since the 1991, Egypt has embarked on economic reform and structural adjustment program. The aim was to restore macroeconomic stability, restructuring the economy and enable it to face the challenge of global integration of financial market. The reforms of the financial sector were reflected in the removal of most regulation affected the banking sector, consistent with the logic of market liberalization . Similarly, several reforms allowed the development of other capital markets such as insurance, bond, and stock markets to complement its other efforts.

The financial structure have several changes since the economic reform and the liberalization policy ,the indicators of size , activity and efficiency improved .the stock market started to take relative importance since the mid of nineties but, the efficiency of the banking sector and stock market compared by the average of the world is very low. Concerning to the other financial institutions their size and activity increased but still relatively small comparing with the average of the world. .Therefore we can classify Egyptian financial structure as underdeveloped.

According to  $q$  theory of investment , in the absences of financial restriction , firm investment depends on the ( $q$  ratio) or the  $q$  value of the firm , which equal to the market value of the firm .

when the firm faces constraints on external finance its investment will be determine by its internal resources .

The degree of leverage of the firm ( debt to capital ratio) also depend on the development of the financial sector and its structure . When the firm face imperfect financial market this ratio decline and deter the availability of external finance, even after controlling the  $q$  value .

The results for the first model test whether, as a result of financial development experienced in 1990s, firms are less depended on their internal resources and balance sheet composition and more responsive to Their Tobin's  $q$  -value, by applied the common coefficient approach, reveal that the constant term is significant at a high level of significant, the investment does not significantly depend on the firms  $q$ -value at 95%but we can accept it at 90% , so it is week significant ,but the

investment is driven positively and highly significant by cash flow and negatively by its level of indebtedness . This conclusion However, does not apply equally to all firms , when we applied the approach of cross-section specific coefficient, little firms are response to it's q- value, such as Eastern company, Baken ,Cement of Alexandria and Cairo for housing. The estimated results of the second model after we add the macro financial variable. The private credit ratio has an independent and significantly effect on the firm investment and also the effect of macro level appears to work through micro economic channels, that is by making the firms investment more responsive to the q- value of the firm and less constrained on the use of external finance. The variable (cap) of stock market capitalization has a negative singe and insignificant . we can conclude that although the development of the financial sector especially the banking sector ,the firms still realize on their internal finance.