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Investment and Development Banking and Its Development in Turkey

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Abstract

Banks, one of the most significant economic means of the nations and international organizations, have occasionally become one of the institutions mostly affected by the financial crisis in the world. Especially in the economies of the developed countries, one of the most important aspects of the financial sector is measured by the size of the financial resources and assets of the banks. The size and place of the investment banks depends on the investment and existing credit reserves appropriated by its members. From this perspective, scrutinizing the Investment and Developments Banks, which is one of the economic growth criteria, is of high importance. To this end, in addition to the operation of the Investment and Development Banks, financial products of these banks in Turkey are also analyzed in this study.

Keywords: Investment and development banking; economic development; Turkish banking sector

1. Introduction

When one looks at the functions of banking in modern world, three types of functions are observed. These are total deposit, credit marketing and the effective distribution of resources. Because the Central Banks in the countries remain the “Bank of the Banks”, they incorporate investment banks within their bodies.

The banks, in practice are classified as Central Banks, trade banks (deposit banks), development banks and investment banks. The responsibilities of Central banks in each country are to control monetary supply and to ensure price stability in the economy. The Central Bank in our country works for that purpose. Investment and Development Banks also conduct activities in parallel with this objective. Mishkin, 1992: 78-88; Mishkin, 2004: 330-337; Grinblatt and Titman, 2002: 4-22; Hubbard, 2002: 52-66; Peter and Marguis; 2005: 45-72)

In narrow terms, the banks can be defined to be the institutions and firms that initiate the stocks and shares of the state agencies and private firms, give guarantee to them and that provide their circulation. In broader terms, investment banking covers all transactions and organizations which comprise capital formations, including the transfer of existing assets and circulation of shares and debenture bonds (Trescott, 1965: 88-102; Grinblatt and Titman, 2002: 4-22; Heffernan, 2005: 18-22).

The activities of today’s investment banking in developed countries are comprised of a range of quite heterogeneous and sophisticated activities such as underwriting (mediation to the public offerings of stocks and shares, financial guarantee), consultancy services, commerce, brokering and asset management. Nevertheless, undertaking and consultancy activities, conventional or “Core Bank” transactions are also considered to be one of the functions of

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investment banking. An investment bank that conducts underwriting services by means of exporting stocks and shares from financial markets constitutes a fund and provides assistance to the firms. In this study, the aim is to put forward the data about the functions of the investment and development banks and the operation and progress of these banks in Turkey and in the world. Hubbard, 2002: 52-66; Peter and Marguis; 2005: 45-72).

2. Investment Banking and Their Progress in the World.

It is rather difficult to make a single definition of investment banks. The definition of investment bank in the industrialized countries is different from that in the developing countries. The use of capital acquisition and funds is more oriented towards real sector, which brings about employment. On the other hand, we can define investment banks with regard to economic situation of the developing countries. Since it is not possible to ascertain whether the investment banks have a legal scope or not, the financial agencies in this group are interpreted as organizations active in the areas which decline deposits and are beyond the scope of development banks. (Randolph P. Beatty and Jay R. Ritter, 1986:213-232; Smith, 1986: 3-29; Chemmanur and Fulghieri, 1994: 57-79; Dugar and Nathan, 1995: 131-160).

When its literature in the developed countries is examined, the main activities of investment banks are found to be; (i) underwriting and consultancy services, (ii) trading and brokerage, most of which constitute a heterogeneous set, (iii) asset management (conventional and alternative). With the use of underwriting services, an investment bank exports securities to financial markets and helps funding companies. They also help those companies use their assets in order to solve their loan problem. This process is labeled to be "securitization" and the securities it exports are called "asset backed securities" (ABS). It is a fact that in the recent years they have increased the value of loans securiticized by several trade banks and triggered the "core-holding" model in trading banking activities (giving credits to banks and hold these credits in their own balance sheet.). This occurs as a "core-distributable" model (providing credits from banks through securitization and then sell them in the market). (Ashcraff and Schuermann, 2006: 191-209; Smith, 1986: 3-29; Chemmanur and Fulghieri, 1994: 57-79; Dugar and Nathan, 1995: 131- 160).

Trade and investment banks still have two different types in functioning. These are; core-distributive trade banking and investment banking that provides underwriting services. The fact is that investment banks help the companies going for capital increase, but not those standing on debt position. Here, the amount of credit that the securities debtor pays the trade company is not certain. Investment banks may demand syndication credits for their customers. It might be risky that the syndication credit is provided by a single bank. The credit is provided to the investor from the credit pool established by several banks collectively. Investment banks are thought to be the ideal for such functions. (Randolph P. Beatty and Jay R. Ritter, 1986:213-232; Smith, 1986: 3-29).

Investment banks also reestablish companies institutionally through mergers or purchases. Similarly, investment banks were functions realized to reestablish problematic railways in the nineteenth century. Thus, they provided consultancy services to help customer companies. Being an investment bank is to buy securities and then sell them to the final investors. In the eighteenth century, the main security was acquired from debenture bonds exported by governments. Chemmanur and Fulghieri, 1994: 57-79; Dugar and Nathan, 1995: 131- 160).

Investment banking cannot be classified as a commercial bank in terms of "deposits and credits". The efficiency of banking activities cannot be defined in a short period of time. In other terms, commercial banks work only in the form of time deposit. Money is mainly provided to families (to purchase cars, houses etc.) and companies (to finance personnel, new installations and equipment). As commercial banks are often financed by deposit, they are sometimes called "institutions for deposit". Commercial banking is slightly more complex compared to investment banks. Transactions for all credit types executed by the banks are unlimited in many ways (except for gathering money and deposits). In addition to this, the main commercial banking activities are deposits and credits. Any type of non-commercial investment banking might have been defined within the scope of banking. Different commercial banking, investment banking activities can be classified into three groups and embrace a rather heterogeneous structure. These are;

- *Core or more dividable conventional investment banking, comprised of functions such as (a) companies and financial markets helping other companies and (b)underwriting services, mergers, purchases, rearrangement of debts etc., which help consultancy* services and capital increase .
- *Trading and brokerage: Transactions of the bank to buy or sell securities using money (registered trade) or in the name of their customers (brokerage).*

- *Asset management: This can be divided into two groups: (a) conventional asset management (e.g. open-ended investment funds) and (b) real estate funds, hedge funds, private capital funds and other investment tools. These are alternative asset management and alternative asset forms.*

Generalized globalization theory has an increasingly growing, productive width of area. In this area, academicians, businessman mentors, politicians, supervisors and other groups make their decisions on business activities and execute them. Generalized globalization theory, beyond academic thinking, is discussed to represent a potentially effective rhetoric. If on the international area, business has provided strong evidence in management consultancy and investment banking areas. As business areas have become globalized, there are strong similarities between academic globalization theorists in terms of meaning. Senior executives of transnational corporations have a more clear understanding of globalizing companies (Kofman and Youngs, 1996: 78-102) .

Firstly, in the three years of time between 1998 and 2001, mainly senior executive consultants and investment bankers of major head offices of global countries, held many globally configured meetings. All the attendants were in one of the two centers in London or New York. The majority have met at their own offices (Mishkin, 1992: 78-88; Mishkin, 2004: 330-337; Grinblatt and Titman, 2002: 4-22).

Secondly, global companies have acquired expansive information and applied a set of researches for other sources of information during their long meetings. These are in the form of annual reports of the companies, web sites, domestic publications, and commentaries & industrial statistics of newspapers. Since these secondary data sources have generally been written about globalization of transnational corporations and economies, the secondary data tend to be of primary importance. In table 9 below are shown executive consultancies of 20 transnational investment banks attending the meetings of global attendants. These corporations continue to be in the strong positional preference for the cities acknowledged to be on the top of the “global city hierarchy” or close to it (Hubbard, 2002: 52-66; Peter and Marguis; 2005: 45-72; Seyidoglu, 2006: 78-92).

Table 1: Head offices and Executive Locations of the 20 Leading Investment Banks (Listed on the basis of their incomes in 2000)

Rank	Bank	Head Office Location
1	**Deutsche Bank**	Frankfurt (Germany)
2	**JP Morgan Chase**	New York (US)
3	**Credit Suisse**	Zurich (Switzerland)
4	**Bank of America**	New York (US)
5	BNP Paribas	Paris (France)
6	**Mitzuho Holdings**	Tokyo (Japan)
7	**HSBC Holdings**	London (UK)
8	**UBS Warburg**	London (UK) /Zurich (Switzerland)
9	Fortis	Brussels (Belgium)/Amsterdam (The Netherlands)
10	**ABN AMBRO**	London (UK)
11	Credit Agricole	Paris (France)
12	Hypo Vereinsbank	Frankfurt (Germany)
13	Santander Central	Madrid (Spain)
14	**Royal Bank of Scotland**	London (UK)
15	Wells Fargo	Chicago (US)
16	Bank of Tokyo-Mitsubishi	Tokyo (Japan)
17	Bank of Corp	New York (US)
18	**Barclays**	London (UK)
19	Sumitomo Bank	Tokyo (Japan)
20	First Union Corp	New York (US)

The Banks are listed on the basis of their incomes in 2000. However, while most of them are both commercial and disposal banks, they do not allow separation of data, commercial and disposal activities.

Source: Andrew Jones, 2003:10-43; Fortune Global 500,2000

Table 1 shows head offices of the 20 leading investment banks in the world. As can be seen in the table, 5 of these are in the US, 5 in UK, 3 in Japan, 2 in Germany, two in France, an the others in Spain, Switzerland, the Netherlands and Belgium. Among these 20 investment banks, **Deutsche Bank (Germany) and JP Morgan Chase (US)** take the lead and create a global pressure on the world economy.

3. Investment and Development Banking in Turkey

When the legal order that arranges Investment and Development Banking in Turkey is analyzed, it is clear that the basic application is established under The Banking Code. "The Banking Code: Code No: 5411, Validation Date: 19.10.2005, (*Published in the Official Gazette on 1 November 2005 with the reiterated number 25983*) The Code has been replaced with codes 5472, 5667, 5754 and 5766. The aim of the Banking Code is explained below in article 1. The first article of the code arranges financial markets for trust and stability. "*Article 1- The aim of this code is to establish procedures and fundamentals in order to provide trust and stability in financial markets, allow the credit system to work effectively, and protect the rights and interests of the beneficial owners.*" Development and Investment Banks in the Turkish banking literature are also defined in Article 3 of the same Code. As defined here:

"Development and Investment Bank refers to organizations, which in addition to accepting deposit and accession funds, functions mainly to provide credit and/or execute tasks assigned to them through specific codes and similar branches of these organizations in Turkey that are established abroad."

In the above definitions of Development and Investment Banks in the Code no: 5411, the responsibilities apart from depositing are also specified. Still functioning in Turkey, these banks continue their activities as public capital, private capital and foreign capital banks. Besides, the position of The Turkish Central Bank in practice is also specified.

- **Arrangement of Development and Investment Banks by The Turkish Central Bank, Dated 2007/01**

On the date specified below, on the basis of the situation created by the Turkish Central Bank, activities of development and investment banks are held to an international level and their banking activities are rearranged. Therefore, The Turkish central bank included development and investment banks in the Central Bank's and other banks' sectoral balance sheets and tables of money stock and set-off entries as new organizational units of monetary sector. Thus;

"Development and investment bank data which is incorporated within "External Financial Institutions" in the monetary and banking statistics is classified as "Domestic bank" from December 2005 onward with regulations established in January 2007. Within this context, the activities between the banks and aforementioned organizations are included in "inter-banks" entry of the related tables." Development and investment banks are considered a part of banking sector in Turkey. Table 23 shows the shares of total credit provided by the investment and development banks in Turkey within Gross Domestic Product (GDP) between the years 2000-2010.

Table 2. The Shares of Total Credit Provided by Investment and Development Banks within GDP between the Years 2000-2010 (Million TL)

	TOTAL CREDIT	GDP	T.C./GDP %
2000	3.157	72.436	4,36
2001	5.328	69.309	7,69
2002	6.000	72.520	8,27
2003	6.588	76.338	8,63
2004	7.242	83.486	8,67
2005	7.704	90.500	8,51
2006	9.879	96.738	10,21
2007	11.414	101.255	11,27
2008	14.955	101.922	14,67
2009	16.391	97.003	16,90
2010	18.880	105.680	17,87

Source: "Banks Association of Turkey" Website.

(http://www.tbb.org.tr/tr/Banka_ve_Sektor_Bilgileri/Linkler.aspx?RId=1007, (28.06.2011)

Table above shows the credit shares of total credit provided by Investment and Development Banks within GDP in Turkey. When we analyze the percentage of total credit within GDP, we see that the total credit are %4,36 in 2000, % 7.69 in 2001, % 8.27 in 2002, % 8.63 in 2003, %8.67 in 2004, 8.51 in 2005, % 10.21 in 2006, 11.27 in 2007, % 14.67 in 2008, % 16,9 in 2009, and % 17.87 in 2010 respectively. This situation is clearer in the Figure 4 above. Average increase in T.C./GDP between 2000 and 2010 is %8.52. The change in percentage in T.C./GDP between 2000 and

2010 is approximately %9.85 (almost %10). This shows that even though investment banks play an important role in the Turkish economy, the support they give to investments is not a major share. Most of the provided support is public weighted banks and some private capital investment banks. It is clear that foreign capital investment banks do not have a big share in the sector comparatively.

Table 3: Total Specialized and Non-Specialized Credits between the Years 2000-2010 (Million TL)

	Specialized Credits		**Non-Specialized Credits**		**Total Credit**
		%(*)		**%(*)**	
2000	**219.238**	**7.0**	**2.938.611**	**93.0**	**3.157.849**
2001	461.733	8.7	4.866.661	91.3	5.328.394
2002	1.739.922	29.0	4.260.723	71.0	6.000.645
2003	1.736.463	26.3	4.852.420	73.7	6.588.883
2004	2.373.426	33.0	4.868.640	67.0	7.242.066
2005	3.029.154	39.3	4.675.070	61.0	7.704.224
2006	3.623.294	37.0	6.256.671	63.0	9.879.965
2007	4.375.423	38.0	7.038.134	62.0	11.413.557
2008	5.640.544	38.0	9.315.442	62.0	14.955.986
2009	6.423.003	39.0	9.968.048	61.0	16.391.051
2010	6.934.000	37.0	11.946.000	63.0	18.880.000

Source: Data, "Banks Association of Turkey" Website.
http://www.tbb.org.tr/tr/Banka_ve_Sektor_Bilgileri/Linkler.aspx?RId=998, (29.06.2011)

Table 3 shows total specialization and non-specialization credits between the Years 2000-2010. Specialized credits consist of project financing, static asset financing, commodity financing, real estate with an income financing, high volatility commercial real estate financing, and transferred organizational claims financing. Investment and development banks mostly finance specialized credits. Non-specialized credits, however, consist of consumer credits, credit cards, export credits, import credits, and other credits of securities. These entries constitute the majority of bank deposits. Table 25 also shows that the percentage of specialized credits is lower than that of non-specialized credits.

There have been 45 deposit, development and investment banks and 9400 branches of these banks in Turkey since the end of 2010. Istanbul has the largest district with 2746 branches and 29 of the whole share. The highest deposit per branch is 103,8 million TL and it occurs in Ankara. 69 percent of the total deposit and 60 percent of the total credit occurs in the three big cities which are the most crowded ones in Turkey. In terms of the cities, the highest credit for each branch is in Istanbul with 71 million TL. Hatay follows this with 55,5 million TL and finally Gaziantep gets 54,6 million TL.

Table 3 shows that there is an increase in the total credits. Credits approached 20 billion TL at the end of 2010. At the same period, total credit stock is 498 billion TL and the percentage of total credit stock is 45 percent of GDP. Table 25 shows that Istanbul alone gets 43 million TL of tourism income and makes %0,5.6 of the total credit. It has %99,3 of specialized credits. Western Anatolia Region has %99,8 of non-specialized credits and Aegean and Mediterranean Regions follow this respectively.

Analyzed in general, development and investment banks have %45 of equity capitals in the total actives in 2010. %31 of sector's total actives is liquid. Sector achieved %6 equity capital benefit in 2010. However, the lowest benefit rate average is that of 2010 from 2002 onwards. The reason for this is that development and investment banks were affected by the financial crisis in 2008 and thus many of private capital development and investment banks did not realize their main activities. Especially when foreign capital investment and development banks are analyzed, big gaps are observed in benefit and equity capital rates in terms of the years.

At this point, serious inspections by relevant authorities on whether the banks under consideration carry out their main activities or not are crucial for a sound operation of the sector. On the other hand, to find out how much development oriented investment groups, who are the main audience addressed by investment and development banks, benefited from the sector might prevent the problems to get worse.

4. Conclusion

In the historical development, banks have been founded and developed. Banking is an economic reality. It developed especially after 1700s and the U.S. Civil War. Activity areas of the bank that have an important place in the world economy are dramatically increasing today. The banks that are founded and operating according to their objectives are organizations for economics service. The banks whose aims are not gathering deposits also take their place in the economy as investment banks.

When operating style and functions of the banks is analyzed, their activities in developed countries are mainly rather heterogeneous and complex activities such as consultancy services regarding underwriting, commercial brokerage, undertaking, and asset management. Investment banks export securities to financial markets through underwriting services and help the corporations. Investment banks also restructure corporations institutionally through mergers and purchases. While the main aim of investment banks was to maintain securities through export, in the 19th century they played an important role in ensuring finance for the railways. The aim of the investment banks here is to finance and council the corporations. Investment banks cannot be classified as commercial banks in terms of 'deposit and credits'. While commercial banks operate in the form of borrowed deposit, they heave helped investment banks in solving their debt problems by using assets together with underwriting services.

When development and investment banks in Turkey are analyzed by and large, it is observed that the rate of equity capitals in 2010 is %45 of the total actives. %31 of sector's total actives is liquid. Sector has benefited %6 of equity capitals in 2010. However, the lowest benefit average from 2002 onwards is that of 2010. The reason for this is that development and investment banks were affected by the financial crisis in 2008 and thus many of private capital development and investment banks did not carry out their actual activities. Especially when foreign capital development and investment banks are analyzed, big gaps are observed in benefit and equity capital rates in terms of the years.

At this point, serious inspections by relevant authorities on whether the banks under consideration carry out their main activities or not are crucial for a sound operation of the sector. On the other hand, to find out how much development oriented investment groups, who are the main audience addressed by investment and development banks, benefited from the sector might prevent the problems to get worse. Investment banks need to rearrange their legal structure in Turkey. Deposit banks are working as investment banks. The most striking example for this is seen in specialized and non-specialized credits of the banks. The monetary aspect of specialized credits is greater. Investment banks are using non-specialized credits. And this leads to a shortage in credit capacity/volume. If investment banks actively support investment credits in the economy, it may add a lot to the Turkish economy.

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