Research in International Business and Finance 27 (2013) 183–208

Contents lists available at SciVerse ScienceDirect

Research in International Business and Finance

journal homepage: www.elsevier.com/locate/ribaf

Does stock market development always improve firm-level financing? Evidence from Tunisia

Thomas Lagoarde-Segot

Euromed Management, School of Management, Marseille & DEFI, University of Aix-Marseille, EA n°4265, France

ARTICLE INFO

Article history:
Received 3 October 2011
Received in revised form 12 October 2011
Accepted 14 October 2011
Available online 20 October 2011

JEL classification:
G11
G12
G15

Keywords:
Economic development
International finance
Middle East and North Africa

ABSTRACT

The question of whether or not increased stock market size allows for improved financing conditions for firms in emerging markets is an important one for policy-making. This paper seeks to investigate this issue by analyzing whether increases in market-level liquidity have indeed trickled down to individual firms over the last decade of stock market development in Tunisia, a fast-growing Mediterranean emerging market. We develop time varying liquidity scores for all firms listed in the Tunisian market over the 1997–2009 period and analyze the extent to which market development, firm-level characteristics and risk exposure affect the magnitude and the distribution of liquidity using a set of fixed effect panel regressions. Our results suggest that massive increases in value traded have created market congestion, thereby increasing the costs of trading, in a context of persistently low efficiency and increased international integration. The main implications of this process are (i) market-level development and international integration are not sufficient conditions to ease access to finance for local firms, (ii) further reforms in the Tunisian market should focus on diversifying corporate ownership and improving the disclosure of information, and (iii) international investors seeking diversification in Tunisia should be aware of a significant illiquidity risk.

1. Introduction

As part of a broader transition agenda backed by the European Union and international institutions, stock market development has for the past fifteen years been a cornerstone of Tunisian financial sector modernization reforms. As early as 1995, the legal status of the Tunis Stock Exchange shifted from a

E-mail address: thomas.lagoardesegot@euromed-management.com

0275-5319/$ – see front matter © 2011 Elsevier B.V. All rights reserved.
doi:10.1016/j.ribaf.2011.10.003

Table 1
Stock market development in Tunisia.

Year	Value traded (DM)	Number of transactions	Average transaction value (D)	Market capitalization (DM)	Turnover ratio (%)
1997	182.5	55,083	3313.18	2562	7.12
1998	170.1	43,115	3945.26	2586	6.58
1999	502.7	142,748	3521.59	3214	15.64
2000	781.4	96,968	8058.33	3880	20.14
2001	455.7	179,372	2540.53	3275	13.91
2002	320.7	93,994	3411.92	2842	11.28
2003	210.1	69,011	3044.44	2976	7.06
2004	281.8	88,948	3168.14	3085	9.13
2005	614.2	156,488	3924.90	3840	15.99
2006	698.7	202,975	3442.30	5490	12.73
2007	774.1	199,395	3882.24	6527	11.86
2008	1769	293,952	6017.99	6381	27.72

Source: Tunis Stock Exchange and World Development Indicators database (2009).

public body to a private corporation held by brokers, and it was one of the first markets in the region to adopt an electronic trading system in 1996. Commissions were reduced to less than 1% of the value of transactions, while dividend and capital gains taxes were suppressed. More importantly, market size and liquidity increased very significantly as a result of privatization programs and seasoned equity offerings. As shown in Table 1, the market capitalization of listed firms more than doubled from 2.562 to 6.381 billion dinars between 1997 and 2008. Over the same period, annual trading volume increased tenfold (from 182.5 to 1769 DM), the number of transactions increased fivefold (from 55,083 to 293,952), average transaction value was multiplied by two (from 3313.18 to 6017.99 DM), and the turnover ratio was multiplied by four (from 7.12% to 27.72%). The Tunis stock market is thus expected to play a pivotal role in the country's export-led, FDI-driven development strategy, in a context where high economic growth is needed to absorb an ongoing demographic shock.

Nonetheless, Tunisian stock market development takes place in a specific institutional context. A civil law country, Tunisia adopted a state-directed financial system after independence, in a context of limited public rights (until the 2011 revolution, the *Destour* political movement had been in power for 50 years). Tunisian capital tended to be allocated strategically by technocrats rather than private financiers, and business lobbies relied on crony capitalist networks close to their political leaders to maintain oligopoly power (Henry and Springborg, 2004).[1]

In addition, crony banks affected resource allocation. In 1996, the banking system owned about two-thirds of stock exchange capitalization and about 90% of the securities listed on the exchange, in a context where government was an active banking shareholder. Tunisia was (along with Egypt) the only MENA country whose banking system was deemed less 'open' in 2000 than in 1996 by international business analysts (O'Driscoll et al., 2000).

Finally, although foreign investment has been liberalized, foreigners willing to buy more than 10% of a company listed on the Tunis Stock Exchange need central bank approval, suggesting potential political interference. Market-based adjustments are hindered by bureaucratic regulations: shareholders breaching the 5, 10, 20, 33.33, 50 or 66.66% thresholds of ownership of a listed company must notify the company, the *Conseil du Marché Financier*, the Tunis Stock Exchange and specify their intentions, while price fluctuation cannot exceed a 6.09% daily margin. Perhaps not surprisingly, the Tunisian stock market is still considered a 'frontier' market by rating agency Standard and Poor's.

[1] The deficit of civil rights also impacted the ease of doing business. According to the FEMISE institute (2006), Tunisian entrepreneurs need about thirteen different accreditations to start their company, an IPO requires supplying 100 documents, and foreign investors need to wait between 6 months and 1 year to get all authorisations and basic services (i.e. land, telephone and water).