6 Structural Changes During Adjustment: Heterogeneity Based on Firm Ownership

6.1 Introduction

The previous chapter explored selected variables in the cost and asset structures of firms based on differences with respect to size of firm. Another area of distinction is firm ownership (foreign/local), which, like firm size, has relevance in the access to and cost of credit to finance investment and working capital. It is argued that foreign firms, as a subgroup of actors in the private sector, are part of a global network that relies on intra-group sales, can have favoured access to banks both local and international, and can borrow internally from parents and affiliate companies (FitzGerald 1993).

The nature of the firm in developing countries, specifically in the Caribbean region, was addressed through looking at the early development of plantation-type economies in which the dual economy feature of foreign/residentiary sectors was identified. This distinction typified the foreign firm as having easier access to markets and modern technologies through their relationship with parents/affiliates abroad, as well as cheaper access to imported raw materials and intermediates. Foreign firms were characterized as operating solely for profit.

The local firms that emerged were viewed as having difficulty in access to cheap raw materials, capital and foreign markets and the foreign exchange necessary to facilitate imported investment and intermediate
goods. In Chapter 2, evidence of credit-rationing in the Caribbean was viewed as being institutionally based with some firms never being able to qualify for credit (Worrell 1985: 120). Farrell & Crichton (1986) saw that credit allocation among firms were biased against small and medium firms. In the analysis of firm size in the previous chapter the possibility of a distinction based on foreign/local ownership surfaced when tracking outliers over time.

Consequently, it is expected that the impact of and response to adjustment will differ based on foreign and local ownership of firms. As in the previous chapter, the aim of this chapter is to look at structural features such as leverage use, interest expenses and raw material expenses as well as profitability and investment, in order to analyse the impact of adjustment. The variable definitions are the same as described in the previous chapter. The chapter therefore continues below in section 6.2 with an exploration of changes in structural factors based on ownership. Section 6.2 also compares the impact of adjustment on the two groups through looking at trends in relative prices. Section 6.3 contains a brief summary of the results. Conclusions follow in section 6.4.

6.2 Structural Changes in Variables Based on Firm Ownership

6.2.1 Leverage use

On average, foreign firms had lower median leverage use ratios than the local firms, and their initial response to increasing real lending rates of interest was different. Leverage use dipped for the foreign firms in 1983/84, and after a small increase in 1984/86, it declined until 1988, when there was a sharp increase. Leverage increased initially for the local firms representing possibly increased indebtedness with declining leverage in 1988. During the adjustment period the tendency was a decreased use of leverage for the foreign firms (1990–92); but little deviation for the local firms (1989–92).

Both groups of firms showed increases in this ratio in 1989 with the peak being more prominent for the foreign firms. In 1989, there was greater liquidity in the economy due to money supply growth of about 10% following two years of declining growth rate at the onset of adjustment. On average, there appears to be a higher ratio of debt to assets and