

THE IMPACT OF TRADE CREDIT ON FIRM PERFORMANCE: A CASE OF COMPANIES LISTED IN PAKISTAN STOCK EXCHANGE

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ARTICLE INFO	ABSTRACT
<p>Keywords: Motivating Language, Job Satisfaction, Teachers' Performance, Leadership, Bridge Program</p>	<p>Trade Credit used the firms to increase sale as well as profitability. This research conducted to explain the effect of trade credit on firm's financial performance of companies listed in Pakistan Stock Exchange from the period of 2006 to 2015. Data was collected from State Bank of Pakistan balance sheet analysis reports. We used ROA and Tobin's Q as proxies of firm performance in wider perspective. This study expand explanatory variables by using control variables that is leverage, growth and size, have an effect on firm profitability.</p>

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1. INTRODUCTION

Firm used as trade credit is the important element to enhanced demand of the product. Horne and Wachowicz (1998) said it is only beneficial for the firm when it maximize the profitability by increasing firm's sale. According to Myers and Brealey (2003) trade credit is the relationship between buyers and seller, in which goods or services is provide on the agreement of later payment without making payment on spot. Ferris (1981) stated that trade credit is a type short-term debt, which is tied in price and duration of transactions. Trade credit has important role in making policy relating to corporate finance. Account receivable investment is crucial part in the balance sheet of the company. Particularly, in western countries, trade receivables show its part approximately 25% of assets (Giannetti, 2003). Kimutai (2006) stated that, trade debtors have larger part in business assets about 15% to 20% of the assets in a firm. Account receivable and account payable used as proxies for measuring trade credit. This is consistent with theory of Petersen and Rajan (1997). Although ,trade credit costly and having an opportunity cost it increase the level of asset's investment that effect the financial and liquidity performance of the organization (Nadiri, 1969). Trade credit involves the risk of credit due to default payment. It may affect negatively on profitability and liquidity. Increasing trade credit also enhanced administrative expenses due to debt management activity (Cheng and Pike, 2003). Level of account receivable can be determined by the benefit received from trade credit granted. Holding cost balances against the benefits received from extending trade credit by the firms (Mian and Smith, 1992). Trade credit is more preferable than credit from banks when there is weak protection for the creditor. Instead of input, cash easily converted while inputs are illiquid, which persuade to receive trade credit (Burkart and Ellingsen, 2004). Demircuc-Kunt and Maksimovic (2002) described with weaker legal protection, trade credit is more important short-term loan for companies (Porta, Lopez-de-Silanes, Shleifer, and Vishny, 1998).

1.1 Trade Credit

Trade credit is oldest as commerce and its practice is world-wide. Trade credit is the relationship between buyers and seller, in which goods or services is provide on the agreement of later payment without making payment on spot (Mian and Smith, 1992). According to Lee and Stowe (1993), it is important element in the goods transaction in which company sold product to consumer and also increased credit terms to him in purchasing. Trade credit has vital role in making policy of financial management. For the customer point of view, through AP it is a source of financing, while for the supplier point of view, it is an investment. This research emphasis on seller point of view of trade credit. Patsula (2001) stated that according to properties of trade credit, it can divide into three categories. In the first category, firm grant credit to customer without charging any interest and down payment it is called open credit. Its common form of credit and time duration is 30 days. The second type is option-terms credit. In this type firms generate credit having fixed time period and payment made with 30 days. Firm charge interest on a particular amount. The third type is the circular charge credit. In which firms provide credit on pre-set term and condition for long time period.

The literature has explained the use of trade credit based on the advantages for suppliers from the financial, operational and commercial perspective. Some motivations for trade credit include reduce transaction costs (Ferris, 1981; Emery, 1987); stimulation of sales in slack demand periods by relaxing the credit terms (Emery, 1984); lack of information asymmetry between buyer and seller (Smith, 1987; Long et al., 1993; Pike et al., 2005), because trade credit acts as a signal for product quality (Lee and Stowe, 1993; Emery and Nayar, 1998); a mechanism of price discrimination between cash and credit customers (Brennan, Maksimovic and Zechner, 1988; Petersen and Rajan, 1997). Finally, credit provision improve the supplier-customer relation (Ng, Smith and Smith, 1999; Cnut, 2007). Consequently, granting trade credit enhances a firm's sales.

1.2 Trade Credit Terms

Ng et al. (1999) and Smith (1987) explained trade credit terms. There are two kinds of credit terms: the first is net trade credit term, its explain that complete payment is made after one month of delivery. After due date buyer consider as default. The second one term is more complex than simple net credit term which have three basic factors: the rate of discount given on invoice, the discounted period and the interest rate charge on the payment due. It represent as credit term of 2/10 30 (Smith, 1987). These credit terms explained that there is a 2% discount on the payment made within 10 days and otherwise complete amount of credit paid in a month. Ramey (1992) defined that mostly small scale firms having low liquidity increased credit term more than 30 days. However, credit term also effect firm reputation .Moreover, Nadiri (1969) stated that when bank provided credit on high cost than firms decrease the trade credit level, not credit terms. Smith (1987) argues the second term relating to trade credit use shows a risk is associated with lending.

1.3 Costs & benefits of trade credit

Petersen and Rajan (1994, 1997) explained trade credit as more costly than bank loans. In their study, interest charged by bank on average is 11.3%; while in trade credit, for the encouragement of customers to paid their loan in time, a simple net credit term was used that is 2/10 net 30. This credit term explained that there is a 2% discount on the payment made within 10 days and otherwise full amount of credit paid in a month. Even there is a high costs of trade credit, still various firms used it as a source of short-term financing. Schwartz (1974) describe trade credit as it makes transactions very easier and it is efficient way to reduce the hurdles in the delivery of goods and help in managing cash. Petersen and Rajan (1997) defined why companies preferred trade credit on the bank credit. They stated that trade credit used as a source of financing by those firms who face difficulty in achieving credit from traditional financial institution. Trade credit is used by the firms during contraction of monetary period, as the risk face by supplier in granting credit is less as compare to the loan provided by the bank. Furthermore, supplier have many financial advantages: first, supplier can easily evaluate the customer's credit worthiness and financial performance and also assess default customers efficiently (Ono, 2001).Supplier have right to reduce supply of commodities or repossess if the buyers is unable to make payments. Second, transaction cost can be minimized by separating delivery and payment, it's also provide assurance of product quality. Third one is price discrimination in which suppliers give credit terms in making early payments like 2/10 net 30 (Garcia-Teruel & Martinez-Solano, 2010a; Atanasova, 2007). To conclude the trade credit advantage from supplier side, Wilson & Summers (2002) explain trade credit as marketing tool, with the help of trade credit supplier can expand their business and build good reputation with customer. New firms provide trade credit to customers who have feel difficulties in obtaining short-term loan. From the buyer's side, Schwartz (1974) explained that due to trade credit buyers have sufficient time to make payment schedules for purchases.

1.4 Value of Firms

The firm's value is the PV of the company's present and future profits (Michael R, 2006). According to Michael, the firm's value is connected with maximization of profit; a firm aim to enhanced profit is actually connected with maximization of the value of the firm. Damadoran (2002) stated that, the firm's value is obtained by discounting expected cash flows to the firm. Dalborg (1999) explained mainly three determinants of creation of firm's value that is growth, free cash flow and profitability. Accordingly, current profitability used as the driver to determined firm's value, expected growth of income and free cash flow considered as drivers to calculate firm's value. According to Rappaport (1998) there are many determinants to measure firm's value: annual sales growth, additional investment in working capital, tax rate, operating profit margin, fixed capital investment, and annual additional growth in value. However, Rappaport stated that for operation decisions these determinants are in broader view and for getting advantage it is necessary to calculate micro value determinants that effect above macro value factors. It is the responsibility of management to arranged micro value determinants at the business unit.

Copeland et al (2000) explained creation of value in the real world by earning a yield received from the investment exceed the opportunity cost. This implies that growth generate more value as long as the return on the capital increase the cost of capital. Shareholder returns depend on expectations which is more than company's current performance. Dalborg (1999) stated that value is create when the shareholder returns in the form of dividend and share price increase the cost of shareholder equity. He argue that return of shareholder should be greater than the cost of shareholder equity to generate value of firm.

1.5 Relationship between Trade Credit and Firm performance

The financial aim of any firm is to maximize the firm's value or shareholders wealth (Berle and Means, 1932). Trade credit helps firms to achieve this goal because it increases the investment in accounts receivables and impact the financial performance of the company. However, trade credit costly and having an opportunity cost it increase the level of asset's investment that effect the financial and liquidity performance of the organization (Nadiri, 1969). Trade credit involves the risk of credit due to default payment. It may effect negatively on profitability and liquidity. Increasing trade credit also enhanced administrative expenses due to debt management activity (Cheng and Pike, 2003). Level of account receivable can be determined by the benefit received from trade credit granted. Holding cost balances against the benefits received from extending trade credit by the firms (Mian and Smith, 1992). Level of investment of account receivable can be measure by balancing the benefits and cost of trade credit extension. The firm trade off the benefits of extending trade credit against the holding cost of large accounts receivable (Nadiri, 1969). The aim of this study was to analyse the effect of trade credit on firm performance. It is expected that opportunity, financing costs and credit risk dominate at higher levels of receivables while financial, operational and commercial motives beneficial for trade credit at lower level of account receivable (Nthenge, 2013). Accordingly, this study will create a non-linear relationship between trade credit and the firm performance. Therefore, it's important for researchers and managers to manage trade credit element which effects shareholder's value.

1.6 Objective of the Study

Literary aspects of trade credit effect on firm performance.

1.7 Research Question

How's trade credit effect on firm performance – descriptive analysis?

1.8 Value of the Study

From the analysis of the effect of trade credit on firm's value, the study will help shareholders to decide where to invest and whether or not to take trade credit decisions in their firms. This study will be helpful to various stakeholders in making decisions related to investment, operation and regulation of the business. It will enlighten market players on how to efficiently manage trade credit and enhance the firm performance. The management will be provided with a tool for managing key business processes in an efficient way. Particularly finance, sales & marketing and operations departments will guided on trade credit practices that supports Cash flow generation for achieving the goal of profit maximizing. Entrepreneur starting new business providing tool for will maximize their investment. They will be provided information for analysis and identifying the best company to invest by considering their trade credit policies. This study will also help for employees to help them in contributing drafting and implementation of trade credit policy that guarantees the growth of revenue, liquidity and profitability. As a result by having a profitable firm, job security and personal career growth of individual firms will be enhanced. The government departments will be provided guideline to control and regulate the operations of the companies with effective trade credit policy for companies. Specifically, security exchange commission of Pakistan will be assisted in rolling out trade credit policy direction to the firms at the interest of not only the shareholder's but also for whole economy. The study contributes to the body of knowledge on trade credit and provides the basis for further research on relationship between trade credit and firm performance.

2. THE USE OF TRADE CREDIT

Trade credit is a transfer of goods or services among business concerns, in order to pay in future (Cole, 1968). Whenever the payments of goods or services do not made on spot, than obligation discharged through trade credit terms. Trade credit used mainly used as source of financing in business organization across in whole world. It is not self-explanatory that why companies involves in granting loan in the form of trade credit to customer even in the presence of specialized financial institution who can assess the risk in lending loan. Numerous motivational theories that explain the trade credit usage. In which some explain financial advantages of trade credit, few focusing on transaction cost motives and others defined price discrimination theories. In the financing of economic activity, the importance of trade credit has been noted in various studies. For example Ng *et al.* (1999) find that in U.S trade credit amount increase the value of M1 by factor 1.5. In general, trade credit terms are different for different companies which depend on company arrangements and time period in which they have been run business (Fishman and Love, 2003). This is advantageous for those who depend on internal financing and on bank credit, specially overdrafts facility consider as a way of short-term fund. While trade credit is generally consider as a short term method of financing (Nilsen, 2002), it also perform vital role in day to day transaction and firm's policy making (Rodriquez-Rodriq., 2010). Traditional theories of trade credit is explain its role examined from a number of different perspectives including, transactions costs, redistribution, substitution, market power, relationship lending and credit worthiness. It's a result of monitoring orders, repayment schedules and ability to enforce repayment or cut off future supplies (Love and Zaidi, 2010). Through favorable credit terms, firms can decrease their borrowing cost, especially receive discount from the payment before due date (Aktas, Bodt and Lobe, 2012).

Trade credit can be more expensive means of fund if firms is unable to avail discount facility from credit terms (Petersen and Rajan 1997), therefore, it can be advantageous for those companies who reserve cash to avoid penalties of late payments (Wu et al., 2011). Although ,trade credit costly and having an opportunity cost it increase the level of asset's investment that effect the financial and liquidity performance of the organization (Nadiri, 1969). Trade credit involves the risk of credit due to default payment. It may effect negatively on profitability and liquidity. Increasing trade credit also enhanced administrative expenses due to debt management activity (Cheng and Pike, 2003). Level of account receivable can be determined by the benefit received from trade credit granted. Holding cost balances against the benefits received from extending trade credit by the firms (Mian and Smith, 1992). Numerous evidence find that trade credit play significant role by compensating unavailable bank credit. Petersen and Rajan (1997) reported that those firms use more trade credit that have weaker relations with banks. Nilsen (2002) also shows that firms without bond ratings depend on trade credit during monetary tightness. Further, Fisman and Love (2003) argue that countries having undeveloped financial system, trade credit provides an alternative source of funds, which increase growth rates of industries. Garcia-Appendini and Montoriol-Garriga (2013) find trade credit during the financial crisis and reported that firms with greater liquidity before crisis extend trade credit to financially restricted firms during crisis and, in turn, realize significantly better performance in financial crisis. Thus, their study concentrates on firms that invest in customer relationships during a market bottom. They also reported firm's better performance that increase trade credit to illiquid customers, their results primarily explain the benefits of excess cash holdings during times monetary contraction. In addition to providing immediate liquidity, trade credit shows positive signal regarding the buyer's creditworthiness. In turn, this may increase the buyer's future access to capital and lead to higher revenue for the seller (Biass and Gollier, 1997). Although, trade credit is used as an less important means of getting fund because of high interest cost containing unattractive position in the pecking order theory (Petersen and Rajan, 1997). According to Cunat (2007), interest charges paid against the trade credit are more as compare to the charges paid on loan taken by bank due to insurance premium. Insurance premiums is the amount which is received by supplier due to providing shield against bad debts occurs.

2.1 Motivation of trade credit

Numerous theories explain the reasons for the supplier's willingness to grant credit to customers use trade credit as a source of financing. Frank and Maksimovic (2004) discussed the trade credit motivation keeps in view following aspects: first one related to real operations. It define the motives of trade credit usage, and it includes the transaction cost theory, price discrimination theory and product quality; the second is related to financial advantage of trade credit. The researchers stated that suppliers provide trade credit to those customer who are facing financial crisis in order to keep good relationships for longer time with customers. Emery (1984) discussed that underdeveloped capital market, seller required cash holding to increase short term financing to earn more yield. Moreover, having less competitive market, seller has better reputation and able to sold goods in large quantity with grater profit margin. Therefore, in this way suppliers increased trade credit to their buyers. According to Cheng & Pike (2003), there are much difference of motivation in trade credit usage among companies. Mostly institution use TC as an opportunity for enhance firm's image and established good repute among customers. TC is also used as a tool to attained higher profitability (Shiraishi and Yano, 2010). Nilsen (2002) discussed many firms based on TC even they can get bank loan at low interest charges. Moreover, they have equal growth of AP and AR to maintain financial statement. Firms used TC to maintain good relation and customer loyalty (Ng et al., 1999) and buyer also have benefits from these trade credit. Many authors have explained more reasons to used trade credit. Garcia-Teruel & Martinez-Solano (2007) explained, those firms that operating in a specialized financial institution system, they have little alternative for getting finance from external sources. So, they rely on short term funding i.e. TC; Schwartz (1974) stated in his work that firms who have limited access to other external financing, grant more TC and achieve high profitability. However, Deloof & Jegers (1996) have done empirical work based on theory of product quality, which show that by using TC customers have enough time period to analyse quality of product before payment.

2.2 Transaction Motives

Trade credit help in reducing the transaction charges to meet the obligation bills payment. Even that making daily expenses, company can added liabilities and make payment on regular basis. Firm enable to make schedule between daily payment expenses and delivery, maintain liquidity flows more certain and decrease the level of holding cash (Ferris, 1981). Firms have fluctuating demand of goods can have option to use credit terms instead of dealing with price elasticity (Emery, 1984; Long et al., 1993). Transaction motive is the reason for trade credit usage by business customers. Due to lack of trade credit, firms must done cash purchase. If delivery timings are unconfirmed and conversion of marketable securities into cash is expensive, mostly companies reserve balances in cash form. Ferris (1981) stated that in some cases TC enables buyers to save transaction charges linked with management of liquidity assets. Ferris (1981) demonstrated that, TC gives information about the cash needs by giving permission to buyers for accumulation of payment invoices. Better information able supplier to analyse the required cash need efficiently. Moreover, firms enable to keep little cash reserve and to paid less brokerage charges if company make payments on invoices promptly. Firms also get advantage from TC. Sellers also benefit from trade credit. It able supplier to forecast receipt upon payments faultlessly, help them to decrease their balances as well. Trade credit has been a largest source of financing and is widely used in business transactions. For example, Wal-Mart used trade credit

as a second largest source of capital after profit, and a larger source of capital than bank borrowing. Trade credit for Wal-Mart is eight times as much as the amount of commercial paper acceptance invested by shareholders (Chluddek, 2010).

However, trade credit received less attention than it should in literature. The neglect might be due to two reasons: (1) the value of trade credit is reflected in specific goods, whereas bank loans do not confine its activities in goods or capital market. (2) Trade credit should be paid off with a short period lag of manufacturing or selling. A firm buying inputs on credit may return products to its supplier if the firm detects defects before the payment is due. Meanwhile, the firm also offers trade credit to its client by specifying a repayment obligation. Trade credit consists of two components: accounts payable, shown on balance sheet as liability, is the money owed by a firm to its suppliers; accounts receivable as an asset, is the money given to its clients. Rather than the explanation on accumulating the payments timing, researchers have pointed out mainly three motivations of transaction for TC usage that are information asymmetric between buyer and firms, benefits getting from price discrimination and from supplier's having stake holding in the customer's firm.

2.3 Information asymmetric between company and buyer

TC looked as a legal solution of information conflict arises from quality of product and customer creditworthiness (Ng et al., 1999). Incomplete knowledge creates problems interchange relationships, chances for opportunity and problem of endangerment that enforce cost of transaction to both institutions. Trade credit reduces the transaction charges creating from information deficiency among sellers and buyers. Customer who makes payment in advance is not sure about product quality that meets expected standards. This occurs due to misconception it may decrease if supplier gives guarantee about product quality and has a good reputation in market. Through TC expansion, it creates opportunity for supplier to lower issues related to product quality by giving incentives to customer about the inspection of product quality prior payments. This is applicable for those commodities who required huge time for verification (Smith, 1987). Ng et al. (1999) demonstrate that supplier assurance and reputation may decrease concerns related to quality of product while customer's reputation and creditworthiness decrease the issues of bad debts. Fame-based approach does not give enough explanation, when customers are new, small or different than others. Credit terms can be used to solve issues stem from deficiency of information asymmetric. First, a seller doesn't have good reputation in market or their products take enough time to maintain standard, required more TC for customer to confirm product characteristics prior payment (Long et al., 1993). In this way TC is the only way for effective assurance. Secondly, Smith (1987) proposed that specific terms enable buyers to predict credit worth through payments schedule. Smith (1987) considers a situation in which deficiency of asymmetric information binds creditors to ration the credit. Creditors have knowledge relating to their default payments than supplier. Banks charge low interest rates and face problems of adverse selection.

2.4 Price Discrimination Motives

TC used by firms to discriminate prices. Trade credit provides opportunity to discriminate price among different buyers. By offering various kinds of TC terms to buyer is basic principles behind of trade credit usage (Meltzer, 1960). Price discrimination concepts can be interpreted when firms were getting high profit margin on goods and having an opportunity to increase sales by incurring more cost. When customer unable to get funds from banks then TC works as a means to finance their day to day operation. A trustworthy firm finds trade credit expensive and pays back quickly. TC gives way to change product's prices without changing the original price of the products (Petersen & Rajan, 1997). The prices of less reputable buyers are flexible. Buyers having less goodwill in market face problems in getting finance from outsiders because these customers are not suitable for TC terms. Credit rationed customer taking interest to buy product from seller without botheration of capital need and continue their operations (Brennan et al., 1988). This is possible only when there is moral hazard in the capital market. On the other side, motivation stems from price discrimination explained that there is high profit margin exists between variable cost and sales. This type of institution has advantage to increase sales without losing the actual price of product to their buyers. When trustworthy buyers find TC will be expensive, try to repay promptly while risky buyers find it beneficial to get because still it is low priced than other means of financing (Petersen & Rajan, 1997).

2.5 Financial Advantage Motives

The supporters of financial motives defined trade credit usage with different aspects that if TC used to decrease cost of transaction then due to improvements in transaction technologies, long-term decline takes place in the use of trade credit. According to Frank and Maksimovic (2005) such type of course doesn't exist, which recommends to use large trade credit. This topic discusses how the financial course locates unsymmetrical information between financial institution and companies, which is beneficial for suppliers giving financial advantage. If financial institutions are not agree granting to any company then suppliers can use trade credit as alternative of bank credit. However, it appears that trade credit comes after the bank loan in funding and use as alternative source of finance.

2.6 Suppliers' Financing Advantage over Banks

Financial motives locate unsymmetrical information between financial institution and companies. This unsymmetrical information impedes to finance in precious projects. Biais and Gollier (1997) recommended a model to explain TC can resolve trouble arising through lack of knowledge by stimulating personal information related to buyers sustain by seller. Personal

information giving financial advantages to supplier on traditional financial institution in scrutinizing the trustworthiness of borrower, as well as appropriate efficiency to observe and has power to force for reimbursement of credit. Supplier can get benefits of financial advantages from four sources. First, seller incurred low cost of observing customer as compare to bank. Supplier collect product wise information in daily business operations just like the timing and quantity of buyer's order and his deficiency to receive benefits from credit terms. So supplier receive advantage in the shape of getting quick information at less charges than traditional information (Petersen & Rajan, 1997). Jain (2001) stated that financial institution and supplier both are superior when financial institution grant credit to supplier with sufficient information, that mediate credit to customers as TC. Moreover, customer bear loss in case when it has to pay greater interest charges than taking loan from traditional financial institution. Secondly, seller have benefits in retrieve worth from already present assets. If buyers become default, firm can grab the products which was sold. Fixed assets used as collateral securities for banks. Financial institutions have right to claim against fixed assets for the payment of the credit. However, Seller's acquiring cost and reselling prices are less than specialized financial lender because they lack network and expertise for selling the goods (Petersen & Rajan, 1997). Longhofer and Santos (2003) demonstrated that trade credit enhanced social activities. When mortgage value of durable goods is greater for supplier than for financial institution, granting interest charges on fixed asset to creditors, while subordinate can claim for remaining amount. It's beneficial for both parties that is trade creditors and other debt holders.

Third one is that seller have benefit to monitor customers particularly when customer completely based on commodities supplied, having little other ways for products and buyer has inability to get huge share of sale from another supplier. In this case, due to the obstacles of discontinuation of further finance supplies would be productive and quick (Petersen & Rajan, 1997; Cuñat, 2007). And end, seller have benefits from information due to better and effective understanding of market. Establishment of corporation with old customers assist to differentiate among customers whose are facing financial problems and down fall in the market (Ng at al., 1999).

2.7 Substitution of Trade Credit and Other Sources of Financing

Financial advantage explain willingness of firms to grant TC to valuable customers while banks lend to the same type of companies. Numerous theories explain that TC and various other means of funding can be alternatives. Huyghebaert's (2006) research explain that when newly firms facing financial constraints problem use more trade credit. Petersen and Rajan (1997) stated in Americans small companies used more TC than large firms and also find that when loan from banks is unavailable then supplier use more trade credit. These results show supplier having an ability to acquire from traditional financial institution granting more TC. Atanasova (2007) found consistent results in his study having U.K. enormous sample of public and private companies, which explain TC demand decreases with traditional finance and internal funds. Pecking order theory suggest trade finance is lower than both internal financing and banks borrowing (Myers & Majluf, 1984). Due to comparatively greater lending cost of TC, taking low position level in Pecking order theory. Huyghebaert *et al.* (2001) and Wilner (2000) suggested that due to easy dissolution policy and agreeeness of lending more convenient credit term offer to buyers in monetary constraints, companies attract higher risk customers. So greater cost of TC reflects the higher credit risk.

Moreover, many institution used TC and bank loan only when other low- priced fundings are unavailable. Biais and Gollier (1997) recommended that sellers have complete knowledge related to their buyers, through the trade credit usage which show signaled to creditors. In their empirical model, accessibility argue that suggest trade credit may use as complement to bank credit. Suppliers regularly grant in the shape of material, but they infrequent grant cash loan. While cash can be used in such a manner, which increase the expected yield. The result shows that the trade credit accessibility enhanced finance which banks agree to grant, because banks foresee that TC increase investment opportunities. Research on developing capital markets also proposed the alternative of bank credit is trade credit. Ge and Qiu (2007) comparing government and private companies in China and results shows that private owned firms, obtain more trade credit than government owned firms because of less availability to credit from specialized financial institutions. They also find that trade credit is predominantly used for funding rather settlement bases. Frank and Maksimovic (2005) stated that less developed countries, where shortage of capital exist, suppliers act as financial intermediaries. Due to increase of TC, supplier want to decreased cost of production and part of profit will be automatically financed. Fisman and Love (2003) found TC has play vital role in under developing markets. There results explain those countries having less developed banking system, firms with greater TC funding achieve more growth than others. Demircuc-Kunt and Maksimovic (2001) research also found relationship between developments of a financial system and statutory regulation of country with trade credit usage. Their research suggest, due to inefficient legal system companies, depend on TC as compare to bank loan. They also find that they are alternative to each other. This appears to understand that manufacturing companies required to work efficient for sound financial system in order to perform as monetary intermediate.

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