Ways to Improve the Access to Finance of Romanian SME

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Abstract

The present study intends to highlight the principal aspects concerning SME's financing in Romania by analyzing the European Union context of SME's financing, the research done by World Bank, OECD and NBR specialists regarding the actual framework of SME's financing and the surveys realized by some Romanian market researchers and the National Council of Romanian SMEs. The starting point is a theoretical approach about SME's financing that underline the role and the importance of SME for the economy and the main issues concerning access of SME to finance. The author tries to emphasize some particularities for SME's financing by European Union in order to better approach the framework for Romania. In this respect, the research undertaken on Romania materializes into a SWOT analysis that encapsulate the internal and external constraints of SME's financing and also factors favoring it in order that entrepreneurs and policy makers take better actions to improve the SME access to finance.

Key words: access to finance, type of finance, internal and external constraints, SWOT analysis
J.E.L. classification: D53, E51, G32, L26, L53

1. Introduction

The present study intends to highlight the principal aspects concerning SME's financing in Romania by analyzing the European Union context of SME's financing, the research done by World Bank and OECD specialists regarding the actual framework of SME's financing and the surveys realized by some Romanian market researchers and the National Council of Romanian SME. The starting point is a theoretical approach about SME's financing that underline the role and the importance of SME for the economy and the main issues concerning access of SME to finance. The author tries to emphasize some particularities for SME's financing by European Union in order to better approach the framework for Romania. In this respect, the research undertaken on Romania materializes into a SWOT analysis that encapsulate the internal and external constraints of SME's financing and also factors favoring it in order that entrepreneurs and policy makers take better actions to improve the SME access to finance.

According to EU recommendation 2003/361 an enterprise could be defined as a SME by taking into consideration the staff headcount, the turnover or the balance sheet total: micro-enterprise comprising less than 10 employees and turnover less or equal to 2 millions euro or a balance sheet total less or equal to 2 millions euro; small-enterprise with less than 50 employees and turnover less or equal to 10 millions euro or a balance sheet total less or equal to 10 millions euro; medium-sized enterprises with less than 250 employees and turnover less or equal to 50 mil. euro or a balance sheet total less or equal to 43 mil. euro.

Framing enterprises in this category brings many potential benefits in terms of financing and not only, such as: eligibility for obtaining support under EU business-support programmes and/or national governments financing schemes, reduced fees or requirements for EU administrative compliance, assistance for financing guarantee schemes.

There is no matter of question that the importance of SME for the economy is reflected by their strong influence on economic growth and job creation, on reducing poverty and leveling living standards, on promoting competitivity and efficiency on a free market, and also on inovation and launching new products and services.

2. General considerations on SME finance

SME business type requires financing, on the one hand, to cover investment needs, i.e. fixed assets, thus involving financial resources in the long term and, on the other hand to ensure a continuous cycle of exploitation that means financial resources in the short term. In the first case, it is about the implementation of the business (start-up) or the maintenance of fixed investment level or the growth of the productive capacity through new investments.

According to the theory of financial equilibrium in corporate finance, financing of fixed assets should be made only on the basis of long-term resources, while financing current assets implies the existence of a working capital, to cover the current assets both through resources on long (partially) and short term.

As with any business, the entrepreneur will need to make the optimal choice debt versus equity ratio in terms of maturity and cost of capital. In this context they must considered different financing options regarding the budget amount, the repayment period, the interest, commissions and other costs involved, the maturity payment, the degree of risk, and the guarantees submitted.

SME are businesses whose dimensional and functional geometry varies depending on certain characteristics which influence the access to finance: company size (micro, small or medium); turnover (up to 2 million euro, 2 to 10 million euro and 10 to 50 million euro); economic sector (industry, trade or services); type of SME (autonomous or subsidiary /branch of an enterprise); length of time active (under two years, two to four years, five to nine years and ten years or more) and ownership structure (family or entrepreneurs, one owner business, business associates, listed company, venture capital or business angels).

There are two basic forms of SME financing: internal and external. On long-term, internal sources of financing are the retained or undistributed profits from the previous years and the new capital injections by the owner.

For SME, the advantages of internal financing or self-financing are represented by: it is a safe, stable and independent way of funding; it ensures freedom of decision and action of the entrepreneur; it gives freedom in choosing investments and capital budgeting; it reduces indebtedness and financial expenses; it helps attract external financing and even access to the capital market (Vintilă, 2006).

On short-term, as an internal own source of financing there is working capital which results from the necessity of permanent renewal of inventories and receivables to ensure continuity of production and sales regularity. In this respect, it is difficult to determine the optimal level of working capital for a company namely due to the influence of several factors: the need to realize a certain level of service or perform a range of products; Payment rules of the branch and the relevant country, as well as the need to synchronize production times with command structure.

There are also the temporarily raised sources from third parties in the period between the creation of debt and the payment maturity that is established on the basis of a favorable difference between the pay gap and the revenues gap. As stable liabilities in this category there are registered the short-term debt of the company by third parties (suppliers, employees, government etc.).

External sources of financing on long term rely on outright loan from banks and some hire purchase and leasing products from other financial institutions. On short-term there are some specialized financial products like factoring.

The access to finance of SME differs also according to the entrepreneur experience (start-up or established business) and to the credit history. It is wellknown that building a start-up it's a difficult task as it is quite unlikely for the entrepreneur to attract external financing, but an easier one for a SME that have already a track record as successful business. Beck et al (2008) highlight the importance of credit history data evolution on SME's financing: 70% of developing country banks and 44% of developed country banks in an World Bank survey stated that the existence of a credit bureau in their country facilitated SME lending.

3. Present issues for European SME's with impact on their financing

Looking at the general evolution of SME's financing in European union, there are a series of surveys taken by the ECB and DG Enterprises and Industry of the European Commission from

2008 under the name of the Survey on the Access to Finance of Enterprises (SAFE). In this regard, for the first time since the first survey was taken, the entrepreneurs perceptions concerning the evolution of the general economic outlook confronted by the EU28 SME was positive in 2015 (Doove, S., Kwaak, T., Span, T., 2015).

Regarding the last years 2014-2015, the majority of EU28 SME revealed an improvement in the availability of finance for any of the types of funding, except for debt securities. Following the development of interest rates, more enterprises recognized a decrease of them than an increase opposite the loan size and maturity that see an increase rather than a decrease. At the same time, there was some increases in the non-interest rate costs of financing and collateral requirements, altering the process of external financing. The principal sources of external financing were revealed to be credit line or overdraft and bank loans as leasing and hire purchase were considered to be the third source in order of relevance.

„In 2015, 30% of EU28 SME applied for credit line, bank overdraft or credit line overdraft. Of these applications, 73% were successful in the sense that these SME obtained at least 75% of the amount applied for. Comparable results were obtained for bank loans and trade credit. Regarding other forms of external financing, 16% of the EU28 applied for these, of which the vast majority obtained at least 75% of what they requested” (Doove, S., Kwaak, T., Span, T., 2015).

In 2015, the use of external sources of SME’s financing in Romania compared with EU28 are presented below:

Table no. 1 Use of sources of financing in EU28 and the main CEE countries (% of total)

Type of finance	EU28	Romania	Bulgaria	Czech Republic	Hungary	Poland
Credit line, bank overdraft, credit overdraft	37%	36%	34%	28%	22%	42%
Bank loans	19%	13%	14%	16%	7%	21%
Leasing or hire-purchase	23%	17%	16%	17%	14%	34%
Trade credit	20%	16%	10%	7%	4%	38%
Grants or subsides bank loans	8%	< 5%	< 5%	10%	9%	11%
Retained earnings or sale of assets	15%	14%	11%	15%	8%	13%
Other loans	10%	18%	10%	12%	8%	8%
Equity capital	12%	10%	< 5%	< 5%	< 5%	7%
Factoring	6%	5%	< 5%	< 5%	< 5%	7%

Source: (Doove, S., Kwaak, T.,Span, T., 2015)

It can be noted that the share of bank loans among the other external sources are low and there is a great appeal for leasing and trade credit in Poland than in the rest of main CEE countries and EU28. On the other hand equity capital is very little used as source of financing and other loans has a notable weight in Romania and Czech Republic.

Changes in access to finance for SME in EU28 and main CEE countries are shown below:

Table no. 2 Access to finance in EU28 and the main CEE countries (% of total)

	2013	2014	2015
EU28	15,40%	13,00%	10,00%
Bulgaria	15,50%	11,00%	8,00%
Czech Republic	9,70%	7,00%	7,00%
Hungary	17,30%	14,00%	11,00%
Poland	8,50%	10,00%	8,00%
Romania	15,00%	14,00%	11,00%

Source: (Doove, S., Kwaak, T.,Span, T., 2015)

As for the entrepreneurs perception regarding changes in the availability of various types of SME’s financing in EU28 in the period 2009-2015, the surveys revealed that bank loans evolved from 8% in 2009 to 20% in 2015 so the net change was -36% in 2009 and 9% in 2015; trade credit increase from less than 4% in 2009 to 20% in 2015 and the net change was -21% in 2009 and 11% in 2015; equity evolved form less than 3% to 13% so the net change was -7% in 2009 and 6% in 2015; debt security issued increased from less than 1% in 2009 to 10% in 2015; and bank overdraft, credit line and credit overdraft rised from 11% in 2009 to 19% in 2015 so the net change was -10% in 2009 and 9% in 2015.

There are some constraints that restrict the ability of SME to have access to finance and the author has tried to highlight the most significant of them in the table below:

Table no. 3 Internal and external constraints in SME's financing

Internal constraints	External constraints
• the nature as smaller companies of SME • lack of critical economic size • less sophisticated management and control of business • lack the understand how to develop an acceptable business plan for loan application • lack of standardized/comprehensive financial data • poor customer knowledge • lack of collateral or capital • low profitability • SME skills and literacy	• information asymmetries in relation with financial institutions • availability of bank loans • non-competitive real exchange rates • bureaucratic procedures in setting up, operating and growing a business • financial situation of banks and other credit institutions due to the financial crisis • developments of macroeconomic environment both national and international

Source: (The World Bank, 2014) and the author

4. Features of SME financing in Romania

In order to analyze the financial conditionality that influence access to finance for Romanian SME it is important to examine the evolution of main financial indicators of SME in the period 2011-2014 (KeysFin, 2015) as highlighted in the following:

• Taking into account the net income less losses, micro-enterprises registered negative rates of this indicator to -8.7 billion lei in 2011, but the trend was decreasing until 2014 when it reached -3.1 billion lei. On small and medium enterprises, they have recorded a positive net result.

• The economic sector with the largest amount of debt is trade which in 2013 reached a percentage of 23% of total debt (14% in 2014), followed by construction (19% in 2013 and 12% in 2014) and manufacturing (15% in 2013 and 10% in 2014).

• Analyzing the total revenues of the SME sector, it appears that the largest share of revenues was recorded by medium-sized enterprises, accounting for about 37% of total SME revenues. Small businesses account for 35% and 28% micro records in total revenue of SME.

A study by National Council of Small and Medium Private Enterprises in Romania (CNIPMMR, 2015) shows that:

- approximately 82.04% of the investigated SME's finance their economic activities from their own sources;
- 24.58% of SME businesses resort to bank loans to finance their activities;
- 18.33% of SME have resorted to supplier credit, 3.85% used leasing, 1.53% used loans from specialized institutions and 1.82% of the units used the European grants;
- SME consider that access to finance should be achieved through: banking institutions (68.95%), guarantee institutions (17.60%), the Romanian Fund of Counter-guarantee (12.29%) and government policy (5, 96%);
- the main destinations of the financing needs of SME are: working capital (58.33%), investments (35.35%), creating jobs (8.80%) and innovative projects and research (2, 84%);
- SME appreciate the contribution counter-guarantee from resuming lending is focused on: reducing interest rates (52%), decreased bank fees (42.76%), reducing the cost of guarantees (18.98%) and enhancing SME access lending to SME (18.98%).

From the survey on lending to non-financial companies realized by the National Bank of Romania for the period 2014-2015 result that the major difficulties faced by SME in accessing finance from banks are: requirements on the amount or type of collateral, high interest rates and fees and the contract terms. (NBR, 2014/2015). The sectors most affected by the credit crisis are those that record high leverage indicators, lack of liquidity, declining productivity, operational bottlenecks (doubling the debt collection periods), namely: trade, textile, hospitality, food industry.

The author of the study consider that an important instrument in analyzing the access to finance of Romanian SME is a SWOT analysis on SME's finance in Romania, in order to reveal the positive/negative aspects and the advantages/disadvantages that SME encounter in their attempt to request finance.

Table no. 4 SWOT analysis on the access to finance of SME in Romania

Strenghts	Weaknesses
• high oriented to customer needs • faster adaptation to market requirements • ability to create new products / services to market demand; • ability for innovation to create products with market demand; • quick to see opportunities • low bureaucracy and flexibility	• lack of the know-how to provide standardized, understandable and credible financial information to potential lenders; • less strategic thinking and planning both operational and financial • inability to present a business plan or a feasibility study in the financial terms a lender needs to process a loan application; • lack of understanding the loan application process, and how to deal with lenders in financial terms; • lack of documenting their debt service to lenders; • lack of understanding their own financial situation and how communicate credibly to lenders • harder to retain qualified staff
Opportunities	**Threats**
• credit conditions remained relatively unchanged, both by size of firms and length of funding for the past year; • by sector, bank lending conditions were stable in most economic sectors, the only exceptions being agriculture and energy; • improving Romanian macroeconomic indicators and the growth of Romanian economy on an annual trend; • government programs for SME's financing and SME's financing guarantee; • improving ways to access and absorption of European funds; • programs to support SME at EU level	• unpredictable macroeconomic environment due to the international financial crisis • changes in regulation in the finance sector influence the behaviour of credit institutes towards SME, as implementation of new capital adequacy rules will change bank approach to SME business and will increase its administrative costs; • Romanian banks believes that credit risk has been growing for micro, albeit at a slower pace than in the previous year; • banks have important cost of evaluating the risk profiles of SME whom they are charged • banks and other financial intermediaries lack the techniques and systems to efficiently assess credit appraisal, credit scoring, credit worthiness and manage the SME repayment risk

Source: (The World Bank, 2014) (BNR, 2014, 2015) and the author

The information obtained in the SWOT analysis will be useful in order to find multiple ways to improve the access to finance of Romanian SME for years to come, as presented in the next subchapter.

5. Ways to improve financing for Romanian SME

The author's proposals resulting from the previous SWOT analysis are considering internal and external ways to improve access to finance for Romanian SME.

Regarding the actions to be taken internally by the SME they could be considered:

- Learn to understand and use a common language lender-borrower based on financial terms for business operations, performance, risk and creditworthiness;
- Take action at operational and financial level to improve the financial indicators regarding liquidity, solvency, debt and profitability;
- Observe the accounting and reporting practices applied both internal and external;

- Ensuring improvement in the financial and economic knowledge;
- Learn to approach a strategic business thinking and planning;
- Keeping up with the latest developments in SME's financing opportunities.

As for external ways to improve SME's financing the author take into consideration four important actors for Romanian financing environment such as: government, National Bank of Romania, commercial banks and European Union institutions.

Romanian government should diversify and amplify the guarantee and counter-guarantee services offered by various governmental institutions in order to decrease interest rates, reduce bank charges, lower the costs and increase guarantees to facilitate SME's access to finance.

National Bank of Romania and banks should improve policies of state-owned banks regarding SME's financing and should provide seed-capital, micro-grants and micro-credits, and also provide venture capital. In this respect, they also take into consideration the elimination of all additional declarative obligations for loan applications; centralization of data about credit products offered by banks on a special portal; establishment and promotion, according to European practice, of the mediator of loans for SME (CNIPMMR, 2015).

European Union through the European Commission should apply specific instruments and procedures for SME's financing corresponding to national particularities of each European country, should improve advertising and information on SME's financing and should supply more funds to put in practice entrepreneurial programmes for enhancing financial knowledge among entrepreneurs.

6. Conclusions

In the suite of SME's financial operations, financing enroll as one of the most important in ensuring an optimal and sustainable activity. At the small business levels it is difficult for entrepreneur to succeed to attract funds according to business needs, at costs and timeframe appropriate to the money flows derived from the activity.

This paper highlighted the associated problems of SME access to finance, highlighting developments from SME financing in European Union and between the main EEC countries and also some Romanian peculiarities. On this analytical basis they were synthesized several proposals for SME internal action, and external, in governmental institutions and banks. In this regard, the proposals made by the author are completing the previous actions for improvement made over the years at micro and macro level.

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