

SME FINANCE: A EUROPEAN PERSPECTIVE



An Evident Gap!

“SMEs are by definition differentiation-minded while banks are fundamentally cost competitors....Banks are fundamentally lenders not investors, whereas SMEs basically need investment”.

Story, M. (2002) “Banks think small: But do they understand SMEs?”
New Zealand Management; Nov



Bank of Valletta

The Great Divide?

Banks charge too much for credit, require too much security, provide insufficient long term finance and are reluctant to grant credit in relatively small amounts. (SMEs)

Risks are too high and with administrative, processing and monitoring costs which are excessive. SMEs do not provide enough attractive investment proposals and suffer from a lack of transparency. (Banks)

European Commission. (1997) "The 2nd Round Table of Bankers and SMEs (1995-1997)"



Bank of Valletta

Local Obstacles to Bank Finance:

4

GRTU Research - Annual General Conference 2005

- Long procedures
- Excessive bureaucracy
- Too much collateral
- High legal fees
- Property guarantees far in excess of loan amount
- High interest rates
- Poor assessment of entrepreneurial abilities
- Banks are not interested in new projects because there is no track record



An unhappy medium?

“It can be safely concluded that the Maltese have always managed to find the resources needed to bring their commercial ideas to light. In most cases, this has come about through the raising of conventional secured banking facilities. This, in turn, was made possible by the fact that most family businesses pioneering commerce in Malta were resourceful and owned a substantial stock of real estate, properties and other resources which satisfied the most stringent of bank regulations. Until today, there is little doubt that the Maltese business community is over-reliant on debt over equity”.

Mr L Apap Bologna, President of the Malta Chamber of Commerce, (2005)



Bank of Valletta

SME sector does not function optimally because of:

- ✓ **a lack of sufficient own capital to finance the enterprise effectively**
- ✓ **a lack of sufficient cash due to late payment by debtors**
- ✓ **insufficient access to credit on reasonable terms**
- ✓ **inadequate knowledge, experience and capacity to ensure good financial management**

Lending Infrastructure in Malta

One can intuitively deduct that weak accounting records, under capitalised companies and an inefficient bankruptcy legal system are the main adverse realities of Malta's lending infrastructure.

This is partly cushioned by the availability of tacit knowledge given the small size of the commercial community.

See Francalanza A, and C. Borg. (2000) "*Small Business Failure and the Maltese Commercial Environment*", Bank of Valletta Review, No.22

Risk Capital Provision – An Elusive Act!

“... we have far fewer stories of the young and unknown Mr or Mrs Penniless who once had a brilliant invention and today has become a successful entrepreneur - because somebody was willing to finance and share that intrinsic start-up risk. ...Past success stories were more likely to be linked to those who were able to raise informal venture capital through family, friends and the like. And so today we still have an equity gap on our hands.....”

(The Finance Ministry Parliamentary Secretary Tonio Fenech Business Times, 2004)

Reasons could be historic....

Malta's main Banks till a few years ago were state owned and supported by the traditional accommodating culture, offered a sufficient number of flexible loans, often allowing payment delays.

Smid S and S Noordam (2002) "Financial services on Malta - Study on the situation of enterprises, the industry and the service sectors in Turkey, Cyprus and on Malta"



Bank of Valletta

Or Cultural...

“The attitude of Maltese SMEs to venture capital is that they welcome the money but they do not welcome equity participation. They would rather fully own their business than 50 per cent of a much bigger and successful operation”.


















PKF, Malta (2003) *“Harnessing resources to tap EU opportunities”*

Times Business-2ndOct 2003



Survey Comparative between Maltese and EU 15 SMEs

- A survey was carried out amongst a number of Maltese SMEs during July and August 2006.**
- Survey covered areas related to:**
 - the types of finance being used,
 - bank's accessibility,
 - use of small loans,
 - use of venture capital and
 - how do SMEs meet their financial management needs.
- Survey was benchmarked with a similar survey amongst 15 European states in September 2005**
- Survey was carried out in collaboration with GRTU.**

Malta/EU 15 Survey's Sampling Comparatives

	Country Results	Sample Size	SME Population 2003	Sample % of SME Population	Country Population 2006
	Malta	93	33,550	0.28%	400,214
	European Union (15)	3047	18,700,000	0.02%	383,031,552
	Belgium	202	440,000	0.05%	10,379,067
	Denmark	206	210,000	0.10%	5,450,661
	Germany	300	3,020,000	0.01%	82,422,299
	Greece	100	770,000	0.01%	10,688,058
	Spain	300	2,680,000	0.01%	40,397,842
	France	300	2,500,000	0.01%	60,876,136
	Ireland	100	100,000	0.10%	4,062,235
	Italy	300	4,490,000	0.01%	58,133,509
	Luxemburg	100	20,000	0.50%	474,413
	The Netherlands	200	570,000	0.04%	16,491,461
	Austria	200	270,000	0.07%	8,192,880
	Portugal	100	690,000	0.01%	10,605,870
	Finland	100	220,000	0.05%	5,231,372
	Sweden	239	490,000	0.05%	9,016,596
	United Kingdom	300	2,230,000	0.01%	60,609,153

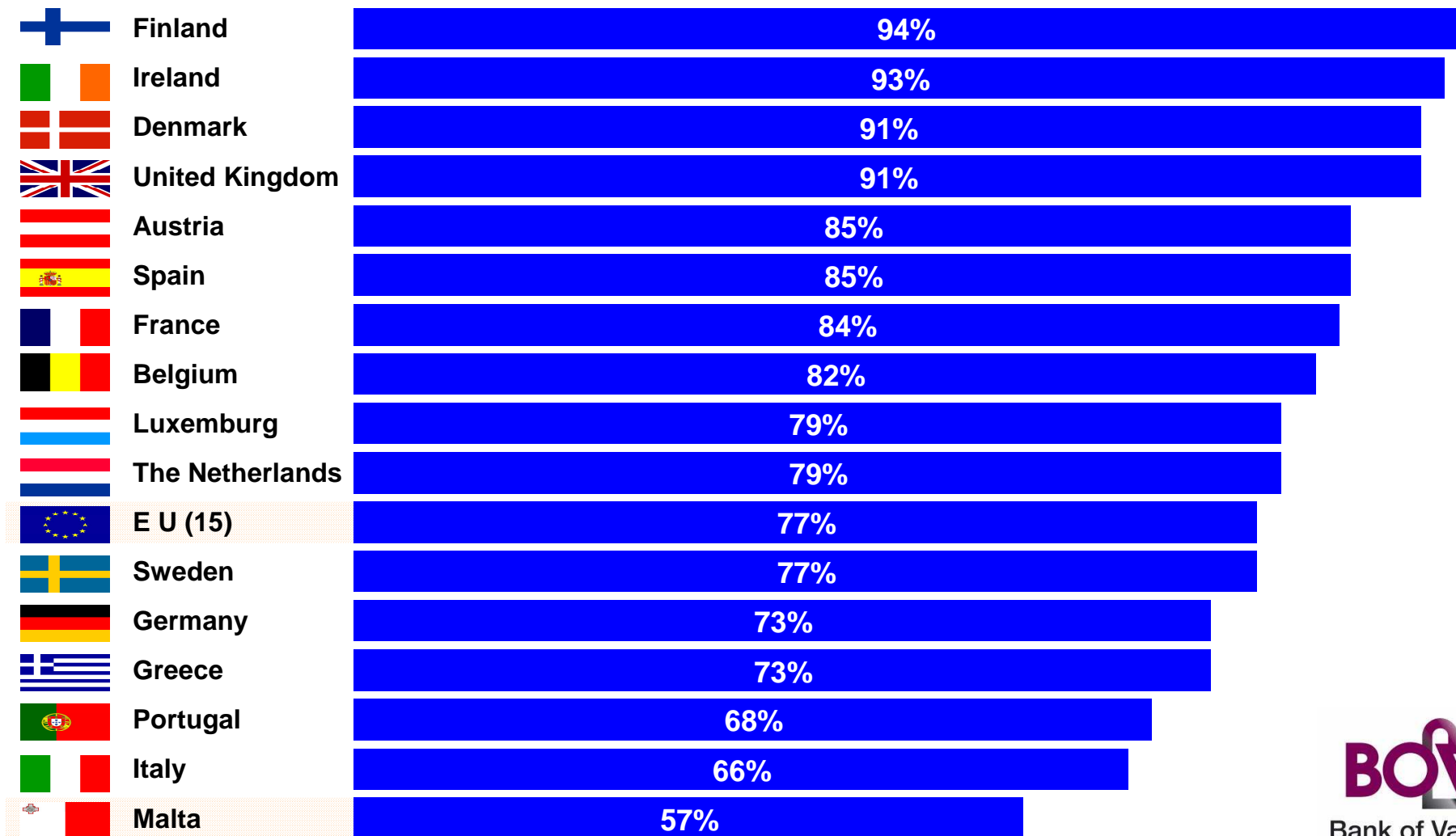
A comparative of local sample characteristics with those of EU 15

	 Malta	 EU (15)	Difference
	Total	Total	
	% of total Sample	% of total Sample	
Company Size			
micro	53	1781	-1%
small	34	811	10%
medium	6	455	-8%
	93	3047	0%
Sector			
industry	14	610	-5%
construction	6	379	-6%
trade	41	1067	9%
services	32	991	2%
	93	3047	0%
Active Since			
+30 years	36	1219	-1%
11 - 30 years	33	894	6%
0 - 10 years	24	920	-5%
	93	3033	0%
Turnover			
Less than €250,000	27	664	4%
€250,000 to €1,000,000	32	824	4%
€1,000,000 to €2,500,000	14	447	-2%
More than € 2,500,000	20	747	-6%
<i>Exchange rate: €1 = Lm0.4293</i>	93	2682	0%

Company's current financing is sufficient to see project through

14

Maltese SMEs lack finance to see their projects through



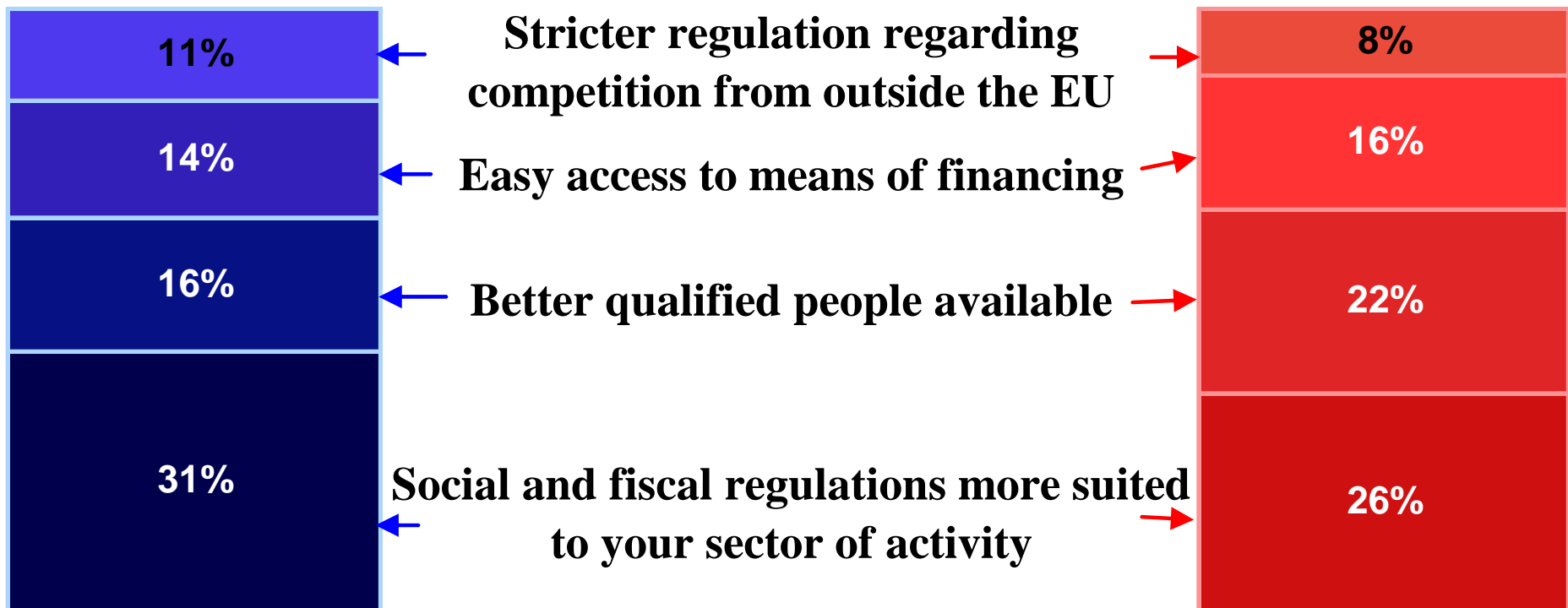
SMEs Priorities to ensure the development of their company

15

An alignment in priorities between Maltese SMEs and EU 15!

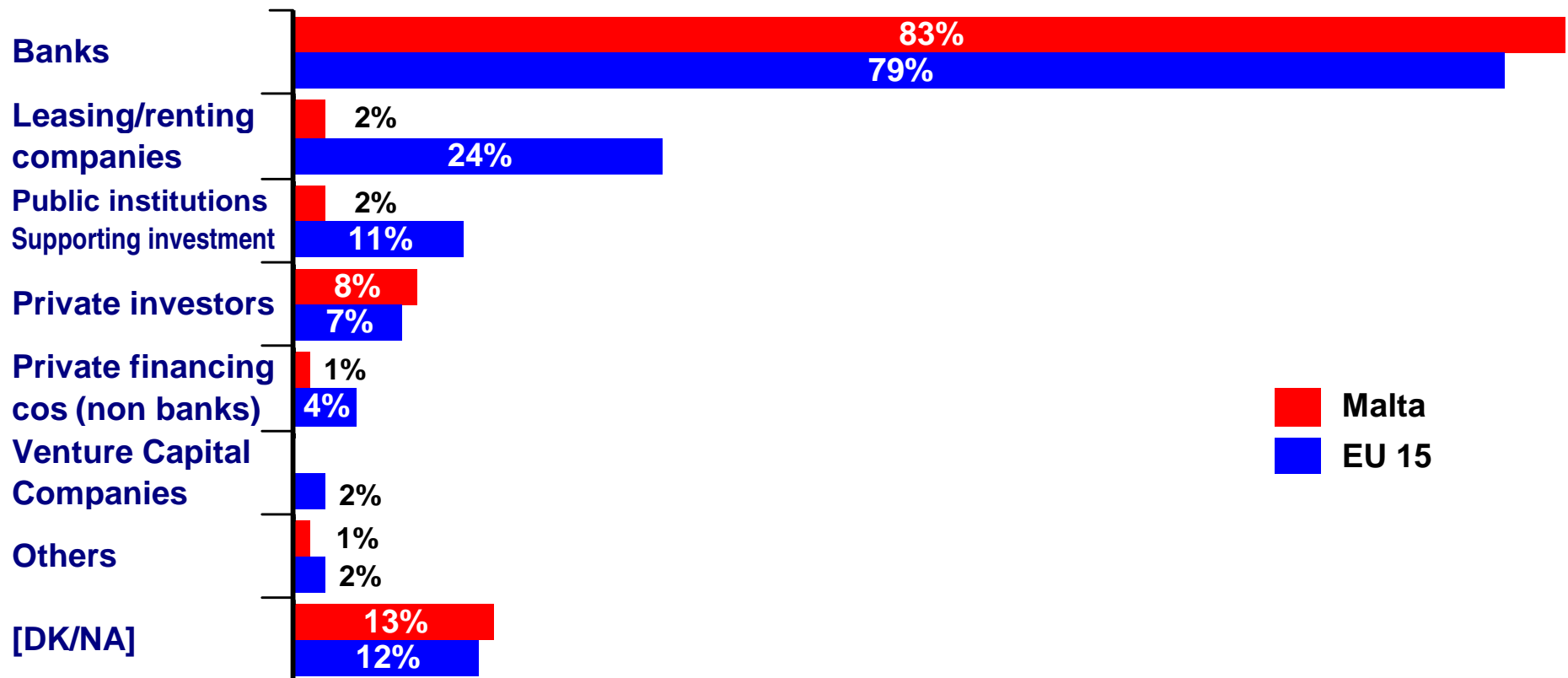
EU 15

Malta



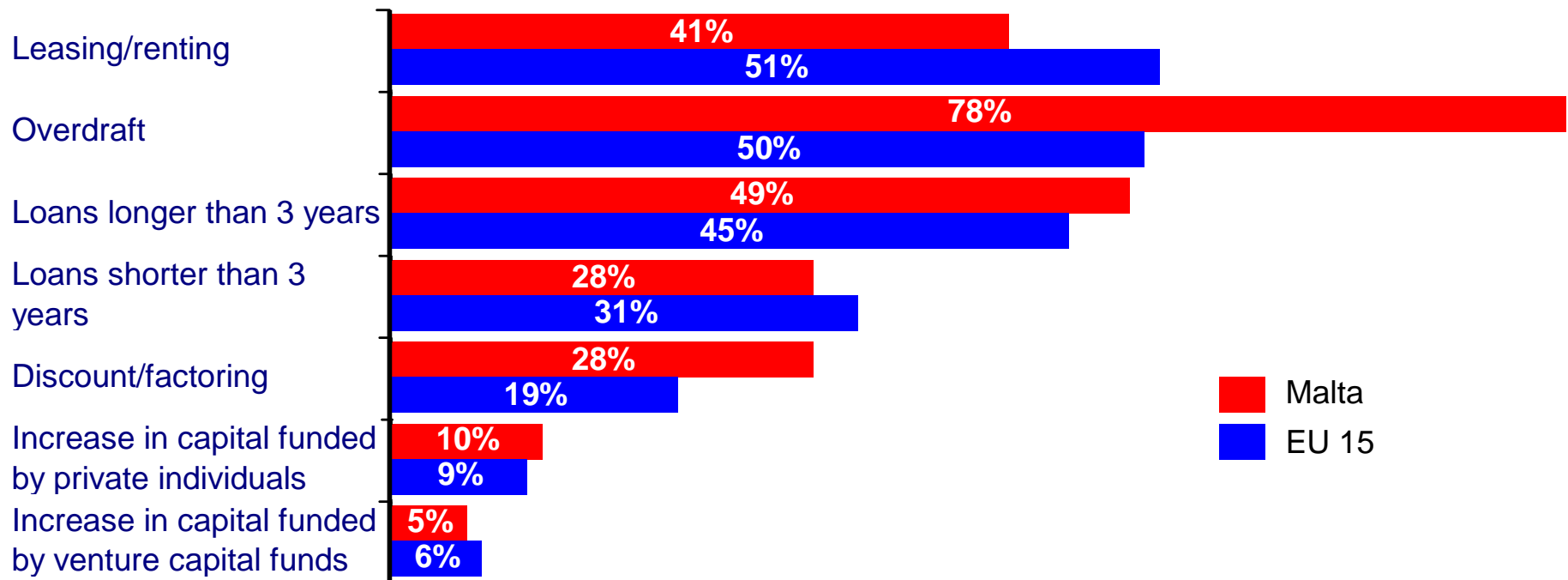
Institutions used by SMEs to obtain financing

Banks are the main institutions used by SMEs to obtain finance



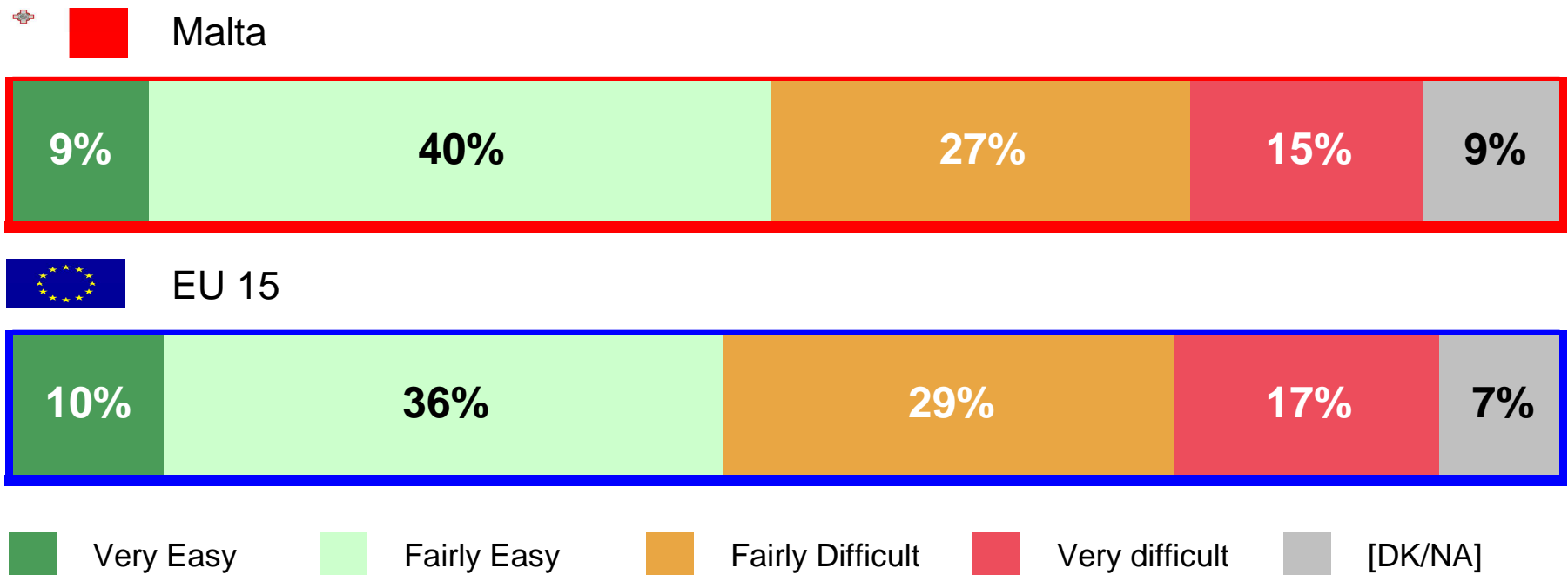
Types of financing used by SMEs

Overdrafts are the most popular type of finance by SMEs in Malta



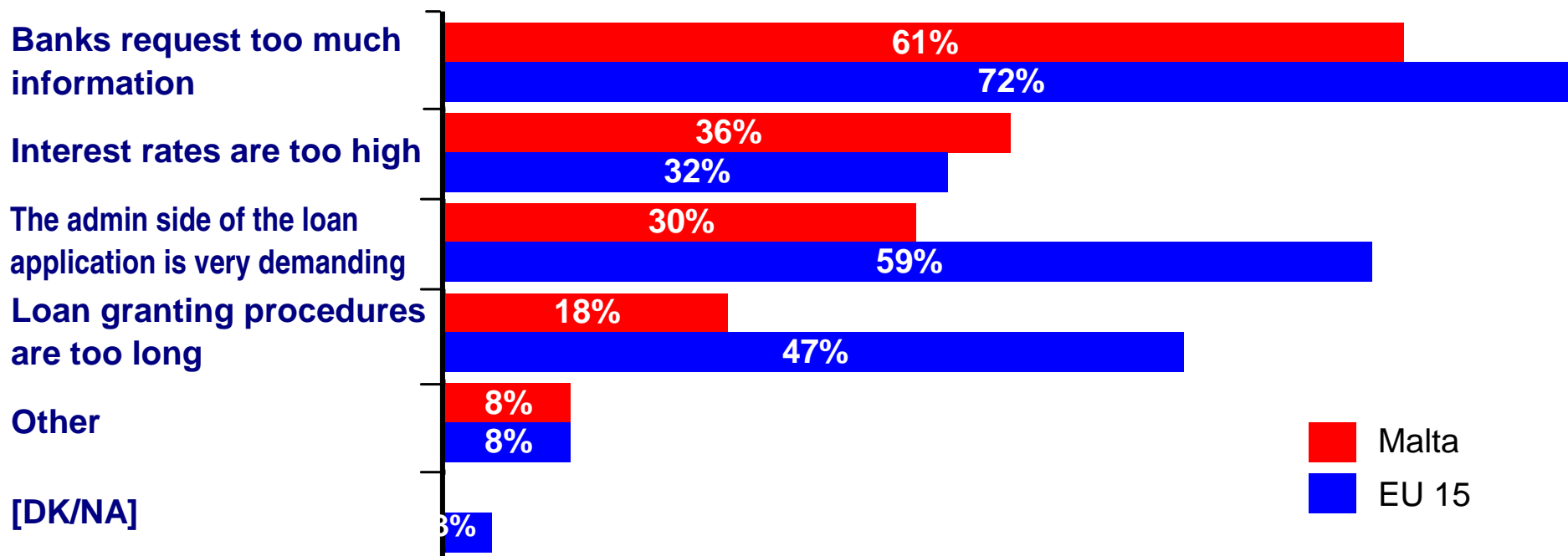
Ease of access to loans granted by banks

There are mixed perceptions regarding the ease of access to loans



Reasons why it is considered not as easy to obtain ¹⁹ a bank loan today compared to a few years ago

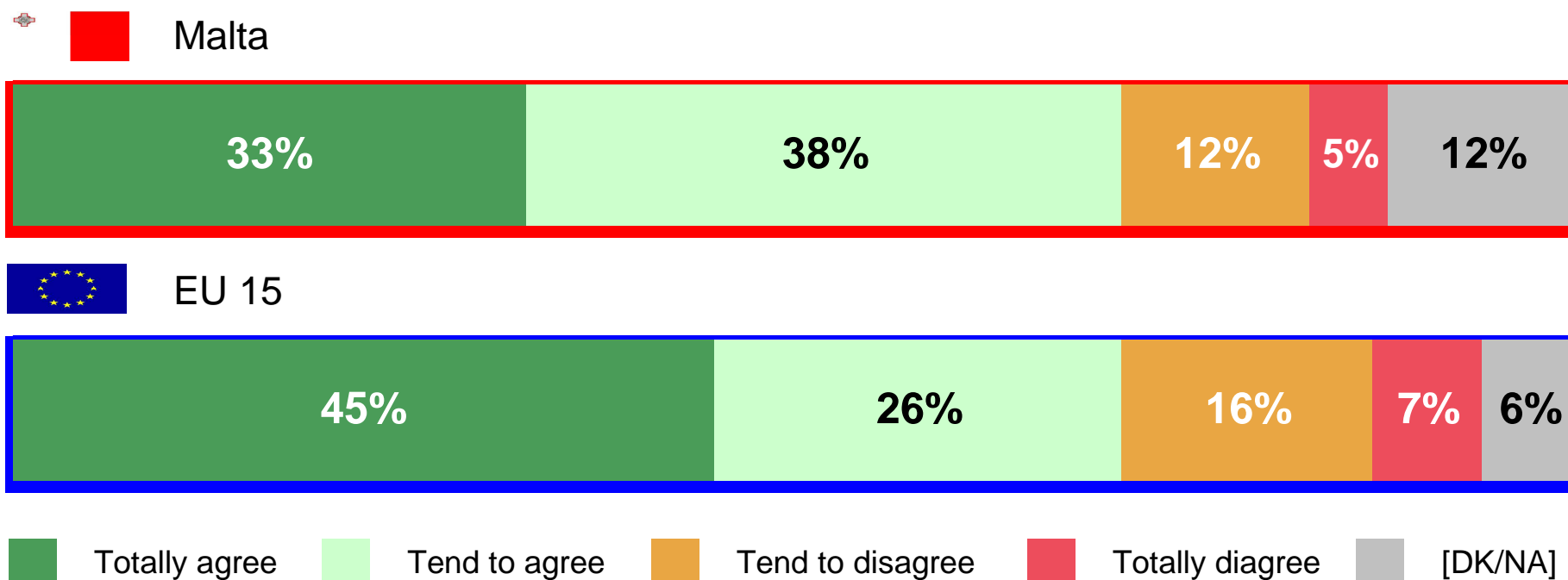
*Request for information by banks is considered excessive
– Pricing and Bureaucracy are also an issue*



"The banks do not want to take risks in lending to companies"

20

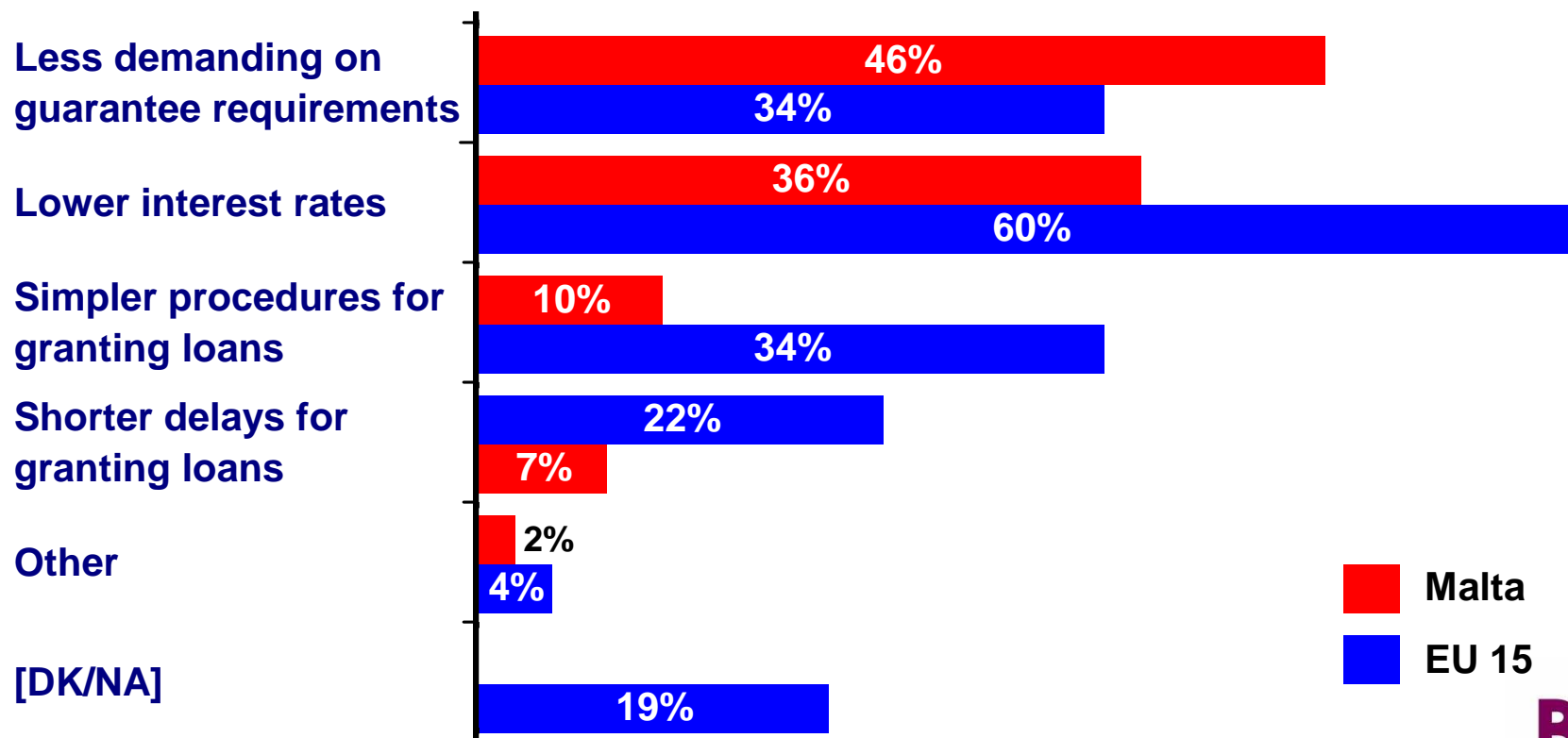
70% of SMEs consider banks as risk averse



Elements that would most encourage SMEs to resort to a loan of less than €25,000

21

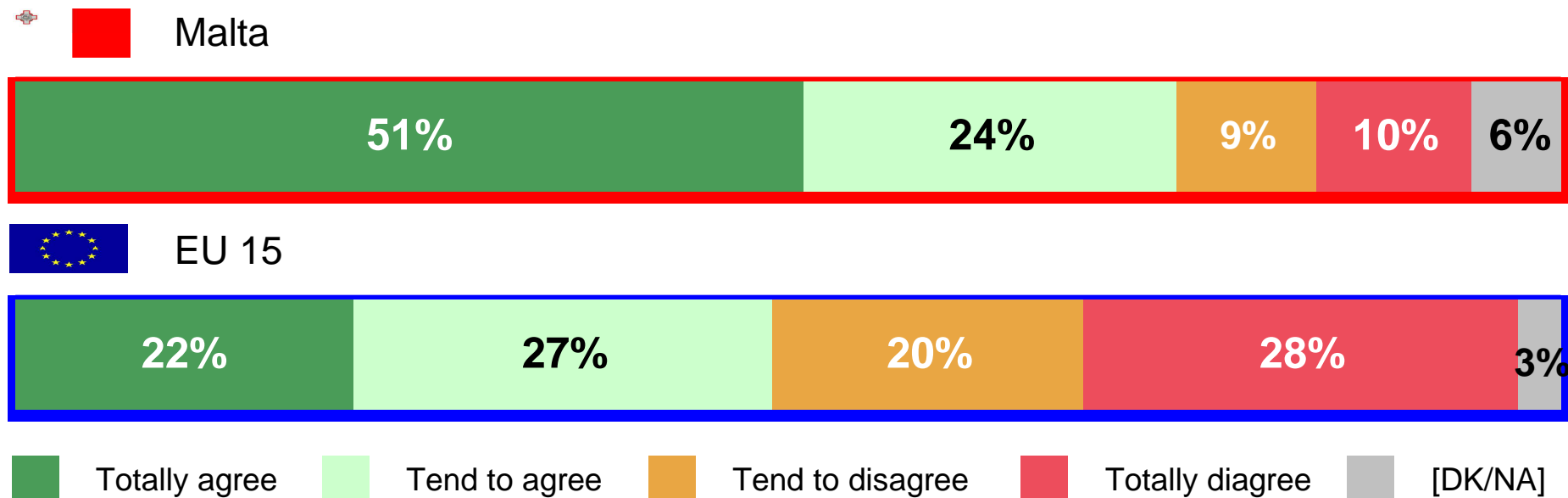
Collateral is the main obstacle for micro finance to Maltese SMEs as compared to pricing for EU 15



Note: Maltese respondents did not have the option of multiple replies as did the EU 15

"Without a loan from the bank, your projects ²² cannot be successfully concluded"

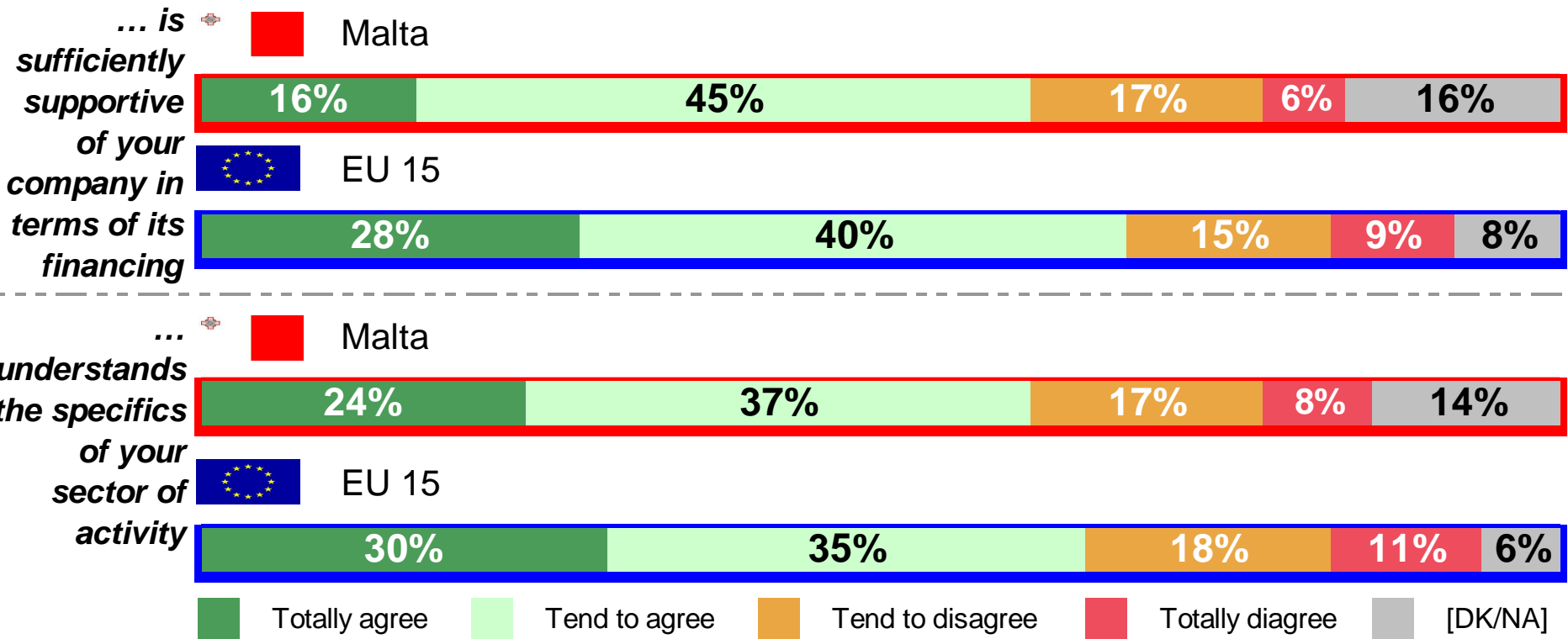
Maltese SMEs reliance on banks is very high



SMEs view on Banks

SMEs consider banks as supportive and understanding

Your banker



Future Prospects –Bank Finance

- Banks will remain important intermediaries for SME finance
- Recently banks have geared themselves more to focus on this important segment
- BOV has a dedicated Unit focused on SMEs with advisory services and tailor made packages for Micro Financing covering start-up and financing for capital and working capital expenditure



Future Prospects – Risk Capital

- Private equity (business angels) and venture capital are just appearing on the Maltese scene
- A venture capital fund is in the making
- Business Promotion Act provides grants, soft loans tax incentives and other supporting tools
- Malta Enterprise - SME Loan Guarantee Schemes
- E C initiatives such as JEREMIE earmarked to be a catalyst for a number of options including venture capital, business angels pilot scheme micro credit, securitisation and guarantees.

Thank You



Bank of Valletta