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EUROPEAN COMMISSION

MEMO

Brussels, 12 November 2014

SMEs access to finance survey 2014

This memo outlines the results of a survey undertaken by the European Commission to provide policy makers with evidence of the financing conditions faced by SMEs across the EU.

Why is access to finance important for companies?

Access to finance is a key determinant for SME success, throughout their start-up, development, innovation and growth phases. Getting a new firm off the ground or expanding it requires money, but borrowing can be difficult for SMEs - particularly if they lack collateral or do not have a long enough track record or credit history. Financial institutions are also reluctant to take on risk in the current economic climate. Governments and other public authorities therefore often facilitate small businesses' access to lending via various loan and guarantee schemes. This is why also easing access to finance by SMEs is one of the priorities of the new Juncker Commission.

How do SMEs obtain finance?

SMEs have different needs and face different challenges when accessing finance compared to large businesses. The latter have ready access to capital markets, which are not accessible to the vast majority of small businesses.

SMEs normally obtain financing through one of the following methods:

- Through equity or debt. Equity consists of retained earnings from profits the business generates and of shares in the business that are issued to investors. Debt refers to funds that are borrowed from a creditor and which need to be repaid at a future point in time.
- Funding can also be divided by source: internal and external financing. Internal funding consists of the part of equity finance that is generated by internal cash flows. External funding is supplied by financiers outside of the enterprise.

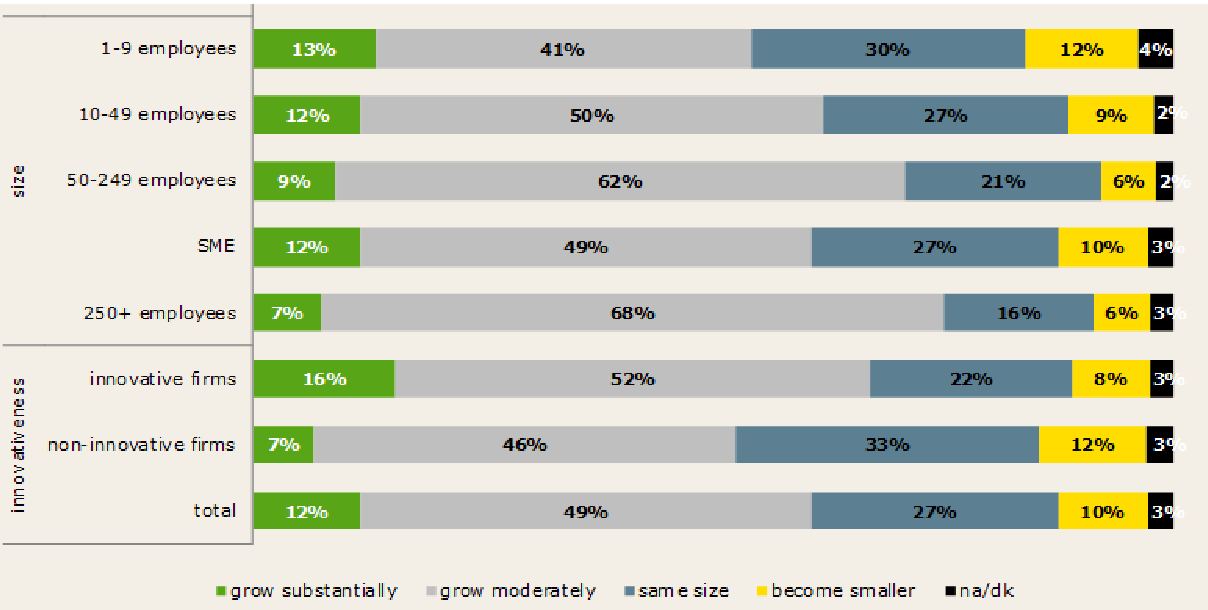
European SMEs expect to grow

The survey shows that over the past few years SMEs have become more positive about expected growth. Between 2009 and 2014 the proportion of SMEs expecting to grow increased from 47% in 2009 to 61% in 2014. The majority of these SMEs expected an annual growth rate up to 20%. 12% of SMEs expected an annual growth rate of more than 20%.

Growth expectations increased with enterprise size: 75% of the large enterprises expected growth over the next two or three years versus 54% of micro enterprises. In contrast, the proportion of enterprises expecting to grow substantially (over 20% per year) decreased with enterprise size: 13% of the small enterprises expected to grow substantially versus

7% of the large enterprises. Additionally, innovative SMEs were the most optimistic about future growth.

Table 1: Growth expectations over the next two or three years.



Demand for finance is increasing ….

SMEs' needs for equity financing increased in 2014 compared to 2013, with a net increase from 2% to 8%. The need for trade credit[1], credit lines and bank loans rose by 13%, 10% and 1% respectively in 2014.

Variations still exist between countries. Net changes of SME needs for bank loans in the EU countries ranged from +25% in Greece, +20% in Lithuania and Malta to -7% in Germany and -10% in the United Kingdom and the Netherlands.

….and there is a perceived improvement in supply of finance

If we look at bank loans, on average SMEs perceived bank loans to be available. However micro enterprises perceived it to be much harder than larger companies to obtain bank loans.

However, across the EU countries there are significant differences. Since the last survey in 2013, net changes of availability of bank loans reported by SMEs ranged from +18% in Malta and Lithuania and +17% in the Czech Republic to -21% in Greece, -25% in Cyprus and -28% in Slovenia.

Construction, micro and innovative companies still have problems

For 13% of EU SMEs access to finance remains the most important problem faced by their business[2]. The issue of access to finance is perceived as most pressing for SMEs in Cyprus,

[1] Trade credit is a common source of short term financing in which credit is extended to a company by suppliers - allowing the company to buy now and pay later. It is granted to businesses who have reasonable amount of financial standing and goodwill.

Greece and Slovenia. Comparing different types of enterprises, SMEs in construction considered access to finance to be the most problematic. Micro enterprises and more innovative enterprises also consider the problem of access to finance to be the most pressing.

Bank loans remain the favourite form of external financing

Bank loans remain the preferred option of firms looking for an external financing solutions to realise their growth ambitions (62% prefer bank loans). 15% of SMEs preferred other sources of financing such as trade credit or loans from related companies, shareholders or public sources. 7% of SMEs with growth ambitions preferred equity investment and 10% preferred other types of financing.

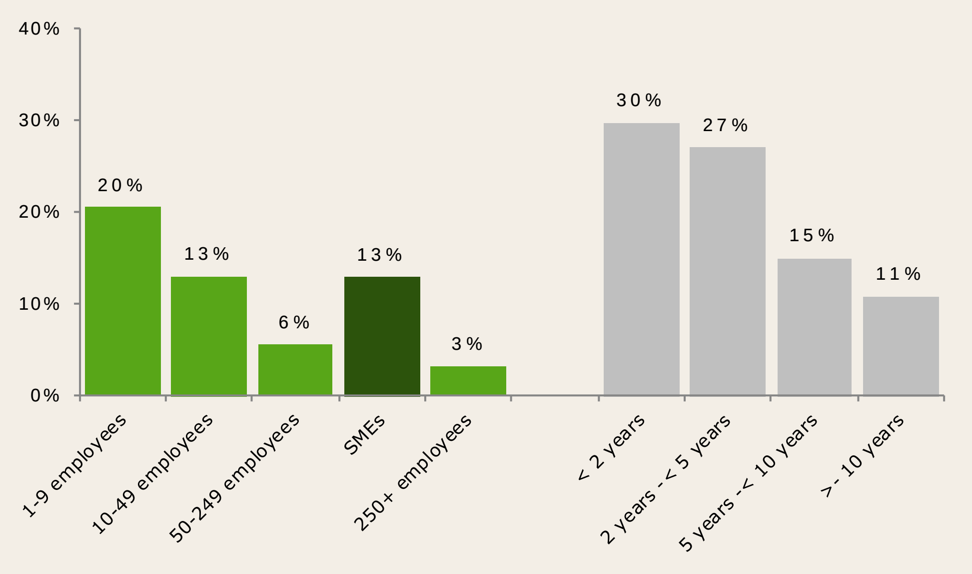
Between April and September 2014, 28% of SMEs actually applied for a bank loan. 8% of SMEs did not apply because of fear of rejection. The fear factor was most often reported in Greece (29% of SMEs), Slovenia (22%), Cyprus (17%) and Ireland (15%).

Overall, 38% of SMEs did not apply for a bank loan as they had sufficient internal funds.

Slight increase in rejection of bank loan applications

Looking at the success rates of bank loan applications, 13% were rejected by banks over the time period analysed by the survey (April to September 2014). This is a slight increase from 11% in 2013.

Table 2: Bank loan rejection rate



The difficulties of accessing bank loans are particularly affecting smaller and younger companies. The highest rejection rate was among micro companies employing fewer than 10 people (20%) and in addition almost half of them did not receive the full bank loan financing they had planned for. Loans applications from SMEs which had been active for less than 5 years were rejected more often: 30% of those from SMEs younger than 2 years and 27% of those from SMEs active between 2 and 5 years. In comparison, only 3%

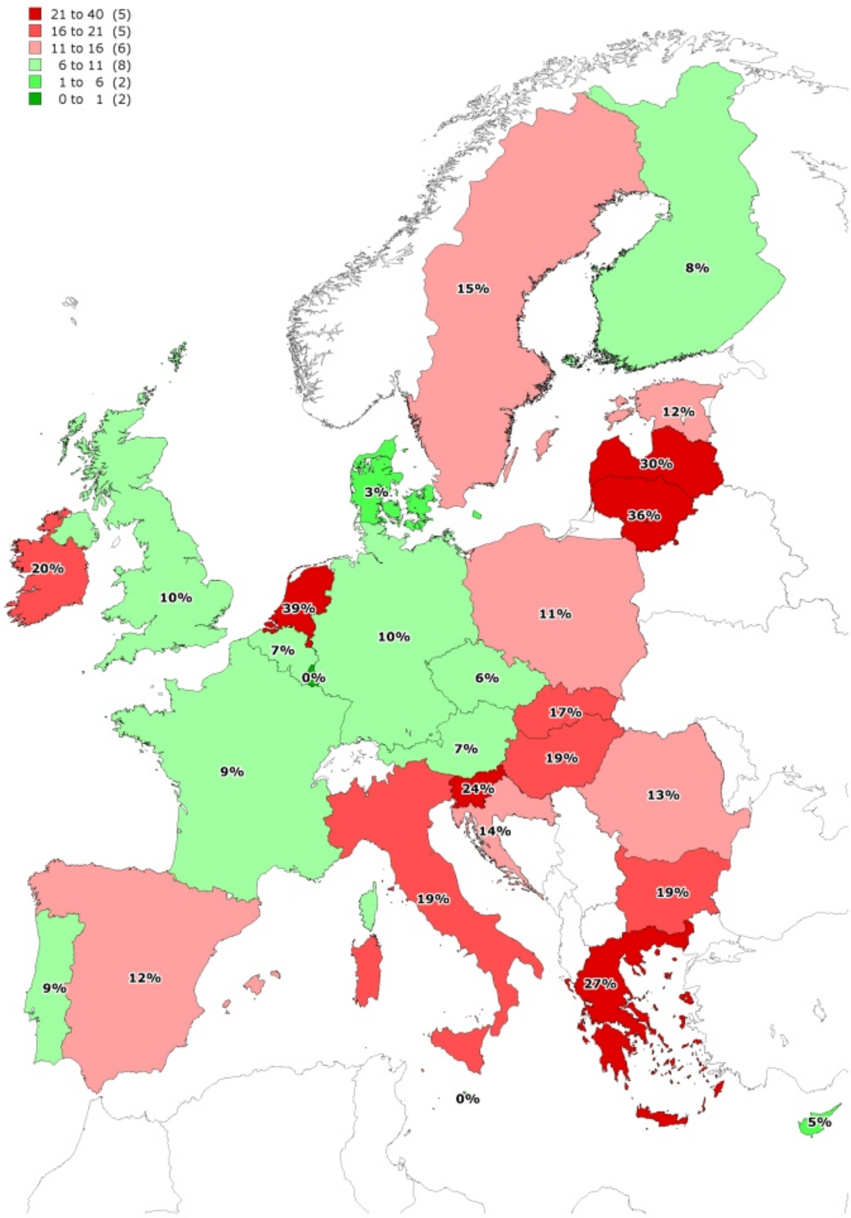
[2] The survey found that on average, SMEs' biggest concerns are finding customers, finding skilled staff, regulation, and competition followed by access to finance

of loan applications from large enterprises (those with 250 or more employees) were rejected.

The highest outright rejection of loan application was reported by SMEs in the Netherlands (39%), Lithuania (36%), Greece (27%), Latvia (30%) and Slovenia (24%).

In addition to the problem of loan applications being rejected, 18% of successfully applying companies received less than they applied for and 4% declined the loan offer from the bank because they found the cost unacceptable. It means that in total more than a third of the SMEs surveyed did not manage to get the full bank loan financing they had planned for during 2014.

Figure 1: Bank loan rejection rates



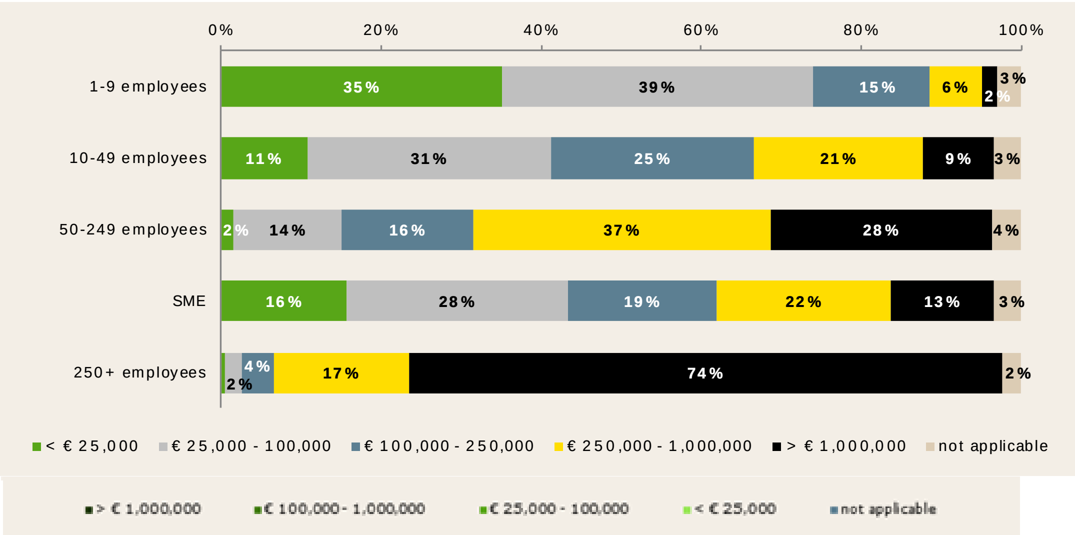
Loan amounts correspond to company size, but are increasing overall

The most often mentioned amount of financing that growing firms expected to ask for was between €25 000 and €100 000 euro (this was for 25% of those SMEs expecting growth) but other amounts were only slightly less often reported. With exception of micro companies, the EU SMEs reported in net terms an increase of the available size of loans.

Regarding size of the last loan actually obtained, most of SMEs had applied for small loans: 16% applied for up to €25 000 euro and 28% between €25 000 and €100 000.

There is a clear correlation between a size of a loan and a size of an enterprise: 3 out of 4 of micro companies received a loan up to €100 000, half of small companies received a loan between €25 000 and €250 000, and half of medium sized companies received between €100 000 and €1 billion. With respect to large companies, 3 out of 4 received a loan exceeding €1 billion.

Table 3: Size of the last bank loan.



A net decrease in size of loans was reported in Slovenia, Greece, Cyprus, the Netherlands and Italy. The highest net increases were observed in the Czech Republic, Denmark, Finland and Portugal.

Interest rates vary, micro firms still face higher rates

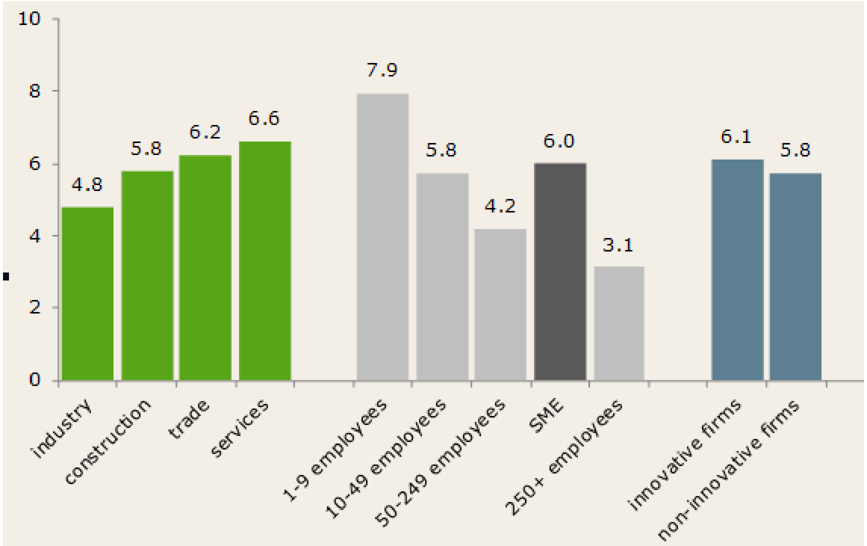
The companies were also asked about the price paid for the last obtained loan – i.e. the interest rate charged for the credit line or bank overdraft. On average, the interest rate reported by the EU SMEs amounts to 6% between April and September 2014. Differences between countries are significant. Interest rate above 7% was mentioned in Portugal and Greece. Conversely, SMEs in Austria, Belgium and in particular Luxembourg reported rate below 4%.

The interest reported by SMEs in industry is well below average, while SMEs in services are confronted with an above-average interest rate. The variation across enterprise size classes is stronger. The data show that the interest rate for smaller enterprises is higher than the interest paid by large enterprises: micro enterprises reported a rate of almost 8%, while for large enterprises it was only 3%. The difference between innovative and non-innovative SMEs was negligible.

With exception of micro companies, the EU SMEs reported in net terms a fall in interest rates. The average loan duration remains stable.

At country level, the highest net percentages of SMEs reporting an increase in interest rate were in Italy, Ireland, Cyprus and Slovenia while a net decrease was most often reported in Sweden, Belgium, Germany and France. Of those SMEs who mentioned that bank loans were not relevant for them - with the exception of the 67% that simply did not need a loan - 11% reported that the interest rate or price was too high. Price considerations were particularly important in Bulgaria (35%), Romania (34%) and Croatia (28%).

Table 4: Average reported interest rate charged for the credit line or bank overdraft



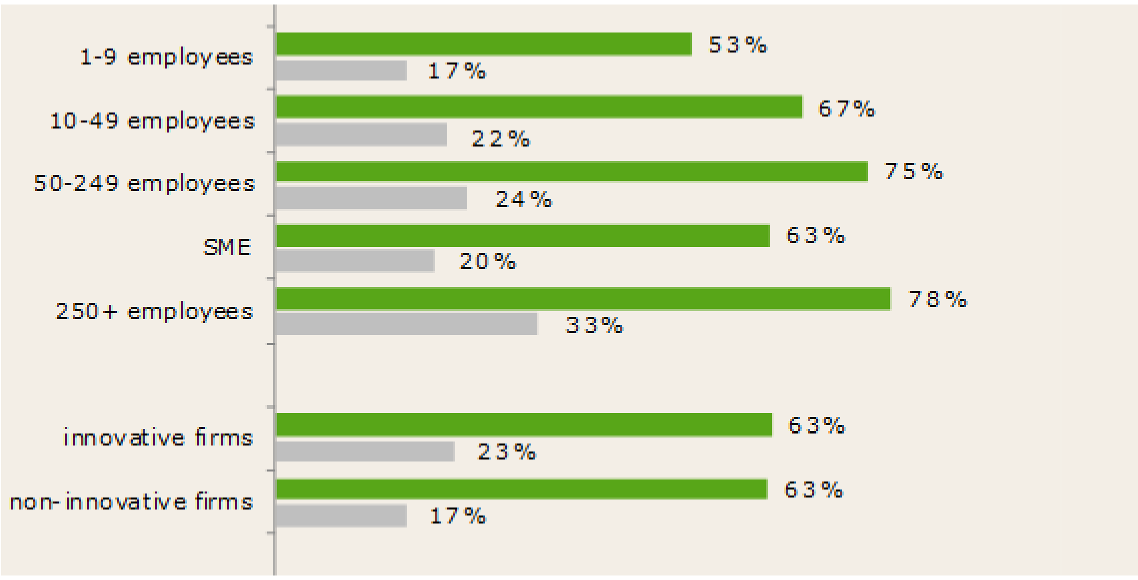
Collateral requirements have been increased by banks

In contrast to their experience with interest rates, SMEs reported a substantial net increase in collateral and other loan requirements by banks to which they had applied for loans. Collateral requirements were considered as tightened by SMEs in all EU countries, with the highest average increases in Cyprus, Greece and Slovenia, while the lowest average increases were reported in Poland, Slovakia and the Czech Republic.

Lack of financial knowledge narrows finance options

The SMEs were also asked about their financial knowledge – if they were confident in talking with banks or investors about financing. When negotiating with banks, about two third of SMEs in the EU felt confident and full quarter did not. With respect to equity, only 20% of SMEs felt confident to discuss financing and obtaining the desired results with equity investors and venture capital enterprises, while 32% did not feel confident. Smaller and non-innovative firms are less confident in their financial competences.

Table 5: Confidence in talking with banks, equity investors and venture capital enterprises about financing and obtaining the desired results



[Report on the Access to Finance of Enterprises (SAFE) in 2014]