Small and Medium Enterprises (SMEs) in Greece - Barriers in Access to Banking Services. An Empirical Investigation

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Abstract

The main purpose of this paper is to describe the main factors restricting the access of Greek small and medium enterprises to banking services. The analysis is based upon a special questionnaire through which are investigated the problem of SME financing. The questionnaire surveys were arranged in such way that representatives of banks and SMEs were expected to answer the same questions, which allowed to confront directly their opinions. It was used a sample of almost 250 respondents from the SME sector and three Greek banks with the biggest shares in the market of banking services provided for the SME sector. The first part of the article presents the role of SMEs in the sustained economic development and the actual development of SMEs growth in Greece. Next we describe the main sources of financing using by the small and medium enterprises in the different phases of their life. The main aim of the next part of the paper is to exam in details the findings of the survey and to identify the main constrains in SME financing. Finally we try to present future opportunities and threats for SME taking into consideration the assumption that the access to banking financing has a considerable influence on the development of SME sector in Greek economy.

Keywords: SME, Banking Sector, Greece

1. Introduction

The small- and medium-sized enterprise (SME) sector is considered crucial to European competitive development. It employs the majority of the European labor force and commands two thirds of sales volume in the non-primary sector. Small and medium enterprises play also a very important role in the economies of the Central and East European transition states. The importance of the SME sector in these economies is correlated with such reasons as demopolization of economy, social stability through the development of the middle class, creation of a significant number of new jobs, etc. (Hyz, A., 2006). In the last decade, SMEs are considered with an increasing interest by European policy makers, public authorities and economists (Acs and Audretsch, 1990) who are trying to support them in finding financial resources and establishing cooperative relationships among them in an effort to help them remain viable and competitive. Greek SMEs represent a very important share of the economy, accounting for a far larger share of total employment and value added than the EU average. Due to this fact the financial performance and viability of SMEs are very important to the Greek economy as well as to investors, bankers and their suppliers. European Union (EU) integration and globalization have brought strong competition to the Greek manufacturing sector, which now faces survival problems. In order to be competitive, the firms must first be financially viable. Although the role of the Greek small and medium enterprises is vital to the Greek economy, the existing literature on this topic is rather limited.

2. Main Characteristics of the SME Sector

The SME[1] sector plays a very important role in today's economy. It is confirmed by the experience of highly developed countries, whose economies are dominated by the network of small (or virtually very small) and

[1]

Enterprise category	Headcount	Turnover	or	Balance sheet total
medium-sized	< 250	≤ € 50 million		≤ € 43 million
small	< 50	≤ € 10 million		≤ € 10 million
micro	< 10	≤ € 2 million		≤ € 2 million

Source: http://ec.europa.eu/enterprise/enterprise_policy/sme_definition/index_en.htm

medium-sized enterprises. Two most important measures of the role played by SMEs in the economy are: the share of this sector in the total number of economic unit and its ability to create new jobs (OECD, European Observatory for SMEs, 1997). The SME sector is practically the only sector of the economy in contemporary developed countries, which generates net jobs. New job creation takes place both through setting up new economic units and through developing already operating firms. The SME sector is also a major source of inventions (OECD, 1995). It distinguishes itself by a high efficiency in the field of innovations launching them at lower costs that big companies. The importance of innovation propensity in the SME sector is emphasised more strongly in developed countries. Small innovative firms and especially those operating in high technology fields contribute significantly to creating and developing new fields of manufacturing, new industrial branches based on modern technologies. Small innovative firms are frequently fast-growing firms creating new jobs (Mulhern, 1995).

The European SME sector has some notable strengths: strong business dynamics (especially a high birth rate); an increasingly higher level of education among its entrepreneurs; increasing internationalization of trade, direct foreign investment, and strategic alliances; and high job creating potential resulting from high birth rates and lower-than-average wages. Its weaknesses include: a high mortality rate, though less than the birth rate; lack of strategic marketing approaches and the custom of operating in highly segmented markets; low labor productivity resulting in high unit wage costs despite lower-than-average wages; and a weak financial situation resulting from a low equity/debt ratio and costly loans (Dunlop, 1992; Acs, Audretsch, 1993).
Economic theory suggests that SMEs differ significantly from the large firms because SMEs have lower productivity and higher production costs due to small-scale of production. Furthermore, they face higher supply cost and shorter supply terms, while they are forced to give longer credit terms to their customers as a means of sales promotion. Micro firms sell mostly to final customers and operate in more segmented product markets. It is the larger firms that are more likely to export. The smaller firms depend more on their local economies than do large firms.

The above result in lower profitability and increased needs in working capital financing (Dunlop, 1992; Cosh and Hughes, 1993; Chittenden et al., 1996, and Rivaud-Danset et al., 1998). The lack of adequate collateral, lack of information, low credibility and higher financing costs, coupled with SMEs reluctance to issue capital, fearing loss of control of the firm, have resulted in lower use of long-term debt and high reliance on short-term financing (Gupta, 1969; Tamari, 1980; Ang, 1992; Chung, 1993). Greece is considered as the country of SMEs with 99.9% of its firms in the non-primary sector employing 100 persons or less, accounting for 82% of the total employment and approximately 69,6% value added (see table 1). According to the data for the Greek economy there are approximately 73 SMEs per 1000 inhabitants in Greece, which is greatly above the EU-27 average of ca 40 (European Commission. Enterprise and Industry. SBA Fact Sheet. Greece). Since this is mainly due to a high overall number of businesses, Greece is only slightly above average in terms of the proportion of SMEs as compared to all enterprises. More than 97% of all Greek enterprises are micro companies[2]. The small size of Greek SMEs is due to their strong domestic market orientation and small market size, in general, the low GDP per capita, tendency to the self-employment and so on.

Table 1: Characteristics of the SME sector in Greece

	Number of enterprises			Number of persons employed			Value added		
	Value	%	EU-26 average	Value	%	EU-26 average	Value	%	EU-26 average
Micro	796.454	97,1	91,8	1.401.286	56,5	29,6	23.379	36,6	21,1
Small	21.235	2,6	6,9	392.668	15,8	20,6	11.845	18,5	19,0
Medium	2.496	0,3	1,1	240.199	9,7	16,8	9.279	14,5	17,8
SMEs	820.185	99,9	99,8	2.034.153	82,0	67,1	44.503	69,6	57,9
Large	462	0,1	0,2	447.752	18,0	32,9	19.387	30,3	42,1

Source: Eurostat SBS data base, 2005 data

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[2] It is worth to notice that the Mediterranean countries (Italy, Spain, Greece, Portugal, and southern France) have a greater preponderance of smaller firms than the generally wealthier northern European countries. The further north one goes in Europe, the larger average firm size tends to become. Denmark, Germany, France, and Britain, for example have an average enterprise size over double that of Portugal, Spain, Italy, and Greece. The Scandinavian countries, shortly to enter the KU, have the largest enterprises of all.

3. Sources of Capital for SMEs

Access to sources of capital is determined, to a large extent, by the firm's development phase, which has a major impact on evaluation of its creditworthiness. During early phases of their development firms have to rely primarily on financial resources possessed by their owners and their families, sometimes on assistance funds or on venture capital. During further phases of its development the firm is financed primarily from accumulation of financial surpluses and additionally by means of external capital. Mature firms (mainly medium-sized enterprises) have an easier access to external capital and, in particular, bank loans than other groups of firms from the SME sector.

External capital becomes the main source allowing to finance the firm's investment projects in the situation when internal accumulation capabilities of SMEs are limited. Insufficient availability of external capital can restrict the firm's growth opportunities. The main sources of external capital for small and medium-sized enterprises are the so-called non-banking sources of financing (trade credit, lease, factoring, franchising, loans from the non-banking sector) and bank loans (short- and long-term). The Greek SME sector has also access to capital provided by different types of the EU's assistance programmes and funds allocated in the framework of government projects assisting small and medium-sized enterprises. In most countries, commercial banks are the main source of finance for SMEs, so if the SME sector is to florish it must have access to bank credit (EOS Gallup Europe, 2005). Taking into account the fact that SMEs (due to their size) are unable to raise investment capital in the capital market, the banking system becomes the only real opportunity of raising additional financial resources. This situation is theoretically advantageous for the SMEs due to the detailed evaluation of an investment project by the bank, which implies, among other things, the feasibility analysis of a project and professional counselling provided by the bank's employees. On the other hand the position of SMEs in the bank loans market is determined by a strong influence exerted by structural characteristics of these enterprises.

4. Results

The survey was developed from June 2008 to December 2009. The draft questionnaire was piloted in 10% of the survey and subsequently amended in the light of the findings from the pilot. The survey was designed to be send by mail. However, because of the specific nature of SME's business culture and based on the experience of previous surveys we decided to conduct the survey by telephone. Specific characteristics of SMEs - their size and big diversity of economic units with a big growth potential cause that they should constitute for banks a desirable group of clients. Meanwhile, the situation looks different. Cooperation between banks and Greek SMEs seems to be at a highly unsatisfactory level. The gaps in the financing of small and medium sized enterprises were observed, both in the start-up phase and in later growth. Our research was carried out to identify causes of such a situation. Around 42% of the managers surveyed feel that the offer from the banks is not suited to their needs. In other words, a key factor is a small demand of SMEs for services offered by banks. In general only about 23% of a SME's turn firstly to banks when they look for information or advice about financing. According to enterprises, the next barriers in access to banking services are: high costs of bank loans, collateral required by banks, complicated and time-consuming procedures connected with obtaining bank loans. According to the survey almost 7% of SMEs representatives believe that banks request too much information, the administrative side of the loan application is very demanding (59%), the loan granting procedures are too long (47%) and around a third feel that interest rates are too high (32%).

These restrictions are faced, first of all, by the smallest firms and business startups. Whereas it can hardly be expected that banks should simplify their procedures and lower the level of a required collateral taking into account only the firm size, it can be expected that costs of obtaining bank loans should decrease in the longer perspective. Taking into consideration the fact that SMEs have very limited possibilities of their development relying solely on their own capital, unavailability of loans in the domestic financial market including investment loans poses a major barrier reducing development potential of small and medium-sized enterprises. It should be noted that many of the SME's included in the survey do not have a development plan for the coming years (65%). The likelihood that a company has a development plan decreases as the number of years it has existed goes up and increases as turnover and employment increases.

The third place was taken by major discrepancies in evaluations given by both sides. According to enterprises, arduous banking procedures are a very important barrier. Although the managers in Greece are most likely to feel that compared to a few years ago it is now easier to obtain a bank loan (85%). Meanwhile banks claim the weaknesses from the financial management viewpoint which include:

small ability to accumulate financial surpluses not giving a guarantee that the invested capital will be returned; high costs of firms' operation and the low profitability; constraints connected with a specific financial management in firms and low level of managerial skills of owners and management.

In the opinion of banks SMEs are not prepared properly to use banking services. The next question was addressed solely to enterprises and it concerned a discriminatory treatment of SMEs by banks during the evaluation of loan applications. The answers should induce banks to draw more serious conclusions: 92,4% of entrepreneurs confirmed that such discrimination did exist, while 76,7% pointed to a harmful character of such discriminatory activities.Banks were asked a question concerning the reliability of data to be found in documents submitted by entrepreneurs. Banks assessed the reliability of data submitted by micro firms at the level of 2.5 points and the reliability of data submitted by small and medium-sized enterprises - at 3.6 points (on the 5-point scale). Entrepreneurs, in turn, stated that it was very difficult or impossible to conceal any information, as banks analysed and verified the credibility of documents very carefully (in the opinion of 96.6% of all respondents).

Another problem raised by firms is the fact that banks are not elastic in the situation when a debtor faces liquidity problems. Half of the interviewed firms assessed that the possibilities of negotiating the repayment of loan rules are very poor.Banks in their questionnaire identified conditions determining possibilities of loan restructuring which include: the debtor's present financial situation and possibility of debt restructuring and the history of co-operation.

It is also worth to notice that:

1. Firms in the SME sector display clear unwillingness to seek external sources of capital. The most important role is still played by the owners financial resources and retained profit. Loans taken by them are usually needed to maintain their liquidity and more seldom for investment projects. It is primarily due to a conviction prevailing among SMEs that procedures of granting loans are very complicated, loan costs are high and small firms are discriminated.
2. Banks do not generally distinguish in their policy specific aspects of the SME
sector and its growing diversity - a major advantage of very small firms and the fact that a significant share of these firms are young firms.
3. The survey indicates that young companies are more likely to open up or increase capital than those that have been operating for many years. Among SME's that have operated for 30 years or more, one in six affirm this intention in the future, compared to about one in three SME's that have existed less long. Companies that have seen an increase in the number of employees in the past year are significantly more likely to consider opening up or increasing their capital (37%) than are companies where the number of employees has stayed the same or decreased (26% and 28%, respectively).
4. SMEs and, particularly, young and very small firms do not have a positive experience from their co-operation with banks and such experience does not encourage them to intensify their co-operation with banks. Cooperation with banks does not usually constitute an integral element in the development strategy of SMEs. It is based in most cases on seeking a bank's assistance in critical situations and not on partnership relations, from which both sides can derive definite advantages.
5. Despite the importance of innovative SMEs, they face particular problems when attempting to access financing as they represent a higher risk than traditional SMEs or large firms.

5. Conclusions

Small and medium sized enterprises are the backbone of all economies and are a key source of economic growth, dynamism and flexibility in advanced industrialized countries, as well as in emerging and developing economies.Improving the access to finance of small and medium enterprises is crucial in fostering entrepreneurship, competition and growth in Europe. Access to sufficient and adequate capital to grow and further develop their activities is a difficulty faced by Greek SMEs. This situation is compounded by the difficulties in accessing finance as SME financing is considered by many financial providers as a high risk activity that generates high transaction costs and / or low returns on investment.

Financing is necessary to help them set up and expand their operations, develop new products, and invest in new staff or production facilities. In the fast-changing knowledge – based economy the financial gap in SMEs is all the more important because of the speed of innovation (OECD, 2006). The small size of the Greek's SME accentuates their financing problem. Furthermore, short-term bank lending is more expensive for small than for large enterprises in Greece because of the higher inherent risk and the lack of collateral.

The financing problem of Greek manufacturing SMEs becomes more pronounced within a liberalized financial system and within an economic environment of fiscal and monetary constraints. Financial liberalization means elimination of quantitative and price controls on domestic banking, thus making the allocation of funds more competitive. Fiscal austerity, on the other hand, leads to a reduction of expansion opportunities for SMEs. Monetary restraints and the maintenance of high interest rates in Greece, especially for the period under study, have been major problems for small firms.

Problems connected with financing SMEs operations constitute the main barrier in development of Greek small and medium-sized enterprises. These enterprises have a restricted access to external capital and, hence, relatively few of them tap such capital relying mainly on their own funds. It restricts their development opportunities, affects negatively growth of their competitiveness and possibility of strengthening their market position. The difficulties that Greek SMEs encounter when trying to access financing can be due to an incomplete range of financial products and services, regulatory rigidities or gaps in the legal framework, lack of information on both the bank's and SME's side. Banks often avoid providing financing to certain types of SME's, in particular, start ups, innovative and very young firms that typically lack sufficient collateral, or firms whose activities offer the possibilities of high returns but with high risk. For such company to be able to grow and operate on a wider scale in the domestic market and next in the international market there are not only needed such factors as good ideas and owners' determination, but also a capital. Availability of investment capital and not only short-term financing of current needs is one of key factors determining growth opportunities of SMEs.

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