# Access to finance – Conference World Saving Institute and World Bank

# Thursday, October 28, 2004, 14.30 to 16.00 – Hotel Marriott

## Working group (3): **How can SME finance be improved?**

Panellists: Mr. Ramalho (Saving Bank Portugal) – Chairman
Mrs. Wallace (Director, European Bank for Regional Development)
Mr. Summa (DG Enterprise)
Dr. Steinpass (Deutscher Sparkassen und Giroverband)
Mr. Müller
Mr. Radcliff (ESBG) - Rapporteuer

# Speaking Points

## Hans-Werner Müller, UEAPME Secretary General

- Short **presentation of UEAPME –** who we are and what we do
- SMEs in Europe **depend highly on external finance** and are much more financed by credits and loans than SMEs in the US for example.
- The environment for credit and loan financing in Europe is changing at the moment, which has created quite serious uncertainty in the SME sector - many of them complain about credit shortening. All our surveys show that **access to finance is one of the main concerns of SMEs in Europe**.
- This uncertainty and the **loss of confidence has several reasons**:
  - ⇒ mergers and take-overs in the finance sector
  - ⇒ more restrictive state aid rules for the credit sector
  - ⇒ pressure for higher profitability from shareholders
  - ⇒ and last but not least "Bale II" and the new capital directive for banks

- As an answer to these challenges, **UEAPME elaborated an encompassing policy approach** in order to improve the access of SME to finance, which addresses the incoming European Commission, the newly elected European Parliament and the Member States.
- This policy paper, which we called "**Crafts, Trades and SMEs need better access to finance"**, is based on intensive discussions with representatives of the European Commission, the Parliament and the European Investment Bank, respectively the European Investment Fund and was yesterday approved by our Member Organisations.
- Therefore, it is a great pleasure for me to present to you, such a distinguish audience, today for the first time the main policy pillars for a better access to finance:

1. **The new capital requirement directive must implement Bale II in a SME friendly way:**

   ⇒ After long negotiations, we achieved much better the regulatory capital requirements for SME lending. Now we have to take care that the implementation of Bale II does not create too much administrative burden for smaller banks, which are very active in financing SMEs. Otherwise, the higher costs will be past on to the SMEs.

   ⇒ The increasing risk awareness in the banking sector, but also Bale II, make it necessary that banks will rate their clients more and more often. Most of the SMEs do not have any experience with rating procedures and feel quite uncertain about this. Therefore, a sufficient transparency of these rating procedures has to be ensured by the new regulation.

   ⇒ UEAPME, in a consortium led by the European Saving Bank Group, is currently implementing a dissemination campaign on the implications of Bale II for SME finance, which includes 60 conferences in 30 European countries.

2. **An extension of credit guarantee schemes has to compensate for less risk taking by the bank sector:**

   ⇒ Especially business start-ups, the transfer of businesses and innovative fast growing SMEs depend on public support and the increasing risk awareness of banks will increase this dependency.

   ⇒ Experiences show that public money, spent for supporting credit guarantee schemes has a much higher multiplying effect than other instruments (one Euro can stimulate 30 Euro investment).

   ⇒ New instruments, like securing the SME portfolios of banks by the European Investment Fund or risk sharing models for equity finance could increase the capacity of the banking sector for SME finance.

3. **Reforms of the company and income taxation systems could strengthen the capacity of SMEs for self-financing:**

   ⇒ Many EU Member States have company and income taxation systems with negative incentives to build-up capital within the company by re-investing the profits. This was already in the past one of the reasons for the higher dependency of Europe's SMEs on bank lending. In future, the results of ratings will also depend on the amount of capital in the company, the high dependence on lending will influence the access to lending. This is vicious cycle, which has to be broken-up.

4. **Access to external risk capital must become an option for more SMEs**

   ⇒ External equity financing has no real tradition in the SME sector. On one hand, small enterprises and family businesses in general have traditionally not been very open towards external equity financing and were not used to inform transparently about their business.

   ⇒ On the other hand, many investors of venture capital and similar forms of equity finance are very reluctant to invest their funds in smaller companies, which is more costly than investing bigger amounts in larger companies. Furthermore, it is much more difficult to get out of such investments.

   ⇒ In order to improve equity finance for SMEs, a threefold approach would be necessary:

   1. The availability of venture capital by tax incentives for private investors has to increase.
   2. The conditions for investing venture capital in SMEs have to improve by developing a secondary market for such investments.
   3. Owner-managers have to become more transparent towards external investors.

- After having most of my time used to talk about our problems within the EU and how they should solved, **please allow me to conclude with some recommendations for policy makers in countries which are in a transition phase**:

  1. A strong and dynamic SME sector is an important precondition for stable economic growth and SMEs will not develop without having access to finance.
  2. A sufficient financing of SMEs will not happen without any form of public support and according to our experiences the provision of credit guarantee schemes is the most efficient and less market destroying way to do this.

Thank you very much for your attention.