

REALISTIC CREDIT AMOUNT FOR SMEs ACCORDING TO A QUESTIONNAIRE RESEARCH CARRIED OUT IN HUNGARY

Ágnes Csiszárik-Kocsir, János Varga

Óbuda University, Bécsi út 96/b., Budapest, Hungary

Abstract

The financing of enterprises, especially small and medium-sized enterprises, is one of the most popular issues today. The crisis of 2008 drew the attention even more to the financing anomalies of the SMEs. Credits are major sources of funding for modern economies, without them many companies can't be able to function and develop. Credits are particularly important for financing investments, especially for small and medium-sized enterprises. This financial source is the most important external source for many SMEs, because these companies can't be able to take another financial sources (e.g. crowdfunding, bond financing, venture capital, etc.). About credit financing there are very different opinions, some are opposed to taking it, but some say that loan money helps businesses if they are reasonably involved. Among the credits, long-term investment and development credits can be used at less risk than short-term variants, because they are able to extract their payback basis. One of the reasons for the 2008 crisis was that companies became irresponsible in borrowing, and banks supported this through their unlimited credit supply. However, the mass spread of markets and credits drew attention to the dangers of irrelevant lending learned by both the supply and demand side. The aim of the study is to show the optimal size of loans taken up by Hungarian small and medium-sized enterprises. The analysis intends to show business opinions about the value of the credits for different purposes in order to draw attention to the optimum lending volume from both creditors and borrowers alike.

Keywords: credit, SME, financing, primary research

1. LITERATURE REVIEW

The small and medium-sized enterprises are key operators of the micro and macro economies, key actors of the economic growth. As Robinson noted in one of his works in 1952, due to economic growth demands appear for certain financial products and constructions that help the financing of enterprises in the service of this prosperity. In response to this, Levine (1997) asserted that the financial system is capable of automatically reacting to challenges like that, although in numerous cases excessive importance is attributed to this ability.

For this very reason financing enterprises has been a topic in the financial literature for many years. If an enterprise needs financial resources, it can basically come from two sources, namely from inner – i.e. produced – or outer – market originated – forms. Using inner financing sources is the best for the companies, since it equals to the complete freedom of self-financing (Brealey – Myers, 2011), contrary to outer financing, which always brings risks and question marks. The outer fundraising can happen through both equity and debt financing. The risk of equity coming from a foreign market lies in the unknown ambition of the new owners and what their intention is regarding the newly acquired company. Hence the other type of outer financing – debt financing – is applied more and more often and bravely. Debt financing can take place through bank loans or bond issuance, but the latter is only available in the Anglo-Saxon countries with developed capital markets. As Masulis (1988) and Jensen (1986) said before the turn of the millennium, the primary source for the enterprises planning to raise funds is debt financing via banks, followed by bond financing and in the end equity financing.

By cause of the crisis that had a huge impact on financing, the ways of thinking have changed in respect of sources of financing, but its practical materialization cannot be discovered yet in several countries. Countless articles and studies have already highlighted that in the field of financing the room for manoeuvre for large corporations is a lot wider than for small enterprises (Beck – Demirguc-

Kunt, 2006), which the crisis has worsened. It is a fact that the SMEs are important actors of the economic growth, but due to their vulnerability they are less attractive from the aspects of the full range of financing. Yet the trends are clear, if we take a look at the financing structure of the SMEs of the Eastern European countries. Debt financing still dominates in the first position, but the proportion of equity and bond financing is continuously improving as well. Therefore it can be stated that after more than thirty years the tendency mentioned by Masulis and his colleagues seems to fall even in the financially underdeveloped Eastern European region, as the below table also illustrates:

Table 1. The corporate financial sources at the percentage of the GDP in the Easter-European countries

	Long-term loans			Shares			Bonds		
	2008	2017	ch.	2008	2017	ch.	2008	2017	ch.
Hungary	53	42	↓	109	141	↑	1,3	1,5	↑
Poland	29	31	↑	73	77	↑	2,7	6,3	↑
Czech Republic	31	32	↑	100	115	↑	4,0	7,0	↑
Slovakia	29	29	=	68	63	↓	2,8	6,7	↑
Romania	38	25	↓	60	48	↓	0,1	0,1	=
Bulgaria	98	71	↓	110	136	↑	1,9	3,9	↑
Slovenia	53	45	↓	96	98	↑	1,3	2,5	↑
Latvia	59	54	↓	55	80	↑	0,4	0,7	↑
Lithuania	41	31	↓	105	100	↓	0,9	1,4	↑
Estonia	70	55	↓	157	189	↑	4,7	6,3	↑

Source: Hungarian National Bank (2018), based on Eurostat

In addition to the above table, the tendencies are worth checking over the past years in bank lending, which is presented by the below table. When grouping the examined OECD member states it can be seen that various patterns emerged recently in lending to SMEs, on top of the dominance of bank loans, as the following table shows.

Table 2. Trends in SME loan shares in 2015-16 in some Eastern-European OECD countries

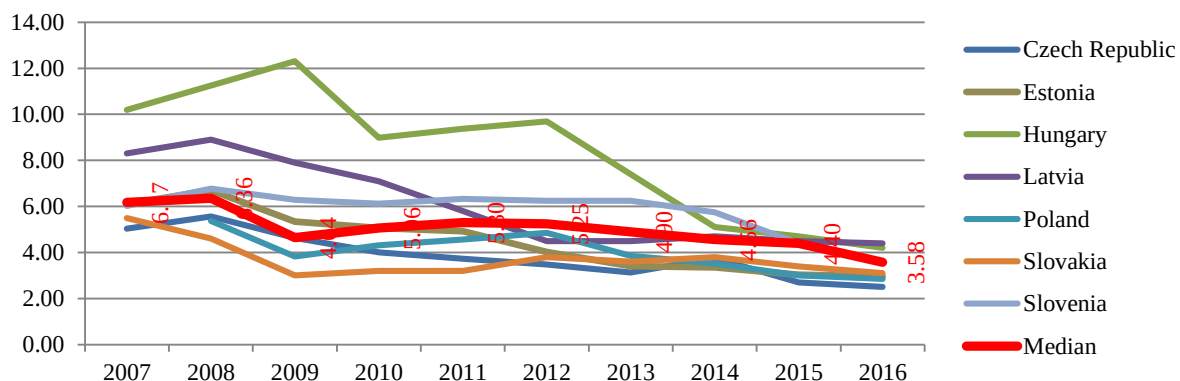
SME loan share change	Countries	Trends
SME loan shares ↑	Czech Republic, Slovakia	SME loans increased than total loans increased
SME loan shares ↑	Slovenia	SME loans increased than total loans decreased
SME loan shares ↓	Hungary	SME loans decreased faster than total loans decreased
SME loan shares ↓	Estonia, Poland	SME loans increased, but not as fast as total loans increased

Source: own compilation based on OECD (2018)

In connection with debt financing the price – or in other words the size of the loan interests – is crucial. In the early 1970s McKinnon (1973) and Shaw (1973) emphasized that financial liberalization is necessary in order for the loan interests to decrease, improving the enterprises' investment activity

and supply of capital. Schumpeter (1973) also underlined the effect of improved financing on innovation incentives. The overall picture is positive with regard to the current global financial situation, since the low interest rates are considered to be general all over the world, as it is illustrated on the below graph. In general the interests had been around 6% before the crisis, while 10 years after the crisis this percentage was only around the level of 3.5%¹.

Figure 1. SME interest rates in some Eastern-European OECD countries



Source: own compilation based on OECD (2018)

Ample sources opened for large corporations that they are able to benefit from due to their size and reputation. Community financing and commercial lending are such forms of financing for which public visibility is essential. Additionally, stock exchange and financial market financing are also viable options mainly for the larger enterprises. However, the small and medium-sized enterprises were struck on the line of bank financing both prior to and after the crisis. Simultaneously to skipping financial market financing, equity financing is given more and more prominence for the purpose of reducing the credit exposure of the small and medium-sized enterprises. On the other hand the global trends show (Végh, 2016) that:

- The corporate lifecycle has significantly declined,
- Risk capital as a form of equity financing is receiving an increasingly bigger role in financing,
- Debt financing has become more attractive in many areas and in many forms due to the low expected returns,
- As a result, capital market financing is less attractive because of the constraints and expectations.

Conversely, at the moment numerous SMEs are incapable of acquiring sources of financing from the stock exchange. There are several known barriers to the financial market financing of small and medium-sized enterprises. Size problems, fear of publicity and lack of knowledge and experience all set the sector back from acting in the capital market. Due to lack of financial knowledge and of not knowing the capital market, obtaining sources from the stock exchange is an unknown territory for the SMEs, thus they are rather oriented towards bank loans. This process is currently highly supported by the international interest environment the banks are offering. Nevertheless, many essays and studies already predict another upcoming crisis. This crisis will be a phenomenon with increased interests, therefore it would be better to direct financing towards the low-interest formats designed in the current

¹ In terms of the Middle European countries examined by the OECD it is clear that the highest interest rates were detected in Hungary. The situation has not changed even after ten years, as the highest interest rate can still be found here. The graph shows that five years after the crisis the interest rates were still record high in Hungary, in addition to the drastic downsizing of the banks' lending activity, and it could only be adequately changed by the Funding for Growth Scheme launched by the Central Bank of Hungary.

situation. The main constraining factors of the SMEs' market-based financing are introduced in the following table:

Table 3. The constraints for SMEs of market-based financing

	Debt-financing	Equity-financing
	Securitisation, covered bonds, mini-bonds, private placements	Public equity offerings
Market infrastructure	Lack of infrastructure for information provision	
	Lack of valuable ecosystems tailored to SMEs	
	Lack of standardised, „off-the-shell” products tailored for SMEs	Dearth of liquidity
	Lack of performance track records, benchmarks	Lack of economic incentives for indispensable constituencies arising from market models
Supply-side	Fundamental structural disadvantages of small SME financing transactions	
	Limited buy-in by institutional investors and patient capital	
	Lack of coordinated and coherent approach for the development of SME finance by all market constituencies involved	
	Lack of standardised, “off-the-shell” products tailored for SMEs	Lack of equity culture in some parts of the world
	Limited internal infrastructure	Limited retail participation
Demand-side	Educational gap: lack of awareness, understanding, financial literacy	
	Information paucity: limited data sharing, insufficient disclosure of information and reporting	
	Discouraged non-seekers	Limited skills to face public market requirements and scrutiny
	Impaired communication channel linking supply and demand encumbers accessibility	Disproportionate cost and listing requirements on main exchanges

Source: own compilation based on OECD (2015)

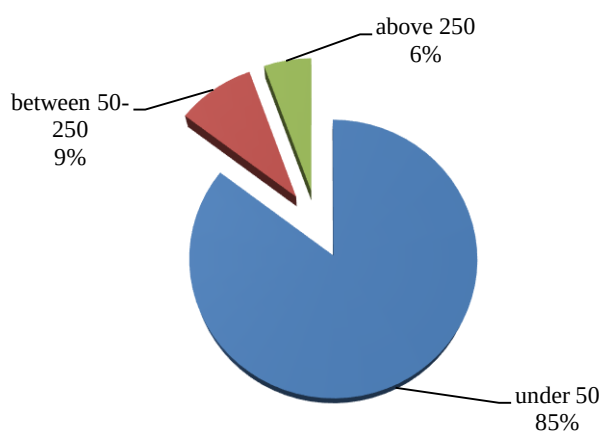
Gertler (1988) and Hubbard (1994) both stated that the smaller enterprises with weaker bargaining power react in an incredibly sensitive way to financial changes (including crises), hence for example to changes in interest rates too. This is why it is important to consider other alternative sources as well, especially when the bank sources are getting more expensive. In addition to the capital market financing of the enterprises, commercial lending could also provide a reachable and obvious solution. Several researches pointed out that at the time of crises the enterprises tend to turn strongly towards commercial loans. Meltzer (1960) flagged it up already in the 1960s that the commercial loans are able to operate as an alternative to bank loans. Jaffee – Russel (1976) noticed that the SMEs – which have weak bargaining power, are vulnerable and have an unfavourable credit risk rating – use this source to a greater extent for obtaining money, since they can access it more easily by paying the invoices later. However, such forced commercial lending has countless risks both in the medium and long term. Reduced trust in the company and the loss of suppliers can often be fatal for the enterprises.

Based on the above it can be acknowledged that there are still a lot of tasks to do before financing of the SMEs can become market-based. Strengthening financial knowledge and trust is paramount. The latter is also important in terms of commercial lending. The new forms of financing, like Community financing, structured financing or even risk capital financing are mostly unavailable to the operating SMEs. Hence there is nothing left but bank loans. On the other hand, the bank loan products can only be designed to the enterprises if the intentions and opinions of the demand side are known. The present study endeavours to help this work, highlighting the opinions and intentions of the Hungarian SMEs on the basis of the amounts and purposes of the loans.

2. MATERIAL AND METHOD

The research results introduced in this study are part of a primary questionnaire research conducted in 2017. The research was carried out in Hungary with the help of a pretested and standardized questionnaire form. The present research was preceded by a previous survey among enterprises, which had been preceded by an in-depth interview analysis. The present questionnaire form was created as a result of these two former rounds, and it was a complex questionnaire, covering the financing and investment activity of the enterprises. The survey paid special attention to the enterprises' financing, project management and project financing practices as well. During the research we received 521 questionnaires, but only 416 of them were assessable enough to be included in the sample. The results of the research are presented in this study based on the employment figures of the responding enterprises.

Figure 2. The composition of the sample according to their financial situation (%)



Source: own research, 2017, N = 416

In the context of this study we are searching for the answer to how big the loans would be that the Hungarian small and medium-sized enterprises would take out for various purposes. The main question is what the optimal loan size is for each purpose, with which the SMEs could operate safely. In the questionnaire used for the analysis the responding enterprises were asked to assign the size of the loan they deemed optimal to the listed objectives. The below value categories were given²:

- less, than 1 million HUF = less, than 3.125 EUR
- 1-2 million HUF = 3.125-6.250 EUR
- 2-5 million HUF = 6.250-15.625 EUR

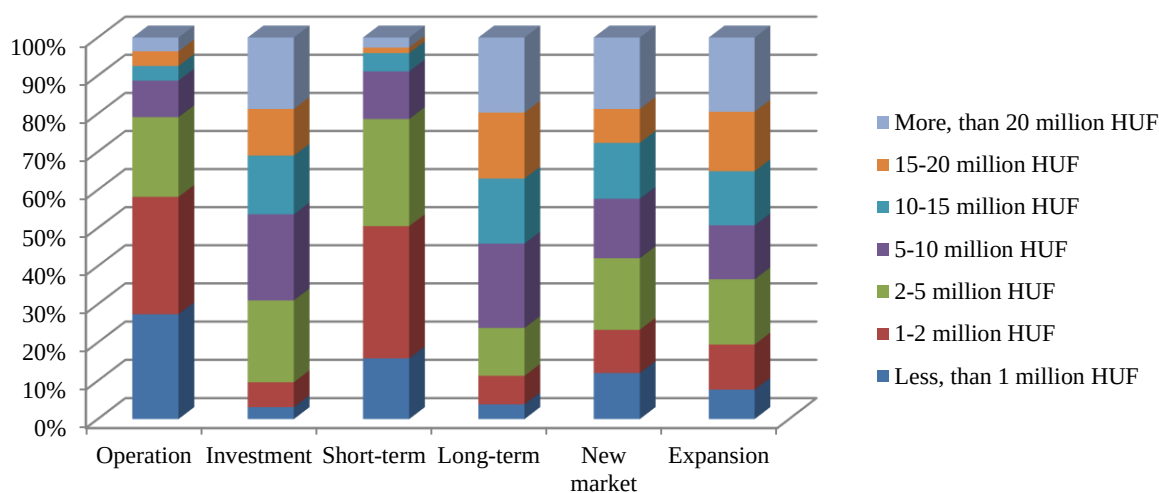
² Calculated with the exchange rate of 1 Euro = 320 HUF

- 5-10 million HUF = 15.625-31.250 EUR
- 10-15 million HUF = 31.250-46.875 EUR
- 15-20 million HUF = 46.875-62.500 EUR
- more, than 20 million HUF = more, than 62.500 EUR

3. RESULTS

As it has been previously mentioned, the goal of this study is to introduce the sizes of loans that the Hungarian small and medium-sized enterprises would safely take out for different purposes. The following graph shows the results of the research with regard to the entire sample.

Figure 3. The optimal loan value according to the deals



Source: own research, 2017, N = 416

The graph reveals that the enterprises would only take out a small amount for their operation. 30.8% of the responding enterprises would borrow only 2 million HUF and 27.4% of them are thinking about less than 1 million HUF. As a conclusion it can be noted that more than half of the responding enterprises would borrow the smallest possible amount for financing their operation. It is a welcome choice, because loans spent on operating costs are really hard to reimburse, and since it is now a general requirement for the enterprises to be able to produce the sources of their operation themselves, it is a sign of an error if a company needs to be indebted for that purpose.

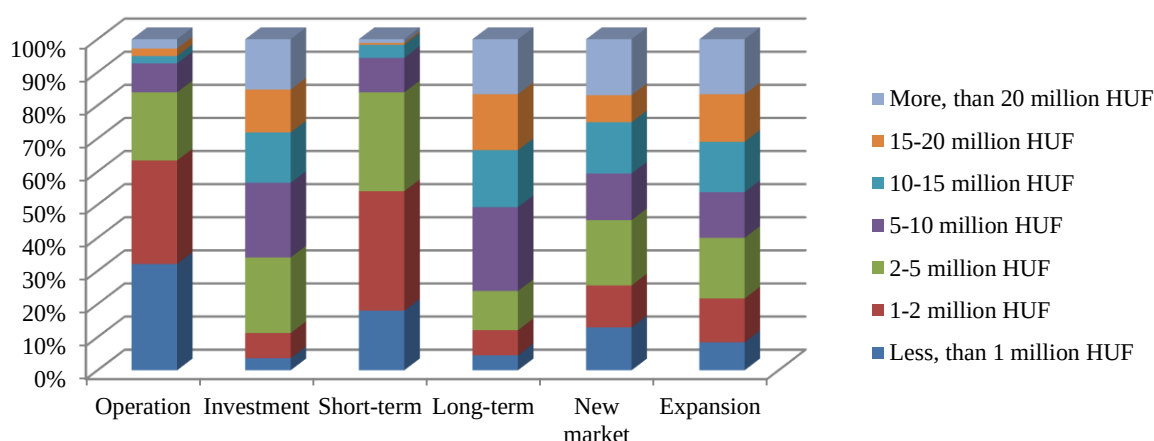
In terms of investments the enterprises are braver. 22.6% of the responding enterprises are considering such a loan between 5 and 10 million HUF, whereas 21.4% of them would spend between 2 and 5 million HUF on investments. The two figures with their 44% in total prove that the enterprise are more optimistic in respect of investment loans, as they believe they will be able to generate the source of paying the loan back.

If a company has to take out a short term loan, then the respondents turn towards the smaller amounts again. The majority of them (31.6%) would only borrow 1 or 2 million HUF in the short term, and 28.1% of them had a figure between 2 and 5 million HUF in their mind. This represented more than 60% of the sample. In the long term the responding enterprises showed higher activity and that is related to the financing of investments too. For a longer period most of the enterprises would think of a loan between 5 and 10 million HUF, but there were plenty of others as well that would be willing to take out long term loans even over 20 million HUF.

In terms of capturing new markets the proportions were a lot smaller and the amounts were more diverse too. In the case of certain loan purposes the enterprises did not share a pronounced opinion anymore, which can presumably be explained with the lower proportion of the larger companies within the sample.

Hereinafter we examine the answers based on the size of the enterprises. First the opinion of the enterprises with less than 50 employees will be presented.

Figure 4. The optimal loan value according to the deals by the smallest companies (under 50 employees)

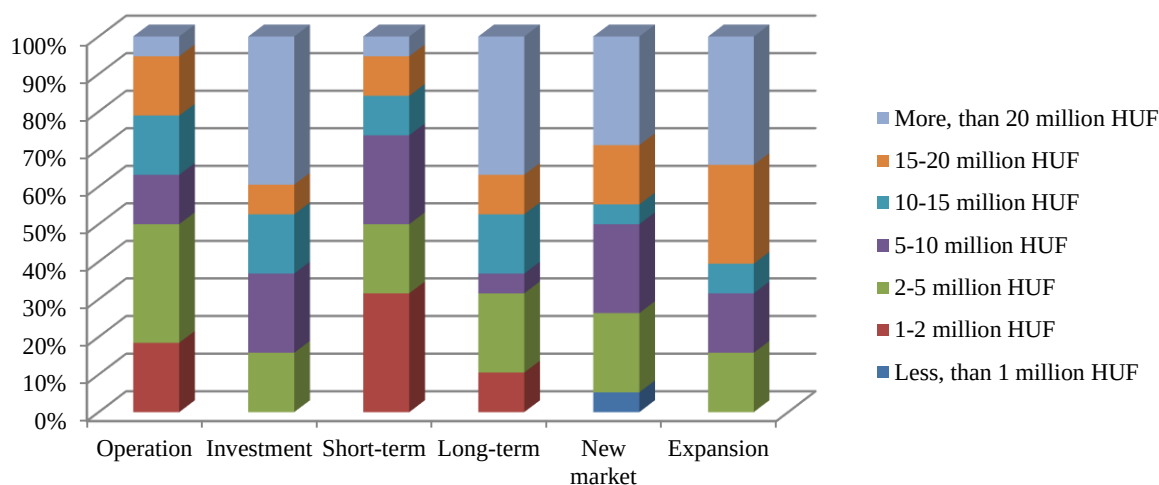


Source: own research, 2017, N = 416

The smallest enterprises with less than 50 people accounted for the largest share of the sample, which is not surprising, since their opinion echoed the opinion of the whole sample in most parts. In terms of loans for operation, investment and both for short and long term the figures and amounts were roughly the same as the ones seen in the case of the whole sample. In respect of expansion and opening to new markets it can be stated that the smallest enterprises are thinking about medium sized loans, between 2 and 5 million HUF. However, there are some smaller enterprises that are even willing to take out a loan higher than 20 million HUF for this purpose.

The opinion of the medium-sized enterprises is completely different than the smallest enterprises' point of view, as the below graph illustrates.

Figure 5. The optimal loan value according to the deals by the medium-sized companies (between 50-250 employees)

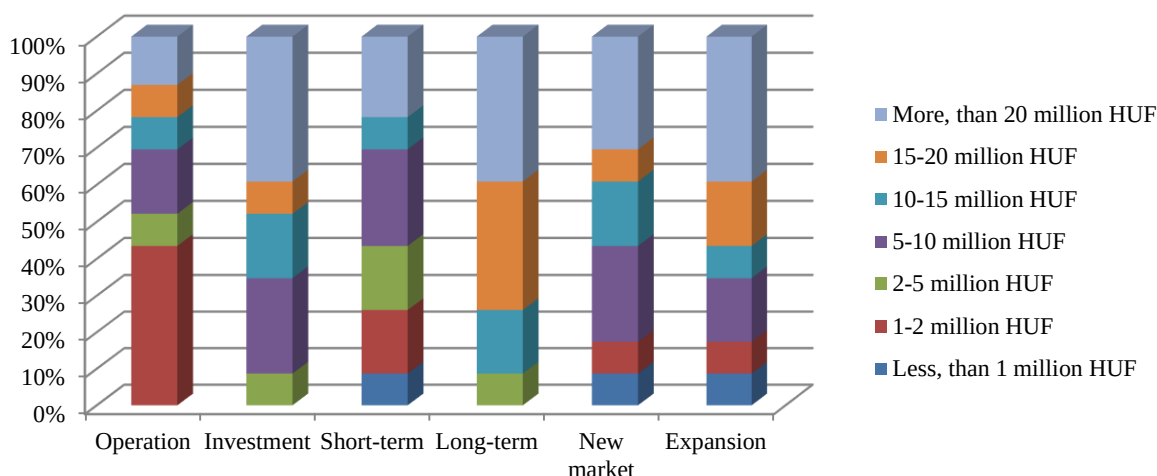


Source: own research, 2017, N = 416

According to the graph the medium-sized enterprises between 50 and 250 employees barely consider amounts under 1 million HUF, in fact, they are willing to borrow sums between 1 and 2 million HUF only for certain purposes. Such purposes are the operating costs, short term and long term loans. It can be inferred from the received answers that for their operation they rather consider the amounts between 2 and 5 million HUF to be the optimal loan size. In terms of investments they always think of high figures, loans over 20 million HUF, as it is confirmed by 39.5% of the total answers. In the case of short term loans there is a little divergence between operating and short term loans, since while 31.6% of them would take out a loan to cover the operating costs in the amount of 2 to 5 million HUF, for short term they only find 1-2 million HUF optimal. In the case of long term loans the opinion of the enterprises echoed what they thought of investment loans, as 36.8% of them have loans over 20 million HUF in their mind. They chose loans higher than 20 million HUF as optimal for acquiring new markets and for expansion in the same percentage (nearly 1/3). It can be concluded that the medium-sized enterprises are braver when it comes to borrowing, as they would consider higher amounts and higher loans for more purposes. This is most likely down to their system of bank relations and to their better credit ratings, compared to the smaller enterprises.

Last but not least, we introduce the opinion of the largest enterprises with more than 250 employees.

Figure 6. The optimal loan value according to the deals by the largest companies (above 250 employees)



Source: own research, 2017, N = 416

The opinion of the largest companies is also completely different than the sample mean. It can be stated about these enterprises as well that, overall, they think of higher amounts. For investments, for long term, for acquiring new markets and for expansion more than 30% of them would borrow more than 20 million HUF, just like the medium-sized enterprises. On the other hand, surprisingly, for operating costs 43.5% of them would only borrow 1-2 million HUF. It is again a bit contradictory that in the short term the loan amounts between 5 and 10 million HUF dominate. It is also true in the case of these enterprises that by their size they are better suited to be attractive targets for the banks, or in other words to borrow larger sums for the sake of carrying out various goals.

4. SUMMARY

In conclusion, the small and medium-sized enterprises constituting the sample are fully aware of their strength, capacity and position in the market of bank loans. The smaller enterprises are typically more cautious, and due to their size and economic power they rather prefer the smaller amounts, both for operation and short term. For longer term and for investment purposes they are inclined to think of larger amounts too. In their opinion, loans over 10 million HUF are risky, so they only prefer them under extraordinary circumstances. The medium-sized and larger enterprises demonstrated more courage, as they would consider loans over 20 million HUF, and in their case the loan amounts around 1-2 million HUF or under 1 million HUF can be deemed negligible. It is very rare that they turn to such loans, because on the ground of their turnover they have bigger capacities. Based on the above it can be asserted that the priority for the banks is to keep tailoring the corporate products that are able to serve the different groups of small and medium-sized enterprises, contributing to their prosperity and to the growth of the macro economy as well. On the basis of the sample the improvement of the enterprises' financial consciousness is noticeable in the context of being able to see their situation realistically. This picture almost 10 years after the crisis definitely inspires optimism, which can also be progressive from the aspect that the enterprises will be more prepared when facing a new economic downturn.

ACKNOWLEDGEMENT

Supported through the new national excellence program of the ministry of human capacities.

REFERENCES

1. Beck, T. – Demirguc-Kunt, A. (2006): Small and medium-size enterprises: Access to finance as a growth constraint, *Journal of Banking and Finance*, vol. 30., no. 11., 2931-2943.pp.,
2. Brealey, R.A. – Myers, S.C. (2011): *Modern vállalati pénzügyek*, Panem Kiadó, Budapest,
3. Gertler, M. (1988): Financial structure and aggregate economic activity: An overview, NBER Working Paper, no. 2559., <http://www.nber.org/papers/w2559>, downloaded: 2013.08.14.,
4. Hubbard, R.G. (1994). Is there a 'credit channel' for monetary policy? NBER Working Paper, no. 4977., <http://www.nber.org/papers/w4977>, downloaded: 2013.08.14.,
5. Hungarian National Bank (MNB): Pénzügyi stabilitási jelentés, <http://www.mnb.hu/letoltes/stabilitasi-jelentes-2018-maj-hun.pdf>, downloaded: 2018.06.18.,
6. Jaffee, D.M. - Russel, T. (1976). Imperfect information, uncertainty, and credit rationing, *Quarterly Journal of Economics*, vol. 90., no. 4., 651–666.pp.,
7. Jensen, M.C. (1986): Agency costs of free cash flow, corporate finance and takeovers, *American Economic Review*, vol 76., no. 2., 323-339.pp.,
8. Levine, R. (1997). Financial development and economic growth: Views and agenda, *Journal of Economic Literature*, vol. 35., no. 2., 688-726.pp.,
9. Masulis, R.W. (1988): *The debt/equity choice*, Ballinger Pub. Co.,
10. McKinnon, R. (1973). *Money and capital in economic development*, Brookings Institution, Washington, D.C.,
11. Meltzer, A.H. (1960): Mercantile credit, monetary policy, and the size of firms, *Review of Economics and Statistics*, vol. 42., no. 4., 429–437.,
12. OECD (2018): *Financing SMEs and Entrepreneurs 2018*, https://read.oecd-ilibrary.org/industry-and-services/financing-smes-and-entrepreneurs-2018_fin_sme_ent-2018-en, downloaded: 2018.06.02.,
13. OECD (2015): *Opportunities and constraints of market-based financing for SMEs – OECD report to G20 finance ministers and central bank governors*, <https://www.oecd.org/finance/financial-markets/Opportunities-and-Constraints-of-Market-based-Financing-for-SMEs.pdf>, downloaded: 2018.04.21.,
14. Schumpeter, J. (1973). *The theory of economic development*, Harvard University Press, Cambridge,
15. Shaw, E. (1973): *Financial deepening in economic development*, Oxford University Press, New York,
16. Végh, R. (2016): Tőzsdefejlesztés – a nemzeti tőke megtartása és megerősítése, presentation at the Hungarian Economic Conference, 2016.09.16., http://www.mkt.hu/wp-content/uploads/2016/09/Vegh_Richard.pdf, downloaded: 2018.03.12.