

## **Constraints on Bank Lending to SMEs from Romania and Supportive Measures**

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**Abstract.** The access to finance is indispensable for the efficient allocation of capital and the enterprise development. However, when compared with large enterprises, small and medium enterprises face many difficulties when pursuing to procure financial resources. In Romania, the financial system is focused on banks so bank loans have an overwhelming share from the resources of external finance for SMEs. However, these companies face many obstacles in terms of applying for bank loans. Thus, we may notice that some banks refuse to grant loans or increase interest rates for operational SMEs that do not offer adequate guarantees or do not have a credit history, because they have just started their activity or they have a degree of solvency that does not fall into the limits imposed by the banks in question. In crisis conditions, SMEs face increasing difficulties in contracting bank loans because the deteriorating macroeconomic environment and the uncertainty about the macroeconomic outlook causes banks to show a greater reluctance in lending to these enterprises. Our paper aims to highlight the main constraints faced by SMEs in accessing bank loans, the implications of the current crisis on SMEs' access to bank loans and the measures taken by public authorities to support bank lending to these enterprises.

**Keywords:** Small and medium enterprises, bank loans, obstacles, global crisis

### **1 Introduction**

The easy access to finance of enterprises in general and of small and medium enterprises (SMEs) in particular is of crucial importance, because it conditions their creation, survival and development and, eventually, the economic growth and the creation of workplaces.

In comparison with large enterprises, SMEs face numerous obstacles in procuring financing resources, even when the economy it is normally functioning. This is due to the reticence of financial markets to take risks (especially due to the incomplete informing of the equity suppliers with regard to the situation and development perspectives of SMEs) and to the insufficient guarantees offered to creditors. In the light of bank lending, we notice that some banks refuse to grant loans or increase interest rates for operational SMEs that do not offer adequate guarantees or do not have a credit history, because they have just started their activity or they have a degree of solvency that does not fall

into the limits imposed by the banks in question. In crisis conditions, SMEs face greater barriers in the way of access to bank loans because the deteriorating macroeconomic environment determines the banks to show a greater reluctance about lending these companies.

This study is structured as follows: *the first part* contains introductory remarks regarding the importance and relevance of the theme; *the second part* is devoted to the literature review and presents the main directions of approach on the analyzed theme; *the third part* reflects the main characteristics of the SME sector in Romania; *the fourth part* of the paper highlights the role of bank credit in the financing resources for SMEs and the impediments in accessing bank loans by these enterprises. In *the fifth part* we want to highlight the implications of current global crisis on the SME sector in Romania, but also the effects of the crisis on bank lending to this sector. The study ends with conclusions.

The research methodology used in this paper starts with the literature review in order to highlight the importance of the discussed subject in this paper. The analysis performed in this paper is based on data and statistics provided mainly by the European Commission, National Bank of Romania, National Council of Private SMEs in Romania(CNIPMMR), Ministry for Small and Medium-Sized Enterprises, Commerce, Tourism and Liberal Professions of Romania, Post-Privatization Foundation. Based on the used methodology, the paper indicates, mainly the major problems faced by SMEs in dealing with banks and the fundamental importance of increasing bank concerns in supporting the access to bank credit of these businesses, but also to resolve the difficulties faced by entrepreneurs when they resort to bank financing.

## 2 Literature review

Many studies show that small firms face important constraints when they try to obtain formal sources of external finance which could sustain their growth. Within the access to finance category, credit conditions – relating primarily to interest rate, maturity, collateral requirements and lending procedures – were perceived to be the most important limiting factors. Schiffer & Weder (2001) show that small enterprises report higher growth obstacles than medium-enterprises or large ones. Beck, Demirguc-Kunt, Laeven & Maksimovic (2006) show that size, age and ownership are the most reliable predictors of firms' financing obstacles. These authors find also that older, larger and foreign-owned firms report lower financing obstacles. The data also show that small firms finance just a smaller share of their investment with formal sources of external finance (Beck, Demirguc-Kunt and Maksimovic, 2004).

Credit availability to enterprises, but especially to SMEs, depends on the infrastructure that supports financial transactions, including the legal system and the information environment. Firms in countries with more effective and more adaptable legal systems report lower financing obstacles (Beck, Demirguc-Kunt and Levine, 2005b) and the effect of financial and legal obstacles on growth is lower in countries with better developed legal systems, especially for small firms (Beck, Demirguc-Kunt and Maksimovic, 2005).

Chavis, Klapper & Love (2010a) showed that in all countries younger firms rely less on bank financing and more on informal financing. However, they also find that younger firms use more bank finance in countries with stronger rule of law and better credit information, and that the reliance of young firms on informal finance decreases with the availability of credit information.

Access to external finance and the ability to undertake profitable investment opportunities is an important ingredient for success of any new enterprise and ultimately for the economic development and growth. Without access to formal financing, start-up enterprises might resort to informal sources such as family and friends which can provide affordable and accessible funding. But, while more firms use informal financing than bank financing, only bank financing is associated with higher growth

rates. The studies realized by Chavis, Klapper & Love (2010a, 2010b) show that younger firms are more likely to use bank finance in countries with better rule of law. This suggests that firms in countries with better investment climates are more likely to enter into formal credit contracts, and hence less likely to rely on informal contracts. Also, in countries with weak rule of law and credit information, younger firms use less bank finance, relative to older firms, than in countries with stronger investment climates. So, developing systems of credit information sharing and a more competitive banking structure can be useful in facilitating greater access to finance. Rapidly expanding literature has shown the positive effect that credit information sharing has on the credit availability to SMEs (Pagano and Jappelli, 1993; Miller, 2003; Love and Mylenko, 2003). Depending on the legal and information environment in their respective country, financial institutions around the world have developed specific techniques to lend to small, opaque firms with little or no collateral.

One of the main factors often cited as a problem in SME bank financing is “opaqueness.” By opaqueness the literature means that it is difficult to observe if firms have the capacity to pay (have viable projects) and/or are willing to pay (due to moral hazard). This opaqueness particularly undermines lending from institutions that engage in more impersonal or arms-length financing that requires hard, objective, and transparent information (De la Torre, Martinez Peria & Schmukler, 2008).

Analyzing all this studies we observe that the banking market structure and regulatory policies influencing this market structure can have an important impact on the availability of SME financing. While a large share of small banks does not necessarily result in more external financing available to small firms, financial systems dominated by government-owned banks seem less effective in providing credit to SMEs. The entry of foreign banks, on the other hand, is mostly associated with greater SME credit availability (Beck & Demircuc-Kunt, 2006). The research of Beck & Demircuc-Kunt (2006) suggests that a competitive business environment, of which access to finance is an important component, facilitates entry, exit and growth of firms and is therefore essential for the development process. A focus on improving the business environment for all firms is more important than simply trying to promote a large SME sector which might be characterized by a large number of small but stagnant firms.

In recent years, credit institutions' exposure to SMEs has grown significantly and currently comprises an important part of their commercial loan portfolio. Banks are adapting their business and risk models by creating dedicated SME units, but loan products and risk management practices are still incipient. Because SMEs have become a strategic sector, banks are changing their organizational set-up to approach and serve this segment efficiently.

The study realized by Schmukler, De la Torre, & Martínez Pería (2008 ) shows that whole private banks (large and small, domestic and foreign) have started to perceive SMEs as a strategic sector. So banks are expanding, or planning to expand, their operations in the SME segment. As a consequence, the SME market is becoming increasingly competitive. These results suggest that banks are learning how to deal with SMEs, and, at the same time, they are making the investments to develop the structure to deal with a growing market in the years to come. So, all banks are trying to attract SMEs and more competition is expected in the future as banks get more involved in this segment.

Lending is only a fraction of what banks offer to SMEs, as banks try to serve SMEs through a wide range of products and services, with fee-based products rising in importance. Banks are currently offering a range of deposit and loan products and other banking services to SMEs. In general, banks are offering some standard products to SMEs that include checking/savings/time deposit accounts and loans for working capital or investment (sometimes with pre-approved limits). Business credit cards are also quite popular, and banks appear to be targeting this segment aggressively as a natural

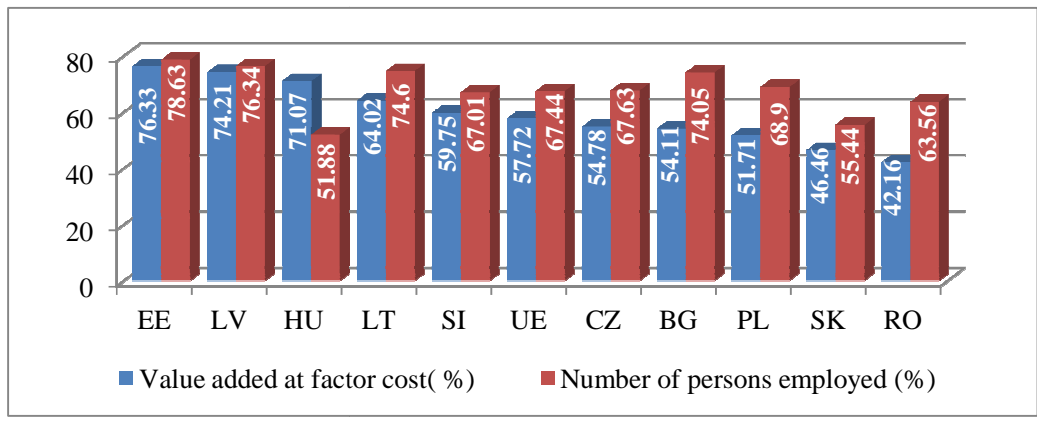
extension of the consumer credit card market. Loan products offered to SMEs are still very standardized and mostly short-term in nature, reflecting banks' historical experience with SMEs (Stephanou & Rodriguez, 2008, p. 31).

Beck, Demirgüç-Kunt & Martínez Pería (2009) show that the differences between banks in developing and developed countries can explain differences in the extent, type and pricing of SME lending, rather than differences in bank ownership type. So, they find that, relative to banks in developed countries, banks in developing countries provide a lower share of investment loans and charge higher fees and interest rates. Also, the differences across countries regarding SMEs financing seem to be driven by differences in the economic, institutional, and legal environment. Finally their findings are consistent with that studies that propose a new paradigm for SME lending, where different bank types, applying different lending technologies and organizational structures can play an important role in financing SMEs (Berger & Udell, 2005; De la Torre, Martinez Peria & Schmukler, 2008).

### 3 Characteristics of the SME sector in Romania

Small and medium enterprises are considered the engine of economic and social development of a country, appreciation resulting from the fact that they generate a great part of a country's gross domestic product and are an important source of job creation. The major importance of these enterprises to the national economy results from the fact that, through their dynamism, they are considered an engine of innovation and growth.

The role of SMEs in the national economy can be highlighted based on the data in Figure 1. Although the SME sector has a significant importance in national economies, there are differences from country to country. In terms of contribution to employment, it appears that this sector contributes from about 52% (in Hungary) and over 74% in Baltic countries. In Romania, the share of employees in the SME sector in total employment is 67.44%, compared to 63.56%, the EU average. More important differences stand out in terms of the contribution of SMEs to the creation of added value. In this respect, the SME sector in Romania, compared to other states, has the lowest level 42.16% compared to 57.72% the EU average; aspect which is due to the micro-enterprises that have weaker performance than the EU average.



Source: own simulation based on the dates provided by European Commission, 2010

**Figure 1** The role of SME sector in the economies of the new EU member states

The evolution of the SME sector in Romania can be highlighted through the number of SMEs and their structure on size categories. Thus, based on the available statistical data it is noteworthy that in 2008 there was registered the largest number of SMEs, namely 662.024, representing an increase of

60.52% compared to 2001 and an increase by 35.76% compared to 2007 (see Table 1). In 2009, in the context of current global crisis, was recorded for the first time after 2004, a decrease in the number of registered SMEs, namely a reduction of 5.85% compared to 2008.

**Table** The evolution of the number of SMEs registered, on total and by size categories, in the period 2000- 2009

| Year | Micro   |       | Small enterprises |      | Medium enterprises |      | Total SMEs |
|------|---------|-------|-------------------|------|--------------------|------|------------|
|      | Nr.     | %     | Nr.               | %    | Nr.                | %    |            |
| 2000 | 375.804 | 91.12 | 29.121            | 7,06 | 7.504              | 1,82 | 412.429    |
| 2006 | 410.763 | 88,62 | 43.419            | 9,37 | 9.322              | 2,01 | 463.504    |
| 2007 | 431.029 | 88,39 | 47.022            | 9,64 | 9.577              | 1,96 | 487.628    |
| 2008 | 602.711 | 91,04 | 49.560            | 7,49 | 9.753              | 1,47 | 662.024    |
| 2009 | 573.299 | 91,66 | 43.724            | 6,99 | 8.435              | 1,35 | 625.458    |

Source: Post-Privatization Foundation, 2010, p. 49 and own calculation

In the structure of SME by size categories, we observe that micro-enterprises have an overwhelming share, respectively about 92% of total SMEs (see Table 1), an aspect that can be explained by the fact that, on the one hand, the establishment of such enterprises is the first step in business realized by most entrepreneurs and, on the other hand, is the result of some important factors such as institutional, legislative and fiscal ones. For example, according to GEO 6/2011 *to stimulate the establishment and the development of micro-enterprises by young entrepreneurs* there are provided facilities for the start-up micro-enterprises led by young entrepreneurs (with the aged up to 35 years), and which perform for the first time an economic activity, through a limited liability company. Also, the predominance of micro-enterprises for a long period of time can indicate a stagnation of business development at micro level. Based on data from Table 1 we observe that the overwhelming share of micro-enterprises is a feature of long-term development of SME sector in our country, which may raise competition issues in the battle of competition in the EU internal market (Post-Privatisation Foundation, 2010, p. 51).

Another feature of the development of the SME sector in Romania is given by the dynamic of the distribution by sector, reflected by the data in Table 2. In the period before the crisis started we observe an increase in the number of SMEs in all sectors, but the most accelerated growth has been registered in the constructions sector, due mainly to the development of the residential real estate and business sector.

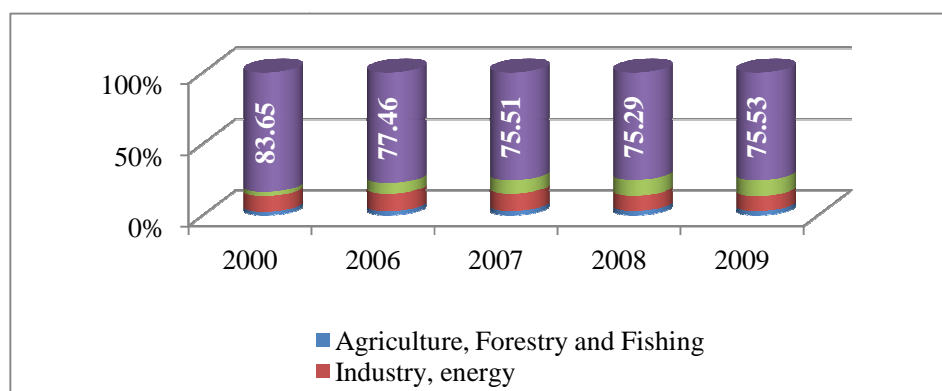
**Tabel 2** SMEs dynamic distribution on the main economic sectors

|      |            |  | Agriculture, Forestry | Industry, Energy | Constructions | Services | Total   |
|------|------------|--|-----------------------|------------------|---------------|----------|---------|
| 2000 | No of SMEs |  | 9.925                 | 45.719           | 11.808        | 344.977  | 412.429 |
|      | %          |  | 2,41                  | 11,08            | 2,86          | 83,65    | 100     |
| 2006 | No of SMEs |  | 12.859                | 56.873           | 34.757        | 359.015  | 463.504 |
|      | %          |  | 2,77                  | 12,27            | 7,50          | 77,46    | 100     |

|      |            |    |        |        |        |         |         |
|------|------------|----|--------|--------|--------|---------|---------|
| 2007 | No<br>SMEs | of | 14.036 | 59.492 | 45.896 | 368.204 | 487.628 |
|      | %          |    | 2,88   | 12,20  | 9,41   | 75,51   | 100     |
| 2008 | No<br>SMEs | of | 19.586 | 70.593 | 73.389 | 498.456 | 662.024 |
|      | %          |    | 2,96   | 10,66  | 11,09  | 75,29   | 100     |
| 2009 | No<br>SMEs | of | 17.939 | 65.483 | 69.619 | 472.417 | 625.458 |
|      | %          |    | 2,87   | 10,47  | 11,13  | 75,53   | 100     |

Source: Post-Privatization Foundation, 2010, p. 53 and own calculation

In terms of percentage distribution of SMEs by sector (see also Figure 2), it is noteworthy that the services sector has the highest share in the total number of SMEs (75.53% in 2009), which is giving to the SME sector in Romania the features of a service-based economy, like many other EU member states.



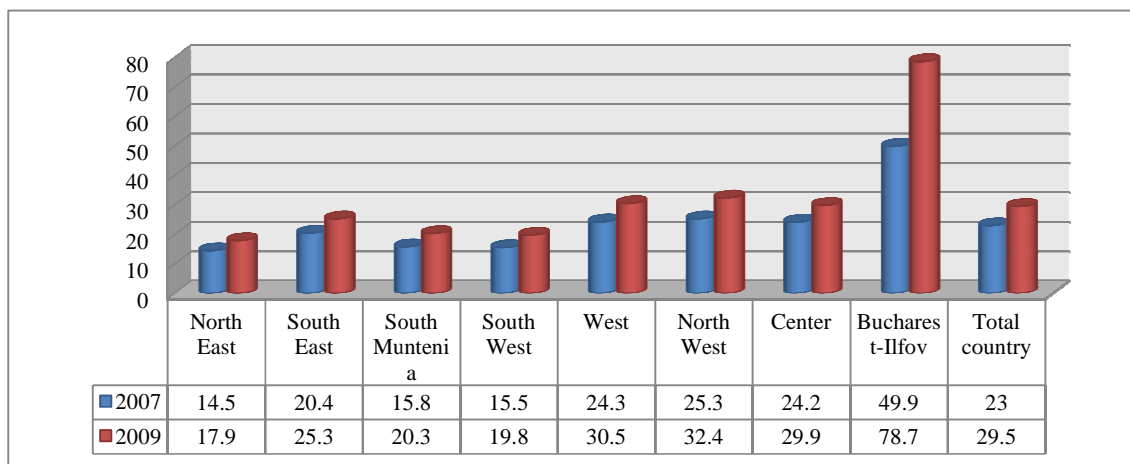
Source: Post-Privatization Foundation, 2010, p. 53 and own calculation

**Figure 2** SMEs dynamic distribution by sector

The dynamic of the SME sector can be highlighted also through another significant indicator, namely the density of SMEs, which represents the number of SMEs per 1,000 inhabitants. This indicator is regarded as a "barometer" of the spirit of initiative of the population and of the attractive economic environment for investors. In Romania, the average density was raised in 2009 to about 30 (29.5%) SMEs per 1.000 inhabitants, which is more than 17 SMEs per 1.000 inhabitants in 2003, and 21.7 in 2006. However, the level is well below the one recorded in other EU countries such as Czech Republic, Cyprus, Greece, Hungary, Italy, Sweden, which recorded values around 70 SMEs per 1,000 inhabitants (Ministry for Small and Medium Enterprises, Commerce, Tourism and Liberal Professions, 2008, p.46).

To emphasize the size of regional markets and the contribution of the SME sector to reduce unemployment in territorial profile, including raising the standard of living of the population, is of major interest the analysis of the SMEs density on development regions from Romania (see Figure 3). It is noted, on the one hand, the enhancement of the spirit of initiative of the population in all developing regions, in the year 2009 compared to 2007, and on the other hand, the existence of significant imbalances between the eight development regions. Moreover, it is reported, that in 2009,

the gap between Bucharest-Ilfov region and the other regions has deepened, fact that highlights the need of intensification of the concerns of the public authorities towards the infrastructure modernization and the increase of the attractiveness of the business environment, particularly in regions with disabilities.



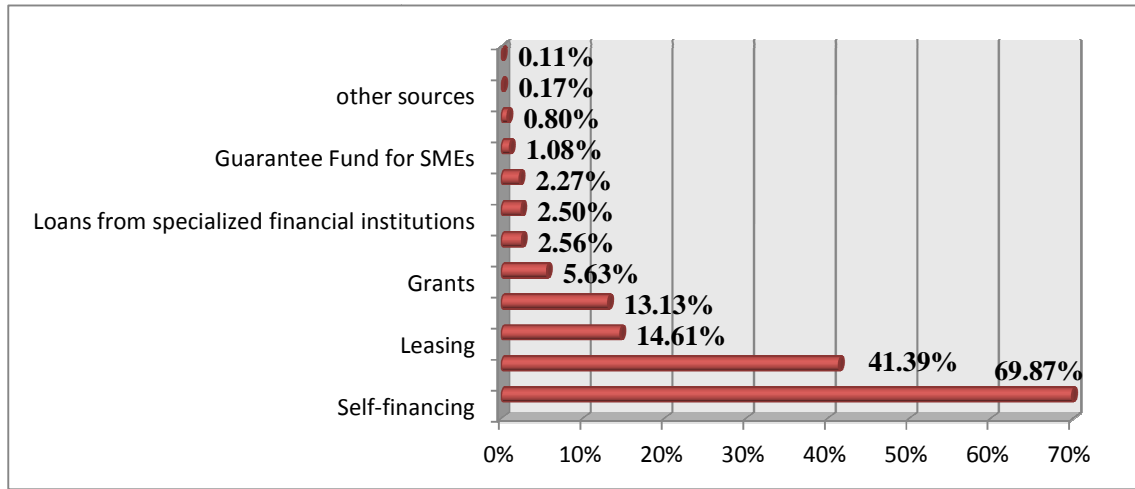
Source: processing based on Ministry for Small and Medium-Sized Enterprises, Commerce, Tourism and Liberal Professions of Romania, 2008, p. 47 and Post-Privatization Foundation, 2010, p. 117

**Figure 3** SMEs density on development regions of Romania, in 2007 and 2009

#### 4 Bank credit, the main resource of external financing of SME sector

In Romania, the financial system is focused on banks, so the bank loans have a significant share in the external financing resources of SMEs. However, these firms preference for financing through bank loans is due also to the fact that, unlike large companies the micro, small and medium enterprises have fewer financing options. The dependence on banks of SMEs, especially of micro and small enterprises makes those enterprises to be affected significantly when there are registered reductions of the volume of bank loans.

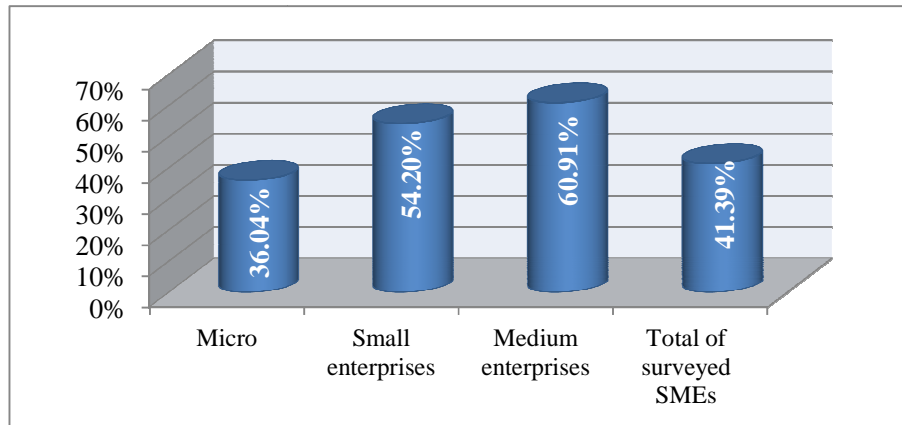
To highlight the role of bank credit in the financing resources of the SMEs from Romania we analyze the investigation conducted by the National Council of Private SMEs in Romania on a sample of 1.723 SMEs which highlights the methods of financing used by these enterprises during 2010 (see Figure 4). Thus, the survey results show that approximately 70% of the investigated SMEs have self-financed, over 41% have used bank loans, about 15% have resorted to use of leasing, 13% used credit providers and more than 5% have used grants to fund their activity. In comparison, SMEs have used in a lower proportion other forms of financing, such as customers' credit, loans from specialized financial institutions, failure to pay bills, guarantee fund for SMEs, factoring etc.



Source: Nicolescu, Haiduc, & Nancu (coordinators), 2011, p. 199

**Figure 4** SMEs financing methods, in 2010

In the external financing arrangements of SMEs it is noted that the dominant form of financing is the bank loans. However, the access to bank financing and the use of bank loans as a source of financing the activity of SMEs presents significant differences depending on the size of these companies (see Figure 5). Thus, the results of the investigation conducted by the National Council of Private SMEs in Romania shows that only 36% of micro enterprises used bank loans while the percentage is much higher for small and medium sized firms. Therefore, there is a close link between firm size and the percentage of use of bank loans.



Source: processed data after Nicolescu, Haiduc, & Nancu (coordinators), 2011

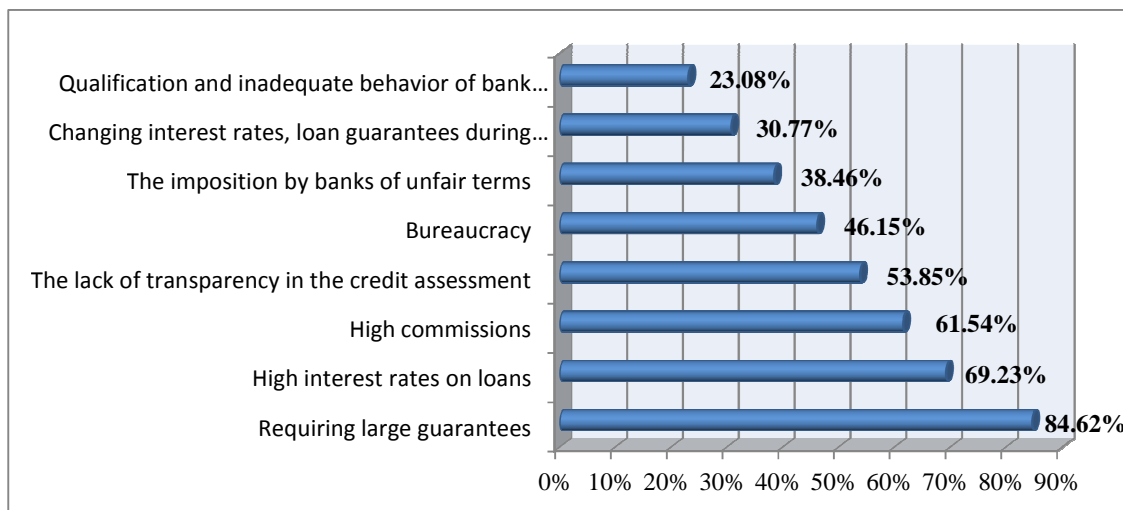
**Figure 5** The use of bank loans according to the size of the enterprise

Overall, the SMEs face many constraints in the conditions under which they aim to procure financial resources and, in particular when they want to use bank financing. Such obstacles are related to both entrepreneurs and economic environment, institutional and regulatory framework (Nicolescu & Nicolescu, 2008, p. 171). Among the obstacles for entrepreneurs, a series of surveys conducted both in Romania and in various countries show



the ignorance regarding the possibilities of obtaining financing resources, lack of counseling institutions, developing business plans which do not meet the requirements of lenders or investors, reduced negotiation skills in the relationships with suppliers of capital and insufficient guarantees available. Regarding the second category of problems, they refer in particular to the reduced availability of financing, excessive guarantees imposed by some banks when lending to SMEs, the high cost of consultancy services for obtaining funding by SMEs, corruption, bureaucracy.

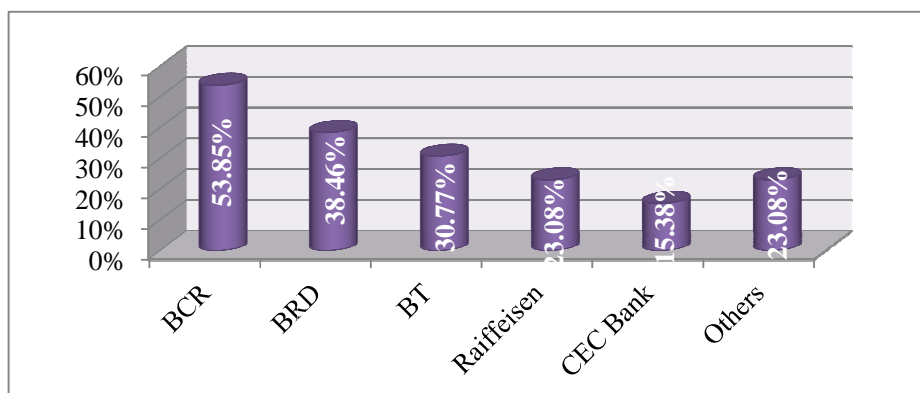
Based on the survey conducted by the National Council of Private SMEs in Romania in the period 20-28 October 2011, it is noted that the three major obstacles raised by entrepreneurs in Romania when they use bank financing are *the request of large guarantees from banks, high interest rates on loans and high commissions perceived by banks*. Thus at the question "Give the major difficulties in the relationship with the bank", over 84% of the surveyed entrepreneurs said the request of large guarantees by banks, about 70% mentioned high interest rates on loans and over 62% indicated high commissions required by banks. Also, approximately 54% of respondents are dissatisfied with the lack of transparency in the credit assessment and 46% are dissatisfied with the bureaucracy (see Figure 6).



Source: National Council of Private SMEs in Romania(CNIPMMR), 2011

**Figure 6** Major obstacles faced by the SMEs in Romania in their relation with banks

Therefore, SMEs from Romania face many constraints when they resort to financing through bank loans. It is also important to specify that the difficulties faced by SMEs in dealing with banks and bank product and service quality are different from one bank to another. Thus, the above investigation shows that entrepreneurs prefer the Romanian Commercial Bank (BCR), which has relationships with over 50% of SMEs. Also, on the top choices of the entrepreneurs ranks second Romanian Development Bank (BRD), followed by Transilvania Bank (BT), Raiffeisen Bank and CEC Bank (see Figure 7).



Source: National Council of Private SMEs in Romania (CNIPMMR), 2011

**Figure 7** Top of the commercial banks from Romania which entrepreneurs have relations with

## 5. Implications of the current crisis on access to bank loans of SMEs and measures taken by authorities

### 5.1 Effects of the current global crisis on the situation of the SME sector

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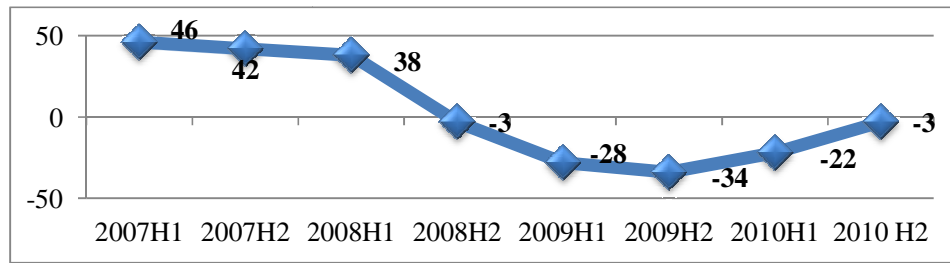
The economic global crisis which started in September 2008 had an extremely negative impact on the Romanian economy and also on the SME sector. The evaluation of the situation of the SME sector in Romania, in the context of the current crisis, can be conducted on the basis of the index of evolution of SMEs, calculated by CNIPMMR by summing up the scores of 11 indicators (registrations of commercial companies, number of defunct commercial companies, number of profitable companies, number of SMEs with losses, SMEs debts, average turnover per SME, average profit per SME, average loss per SME, average number of employees per SME, SMEs investments, exports of private enterprises). The maximum value for this index is 100 and its significance is presented in Table 3.

**Table 3** Score grid, according to the index of evolution of SMEs

| Index of the evolution of SMEs | Grade               |
|--------------------------------|---------------------|
| - 64 – 0 points                | Very unsatisfactory |
| 0 – 20 points                  | Unsatisfactory      |
| 20 – 45 points                 | Satisfactory        |
| 45 – 70 points                 | Good                |
| More than 70 points            | Excellent           |

Source: CNIPMMR, 2010

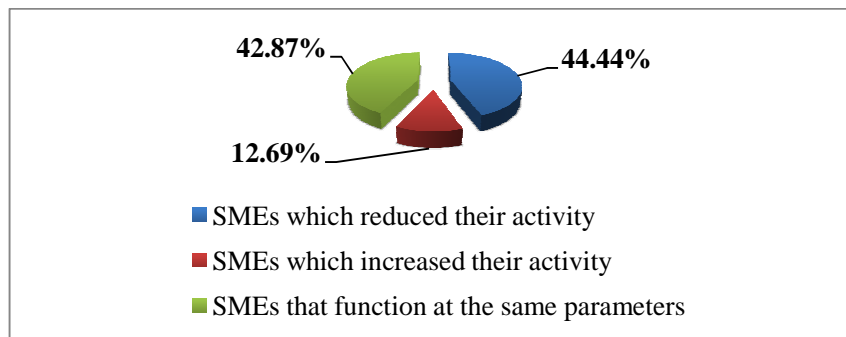
The evolution of the situation of the SME sector in Romania has been subjected to a descending trend, especially in the second semester of 2009, being evaluated as extremely unsatisfactory (see Figure 8). In 2010, Index of the evolution of the SMEs sector in Romania also reflects a very unsatisfactory evolution of the SME sector.



Source: centralized data on CNIPMMR, 2007-2010 H2

**Figure 8** Index of the evolution of the SMEs sector in Romania over the period 2007 – 2010H2

The extremely negative effects of the current global crisis can be highlighted based on the survey realized by The National Council of Small and Medium Sized Private Enterprises in Romania (CNIPMMR). Thus, the survey results show that during October 2008-March 2011 out of 1723 investigated SMEs, over 44% decreased activity and only 12.69% have seen an increase in activity while about 43 % are working at the same parameters (see Figure 9). Therefore, a significant part of the SME sector in Romania is strongly affected by the crisis, similar situation in other countries of the world, because compared with large firms, SMEs are more vulnerable to economic and financial turmoil (Nuță, F.M., Nuță A.C., 2011p. 1156).



Source: Nicolescu, Haiduc & Nancu (coordinators), 2011, p. 69

**Figure 9** The dynamic of surveyed SMEs activity between October 2008 and March 2011

If we analyze the impact of the crisis on SMEs, depending on their size, the results of CNIPMMR survey, shows that in the period between October 2008 and March 2011 the highest percentage of firms that have reduced activity are micro-sized, followed by small size enterprises. Also, the results reflect that the percentage of firms operating at the same parameters or increased their activity increases proportionally with business size (see Table 4).

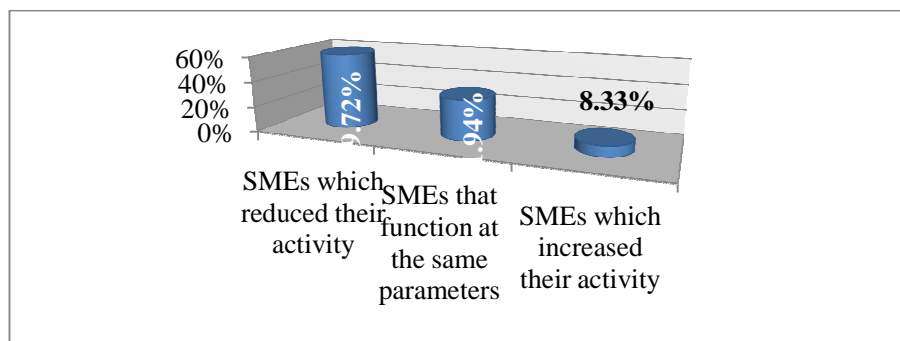
**Tabel 4** The dynamic of the surveyed firms depending on their size, in the period between October 2008 and March 2011

|                                    | The size of the firm |                   |                    |
|------------------------------------|----------------------|-------------------|--------------------|
|                                    | Micro                | Small enterprises | Medium enterprises |
| SMEs which reduced their activity  | 45.83%               | 40.32%            | 35.79%             |
| SMEs which are working at the same | 43.22%               | 43.87%            | 44.21%             |

| parameters                          |        |        |        |
|-------------------------------------|--------|--------|--------|
| SMEs which increased their activity | 10.95% | 15.81% | 20.00% |

Source: Nicolescu, Haiduc & Nancu (coordinators), 2011, p. 71

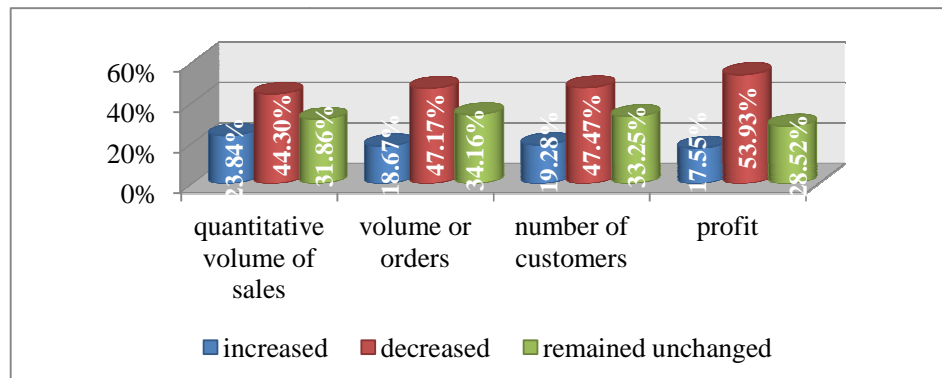
Through the impact of the crisis on SMEs by sector of activity in which they operate, the CNIPMMR survey shows that between October 2008 and March 2011 in the construction sector has been the highest percentage of SMEs that have reduced their activity, but also the lowest percentage of SMEs that operate at the same parameters and have increased activity (Figure 10). Such developments in the construction sector have been due to tighter lending standards, housing market collapse and significant decrease in the population income.



Source: processed after Nicolescu, Haiduc & Nancu (coordinators), 2011, p. 72

**Figure 10 The dynamic of the surveyed SMEs from the construction sector in the period October 2008-March 2011**

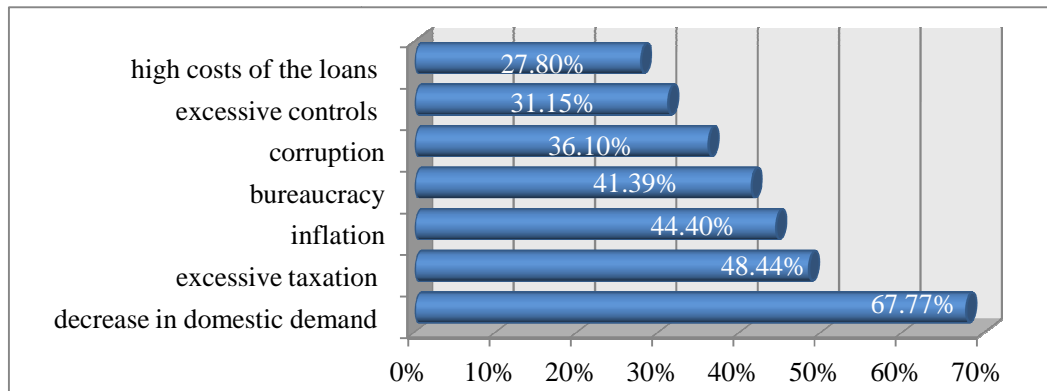
The impact of the current crisis on SME activity can be highlighted based on some significant indicators, namely the physical volume of sales, volume of orders, the number of customers and the size of obtained profit. Thus, the investigation conducted by CNIPMMR reveals that over 44% of the entrepreneurs reported a decrease of quantitative volume of sales, volume or orders, number of customers and hence of the profit in 2010 compared to 2009 (see Figure 11). Therefore, SMEs activity in Romania has deteriorated significantly in the context of the current global economic crisis.



Source: processed after Nicolescu, Haiduc & Nancu (coordinators), 2011, p. 41

**Figure 11 The evolution of the main indicators of the SMEs in Romania in 2010 compared to 2009**

In the context of an economic environment characterized mainly by economic recession, major macroeconomic imbalances, but also by insufficient measures taken by public authorities to counter the crisis, SMEs are facing major difficulties. From this perspective, the investigation conducted by CNIPMMR, on a sample of 1.723 SMEs, highlights that the major problems faced by entrepreneurs in the year 2010 (see Figure 12) were: a decrease in domestic demand (reported by about 68 % of SMEs), excessive taxation (reported over 48% of SMEs), inflation (44.40%), bureaucracy (mentioned by about 42%), corruption (36%), excessive controls (31%) and high costs of the loans (approximately 28%).

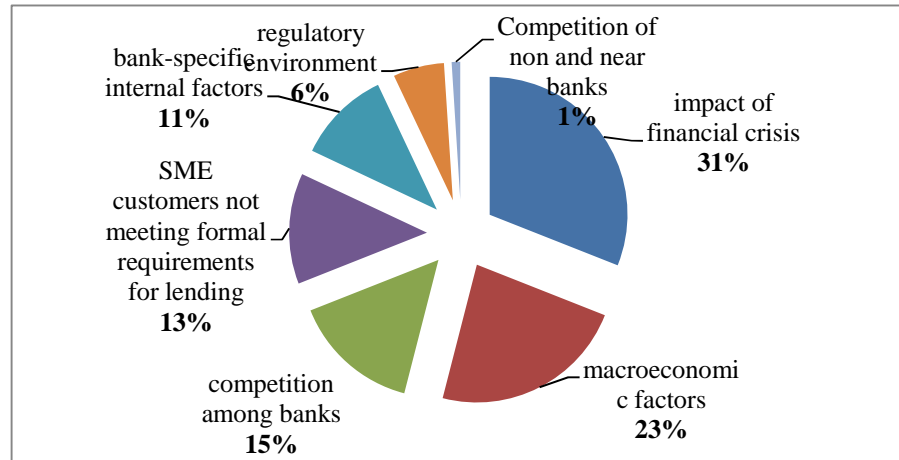


Source: Nicolescu, Haiduc & Nancu (coordinators), 2011, p. 41

**Figure 12** The frequency of the major problems faced by SMEs in Romania, in 2010

### 5.2 Effects of the crisis on the SMEs bank lending

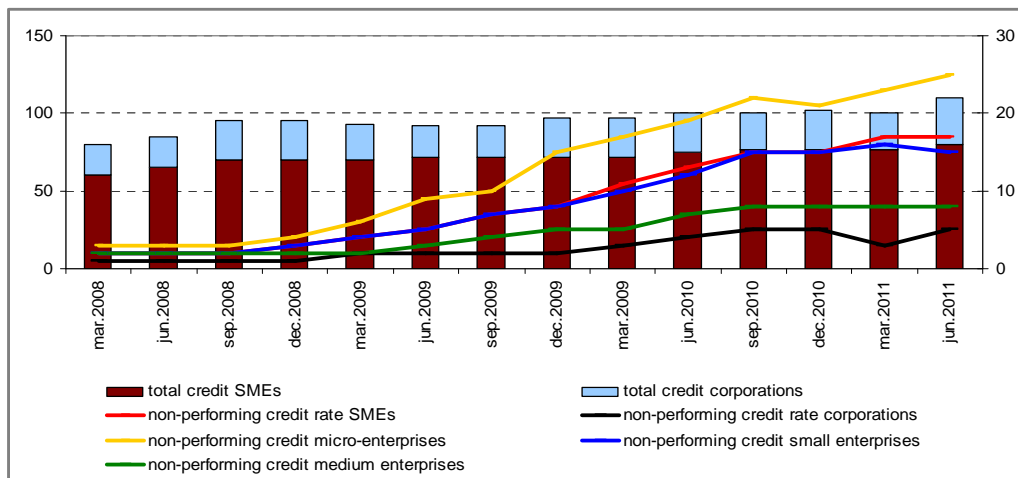
To highlight the impact of the current crisis on SME Banking it is of interest the analysis of data presented in Figure 13. As we can see the current financial crisis is the threat with the largest share (31%) on SME banking in Central and Eastern Europe, followed by macroeconomic factors with a share of 23%, competition among banks (15%) and SME customers that do not meet the formal requirements for obtaining a bank loan (13%). Internal factors specific to banks is a low threat (11%) as well as the regulatory environment (6%) and competition with non-banking financial institutions (1%). Regarding the impact of the financial crisis on the banking business in SMEs area, 69% of the bankers surveyed in the study saw a worsened quality of the loan portfolio as an issue. In this context, the banks in most countries examined did tightening the lending standards (most notably, by requiring additional collateral), especially for SMEs, and to raise interest rates on loans. According to the surveys conducted by central banks from the most surveyed countries including the European Central Bank, the main factors which led to tighter bank lending standards were the expectations regarding the general economic situation, the risk of the industry in which firms operate and the risk of the security required.



Source: processed data after Zeb, EFMA, ERSTE Group, 2009, p. 10

**Figure 13** The biggest threats to SME Banking in Central and Eastern European countries

The deterioration of the economic activity and hence of the financial situation of SMEs, the increased cost of financing resources on the international financial markets, increasing risk aversion have led banks to be reluctant to grant loans, tightening credit standards and rising the interest rates. However, the reluctance of banks in providing credit, especially for small and medium enterprises was driven by strong increases in non-performing loans and the related risk, guarantees. According to data published by the National Bank of Romania, the highest percentage of bad loans is generated by SMEs (see Figure 14).

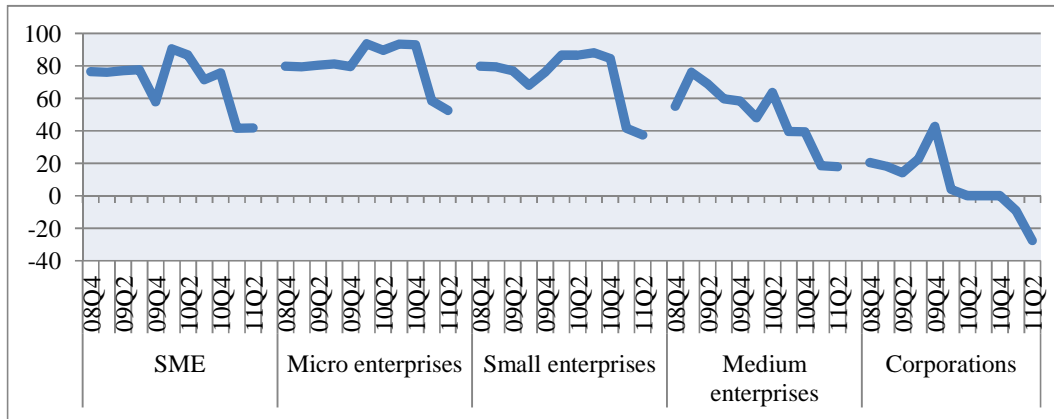


Source: National Bank of Romania, 2011, p.100

**Figure 14** The evolution of the rate of non-performing loans, according to the size of the firm

Thus, during December 2009 and June 2011, the non-performing loans rate generated by SMEs increased from 8.2% to 16.7%. Moreover, in the case of the micro-enterprises the credit quality has deteriorated significantly, between December 2009 and June 2011 from 14% to 24.1% (National Bank of Romania, 2011, p. 100). Compared, for the corporations the indicator showed a much lower level, moving from 1.3% to 3.7% for the same period (National Bank of Romania, 2011, p. 100). Therefore,

SMEs and particularly micro and small firms are considered by banks as posing a much higher risk than large firms (see Figure 15) and thus face significant difficulties in the procurement of financial resources in the form of loans.

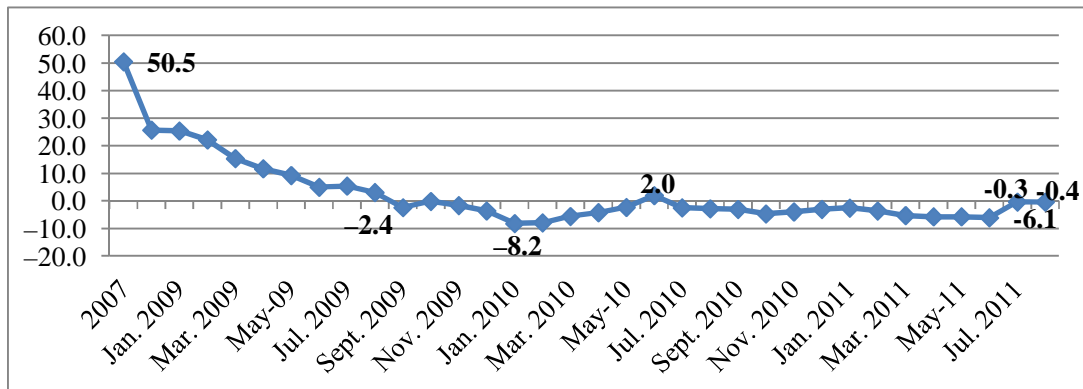


\*Net percentage positive values indicate an increase of credit risk

Source: centralized data after National Bank of Romania, (2008-2011).

**Figure 15** The evolution of credit risk on types of enterprises (net percentage\*)

In addition to decreasing the supply of bank loans, which reflects the increased risk aversion of banks, has registered also a decline in loan demand, particularly from the micro-enterprises and the small ones, which was determined both by tightening credit standards, the increase of interest costs and the uncertainties about the evolution of the economic environment. In this context there was a significant reduction in bank lending to the private sector (see Figure 16).



\*real annual percentage change

Source: <http://www.bnro.ro/Inflation-Reports-3343.aspx>

**Figure 16** The evolution of the bank lending to the private sector\*, in the period december 2007-august 2011

The deterioration of the financial situation of SMEs and hence the quality of bank loan portfolio has determined the intensification of the bank loans restructuring process, which was started both at the request of the debtor enterprises and on banks' own initiative. Thus, in late 2009, the share of loans

restructured in the total loans granted to non-financial enterprises stood at 10%, and SMEs held an overwhelming share of 85% on total restructured loans [National Bank of Romania, 2010, p. 105].

The vital role of the SME sector in the national economy and the extremely negative implications of the recent crisis on the activity of the enterprises, in particular on the micro, small and medium enterprises have imposed the adoption by the public authorities of measures to stimulate investment, improve the cash flow of the firms and their access to finance. From the measures adopted we can note in particular:

- Non-taxation of the reinvested profit;
- Offsetting the VAT to be recovered with VAT payable;
- Delaying the payment of outstanding obligations to the state budget;
- The state aid;
- Support for the export production by guarantees and counter-guarantees (by Eximbank);
- Capitalization of CEC and Eximbank to support SMEs;
- The establishment of the Counter-guarantee of Credit for SMEs Fund;
- Improving the investment law, including by reducing the amount of eligible investment which can generate facilities, from 50 million Euro to 10 million Euro etc.
- Granting state aids and de minimis aid up to 200 000 euro for SMEs.

Since September 2010, have been adopted new measures to support the enterprises, including: *establishment of a state aid scheme to facilitate the access to finance of the companies during the current crisis*, consisting of guarantees granted to SMEs and to large firms; *eliminating the minimum taxation* from 1 October 2010; *supporting young entrepreneurs* by providing a grant of up to 10,000 Euro to start a business; *the additional capitalization of the Counter-guarantee of Credit for SMEs Fund* for these firms to have an easier access to bank credit; *providing additional guarantees* for the beneficiaries of projects financed from structural funds in priority areas for the Romanian economy.

At the end of June 2011, the Romanian government adopted new measures to support the access to finance for SMEs in the government program called "*Mihail Kogălniceanu Programme for SMEs*", which aims to encourage and stimulate the establishment and development of SMEs. Through this program it is aimed to support the access to finance for SMEs by the state by granting a credit line of maximum 125.000 RON/year, with the interest partly subsidized and the guarantee of the state for this credit.

## 6 Conclusions

In general, bank financing of the SMEs is an issue of significant importance for both researchers and decision makers, following the major role of these enterprises for the development of national economies but also because they face important obstacles when they request bank loans. Thus, we may notice that some banks refuse to grant loans or increase interest rates for operational SMEs that do not offer adequate guarantees or do not have a credit history, because they have just started their activity or they have a degree of solvency that does not fall into the limits imposed by the banks in question.

The current global crisis has had an extremely negative impact on the SME sector in most countries including Romania because compared to large firms; SMEs are more vulnerable to the economic and



financial turmoil. The deterioration of the economic activity and hence of the financial situation of SMEs, the increased cost of financing resources on the international financial markets and increasing risk aversion have led banks to be reluctant to grant loans, tightening credit standards and rising the interest rates. However, the reluctance of banks in providing credit, especially for small and medium enterprises was driven by strong increases in non-performing loans and the related risk, guarantees. According to data published by the National Bank of Romania, the highest percentage of bad loans is generated by SMEs. Therefore, SMEs face major difficulties in purchasing loans.

Based on the survey conducted by the National Council of Private SMEs in Romania in the period 20-28 October 2011, it is noted that the three major obstacles raised by entrepreneurs in Romania when they use bank financing are the request of large guarantees from banks, high interest rates on loans and high commissions perceived by banks.

The vital role of SMEs in the national economy and the implications of the current crisis have imposed the adoption of measures by public authorities to support their activities and, in particular, their access to bank financing. However, for now, the serious situation of the SME sector in Romania and the timid recovery of bank lending shows that the effectiveness of these measures is reduced. Given the fact that easy access to financing through bank loans is vital for the recovery of the SMEs activities and their development, we believe that banks are not sufficiently concerned to resolve the difficulties raised by entrepreneurs when they resort to bank financing.

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- \*\*\* Romania's Government Emergency Ordinance approving Mihail Kogălniceanu Programme for SMEs, published in the Official Gazette, Part I, no. 460 of June 30, 2011.