Urgency and Smart Allocation: SMEs in dire need of funds

Notes on the Proposal for a Regulation of the European Parliament and of the Council establishing a Programme for the Competitiveness of Enterprises and small and medium-sized enterprises (2014 - 2020) COM(2011) 834 final

Summary of ESBA's recommendations to the institutions:

- In the negotiations for the Multiannual Financial Framework, the proposed **budget** for COSME is the bare essential and should by no means be lowered. COSME should be recognised as one of the few programmes that provides for a hands on approach to assist micro and small business that are in dire need of credit. ESBA recommends for more funding to be allocated towards the COSME programme.
- Particular emphasis should be placed on micro businesses. This group is responsible for over two thirds of the EU's private sector employment, yet is struggling the most as a result of the crisis.
- The European Commission proposal does not make reference to the transfer of business. ESBA is pleased to see that the rapporteur has taken on this crucial element for growth and development of SMEs. Every year 150.000 businesses, representing 600.000 jobs, risk closure of operations as a result of lack of support or finance to take over existing businesses. Of this group, in particular micro businesses and start-ups are the most vulnerable. ESBA urges the co-legislator to include this element in the final document.
- A link to Horizon 2020 should be made with caution, as Horizon is highly exclusive and does not cover most 'everyday' micro- and small businesses.
- Further to the point above, ESBA believes that there is too much focus on highly innovative SMEs. Only a fraction of all small businesses fulfills this criterion (what is highly innovative anyway?). Moreover, more alternative sources of finance (such as venture capital) are available to highly innovative companies. The European Institutions look to SMEs to get Europe out of the recession. Then why focus only on such an exclusive group of SMEs when allocating funds?
- The Equity Facility for Growth should focus on SME friendly equity financing such as Business Angels rather than putting a strong focus on venture capital. The expectations for the use of venture capital for small businesses are too high.
- ESBA stresses that it is highly unlikely for supply to exceed demand. Provided an adequate information campaign by the EU towards SMEs at Member State level runs parallel to the implementation of COSME, informing SMEs of the instruments available for them, demand exceeding supply is a much more realistic scenario.
- It is essential that the funds, made available through COSME, do in fact reach the small businesses. A monitoring system should be put in place to ensure that banks use the funds and guarantees to actually increase their SME lending. One way to do this could be through reporting schemes and a code of conduct for SME lending by banks.
- ESBA welcomes the allocation of funds to the Enterprise Europe Network and the promotion of entrepreneurship. However, as only 13 % of SMEs export outside the European Union, it is therefore advisable that COSME funds allocated to the EEN are not used primarily to promote activities in third countries.

Facts and figures:

On 30 November 2011, the European Commission has adopted a proposal for the Programme for the Competitiveness of Enterprises and small and medium-sized enterprises (COSME). The programme will start as of 1 January 2014 and will run until 2020. The programme has an envisaged budget of € **2.662** billion for the total period 2014- 2020; **€690** million is reserved for the equity instrument and **€746** million for the debt instrument. The remaining funds will be used to finance the Enterprise Europe Network, in order to promote entrepreneurship and to facilitate SME access to markets outside the EU.

SME financing: urgent action is needed

An OECD study of 19 April 2012 shows that the crisis has hit entrepreneurs and small business hardest[1]. The interest rate on loans is higher for SMEs as compared to the rates for large companies and SMEs have to provide more collateral in order to obtain loans. Since 2007, the rate of loans provided to SMEs has fallen sharply.

Furthermore, Commission and ECB figures show that in the period of March to August 2011, 1/3rd of SMEs did not receive the lending they had initially requested[2], 6% did not even apply, out of those who applied 11 % rejected, 4% refused on the basis of high costs, and 17% did get less. It is safe to assume that this trend has not improved since August 2011. [3]

Bank loans are by far the main source of finance for SMEs. An EU survey from the year 2005 concluded that 80 per cent of traditional SMEs rely on bank loans to finance their operations.[4] Further data show that bank loans are also the preferred source of finance for at least 60 % of SMEs[5].

According to estimations by the EIB, over the period 2007-2012, the SME Guarantee Facility has had a multiplier effect of 14 times the initial investment and has been beneficial to 190000 SMEs. [6]

Venture capital is only used by 7% of SMEs. As much as 60 % of businesses state that venture capital is not applicable to their businesses and an additional 22 % is not confortable in doing business with venture capital funds[7].

Commission figures have shown that SMEs most often rely on local credit providers who know the local market to obtain financing[8].

Only 25 % of SMEs export beyond the national borders and only 13 % exports beyond the borders of the EU[9].

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[1] OECD, *Financing SMEs and Entrepreneurs*, 19 April 2012 (link)
[2] ECB and European Commission, *SMEs' Access to Finance Surveys, 2009-2011*
[3] Ibidem
[4] Flash Eurobarometer 2005, *Access to finance for SMEs* link)
[5] ECB and European Commission, *SMEs' Access to Finance Surveys*, 2009-2011
[6] EIF, Workshop on "Financial Instruments in COSME and Horizon 2020", 11 April 2012. (link)
[7] ECB and European Commission, *SMEs' Access to Finance Surveys, 2009-2011*
[8]Commission Staff Working Paper SEC(2011) 1527 final

The European Commission's study (2011) "Business Dynamics: Start-ups, Business transfers and Bankruptcy" estimates that Approximately 450.000 firms are being transferred each year in the EU – 27, affecting 2 million employees[10]. Every year, there is a risk of losing approximately 150.000 firms and 600.000 jobs due to inefficiency in transferring businesses. The smallest businesses are the most vulnerable to transfer failure and companies in sole proprietorship and those that are less than 3 years old are also prone to be more vulnerable.[11]

[9] EIM, 2010, *Internationalisation of SMEs* (link)
[10] European Commission (2011) "Business Dynamics: Start-ups, Business transfers and bankruptcy (link)
[11] Ibidem