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MOKRA GORA SCHOOL OF MANAGEMENT

PANEL 2: NEW FINANCIAL SERBIAN ARCHITECTURE FOR STIMULATING THE REAL SECTOR

A NATIONWIDE STUDY ON SME ACCESS TO FINANCE: IS THE FINANCIAL SECTOR PERFORMING?

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Šta i kako dalje?



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Market Snapshot





Weak access: a national problem with regional/sector variations

- Credit –to-GDP: 50%+ (Serbia) 100%+ (Europe); 70% (Croatia); 85% (Hungary); 123% (Austria) 200% (UK and US)
- 60% of SMEs not taking any formal loans right now
- Of SME that take finance:
 - Half get € 10k or less; only 25% (10% of SME's) get more than € 50k
 - Over 80% borrowing is for liquidity - less than 20% for investment
 - Under-leveraged by factor up to 6 times the developed market norm (30% debt-to-equity vs. 150%-200%)
- Financial system intermediates most market risk by transferring it (not managing it)– FX risk big problem, 85% of SME's; rate risk a problem, 60%



Market Snapshot

The trend and composition is not good for strategic sectors...

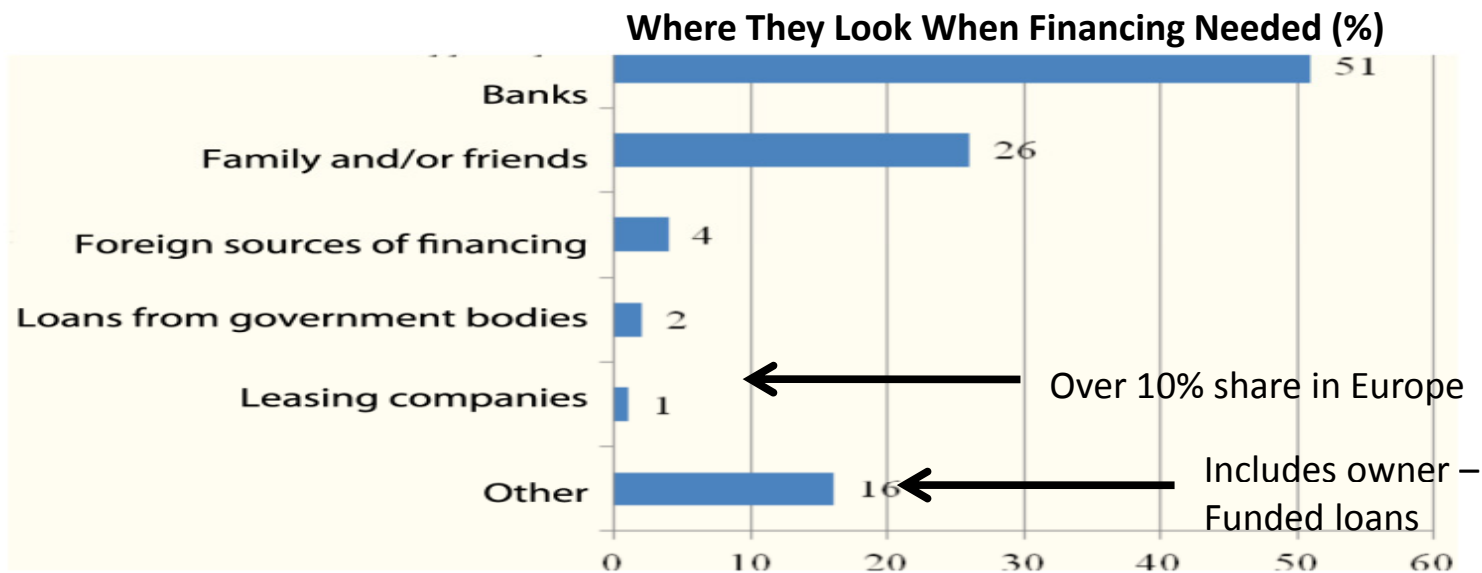
SECTOR	% SHARE OF SME DEBT FINANCE			
	2010	2009	2008	2007
 Agriculture	3%	5%	4%	6%
 Production	19%	28%	27%	29%
 Trade	18%	20%	21%	22%
 Other	60%	47%	48%	43%
TOTAL	100%	100%	100%	100%

Source: Business Registry, USAID BEP, National Business Survey 2011, author calculations



Market Snapshot

SME's are beholden to banks, followed by informal sources – essentially few viable non-bank alternatives



Source: USAID BEP, National Business Survey 2011



Market Snapshot

Product range and suitability not satisfactory

% of Dissatisfied SME's	By Sector			By Region					SME Average
	Prod.	Service	Trade	Vojvod	Belgrade	West	Central	South East	
Loan duration	56	56	66	38	74	47	49	47	59
Currency	48	43	64	41	52	56	48	71	51
Repayment terms	60	62	56	50	64	52	56	66	60
Collateral	67	64	64	50	72	52	57	79	64
Rates and fees	88	82	85	73	91	72	74	90	84
Length of Process	48	50	58	41	57	46	52	57	52
Quality of Service	37	38	55	34	48	42	42	40	43

Source: "Business Survey – Serbia 2011," USAID Business Enabling Project



Market Snapshot

70% of SME's have problems getting finance, see no improvement

World Economic Forum Rankings (140 countries)

Ranked higher than Serbia

Ranked Lower than Serbia

Country	Total Market	Ease of access to loans	Equity market	Venture capital	Regulations and securities exchanges
RANKING 2011-2012					
SERBIA	96	97	112	121	121
ALBANIA	107	121	140	124	132
BULGARIA	75	122	111	125	123
CROATIA	87	84	102	108	79
MACEDONIA	82	96	83	65	60
ROMANIA	84	82	89	77	106
SLOVAKIA	47	55	118	68	85
Ranking Trend Serbia	↓	↓	↓	↓	↓

Ranking data from World Economic Forum, Global Competitive Indicators



Constraints

A complex of constraints affect SME lending

Supply-Side Constraints

- High Costs
- Collection risk
- Regulatory disincentives
- Poor product suitability
- Few alternative sources
- Infrastructure gaps



Demand-Side Constraints

- Weak capacity
- Borrower psychology and risk aversion
- Information asymmetries
- Poor SME market leverage



Constraints

A closer look at the supply-side and infrastructure issues

High Costs

- Externalities
- Regulatory costs
- Poor economies

Weak Credit Enforcement

- Weak court Administration
- Challenges w/ mortgages and pledges
- Misuse of bankruptcy

Impact of Financial Regulation

- Loan classifications
- Credit files
- Tax compliance monitoring
- Potential impact from Basel II

Poor Bank Product Suitability

- Business models
- Funding structure
- Poor risk intermediation
- Weak knowledge of SME's

Lack of Alternative Sources

- No NBFIs
- Poor capital market
- Few value chains/clusters

Lacking Supporting Services

- Poor appraisals
- Under-developed reporting
- Weak information services



Constraints

A closer look at enterprise-side issue

Weakened Financial Capacity

- Systemic liquidity shortages
- Insufficient collateral
- Poor fundamentals

Borrower Psychology & Risk Aversion

- Low tolerance for risk
- Expectations of state support
- Negative sentiment about formal lenders
- Distorted credit culture

Information Asymmetries and Legitimacy Issues

- Weak capacity to present the business
- Informality

Poor SME Market Leverage

- Weak national advocacy
- Weak negotiating position and communication



Responses

Need for a comprehensive, targeted approach

- **Strengthen credit enforcement**
 - Accelerate implementation of enforcement law; build capacity in courts
 - Standardize court practices
 - Enforce laws against fraud and misappropriation
 - Legal refinements needed to strengthen security position of lenders
- ***Reduce Transaction Costs and Burdens***
 - Conduct cost impact assessment of financial regulations
 - Incentives for investments in shared services platforms
 - Take credit reporting to next stage (scoring, rating, widen access)
- **Tailor financial and tax regulations**
 - Rationale standards for SME's - lenders do the lending and risk management
 - Modify timing of tax payments?
- **Reform rules and certifications for appraisers, accountants/auditors**



Responses

- **Deepen financial system and incentivize specialization and product segmentation**
 - Regulatory frameworks for non-bank credit institutions
 - Promote specialized investment and market segmentation
 - Mandated interventions to create markets/products for risk management
- **Re-formulate government's role**
 - Enhance reporting and data collection
 - Re-design state financing programs (more targeting, more private sector leverage)
 - Re-focus technical support programs towards facilitating industry cluster/value chain financing
 - Get the consultative bodies working and addressing the issues
 - Create SME finance observatory or similar function
 - Public campaigns: strengthen credit culture; promote entrepreneurship, etc.
- **Better targeted and informed advocacy from business associations on SME needs**
 - Improve SME, lender, and government communications
 - Strengthen the market leverage of SME sector



Final Comment

“Each country should have a continuum of financial institutions that, together, offer appropriate products and services to all segments of the population.”

This quote borrowed from a UN publication on inclusive financial services highlights an important aspect of financial sector development that is missing in Serbia.