The Role of Subventioned Micro Credit in Financing Small and Medium-sized Enterprises in Hungary

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The economic role of small and medium-sized enterprises (SMEs) is pivotal: they create new jobs and economic growth. At the same time SMEs are at a disadvantage in getting various financial funds, in relation to both equity and foreign capital, as compared to large enterprises. Therefore they need collective or national subvention. Much research prove that bank loans play the most important role in foreign capital financing: at the end of the 1990’s Hungarian banks were open to SMEs, which increased the ratio of the SME’s credits in bank loan portfolio. This paper studies the characteristics of subventioned micro credits in Hungary, the impact of micro credits on enterprise loan portfolio and on the competitiveness of the Hungarian SME sector.

Keywords: SMEs, financing, supported credit

1. Introduction

The economic role of the small and medium-sized enterprises changed radically in the last decades. Today they are the most important inducement of the economic growth and the workplace creation, and play role in sustainment of the competitiveness and economic adaptiveness and in the development of the regional and the national economy.

Today the importance of SME’s policy is confirmed both in European Union and in Hungary by their role in economy and labour market. At the end of 2007 more than 19.6 million enterprises were in the EU 27 countries: 91,9 % of all enterprises are micro enterprises from one to nine person, 6,8 % are small, 1,1% are medium sized, and hardly more than 0,2 % fall into the category of large companies. In Hungary 95,5% of the 740000 enterprises were micro enterprises in 2007, and this ratio is larger with 0,5 % than in 2005, the medium sized enterprises’ rate decreased from 4,2% in 2005 to 3,6% in 2007.

46 The category of micro, small and medium sized enterprises consists of enterprises which employ fewer than 250 people and which have either an annual turnover not exceeding 50 million euro, or an annual balance sheet total not exceeding 43 million euro.
The Role of Subventioned Micro Credit in Financing Small and Medium-sized Enterprises

Table 1
Number of enterprises in Europe and Hungary in 2005 and 2007

<table>
<thead>
<tr>
<th>Number of enterprises</th>
<th>SME's</th>
<th>LSE's</th>
<th>total</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>micro-sized</td>
<td>small-sized</td>
<td>medium-sized</td>
</tr>
<tr>
<td><strong>EU-27 (million)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>18,04</td>
<td>1,35</td>
<td>0,21</td>
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<tr>
<td>2007</td>
<td>18,79</td>
<td>1,40</td>
<td>0,22</td>
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<tr>
<td><strong>Hungary (thousand)</strong></td>
<td>672</td>
<td>30</td>
<td>5</td>
</tr>
<tr>
<td>2005</td>
<td>95,0%</td>
<td>6,8%</td>
<td>1,1%</td>
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<td>2007</td>
<td>95,5%</td>
<td>3,6%</td>
<td>0,7%</td>
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</table>

Source: Edited from EUROSTAT and Hungarian Central Statistical Office data [2010]

The distribution of their numbers and company headcount categories show scarce about contribution of SMEs to the economic growth. Examining their role in labour market 67,2% of 131 million employers were employed in 2007 in the EU 27 countries by SMEs, but this rate is larger with about 9% in Hungary.

Source: Edited from EUROSTAT and Hungarian Central Statistical Office data [2010]

Figure 1. Proportion of employments in Europe and Hungary in 2005 and in 2007

The difference was generated by the employment’s rate of the Hungarian micro sized enterprises: the 41% rate in Hungary was more than 11% larger, than in the EU 27 countries, but the employment’s rate of small and medium sized enterprises was 2% smaller and 1% in Hungary.

Source: Edited from EUROSTAT and Hungarian Central Statistical Office data [2010]
Economic importance of this sector is also confirmed by data of the gross added value: in 2005 the 50.2% proportion of the gross added value was produced in the economy of Hungary by SMEs, and this rate was 7.4% larger in the EU 27 countries. So with respect to component of the business output the role of small and medium-sized enterprises is determinant in employment and in growing of the gross domestic product, but at the same time an important problem of the competitiveness is the financing. (Ministry for National Development and Economy [2008])

2. Credit financing of SMEs

The internal finance (e.g. the operating cash-flow) have an important part in financing of SME’s, at the same time numerous studies have confirmed, that the enterprises have recourse to external finance when they can’t satisfy their own financing requirements with internal finance. In the case of external finance the enterprises draw on cash from external organizations and investors. Examining the external finance the public offering and the bond issue is not characteristic to this sector, because of its high cost and big time-consumption, and the trade debt and trade credit are applied occasionally depending on the dealposition of the enterprise. In the case of external debt the role of the bank loan and overdraft, the leasing and the factoring (and forfeting) can be emphasized, but this enterprises can get loan and overdraft just by higher interest and collateral because of the relatively high cost of the credit assessment and higher operating risks. To sum it up it can be declared, that “the SME’s are in more disadvantageous situation than the large size enterprises on the admittance of financing sources with respect to both equity and debt”. (Csubák, [2003b], p. 34.).

The typical financing source is different in countries, at the same time numerous paper prove, that the bank loans and overdrafts bear the most important part in SME’s financing in Europe. In the research of Flash Eurobarometer47 emphasizes that the problem of the competitiveness is the financing and the importance of bank financing. In all other countries in this study, the 16% of respondents said that access to finance was the most pressing problem for their company (Figure 2.), assigned this second. At the same time this rate was 3% larger in Hungary. Examining the characteristics of the company, access to finance was more often selected as the most pressing

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47 This Flash Eurobarometer Access to finance (No. 271) was commissioned by the European Commission’s DG Enterprise and Industry, in cooperation with the European Central Bank (ECB). More than 9,000 managers of SME’s in the 27 Member States (in between 228 in Hungary) were interviewed between 17 June and 23 July 2009, using a fixed-line telephone methodology.
problem of companies with a turnover of less than 2 and 2-10 million EUR (16.9% and 16.4% vs. 9.2% for companies with a turnover above 10 million EUR). Analysing loans as external source of financing, the proportion of use of loans (past two years) per all companies was 20% larger in the EU 27 countries, than in Hungary. This—and the third worst place of the EU 27 countries—indicate the low credit financing of domestic micro, small and medium sized enterprises. (*Flash Eurobarometer*, [2009])

![Diagram](image.jpg)

**Figure 2. Companies’ most pressing problem**

### 3. Financing SME’s by bankloans

From the changing of regime until 1995 the number of the enterprises heightened and many banks came into the market, therefore the total credit amount of this sector increased. In 1993 the proportion of credit amount of small per all companies was 11.2%, but from 1994 it was reduced, the ratio was just 3.6% in 1998.

This phenomenon could be eventuated by the next causes (*Csubák*, [2003a]):

- the small companies were characterised by low capital,
- the high costs and risks of low credit amount, and
- the low information of activity of enterprises caused by the simplier accountant regulations.
From the 2000s this field shows signs of improvement. The creditmarket of large scale enterprises has been filled, several banks have been opened towards the unexploited SME’s sector on account of open competition. The risks of this sector have been decreased through improvement of credit assessment, and improvement of bankservice has reduced the costs of rating and riskmanagement (Csubák, [2003a]). Therewith the development policy of the government for SME’s can be promotive of credituse with the state supported credits (see next part) and guarantee schemes (which support the creditusing with solving the collateralproblems).

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<tr>
<td>85,7</td>
<td>89,2</td>
<td>71,1</td>
<td>62,9</td>
<td>64,7</td>
<td>63,8</td>
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<tbody>
<tr>
<td>761,9</td>
<td>875,5</td>
<td>982,6</td>
<td>1260,1</td>
<td>1766,3</td>
<td>1773,1</td>
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<tbody>
<tr>
<td>11,2%</td>
<td>10,2%</td>
<td>7,2%</td>
<td>5,0%</td>
<td>3,7%</td>
<td>3,6%</td>
<td></td>
</tr>
</tbody>
</table>

* data in milliard HUF

Source: Institute for Small Business Development [1999]

Bankloans of SME’s were increased from 461 billion HUF at the end of 1999 to 4,090 billion HUF till the end of 2008, this means ninefold expansion (Figure 3.). The total credit amount of this sector has been augmented in all category more considerably than the LSE’s, and it’s percentage has been grown from
19.3% in 1999 to 57% at the end of 2008 in conformity with total credit amount of enterprises.

In 1999 from the total credit amount of the SMEs the medium-sized enterprises were 52%, the micro and the small enterprises were 24-24%, but at the end of 2008 the medium-sized enterprises was 34%, the micro enterprises were 36% and the small enterprises were 30%. The total credit amount of the micro and the small enterprises were thirteenfold and elevenfold separately during the tested period, and the amount of the medium-sized were increased sextuple. Therewith the ratio of the micro enterprises credits and the total credit amount increased continuously, from 12.9% in 2001 to 20.3% in 2008.

Notwithstanding the dynamic expansion, the domestic enterprises in proportion to developed countries can draw on fewer loan and overdraft sources by the ratio of the nonfinancial enterprises credits per GDP. In European countries the SME’s credits per GDP ratio is high, correspondently to the distinctiveness of the financial systems, but in Hungary it was only 14% in 2008 (at the same time this was higher, than the 4% in 1999).

4. State supported credits for SME’s in Hungary

The state support for SME financing will be presented through the analysis of the Microcredit Program, the Széchenyi Card, the Loan Programmes for SMEs by Hungarian Development Bank and the New Hungary Enterprise Micro Credit.

Microcredit Program

The several modified programmes in regard to conditions have been run since 1992 in maintenance of the Hungarian Foundation for Enterprise Promotion. Its target group are the micro enterprises. In 2003-2004 the amount of accommodation was decreased through sharpening the conditions, the program generated in 2002 just scarcely 2% of the total credit amount of micro enterprises, and this meant only 0.13% at the end of 2008. So this program granted financing source just for small part of the micro enterprises, but several studies made an inference of the improvement and sustainably (Kállay, [2002]; Kállay-Imreh, [2004]; Ministry of Economy and Transport, [2005a]).
Table 3
Microcredit disbursement between 1999-2008 (in million HUF).

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>microcredits</td>
<td>6 792</td>
<td>9 023</td>
<td>3 559</td>
<td>1 416</td>
<td>4 154</td>
<td>4 824</td>
<td>1 677</td>
<td>1 662</td>
</tr>
<tr>
<td>ratio*</td>
<td>1.63%</td>
<td>1.72%</td>
<td>0.52%</td>
<td>0.19%</td>
<td>0.46%</td>
<td>0.53%</td>
<td>0.13%</td>
<td>0.13%</td>
</tr>
</tbody>
</table>

* microcredits by Microcredit Program per the total credit amount of micro enterprises
Source: Edited from Hungarian Foundation for Enterprise Promotion data [2010]

Széchenyi Card
Széchenyi Card is a credit-card based, low-interest loan for SME’s on state supported preferential terms. Its aim is to provide enterprises with a minimum business history of one year with unrestricted-use credit managing liquidity risks. The attraction of this financial source is that it provides quick access to funds and it is not necessary to demonstrate own contribution.

Comment: green line (with triangle) is the ratio of the micro enterprises allocated credit portfolio of Széchenyi Cards per the total credit amount of micro enterprises, black line (with square) the ratio of the allocated credit portfolio of Széchenyi Cards per the total credit amount of SMEs.
Source: edited from KA-VOSZ Financial Services Trading Close Co. and Hungarian Financial Supervisory Authority data. [2010]

Figure 4. Successfulness of Széchenyi Cards between 2002 and 2008.
Enlargement was enabled by the improvement of credit conditions in 2004-2005, the credits meant more than 124 billion HUF in 2008, additionally more than 105,000 cards were issued during seven year with assistance of this in the summer of 2002 starting program and in the aggregate 582 billion HUF. Examining the distribution of the credit amount of micro, small and medium-sized enterprises, it can be traced, that the sharing of the micro enterprises was steadily more than 70%.

Confirming the successfulness of this program, it was generated between 2004 and 2006 3.6% of the total credit amount of SMEs and for the micro enterprises allocated credit portfolio of Széchenyi Cards was about 8% of the total credit amount of micro enterprises. The ratios slightly decreased in 2007 and 2008, but even they were 3.03% and 6.05%. Therewith the international approbation is indicated by the first prize at the European Enterprise Award 2007.

**Loan Programmes for SMEs by Hungarian Development Bank**

The New Hungary Enterprise Promotion Programme by Hungarian Development Bank (MFB) was started in the summer of 2005. It provides financial assistance to support the investment and development goals of companies in the SME sector. This loan programme was extended in 2008 with a new sub-programme referred to as the New Hungary Small and Medium-sized Enterprise Loan Programme, which thanks to equal funding from the EU and MFB constitutes another preferential loan opportunity for SMEs investing outside the Central Hungary region. The loans were primarily offered under refinancing schemes, at the end of 2008 the MFB had refinancing agreements with roughly 40 credit institutions. The ratio of the credit amount of these programmes and the total credit amount of SMEs (data for micro enterprises is not available) was 4-5% between 2006 and 2008. In 2008 the credit amount of SMEs was 202 billion HUF by 3,630 agreed contract, which means 4.94% share.

In a similar manner, the MBF responded positively to market trends by restructuring the loan programmes to expand the opportunities for micro and small enterprises to draw small development loans. In this context the New Hungary Small Enterprise Loan was introduced alongside the Micro-Credit Plus Programme in 2006. This direct financing scheme is available to micro enterprises that are offered by the Bank through agent networks. (Hungarian Development Bank, [2008]) The program was generated in 2008 just scarcely 0.3% of the total credit amount of micro enterprises, demonstrating the resultlessness so far.
New Hungary Enterprise Micro Credit (NHEP Micro Credit)

The aim of the this programme is to develop micro enterprises with seat in Hungary that cannot be, or cannot sufficiently be financed with commercial banking methods, by improving their credit options. Within NHEP Micro Credit, Venture Finance Hungary Plc. relays refinancing credit and guarantee options to the contracted financial intermediaries, thus it provides the micro enterprises reimbursable funds with favorable interest rates, and it eases the collateral expectations faced by the SMEs by giving them guarantee.

The funds (JEREMIE initiative, 85% EU and 15% Hungary) that can be invested for this purpose amount to 58,5 billion HUF between 2008 and 2013. Credit institutions and specialized micro-financing organizations could become financial intermediaries following selection by open tendering, from the end of 2007. Contracts have been signed by 43 financial organizations so far, and 870 enterprises with 4,4 billion HUF credit amount (this means 0,3% of the total credit amount of micro enterprises) was became beneficiary in 2008.

5. Conclusion

In this paper credit instruments for SME’s were examined. The credit financing of the sector has changed for the better as a result of the strengthening competition on the bankmarket in the recent years. The subventioned programmes discussed in the paper, and especially the Széchenyi Card, have stimulated the prevalence of micro credits and quick credits without collateral, and in response to the government initiative banks have also launched similar market-based products. These developments of the Hungarian capital market have fostered both bank loan portfolios and the SME sector.

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