

# GAZDASÁG & TÁRSADALOM

Journal of Economy & Society

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## **Financial instruments used by the Hungarian SMEs**

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ABSTRACT: SME sector plays a significant role in the economy of Hungary. 97-99% of the companies takes part of this sector and has importance in the field of employment and production. In my study I analyse the external financing opportunities such as credits and tenders, which are available especially for SME sector. I analyse these data between 2007 and 2011. The range of credit possibilities for SME sector is expanding. There are more opportunities allowing companies to take loans not only from banks but from credit intermediaries. The European Union also provides refundable support to start-up and working companies besides tenders mostly from JEREMIE program.

KEYWORDS: entrepreneurship/tender/loan

### **Introduction**

The SME sector plays a significant role in the economy of Hungary. 97-99% of the companies takes part of this sector, and has importance in the field of employment and production.

The Hungarian economy has gone through significant changes since the regime change in 1989. In this period the roles of micro-, small and medium-sized enterprises in the market have become more and more important. However the main focus was only awarded right before the European Union accession when it was possible to strengthen the enterprise sector with pre-accession applications.

During this period important developments took place which helped to encourage entrepreneurship and contributed to create new companies. After joining the European Union the number of enterprises showed a fluctuating trend however the growths of operating and already developed companies were constant.

The years at the very beginning of the 21th century have greatly helped people who work in agriculture to start up new family businesses in production and service sectors.

## Distribution of SME sector

In the pre-crisis period entrepreneurship has increasingly boosted shows the unified 770.000 number of enterprises in *Table 1*. There were a downturn around 2006 and 2007, but in 2008 it is rising to the original number. Since 2009 a drastic downturn has occurred caused by micro-sized companies suffered loss. Mainly the number of these enterprises declined while the number of small and medium-sized ones remained the same.

In 2010 according to latest data it seems that the trend of last year turned the other way around and medium and bigger sized enterprises break off, while smaller ones continue to increase. Compared to 2009 micro-sized companies increased about 2% and small-sized ones grew 1,6%.

In 2011 decline occurred again, further businesses had been closed since crisis had had infiltrated all markets. For this period only estimated data can be obtained from the KSH surveys, therefore drawing reliable conclusions is not possible.

**Table 1. The number of the companies between 2004 and 2011 (piece)**

Number of capita	2004	2005	2006	2007	2008	2009	2010	2011*
1-4	702 221	693 050	679 214	672 674	696 002	681 220	694 434	0
5-9	41 265	41 869	42 486	41 229	40 946	38 251	39226	0
1-9	<b>743 486</b>	<b>734 919</b>	<b>721 700</b>	<b>713 903</b>	<b>736 948</b>	<b>719 471</b>	<b>733 660</b>	<b>676 264</b>
10-19	18 902	19 240	19 612	18 906	19 343	17 693	18 612	20 578
20-49	11 050	11 201	10 620	10 143	10 231	9 256	8 770	10 606
10-49	<b>29 952</b>	<b>30 441</b>	<b>30 232</b>	<b>29 049</b>	<b>29 574</b>	<b>26 949</b>	<b>27 382</b>	<b>31 184</b>
50-249	<b>5 130</b>	<b>5 067</b>	<b>5 085</b>	<b>5 145</b>	<b>5 222</b>	<b>4 811</b>	<b>4 696</b>	<b>4 682</b>
250 and more	<b>959</b>	<b>927</b>	<b>926</b>	<b>929</b>	<b>962</b>	<b>875</b>	<b>877</b>	<b>859</b>
all	<b>779 527</b>	<b>771 354</b>	<b>757 943</b>	<b>749 026</b>	<b>772 706</b>	<b>752 106</b>	<b>766 615</b>	<b>712 989</b>

Source: Own compilation based on Central Statistical Office data

\*Estimate based on KSH data

## Financial instruments

The enterprises have more and more possibilities to use external financing opportunities for their everyday work. The state and the government have always conducted to the improvement of this sector. More and more credit and support opportunities have been created for SME's. That is the reason why more companies have a chance to develop.

The policy of support and development of small and medium-sized companies have been in the front line of the argues for a long time. Several tries to reduce

the competitive disadvantage of SME sector have been carried out, but big differences between these companies and the large enterprises have still remained. Despite the fact SME's are able to produce high value-added products, many factors have a strong influence on their development of, which are:

- low capitalization
- under-funding
- low efficiency and productivity
- lack of entrepreneurship
- strong dependence of the internal consumption
- exposure of the black economy.

SME's that use mainly internal financing sources down to their size, may be prevented to use international funds (bank loans, leasing, factoring) as well as to access to resources of foreign investments. Due to their small sizes they can rarely be beneficiaries of government incentives which help greater investments and job-creations. Many of them have difficulties to fulfill administrative obligations.

The most accessible opportunities for SMEs:

- credits
- supports

In the Hungarian economy factoring and leasing has only a brief past therefore these opportunities are taken advantage of by a few. However these opportunities get increasingly important role in recent times.

Commercial banks intend to give emphasis on providing accessible and favourable opportunities to these companies. Among their financial services the following are preferred:

- credits and loans
- leasing
- surety bonds and bank guarantees
- credit reference services

## Credits

The range of credit possibilities for SME sector is expanding. There are more opportunities allowing companies to take loans not only from banks but from credit intermediaries. KA-VOSZ Zrt and the Magyar Vállalkozásfinanszírozási Zrt provide the most reliable information about the possibilities to the members of the market. The first three – perhaps the most popular – possibilities are Széchenyi Kártya, Új Magyarország Hitelgarancia and Garantiqa Hitelgarancia that have more favourable conditions than bank credits. The European Union also provides refundable support to start-up and working companies besides tenders mostly from JEREMIE program.



Disbursements of low loan applications are taken over by county enterprise development foundations from banks, through which the National Microcredit Program is available for investment and working capital loans. The Program also offers loans for new companies with preferential rates without additional costs. The conditions of the Program are flexible to the needs of micro-, small- and medium-sized enterprises.

The Új Magyarország Kis- és Középvállalkozói Hitel is based on a similar principle which also helps these companies to grow and invest. „The aim of this loan program is to develop micro and small enterprises with seat in Hungary that cannot be, or cannot sufficiently be financed with commercial banking methods, by improving their credit options. The program takes part of a government package to relieve the effect of the financial crisis.

The sources reach the final beneficiaries through those credit institutions which are direct partners of the MV Zrt and the MFB Zrt. The credit institutions which joined to the program can outsource an investment loan of 10-100 million forints with a maturity of maximum 10 years to the enterprises.” (Magyar Vállalkozásfinanszírozási Zrt, 2012.)

### **Support options**

Since the European Union accession more and more enterprises have intended to take advantage of this financing resort in order to get new sources for their investments. In some cases these opportunities not only contribute to development but also provide new tools for keeping the enterprises running. Benefiting in tenders has yielded great results not only for developing companies but also for the whole country. While NFÜ publishes the best projects regularly in order to encourage companies for further development and implementations.

Certain amount of the investment costs are paid as non-refundable grants assuming the tender is successful so as to realize economic policy objectives and strengthen competitiveness, job creation and reduce environmental burdens. Applying for these grants European Union funds can be used within the Operational Programs.

Nowadays the tenders of “Új Széchenyi Terv” give opportunities to investments. The methods of subsidized interests have similar policy objectives as non-repayable loans and give new possibilities for SME’s to contract for credits with refinancing institutions in a market-conform way.

The Economic Development Operational Programs also provide several funding opportunities for supporting business innovations in SME sector, research and development activities, promotes to become permanent suppliers and also contributes to their technological innovations as well as implements new information-, quality- and environmental management systems. JEREMIE is a specific program for micro-, small- and medium sized enterprises to promote financial arrangements which give a better access to have financial resources. The aim

of the program is helping to eliminate limited access to the credit, equity and guarantee resources.

The European Union's main support instruments are the Structural and Cohesion Funds which allocate the resources for the national strategy for the period 2007-2013. Between 2007 and 2010 it was called "Új Magyarország Fejlesztési Terv" and until 2011 it was "Új Széchenyi Terv". In the examined period our country is eligible for almost 22.4 billion euros, nearly 6,000 billion forints. The available resources are distributed between 8 sectorial and 7 regional operational programs.

Access to financing resources for SMEs is primarily connected to the Economic Development Operational Program where approximately 700 billion forints is provided. These applications are organized around 4 priorities:

1. R&D and innovation for competitiveness
2. Complex development of businesses, especially SMEs
3. Strengthening modern business environment
4. Measure of financial instruments (JEREMIE program)

Besides the tenders of the Economic Development Operational Program there are many regional or other operational programs which have tenders targeted at businesses and one of the most popular is the site development application.

Since 2011 EU co-financed project tenders are available for start-up companies combined with a favourable credit access. It was the first time in 2011 that start-up companies were eligible for funding in the scheme of Micro-enterprise development. From 2012 the tender was transformed in order to be available for more enterprises that have greater economic importance but still keep micro-sized status.

Small and larger sized companies have far more opportunities than micro-sized since they do not have to pay attention to locational restrictions; furthermore they have a greater choice of tenders available. The opportunities for acquiring instruments, tools and equipment are mainly available that may also be used for real estate and infrastructural improvements. Companies with over 10 employees can implement an investment anywhere no matter of the location size. In contrast micro-enterprises are restricted to a limited area with a minimum population of 5,000 capita as defined in the settlement list. According to Magyar Közlöny of 12th April 2012 a draft was proposed to the European Commission to abolish the restriction of the settlements.

The aim of the above measures is to decentralize enterprises and support the operation of small municipalities' strengthening their survival chances compared to cities.

These tenders were available with strict conditions however in the last few years efforts have been taken to facilitate tendering methods regarding administration as well as procedure.

New constructions have been prepared for businesses not only in the field of investments but also for funding operations. Supporting job creation in SMEs is one of these tenders that can be used anywhere regardless of region while wages and social security contributions of employees are funded.



## Leasing

This financial instrument can be also used by the start-ups, although similarly to credit rating system the company has to meet the credit assessment criteria.

There are some differences between using credit and the use of leasing. However there are overlaps such as application and judging process.

The types of leasing are the following:

- financial leasing
  - o closed-end financial leasing
  - o open-ended financial leasing
- operating leasing

Hungarian SMEs use mostly the closed-end financial and operating leasing, because in these cases they do not have to allocate the total amount of the investment at the beginning, it is sufficient to provide it by the end of the period.

The closed-end financial leasing is more popular, because the ownership will be passed to the buyer in any case. In contrast, in case of an operating leasing it is optional to claim the ownership of equipment or it is possible just to use it as a long-term lease.

## Summary

In recent times developing domestic SME sector has a great emphasis, therefore there are more and more credit opportunities available for them as well as support possibilities due to EU accession. A significant proportion of businesses take advantage of these possibilities and as a result their operational problems can be resolved. In the first 3-year period outsourcing of loans were 100% said György Vadász the president of the Magyar Iparosövetség in an interview given by OKISZ. However we can say that only 1/3 of the businesses used these sources.

The number of small-, medium and large companies tendering is increasing. However companies tend to require and obtain these supports who can afford to implement the investments from their budget anyway. These companies have more courage to start the application and investment processes the rather than small enterprises who are struggling and cannot afford purchasing and renovations essential and indispensable for their survival.

There are some new financial assets owing to the growing number of leasing options. Many companies use this opportunities to overcome the financial difficulties by deferring the allocation of the total investment cost.

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