

# Spanish SMEs' financial restrictions: The importance of bank credit

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**The ECB's Survey on access to finance of SMEs in the euro area clearly shows the restrictions companies are facing and that tensions have intensified in 2012. The predominance of SMEs in Spain makes borrowing even more vulnerable to stricter conditions.**

*According to the ECB survey on SMEs, access to finance has been an ever-increasing key challenge for European SMEs during the crisis, both in terms of quantity and conditions of available bank credit. European SMEs in general perceive that: i) banks are less willing to lend, ii) available credit terms and conditions have deteriorated; and, iii) the outlook regarding future availability of bank credit is worsening. In addition, the closure of wholesale markets to Spanish banks, their increased default rates, and financial institutions' risk aversion is exacerbating negative conditions, with low expectations on the part of Spanish SMEs that the situation will improve over the coming months.*

Since mid-2009 bank credit to the private sector in Spain has contracted by 9.2%, a drop of around 172 billion euros (equivalent to 17% of GDP). This decrease in the availability of bank credit is due to both demand and supply side factors. On the demand side, in a complicated macroeconomic context characterised by falling or even negative GDP growth rates, it is only to be expected that demand for finance will be affected, given the difficulty of finding profitable investment projects. On the supply side, it is also understandable that the difficulties the banking industry is currently facing, such as escalating default rates and an outstanding stock of troubled assets, will heighten risk aversion, driving up the risk premium banks demand from

borrowers, thus tightening the financial constraints faced by businesses and households. What is more, the sovereign-debt crisis is compounding the difficulties Spanish banks face in obtaining finance from wholesale markets, which is having a huge impact on credit growth.

The European Central Bank's (ECB) regular surveys show that the banks themselves acknowledge that the criteria applied for new loan approvals have become stricter in recent years. Businesses share this view, as in the ECB's six-monthly survey they report that the conditions under which bank finance is available have become stricter during the crisis.

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Against this backdrop, this article aims to analyse the conditions under which Spanish SMEs are able to access finance, in comparison with those of the rest of the euro area, based on the wealth of information provided by the ECB's *Survey on the access to finance of SMEs in the euro area*. Since the ECB began publishing this information in 2009, there have been seven rounds of the survey, the most recent referring to the period from April to September 2012. Although the survey includes information on both SMEs and large firms, the analysis here will focus on SMEs in view of their greater importance in Spain. Nevertheless, information on large firms will also be offered, as well as for businesses of various sizes within the category of SMEs (micro, small and medium-sized enterprises).

## The importance of SMEs in the Spanish economy

One of the distinguishing features of the Spanish economy is the small average size of its firms. As shown in Table 1, which reproduces Eurostat data for 2010, in Spain 99.9% of businesses have fewer than 250 workers<sup>2</sup>. Although similar to Italy, this is a much larger share than in Germany or France. However, more significant than the number of companies, is the percentage of total employment SMEs account for. And in this case, Spain is also above the euro area average. Thus, whereas in the euro area (referring to the 11 founding member states) SMEs provide jobs for 63.6% of the economy's workers, in Spain the percentage is 74.5%, a long way from the level of approximately

Table 1

### Distribution of firms and employees by size, 2010 (percentage)

<b>a) Number of firms</b>					
Firm Size	Euro area <sup>1</sup>	Germany	Spain	France	Italy
From 0 to 9 employees	92.0	82.0	93.3	94.0	93.6
From 10 to 49 employees	6.7	14.8	5.8	4.9	5.6
From 50 to 249 employees	1.1	2.7	0.8	0.8	0.6
More than 250 employees	0.2	0.5	0.1	0.2	0.1
<b>b) Number of employees</b>					
Firm Size	Euro area <sup>1</sup>	Germany	Spain	France	Italy <sup>2</sup>
From 0 to 9 employees	27.8	17.9	37.5	27.6	42.1
From 10 to 49 employees	17.0	22.3	21.8	18.7	22.6
From 50 to 249 employees	18.8	21.1	15.2	15.4	14.0
More than 250 employees	36.4	38.7	25.5	38.2	21.3

<sup>1</sup> Euro area is formed by the 11 founding countries (Germany, Austria, Belgium, Spain, Finland, France, Ireland, Italy, Greece, Netherlands and Portugal).

<sup>2</sup> 2009.

Sources: Eurostat (2012) and own elaboration.

60% in Germany and France. Although this is not shown in the table, of all the euro area countries, only Italy exceeds Spain in terms of the percentage of employment generated by SMEs.

It should be noted that as a group, SMEs comprise companies of very different sizes. If we distinguish between micro, small and medium-sized enterprises, the key feature in Spain is the strong presence of businesses with less than 10 employees (in many cases, these are companies with just one self-employed worker), as they represent 37.5% of total employment, a value above the European average (27.8%) and only exceeded in Italy (42.1%). This is also quite different from the situation in Germany (17.9%) and, to a lesser extent, from that in France (27.6%). In Spain too there are also more small enterprises (with between 10 and 49 employees), but the difference with other countries is much less marked.

In the euro area as a whole, medium and large firms (i.e. all those with 50 employees or more) together account for 55.2% of jobs, whereas in Spain this percentage is 14.5 points lower.

In this context of a predominance of small businesses in Spain, bank credit takes on much more importance as one of the main sources of finance (together with trade credit and cash flow funding). This makes Spain's borrowing more vulnerable to stricter conditions of access to bank finance, both in terms of quantity and cost.

### **Pressing problems of SMEs: The importance of access to finance**

Since 2009, which is the first year for which ECB survey information is available, European companies have reported that difficulties accessing finance are their second biggest concern, following only their difficulty finding customers. As Exhibit 1 shows, after a slight improvement in 2010, the sovereign debt crisis which broke out in April 2010

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with Greece's request for a bail-out, has led to the economic crisis and closure of the wholesale financing markets (both the debt and inter-bank markets), and has further tightened the restrictions on businesses' access to finance. Thus, the most recent survey reports that 18% of European SMEs said that access to finance was their most pressing problem, an increase of one point in the percentage from the preceding survey. In the case of micro-enterprises the percentage rises to 20%, whereas in medium-sized enterprises it is 14%.

In this context, the difficulty of accessing finance is more serious in Spain, as 27% of the country's SMEs say that it is the most serious problem they currently face, many more than do so in Germany (10%) or France (13%). Of the SMEs in the eleven countries for which the ECB provides information, only in Greece (31%) did more SMEs say they faced difficulties than did those in Spain. Moreover, the financing problem is common to all Spanish companies, as alongside 27% of SMEs reporting access to finance as their main pressure, among large firms the figure is 26%. The only positive point to emerge is that in the latest round of the survey the percentage of Spanish SMEs that mention financing as a problem has dropped from 29% to 27%.

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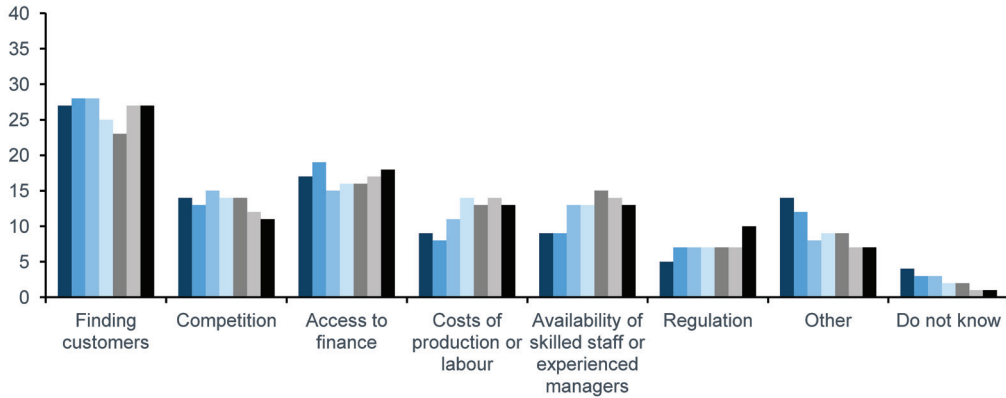
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Exhibit 1

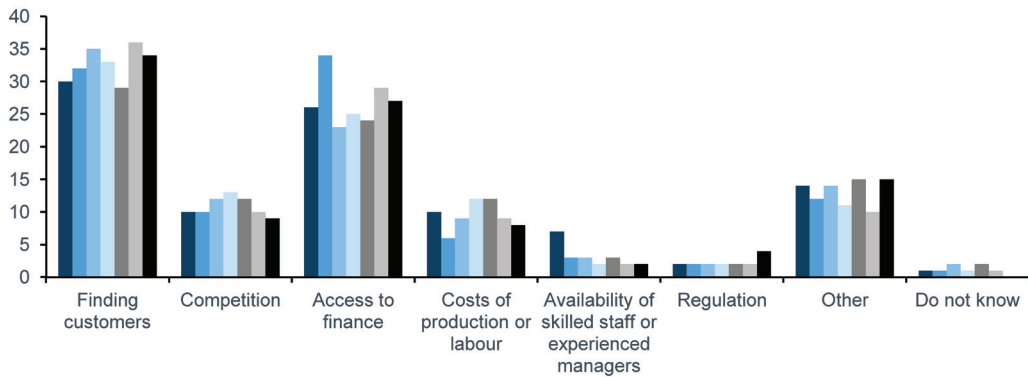
# The most pressing problem faced by SME's

(percentage of respondents)

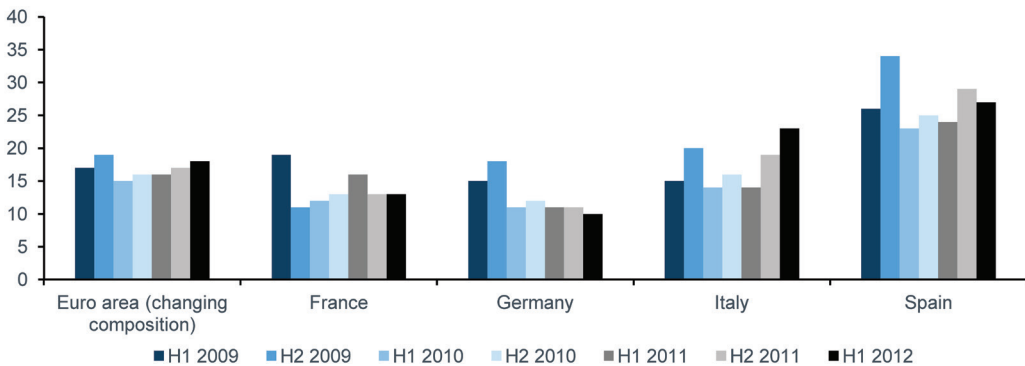
a) Euro Area



b) Spain



c) Pressing problem: Access to finance



Sources: European Central Bank, Survey on the access to finance of SME's (November 2012).

## The availability of bank credit

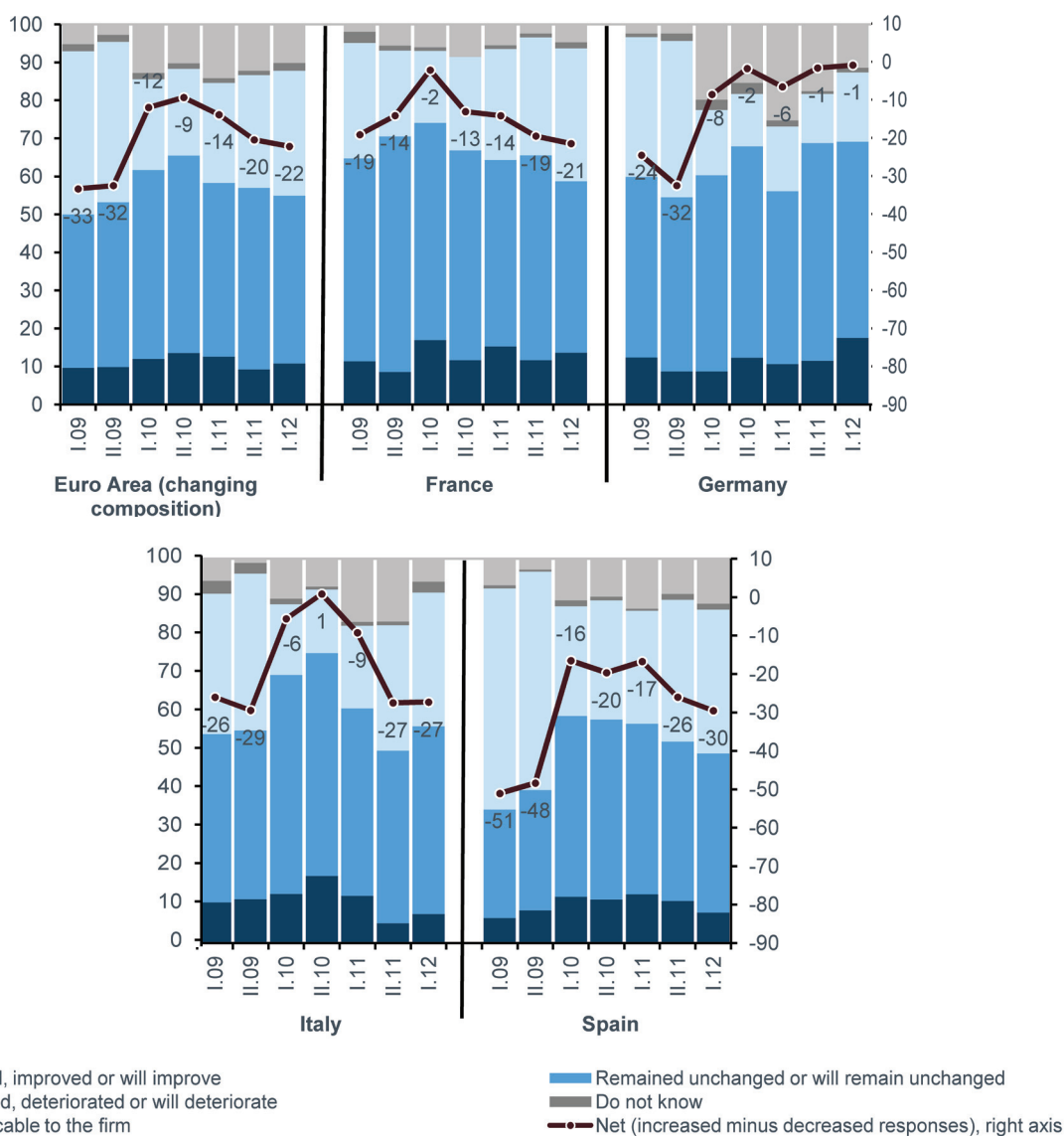
One of the characteristics of the current crisis is the credit crunch or credit squeeze from which all European countries are suffering to some extent.

This is supported by the answers given to the ECB survey's question: Would you say that the availability of bank credit for your company has improved, remained unchanged or worsened over the last six months? In particular, as the information

Exhibit 2

### Availability of bank loans over the preceding six months

(percentage of respondents)



Sources: European Central Bank, Survey on the access to finance of SME's (November 2012).

in Exhibit 2 shows, since the second half of 2010, the percentage of European SMEs reporting a deterioration in the availability of bank credit has been rising, reaching 32.8% in the most recent survey in 2012. Also, since mid-2010, the difference between the percentage of positive (improvement) and negative replies (deterioration) has increased, from -9% in the survey in the second quarter of 2010 to -22% in the most recent survey.

Disaggregated by countries, the information shows that, of the four major countries in the Exhibit, it is in Spain that SMEs are suffering most severely from the restriction in bank credit, with a percentage of negative responses (those predicting credit will become harder to obtain) of 37.5% in the most recent survey, well above the figure for Germany (18.2%), although closer to that of France (35%) or Italy (34.8%). Nevertheless, the perception of the deterioration of the availability of credit is worse still in Ireland (41%), Greece (54%), the Netherlands (46%), and Portugal (48%). In net terms (percentage of companies reporting an improvement less the number reporting a worsening), the ranking is similar, with Belgium, France, Austria and Finland above the euro-area average.

The ECB's information reveals that it is the smallest SMEs (micro-enterprises, with less than 10 employees) that are hardest hit by the credit squeeze, as across the euro area on average 40% respond that the availability of finance has worsened in 2012, 14 percentage points (pp) more than in the case of enterprises with workforces of between 50 and 249. Similarly, while just 7% of micro-enterprises reported an improvement, the percentage doubles in the case of medium-sized enterprises. In Spain, on the other hand, the size-related differences between SMEs are much smaller: just a 4 pp difference between the number of medium-sized and micro-enterprises reporting a worsening in the availability of credit.

Another salient feature in Spain is that the perception of a worsening in the availability of

finance is also shared by most large firms. Thus, in the most recent survey, there was a difference of just one percentage point between large firms and SMEs reporting a deterioration in access to credit (36% vs. 37%). Similarly, the difference is just two percentage points in the case of companies that consider there to have been an improvement (10% vs. 8%).

### **Banks' willingness to give credit: Businesses' perceptions**

As well as the availability of bank finance, another aspect that it is worth examining to evaluate the restrictions companies face is their perception of banks' willingness to provide credit. The availability of credit depends on a number of factors, some of which are related to the economy in general, the situation of the specific company, and the attitude of the banks. It is this latter factor that we will now look at.

As Exhibit 3 shows, the majority of European SMEs consider that banks have become less willing to give loans or overdrafts over the last six months, reaching a percentage of 36.6% in the most recent survey conducted in 2012. This percentage has been increasing steadily since the survey conducted in the first half of 2010 and is currently at its peak since the first survey in 2009. At present, only 9.8% of SMEs are of the view that banks have become more willing to lend. Subtracting the negative responses (those reporting a worsening) from the positive ones (an improvement) yields a net balance of 27%, the highest since 2009.

There are considerable differences between the figures for individual countries. Among the large countries shown on Exhibit 3, based on the latest data available, only in Germany do SMEs that consider banks to have become more willing to grant credit outnumber those holding the opposite view, the difference being 1 pp. In France, the difference is -25 pp and in Italy it is -42 pp. In relation to these values, Spanish SMEs' perceptions are worse, as against the 56.9% that consider banks to be less willing to grant finance,



only 6.8% think that the situation has improved, yielding a net balance of -50 pp.

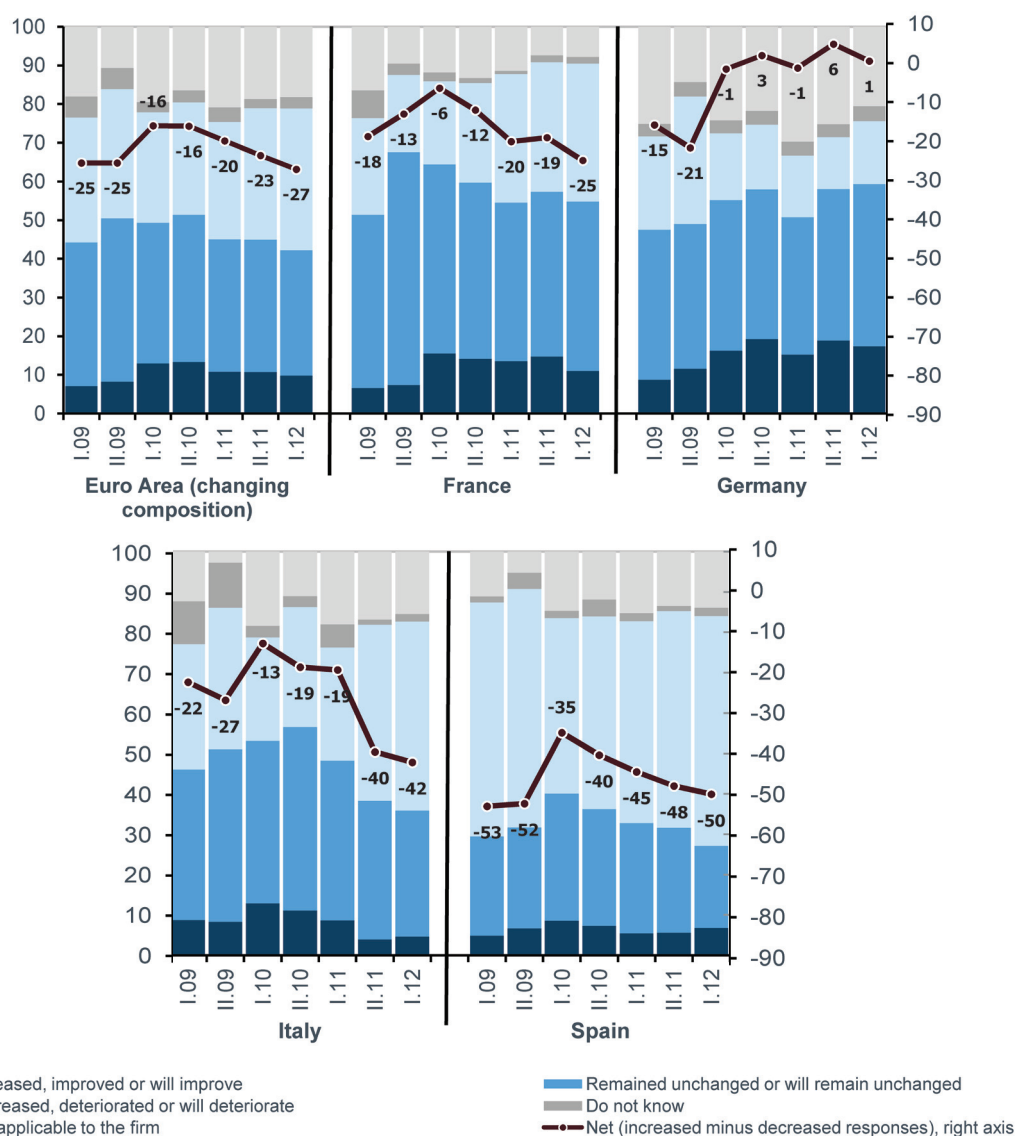
Compared to the rest of the countries of the euro area, it is Spanish SMEs (56.7%) that perceive the greatest reluctance on the part of banks to grant

credit, their perception being even more negative than that of their counterparts in Greece (49%), Portugal (45%), and Ireland (38%). Moreover, it is again this sense of a worsening that is widespread among all companies, regardless of their size, such that the percentage is the same among Spanish

Exhibit 3

### Willingness of banks to provide a loan to SME's over the preceding six months

(percentage of respondents)



Sources: European Central Bank, Survey on the access to finance of SME's (November 2012).

SMEs and large firms. Among SMEs, micro-enterprises have the strongest sense of a deterioration (59%).

### The terms and conditions on which banks grant finance

One of the questions on the ECB's questionnaire which provides the most information about the restrictions businesses face in obtaining bank finance is that describing up to six different aspects of the terms and conditions of financing: interest rates, other (non-interest) costs, the size of the loan or credit line, loan maturity, collateral requirements, and other aspects. It is important to note that in this case, the question refers to bank finance as a whole, including both loans and credit lines.

Exhibit 4 shows the four aspects of financing that we consider most important. In the case of interest rates, the situation of European SMEs improved in the second half of 2012, as the difference between the percentage of companies that considered rates to have increased and those that considered they had fallen was 27 pp, compared with 42 pp in the previous survey. Since the first survey in 2011, this net percentage of responses has fallen by half.

In the case of Spanish SMEs, the net response in 2012 was 71 pp, almost three times the average ratio in the euro area. The range of variation between countries is very wide. Thus, in Germany the majority response was a fall in interest rates (45.7%), whereas in Spain just 4.6% of SMEs reported a cut in rates. Similarly, while in Germany only 15.1% of SMEs reported that the interest rate had risen, in Spain the percentage was 75.8%.

Taking the net response (increase-decrease in rates), in four of the countries for which the ECB publishes data (Belgium, Germany, France and Austria), a drop in interest rates predominates, while in the remaining seven countries, an increase predominates, with the worst case being in Greece (72%), although Spain (71%) and Italy (70%) are

close behind. Spain therefore stands out in the European context on account of the increase in interest rates SMEs have experienced in 2012.

In the case of other costs of finance (i.e. costs other than interest charges, such as bank charges, fees and commissions), the percentage of European companies reporting an increase has grown steadily over the seven editions of the survey,

*Spain stands out in the European context on account of the increase in interest rates SMEs have experienced in 2012.*

reaching a maximum of 54.8% in the last survey. In net terms (increase-decrease), the value has also risen continuously, currently reaching a level of approximately 52%.

The most recent survey shows that in Spain 80% of SMEs say there has been an increase in their cost of finance other than in terms of interest rates that is 25 pp above the European average. In terms of net responses the value is also much higher in Spain (78%) as only 1.8% of SMEs replied that they had seen these costs of financing decrease. Of the SMEs in the eleven euro area countries covered by the ECB survey, those in Spain have seen their non-interest borrowing costs rise most, with the increase outstripping that in Italy, Portugal and Greece. The country with the smallest share of SMEs reporting a cost increase is Germany (19.3%). It is also worth noting that in Spain, on balance, more large firms report increases (83%) than do SMEs (78%).

The third of the bank financing conditions examined is the amount available as a loan or credit line. On average, the share of companies in the euro area reporting an increase is less than that reporting a drop, with a net value of -8%, the biggest value in absolute terms since 2009. This highlights that the credit crunch is currently at its most severe.



Spanish SMEs are suffering the current limitation on credit much more than in the last ECB survey, compared with 12.1% of companies that are of the view that the amount of finance has increased, 42% hold the opposite view, the net responses (-30%) being almost four times higher than the average for European SMEs. In 2012, Spain was also where the credit squeeze reached its peak, exceeding even that in 2009. It is worth noting that in Spain the difficulties obtaining the desired amount of credit have intensified enormously in 2012 with respect to 2011. Spain's large firms also faced serious difficulties, although these were

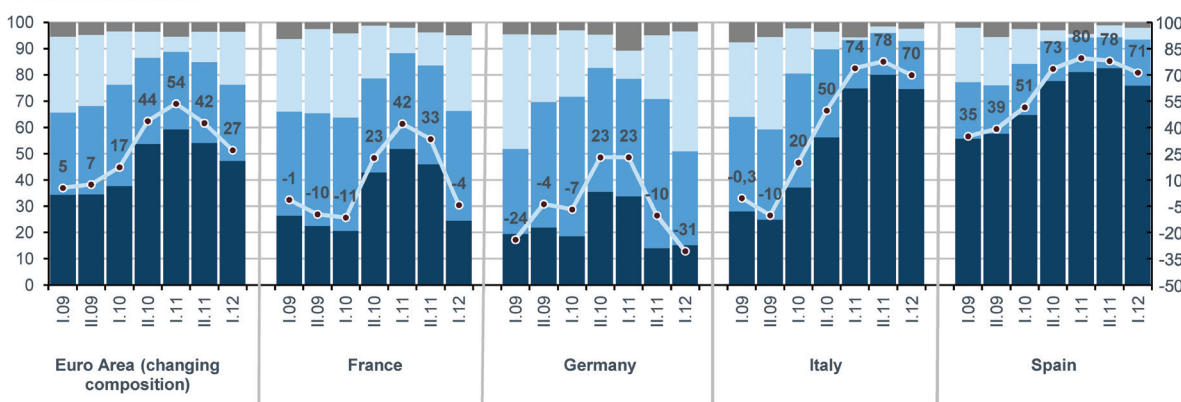
somewhat less severe than those affecting SMEs. In 2012, only Italian and Greek SMEs faced stricter limitations on the quantity of bank finance required than did their Spanish counterparts.

Finally, a fourth aspect of the financial conditions it is worth analysing is the extent of the requirement for collateral. On average, SMEs in the euro zone again came under maximum pressure in 2012, as against the 40.7% that reported that collateral requirements had increased, only 2.2% stated the opposite. In terms of net responses, in all countries the increase in collateral requirements prevailed,

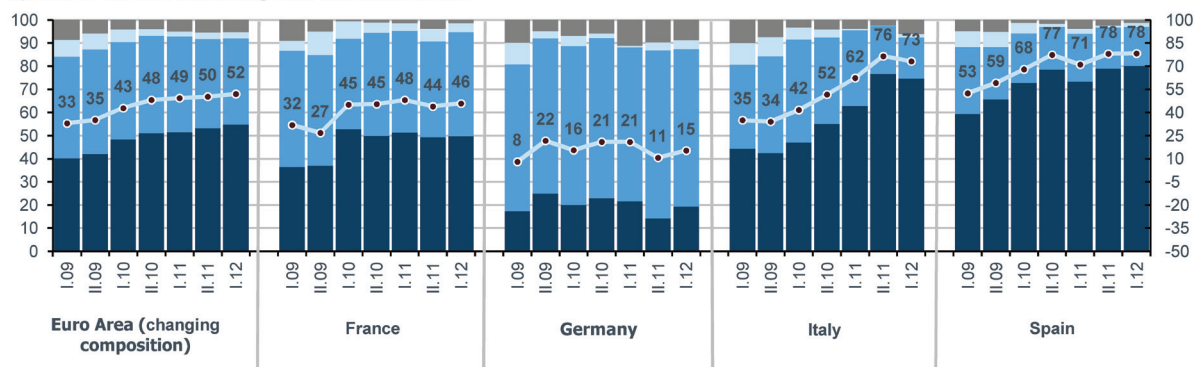
Exhibit 4

### Terms and conditions of the bank financing available to SME's over the preceding six months (percentage of respondents)

#### a) Level of interest rates



#### b) Level of the cost of financing other than interest rates

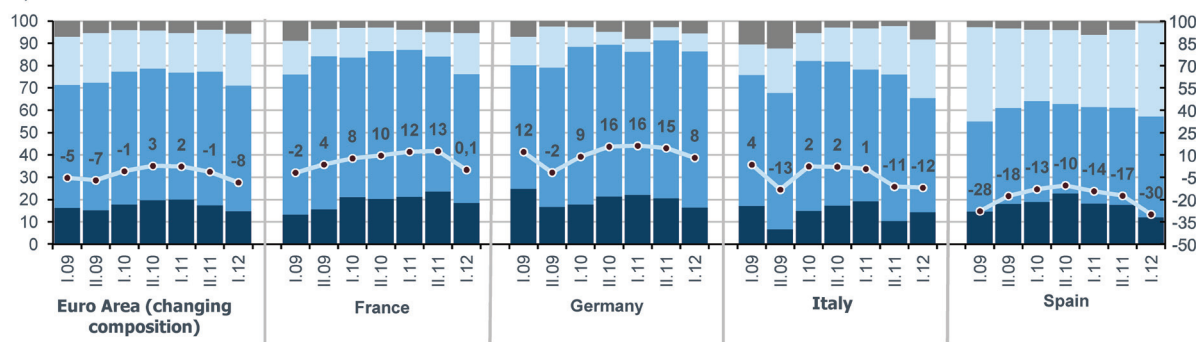


Sources: European Central Bank, Survey on the access to finance of SME's (November 2012).

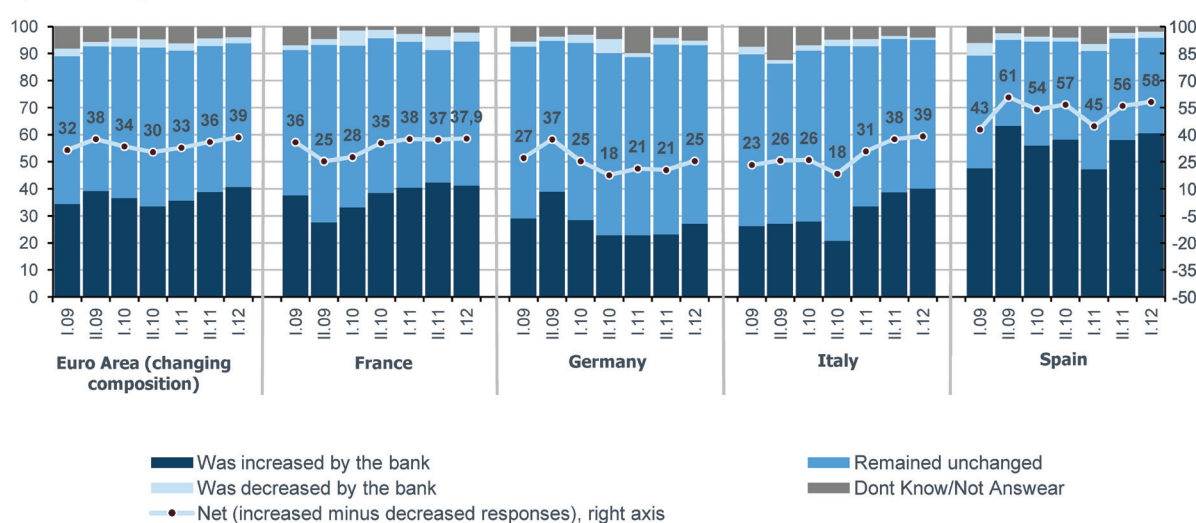
Exhibit 4 (Continued)

### Terms and conditions of the bank financing available to SME's over the preceding six months (percentage of respondents)

c) Available size of loan or credit line



d) Collateral requirements



Sources: European Central Bank, Survey on the access to finance of SME's (November 2012).

with Greece at the upper end (a balance of 68%) and the Netherlands at the bottom (23%). In this context, the net percentage in Spain is 58%, just below that in Greece. Consequently, Spanish SMEs also have more difficulty accessing bank finance in terms of the elevated collateral requirements. The situation is somewhat better in the case of large firms, with a balance 14 pp lower than that of SMEs.

### SMEs' expectations as to the future availability of bank credit

Although the ECB's survey focuses primarily on analysing recent trends in businesses' access to external finance, it includes a question that is of considerable interest when trying to glimpse the future difficulty of financial conditions. In particular, the questionnaire asks about expectations regarding

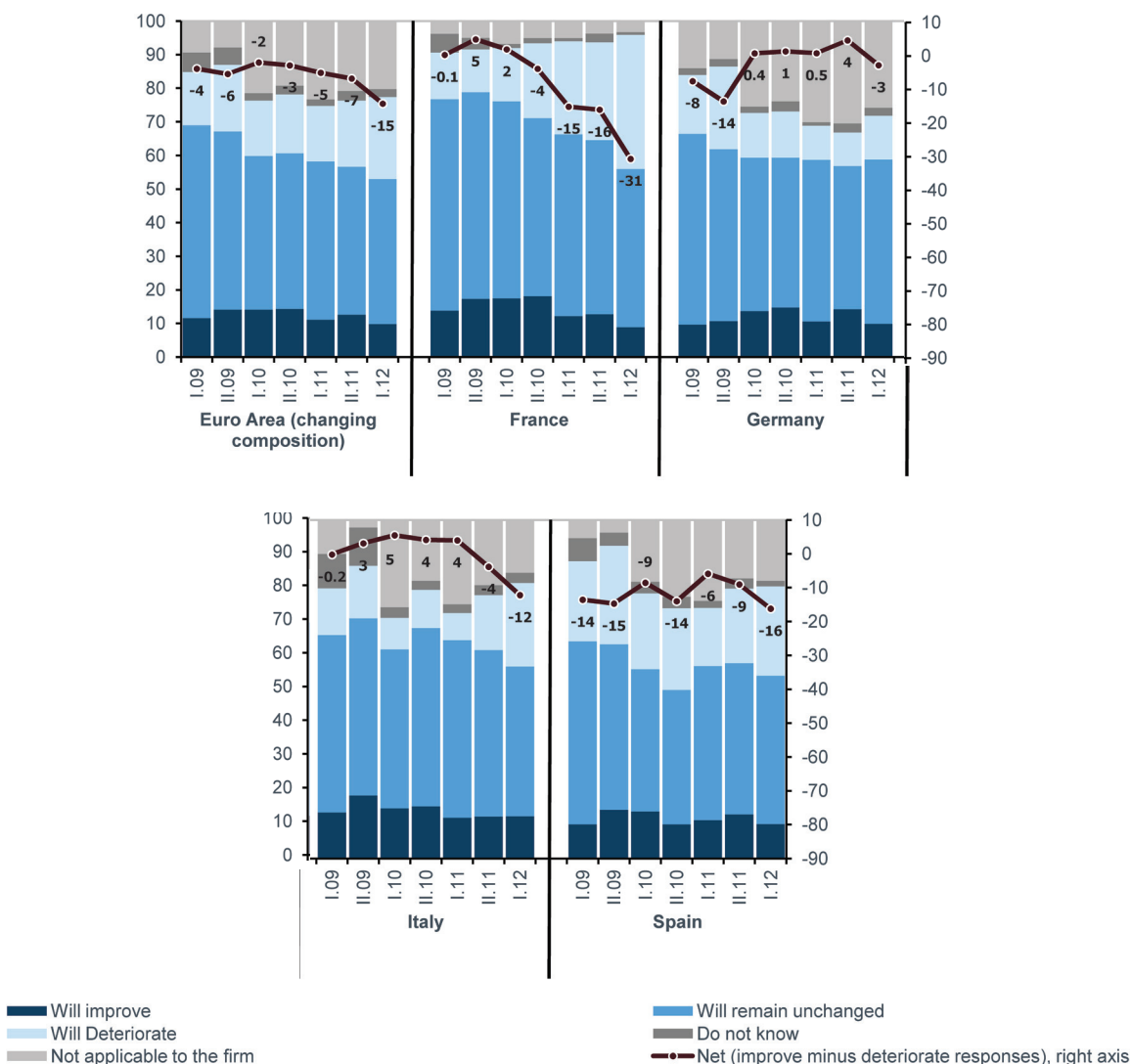
access to bank finance over the next six months relative to the prevailing situation.

As Exhibit 5 shows, in 2012 there was a serious downturn in future expectations, as while 9.8% of European SMEs considered that access to finance would improve, 24.4% believed it would get worse.

On balance (-15%) responses were twice as negative as in the previous survey, and the most negative by far since 2009. Of the four largest countries in the euro area shown on the Exhibit, SMEs in France are the most pessimistic, with 39.9% believing that access to finance is set to worsen over the next six months. By contrast, German firms

Exhibit 5

**Expectations of SME's about their availability to access to bank loans over the next six months**  
(percentage of respondents)



Sources: Central Bank, Survey on the access to finance of SME's (November 2012).

are much more optimistic, although those that believe access to finance will be more difficult in six months' time also outnumber those that do not. In the case of the other countries, Greece's SMEs, together with those of France, are those envisaging the severest worsening in conditions of access to bank loans and overdrafts.

In this context, the degree of pessimism among Spanish SMEs is close to the European average, with a balance of replies of -16% compared with -15% for the euro area. In 2012, Spain was also the country in which pessimism was strongest, as the net reply percentage reached its maximum negative value in 2009. Large firms' expectations coincide with those of SMEs, but micro-enterprises are slightly more pessimistic.

## Concluding remarks

The ECB's survey on SMEs' access to financing clearly shows the restrictions companies are facing, and that tensions have accentuated in 2012. It is precisely in the most recent of the surveys conducted (between September and October 2012) when the immediate future of access to bank credit is viewed with most pessimism— the percentage of European SMEs believing that conditions are going to deteriorate far outnumbering those that anticipate an improvement over the next six months.

In the case of Spanish SMEs, the future is viewed with even more pessimism, and this negative perception is also common among large firms.

Looking at the recent history of conditions of access to bank finance, one of the most negative issues affecting Spanish SMEs is the high cost of finance, a situation which they shared with Greek and Italian SMEs in 2012. No fewer than 78.5% of Spanish SMEs stated that interest rates had increased over the six preceding months, compared with a European average of 47.3% of SMEs. This situation is even more dramatic in the case of non-interest costs (such as bank charges), where 80%

of Spanish SMEs say that they increased in 2012, which is the highest percentage among the eleven countries analysed by the ECB.

In short, the closure of wholesale finance markets to much of the Spanish banking industry, the increased default rate banks are facing, and financial institutions' consequent risk aversion, is greatly hindering companies' access to bank credit, in terms of both the quantity of finance available, and the conditions attached to it (high interest rates, demand for more collateral, etc.). The highest level of financial restriction was reached in 2012, and SMEs do not expect the situation to improve over the coming months.

In the current context, in which it is essential to recover investment in order to return to growth and create jobs, the recent recapitalisation of part of the Spanish banking system is a necessary condition to enable bank financing to again function correctly. Nevertheless, although improved solvency is a necessary condition, it is not a sufficient one while Spain's government debt is subject to such a high risk premium that it is spreading to private debt, both inside and outside the banking system.

However, it is important to remember that a portion of the Spanish sovereign's risk premium is attributed to the problems of the euro area, whose solution will require advancement on the construction of a banking union. According to recent IMF estimates, the deleveraging of European banks will be more traumatic without progress on the banking union (with a 10% reduction in total assets, compared to less than 5% under a scenario including a banking union). Therefore, in the absence of said progress, the credit crunch companies face will be more severe.