Institutions

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To provide SMEs with an adequate credit flow and access to finance, especially during the recent economic crises, European and national legislators intervened in different ways, with direct financing measures, (public or private) credit guarantees, fostering securitisation of SMEs loans, and adjustments on capital requirements related to SMEs loans.

Direct measures

Direct measures to foster SMEs lending have been promoted by national legislators and European institutions following the conclusions of the June 2013 European Council, where public intervention was urgently recommended because of the weakness and fragmentation of the European banking sector, because of the high dependence of SMEs on bank lending, and, last but not least, because of the economic role played by SMEs.

Hence, SMEs support is at the core of the 2014-2020 Multiannual Financial Framework, the Budget of the European Union. One of the target of this long-term plan is to tackle specific market failures. To this purpose, the EIB Group (EIB and EIF) and national promotional banks will use more widely certain financial instruments (loans, guarantees, equity, as well as other risk sharing instrument) to improve SMEs access to finance. Within this framework, the EIB Group has so far supported new SMEs financing operations for a total of 28.1 billion €, as discussed by Kraemer-Eis and Revoltella (2015) in this issue. EIB Group support mainly involves intermediated debt-financing, risk-sharing instruments, as well as other capital instruments (private equity, venture capital, or growth capital). In 2015, the EIB Group, together with the European Commission, also launched the EU SME Initiative, co-funded by COSME and Horizon 2020, to encourage SMEs financing and to provide a partial risk-cover for SMEs lending to selected financial institutions. Selected financial institutions can receive an uncapped portfolio guarantee and/or a securitisation instrument in exchange for their advantageous SMEs lending, in terms of interest rates and collateral requirements. So far, the initiative has been launched in Spain and in Malta; the SMEs expected financing are, respectively, 3200 million € and 60 million €. Other specific SMEs initiative have been also undertaken at the country level: the measures in the Small Business Act package implemented by the Italian Government include, for instance, tax exemptions on R&D expenses, innovation incentives, and the extension of government guarantees on SMEs loans through the *Fondo di Garanzia per le PMI.*

European institutions also considered alternative measures to support SMEs: for instance, the Directive on Late Payments, ruling transactions with government bodies, is expected to benefit SMEs through its improved effect on cash-flows, and hence on the access to finance.

Other country level initiatives are collected and implemented under the Small Business Act for Europe. A detailed, though not exhaustive, list of these measures is available for 2014.[8]

Credit guarantees

As stressed by Kraemer-Eis et al. (2015) in the EIF European Small Business Finance Outlook, a careful analysis at government intervention suggests that, when dealing with SMEs access to finance and addressing market failures, SMEs guarantees are the most widely used policy instrument, as displayed in Figure 18 in the Number section. Through Credit Guarantee Schemes (CGS), governments offer partial protection on SMEs exposure, working, *de facto*, as a

8. Database of SBA policy measures.

substitute for the collateral requirements often imposed by banks unwilling to provide loans to SMEs. The mutual, public, and private institutions ultimately providing this form of credit protection are gathered under the European Association of Guarantee Institutions: its 41 institutions, in 20 countries, account for almost all the SMEs guarantee activity.

SME securitisation

There is a general consensus on the importance of creating and developing a SMEs dedicated securitisation market. Institutional representatives have stressed the need for developing such a market. In his speech in 2014,[9] Yves Mersch, member of the ECB Executive Board, states that a well-developed SMEs securitisation market may indeed benefit the match between capital demand and capital supply, and that all the implemented safeguard measures[10] proved to be efficient in determining a contained default rate since the onset of the financial crises.[11] To this purpose, he suggests to "distinguish securitisation instruments in several categories, and assigning preferential treatment only to instruments meeting the strictest requirements", but the most suitable criteria and the treatment still need to be formally identified.

The development of a Capital Union Market may ease fund raising, and it may also develop the SMEs securitisation market. According to Jonathan Hill, Commissioner for Financial Stability, Financial Services, and Capital Markets Unions,[12] the ECB, together with the Bank of England, is working on plan to revitalize the securitisation market, and the proposed securitisation instruments are "simple, transparent and standardised". The Action Plan on Building a Capital Market Union, released in September 2015, suggests a series of intervention to support SMEs seeking access to finance. The main pillars of this intervention mainly target the reduction of information barriers that impede SMEs from identifying investment opportunities. These two messages are just an example of the intensity of this debate.

9. Overcoming the current challenges faced by small firms, Deutsche Boerse – Clearstream 'Exchange of Ideas' event, London, 7 April 2014.
10. Such as in increased transparency, following the introduction of the loan-by-loan reporting requirement.
11. The average default rate from 2007/2008 ranged between 0.6-1.5%, against the 9.3-18.4% US average.
12. http://europa.eu/rapid/press-release_SPEECH-15-5290_en.htm

In an attempt to revitalize the Asset-Backed-Securities (ABS) market, the ECB imposed loan-by-loan disclosure requirements also on SMEs ABS. By providing more detailed and accessible information to market participants, the ECB aims at improving ABS transparency and to facilitate the risk assessment of these instruments, used as a collateral in the Eurosystem credit operations. This new, and more prudent, information requirements were introduced at the beginning of 2013 to reduce asymmetric information and to increase transparency. Still, as stressed by both the ECB and the Bank of England, SMEs ABS account only for 8% of the overall outstanding ABS amount. These institutions jointly worked in this direction: the joint ECB and Bank of England document recalls the Risk Retention Rule in 2011, measures to increase the transparency of the securitisation structures, and the EU Credit Rating Agency legislation in 2013. The loan-by-loan principle has also been implemented at the country level, with the introduction of loan-level data in all ABS classes.

Also the EIB Group introduced a specific scheme to revitalize the SMEs ABS market: ABS Credit Enhancement Initiative aims at providing guarantees on SMEs securitisation, by offering credit enhancement for senior and mezzanine tranches of securities backed by SMEs loans. Still, much has still to be done, and the main issues relate to the regulatory treatment, to the reliance on credit rating agencies, on the transparency of information.

The development of a sound securitisation market reflects the need to diversify available financial instruments, such as markets for external equity, and venture capital. In addition to these solutions, member states proposed alternative measures to facilitate SMEs access to the securitization market and to encourage the issuance of securities by SMEs:

- The Initial bonds offering market in France, where listed and unlisted SMEs can issue bonds to retail investors;
- The Bond – M (mid-cap bond segment) in Germany, where companies can get finance directly from institutional investors;
- In Italy, specific SMEs-oriented measures, providing a more favorable stock market listing and an enhanced capitalization and including the development of the Minibond Market, where unlisted, mid-sized SMEs and small mid-caps can issue short-medium term ordinary and convertible bonds, are part of the banking industry reform (that is, for instance, transforming large cooperative banks into joint stock companies and lay-

ing out NPLs management rules, and introducing new tax provisions on loan losses);

- The Bond Market for Small Businesses in Spain, to set a corporate bond exchange for small and mid-sized companies;
- The Funding for Lending Scheme in the UK, to the reduce the cost of bank funding in exchange for lending commitments.

Still, these initiatives have been only recently implemented, and the volumes achieved so far are not very significant.

Capital requirements

Capital requirements for banks have been discussed in the first issue of European Economy, that focused on capital regulation from the point of view of the financial stability vs. economic recovery trade-off.

The Recital 44 of the CRR Directive introduces a SMEs supporting factor to reduce the total risk weighted exposure of SMEs lending. This capital discount, implemented in January 2014 and subject to a potential revision in 2016, aims at reducing capital requirements for banks active in SMEs lending, that should in turn use the consequent capital relief to provide credit flows to this specific counterpart category. More specifically, this factor applies a 0.7619 discount factor to the exposure to those SMEs, classified either as retail or corporate, that satisfy the 2003 European Commission definition,[13] and with a total exposure to the credit institution lower than 1.5 million €.

The EBA Discussion Paper, published in June 2015, launches a call for evidence to assess the effectiveness of the supporting factor. The reported preliminary evidence shows that EBA's reporting banks increased their CET1 ratios by 0.19% on average in 2014Q4. In terms of capital saving, this increase generated a 10.5 billion € capital relief for EBA's reporting banks, although the distribution across countries displayed strong heterogeneity, because of the different exposure to SMEs.[14]

The Basel Committee on Banking Supervision has recently issues a consultative document on a revisions to the standardised approach for credit risk. In

13. Turnover up to 50 million €.
14. More than 50% of this freed up in capital can be traced back to Italy, France, and Spain.

particular the Committee is investigating the suitability of substituting external ratings with a some measures of risk drivers that should be simple to use, intuitive, readily available and capable of explaining risk consistently across jurisdictions. It is indeed a challenging revision that will significantly affect the attitude towards lending to SMEs, as forcefully indicated in the comments received by the consultation.[15]

As stressed in the Study for the ECON Committee by Ayadi et al. (2015), this discount factor may be complemented by other efforts. After the recent financial crises in fact, national governments often had to provide financial support and State aid to banks that suffered significant losses because of their extremely risk-taking portfolio composition. The principles and guidelines for State aid intervention in the banking sector are contained in the 2013 Banking Communication of the European Commission, that replaces the temporary Banking Package released in 2008. This institutional package defines the conditions for granting State aid to the banking sector and identifies four alternative intervention measures: bank recapitalisation, asset relief, guarantees on bank liabilities, and liquidity measures.[16] On top of targeting financial stability, this memorandum explicitly addresses the issue of SMEs lending, so as to avoid any potential disruption in the funding flow. In addition to the imposed below-market remuneration, the ailed bank must also comply with restructuring plans, which generally range from selling certain activities to merging with more sound credit institutions. Still, in certain cases, the ailed bank must commit, or promise to commit, to satisfy certain lending SMEs targets. As discussed in Ayadi (2015) and in Ayadi et al. (2015), being active in Small Business Lending positively contributed to the State aid granting process. In 2009, for instance, BPCE, resulting from the imposed merger between the groups Caisse d'Épargne and Banque Populaire, had to comply with specific SMEs, individuals, and local authorities lending targets: its lending volumes had to increase by 3 to 4% per year. Until 2012, the group fulfilled the lending requirements, but failed to do so in 2012, in line with market trends. Ayadi (2015) and Ayadi et al. (2015) discusses the impact on SMEs lending, as well as the feasibility, of imposing a conditionality clause in granting State aids.

15. Annex 1 of the Consultative Document includes the proposals for exposure class: paragraph 22, page 33, reports the proposed weights for senior corporate exposure, and paragraph 33, page 35, contains those for retail lending.
16. See Ayadi (2015) in this journal for a complete overview of the institutional background.