SMEs' Access to Bank Loans in Slovakia During the Coronavirus Crisis

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Abstract: The crisis caused by the coronavirus COVID-19 pandemic has hit the corporate sector from an economic point of view particularly hard. The forced closure of operations led to a dramatic drop in sales and disruption of normal cash flow. In this regard, SMEs have been affected the most. Because of their economic and social importance for the economies, it is necessary to improve the business environment for their development, esp. to improve their access to sources of finance. As we present, SMEs in Slovakia are primarily financed from their own sources, respectively from loans and leasing. Compared to large businesses, they are supposed to be more vulnerable, riskier, and so it is more difficult to obtain external sources of finance for them. The aim of the article is to evaluate the access of SMEs to bank loans in the Slovak Republic at the times of coronavirus crisis. For this purpose we processed the statistical data on corporate loans provided by the National Bank of Slovakia. We found that the dynamics of credit growth maintained stable concerning the corporate sector as a whole in 2020, but the availability of financing was limited for riskier groups of companies.

Key Words: Small and medium – sized enterprises, loans, banks, coronavirus crisis

1. INTRODUCTION

Small and medium-sized enterprises (SMEs)1 are traditionally referred to as the pillar or backbone of the economy. They form a key segment of the business sector of almost every economically developed country.

They bring innovative products to the market, represent an important source of economic growth and they are of great importance in job creation.

According to the Report on the State of SMEs prepared by the Slovak Business Agency (2020a), SMEs accounted for 99.9% of the total number of business entities in the Slovak economy in 2019. SMEs accounted for 73.8% of employment in the corporate economy and contributed by more than half (54.9%) to total value added.

One of the basic prerequisites for the development of the SME sector is access to finance. Small and medium-sized enterprises, given their distinctive features, have different financial needs compared to large enterprises.

These businesses require different spectrum of financial tools in various stages of life – cycle. They often depend on the informal sources of finance at the initial stages of their life. External sources are getting to be important with the beginning of the expansion stage and access to them can influence the development trajectory significantly.

As OECD (2016) states, bank lending is the most common source of external finance for many SMEs and entrepreneurs, which are often heavily addicted to straight debt to fulfil their start-up, cash flow and investment needs. SMEs, however, typically find themselves at a disadvantage with respect to large firms in accessing debt finance. It is connected with their smaller size, lower degree of diversification, more limited market and higher riskiness. As Covaci (2008) presents, SMEs are in generally riskier than large companies, because they present a high sensitivity to economic shocks while disposing of an inferior capacity to absorb variations. This makes it more difficult for SMEs to borrow than for larger companies, and may make it effectively impossible for many SMEs to borrow money at all. From this reason, SMEs rely on internal or "personal" funds, increasingly suffer from information asymmetry problems and have a small internal rate of return.

[1] The size categorization of enterprises used in this article is in accordance with the recommendation of the European Commission no. 2003/361 / EC valid from 1.1.2005. The SME category consists of enterprises with less than 250 employees and the large enterprise category includes enterprises with 250 or more employees. Within the SME category, a distinction between micro-enterprises (0-9 employees), small enterprises (10-49 employees) and medium-sized enterprises (50-249 employees) is made. In cases where the category of micro-enterprises is not distinguished separately, all enterprises with the number of employees 0-49 are included among small enterprises. The criterion of the number of employees is not the only one that characterizes SMEs. The criteria of turnover, asset value and ownership structure are also taken into account. However, due to the unavailability of current data in the classification according to all SME criteria, we take the number of employees as a relevant criterion.

In Slovakia, SMEs are primarily financed from their own sources, respectively from loans and leasing. These are the sources that they know and therefore they most often use them (Belanová, 2015).

Table 1 presents that SMEs are not very indebted at the beginning of their establishment. They prefer the use of own sources of financing, the share of which in total assets was about 81% to 85% in the first year. As for loan financing, we see that only about 3% of companies use this form. A short credit history of the company, as well as insufficient security of new business entities can be marked as the reasons.

Table 1: Indebtedness indicators of newly created SMEs (%)

	2017	2018	2019
total indebtedness	17,96%	15,92%	18,85%
Own sources	82,04%	84,08%	81,15%
Bank loan	3,16%	3,07%	3,22%

Source: Own processing according to the data of the Statistical Office of the Slovak Republic

Belas, Bartosa, Habanik, and Novak (2014) state that conditions for SMEs have worsened because of the global financial crisis.

However, the current coronavirus crisis has even a greater impact.

The aim of the article is to evaluate the access to bank loans of SMEs in the Slovak Republic at the times of the coronavirus crisis. The first case of COVID–19 was recorded in Slovakia at the beginning of March 2020.

The pandemic is, among others, associated with a trend of growing corporate indebtedness. The growing debt in the corporate sector mainly compensates for significant shortfalls in revenues of the companies.

The negative consequences of the pandemic are reflected by entrepreneurs on the supply, as well as on demand side. Many companies are not using their capacity to the full for several reasons:

- the measures taken to control the disease limit or make it completely impossible for entrepreneurs to carry out their business activities;

- staff must take care of children as a result of school closures;

- the staff is not in good health;

- supply chains are interrupted or limited, leading to a lack of inputs necessary for business.

Potential problems for SMEs can be caused by a relatively low level of digitization. In this regard, SMEs are not able to make sufficient use of their work capacity. SMEs will be more burdened by the cost of underutilized labor and technology equipment in case of decline in production than large companies.

According to the Analysis by Slovak Business Agency (SBA, 2020b), a total of 53,243 SMEs (i.e. 8.9% of active SMEs) operated in the sectors affected by quarantine measures the most, and these were forced to close down completely in the first phase of the measures. Within this group, micro-enterprises employing less than 10 employees were affected the most. They account for almost 96.2% of affected SMEs. In terms of legal form, sole proprietors, who make up almost two thirds (59.7%) of the total number of vulnerable SMEs, are the most vulnerable group. Quarantine measures which required the closure of establishments, were operated by small and medium-sized enterprises in the areas of retail trade, accommodation and food service activities, transport and business and other services.

The impact of the pandemic on the Slovak economy may be in combination with a high degree of openness of the economy and, as a rule, with a limited number of SME suppliers, much more pronounced than in less open countries.

As the supply of manufactured products or services has decreased, so has the demand for goods and services. It causes a significant reduction in corporate incomes. In particular, consumers' fear and uncertainty raise consumers' concerns about loss of income, and, as a result, consumers are radically reducing consumption costs. As we present in our previous study, companies faced a significant drop in sales during the first, spring wave of the pandemic (Belanová, 2020). During the summer months, the situation began to improve gradually. This improvement was extremely fragile and accompanied by significant risks. In autumn 2020, a second, even stronger wave of the pandemic broke out and the result was the introduction of even more significant restrictive measures at the end of 2020. While in 2020 the crisis mainly affected companies that were in a worse financial situation even before the crisis, in 2021 the crisis may get even healthier businesses into existential problems. Vaccination of the population could play an important role, but this will take some time.

Many small and medium-sized enterprises are currently struggling with a lack of liquidity, which results in a subsequent insolvency.

As the impact of the prevailing pandemic is also felt in the financial sector, many commercial banks are much more cautious in lending - some of them have responded by tightening of credit standards, making it much more difficult for businesses to access credit financing.

2. MATERIAL AND METHOD

For evaluation of access of SMEs to bank loans during the coronavirus crisis we processed the statistical data on corporate loans provided by the National Bank of Slovakia. In accordance with the statistics of the National Bank of Slovakia, we present the volume of loans provided to enterprises (non - financial institutions) in total and broken down into short - term (up to 1 year), long - term (1 - 5 years), long - term (over 5 years). We surveyed the annual growth in bank loans to non – financial businesses. Moreover, we surveyed the development of the loans by type. We compared the development in the Slovak Republic with the development of the euro area. We state the development of credit standards and we compare it with other euro area countries. One of the measures provided by the Government of the SR was possibility of deferral of repayment. In this regard, we survey, which kind of businesses made the greatest use of this measure and in which sectors. Within our research (*desk research*), available secondary sources of data and information on SME finance were processed, for example, reviews, articles, publications and websites (especially those of National Bank of Slovakia, Statistical Office of the Slovak Republic, Ministry of Economy of the Slovak Republic, Ministry of Finance of the Slovak Republic, Slovak Business Agency). Because it is a world wide problem, we also surveyed international materials dealing with this issue, e.g. World Bank (2020), resp. OECD (2020).

3. RESULTS AND DISCUSSION

Table 2 shows that the dynamics of corporate loans recorded a stable development during the first wave of the pandemic, July brought even its acceleration.

Table 2: Year-on-year growth in corporate loans in 2020

month	**Growth rate (%)**
January	2.3
February	3.0
March	3.7
April	3.5
Mai	3.5
June	3.8
July	4.7
August	4.3
September	2.9
October	2.8
November	2.6
December	2.2

Source: Own processing according to the data of the National bank of Slovakia

Corporate loans recorded stable growth at 3.6% in the first half of 2020 during the duration of the pandemic measures. As mentioned, lending activity even accelerated in July, reaching 4.7%. This is the fastest growth in the region of the central and eastern part of the EU. The growth of loans was heavily affected by the significant economic downturn. Compared to the beginning of the year, the credit dynamics even increased in the period from March to June. In March and April, short-term loans in the form of drawdowns of approved credit lines increased significantly, which was reflected in an acceleration of lending activity from 3.0% in February to 3.7% in March. The second quarter was already stable, with month-on-month increases in this period at the level of the average of previous years.

The situation across economic sectors was relatively diverse, with several sectors experiencing a slowdown in credit flows. Developments in industry shaped credit growth significantly, which accounted for almost half of the growth. In addition to industry, loans also grew in the case of car sales, accommodation services and selected professional activities. In the context of economic sectors, July remained relatively diverse, although there was some improvement in some other sectors. Construction and professional activities thus joined the above-mentioned sectors with a recovery in credit growth.

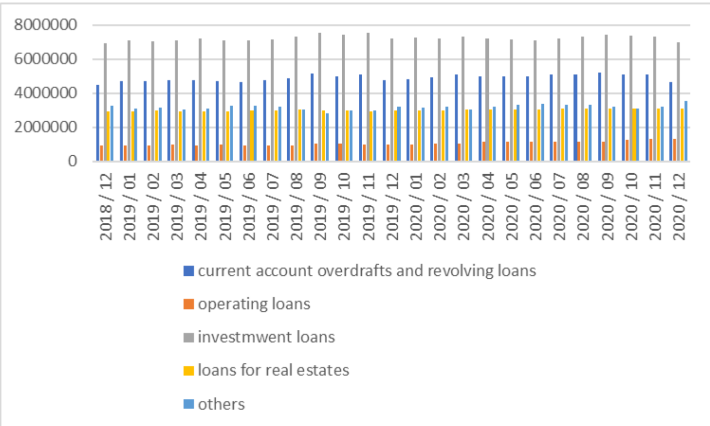
Two trends can be observed among EU countries in the context of the development of the volume of corporate loans. The first is the gradual slowdown in credit growth in the countries of the Central and Eastern EU region. As a result, Slovakia has moved to the first place in the dynamics of corporate loans within these countries. The second trend is the development in several large western EU countries, where lending to the corporate sector has accelerated significantly against the background of strong fiscal stimulus.

In July 2020, lending activity increased thanks to the improving situation in the economy following the release of epidemiological measures. Since the onset of the crisis, several important economic sectors have seen significant declines in sales from March to May. The end of the first half of the year has already brought a relatively significant improvement in the situation in the development of corporate sales.

After the situation improved in the summer months, credit growth declined to 2.9% in September 2020.

However, growth rate in the volume of loans granted to non-financial corporations compared to previous periods of 2020 continued to grow in fourth quarter of 2020. The year-on-year growth rate was highest for long-term loans over 5 years with a year-on-year growth of 6.0%. These were not investment loans as they continued at a subdued pace (Figure 1). As for the volume of short-term loans, we recorded a year-on-year growth of 1.1% compared to the same period last year. On the contrary, we recorded a year-on-year decline in the growth rate in IV. quarter of 2020 at the level of 4.5% for long-term loans from 1 to 5 years.

Figure 1 Loans to non - financial corporations by type, in ths. EUR



Source: Own processing according to the data of the National bank of Slovakia

If we look at the situation from the point of view of the euro area, the volume of loans to non-financial corporations in the euro area increased by 5.5% in December 2020 compared to the same period of the previous year, while in Slovakia we recorded growth of 2.2%. In the euro area, apart from two months, we were able to observe a year-on-year decline in short-term loans to non-financial corporations throughout 2020. The year-on-year decline in these loans was 7% in December 2020. On the contrary, the volume of short-term loans to non-financial corporations in Slovakia in December 2020 increased by 1.1% year on year. During the last two years, we have recorded a year-on-year growth in short-term loans in Slovakia each month.

Throughout 2020, we recorded year-on-year growth in long-term loans in the euro area from 1 to 5.1% in 2020, with the dynamics increasing significantly in the months of March to May. Year-5 years, while in Slovakia we have seen a year-on-year decline in the value of these loans since February 2020.

We have been observing continuous year-on-year growth in the euro area in the item of long-term loans from 1 to 5 years since May 2015, and in December 2020 the year-on-year growth was 15.8%. Year-on-year growth in loans increased significantly in March and April 2020, when the growth rate accelerated from 3.4% in February 2020 to 12.1% in April 2020. The year-on-year decline in the value of loans with a maturity of over 1 year to 5 years in Slovakia reached minimum value in June 2020, when it represented -8.7%.

Long-term loans over 5 years to non-financial corporations in the euro area grew by an average of

on-year growth in loans over 5 years to non-financial corporations in December 2020 was 6.8%.

In Slovakia, long-term loans over 5 years to non-financial corporations grew at a relatively fast pace in 2020, with more significant growth in June to September. The highest growth was achieved in this category of loans in September, when year-on-year growth was 8.8%. Year-on-year growth in December 2020 for long-term loans to non-financial corporations was 6%.

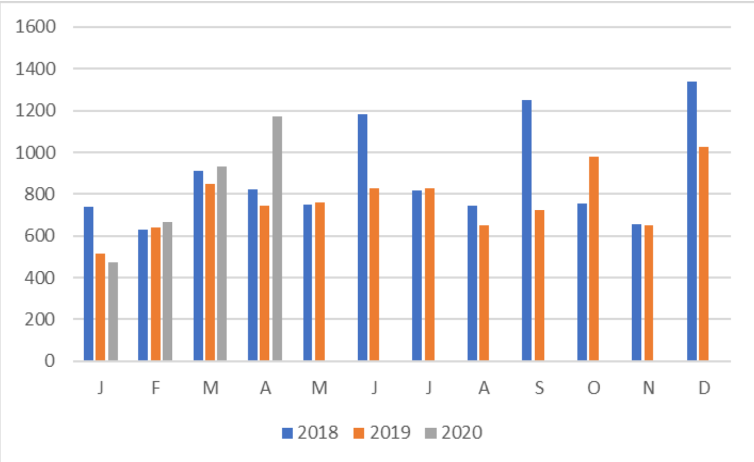
Although almost no impact of the coronavirus crisis can be seen on the overall growth rates of corporate loans, the availability of financing has been limited for riskier groups of companies. In terms of business size, credit growth was driven mainly by large enterprises, a large proportion of which were state-owned enterprises. Lending activity in the case of small and medium-sized enterprises, which are marked as a riskier group of enterprises, remained markedly subdued, with average growth exceeding 1%. However, it is important to note that the decline in lending to small and medium-sized enterprises took place even before the coronavirus crisis at the turn of 2019 and 2020.

In this regard, July has already brought a slight improvement in the case of growth in loans to small and medium-sized enterprises. Lending, especially to large state-owned enterprises, played an important role in maintaining credit growth. On the other hand, the flow of loans to privately owned enterprises has slowed markedly. The July improvement was only partial in this case, with credit growth for foreign-controlled enterprises rising from 5.5% to 8.3% between June and July, while credit growth remained subdued at 1% for privately owned enterprises.

At the beginning of the coronavirus crisis, banks increased the share of loans provided to their clients. The increase in uncertainty associated with the COVID-19 pandemic was reflected in a partial reduction in funding for both new clients and clients of other banks. While in 2019 the share of loans provided to clients outside the own loan portfolio reached almost 8%, in the first half of the year it was just over 5%. July has already brought a partial correction.

The figure 2 documents that the volume of the new loans is very volatile, but it did not decrease even in the first wave of coronavirus crisis.

Figure 2: Volume of new loans provided to companies in the Slovak Republic (EUR million)



Source: Own processing according to the data of the National bank of Slovakia

Although the tightening of credit standards was reported by almost all banks, the restriction on the availability of financing concerned mainly riskier groups of clients.

The reduction in supply in the credit market in the second quarter of 2020 was reported by almost all banks, but without a significant impact on credit growth. Measures against the spread of the disease taken by both the domestic government and the governments of other countries were almost immediately reflected in the decline in sentiment and the perspective of individual economic sectors. The result was a quick reaction of individual banks in the form of tightening of credit standards. The tightening affected all credit conditions, but most of all the amount of credit and the required collateral, to a lesser extent the maturity of loans and covenants. Non-interest charges remained the least affected. The interest margin increased mainly for riskier loans.

Restrictions on the capital or liquidity requirements or the cost of resources of the bank were mentioned only to a small extent as factors influencing the tightening of credit standards. The banks cited the absence of state guarantee schemes as an important fact influencing the tightening of credit standards. Despite the tightening on the supply side, whether from the point of view of banks or individual credit conditions, mostly riskier groups of clients were affected. This corresponds to the development of the volume of loans, where the slowdown in credit growth occurred mainly in selected groups of companies.

Despite the slower and more complicated start-up of state aid, loans with a state guarantee accounted for 13% of all loans granted in the third quarter of 2020. On the positive side, loans also grew in several sectors more affected by the crisis.

If we compare this development with other eurozone countries, according to the results of Euro area bank lending surveys by ECB (ECB, 2020) the impact on credit standards was included in the first quarter of 2020 and the net percentage of banks reporting a tightening of credit standards for loans or credit lines to companies was small when we compare it with the previous financial and sovereign debt crises. This is connected with the size and timeliness of policy measures and the higher resilience of euro area banks. Credit standards on loans or credit lines to firms remained unchanged in the second quarter of 2020. Fiscal and monetary policy measures played a significant role for maintaining favourable credit standards for loans to firms. A tightening of credit standards on loans to firms was recorded in the third quarter of 2020 indicating credit risk considerations due to the coronavirus pandemic. This tightening was in line with banks' expectations from the previous quarter and was mainly driven by banks' risk perceptions, while banks' cost of funds and balance sheet situation did not contribute to the tightening. Credit standards for loans to enterprises continued to tighten in the fourth quarter of 2020, which was somewhat higher than expected in the previous round (net percentage of 25%, after 19% in the third quarter of 2020). While the tightening was above the historical average (8%), it remained below the peaks observed during the great financial crisis and the sovereign debt crisis (average tightening of 52% from the fourth quarter of 2007 to the first quarter of 2009; peak of 30% in the fourth quarter of 2011). As we mentioned, this smaller net tightening over the course of the pandemic compared to previous crises is likely related to supportive monetary and fiscal policy actions. Notably, banks reported a significant easing of credit standards on loans with COVID-19-related government guarantees in 2020. The stronger net tightening in the last two quarters of the year is also consistent with the observed decline in the actual take-up of guaranteed loans and the moderation of overall loan flows to non-financial corporations. The net tightening in the fourth quarter of 2020 was stronger for loans to SMEs (25% vs. 16% for large enterprises) and for long-term loans (26% vs. 19% for short-term loans).

Across the largest euro area countries, credit standards on loans to enterprises tightened in Germany, Spain and France, while they remained unchanged in Italy in the fourth quarter of 2020. This is consistent with the continued increase in realised loan flows to Italian firms in the autumn of 2020. Banks in Germany, Spain and France referred to the heightened perception of risk as the main factor contributing to the tightening (ECB, 2020).

It is not possible to observe the impact of the crisis associated with the COVID-19 pandemic on credit risk indicators. By taking advantage of the deferral option, many companies have gained additional time to deal with a temporarily deteriorating financial situation. Several trends have continued in the development of previous years. The volume of non-performing loans also remained at low levels. The volume of non-performing loans taken out by non-financial corporations amounted to approximately EUR 648.9 million at the end of 2020. The volume of non-performing loans is generally much lower than in the past, as it remained above one billion euros between May 2010 and April 2017. If we compare the situation with the Czech Republic, at the end of December 2020, the Central bank registered non-performing loans in the amount of about 2.5 billion euros.

At the end of September 2020, the deferral of repayments was approved for 12% of corporate loans. Thanks to the possibility of deferring repayments, the share of non-performing loans has not increased yet, but banks will face an increase in non-performing loans in the coming period.

As table 3 reveals, the possibility of deferral of repayment was used to a greater extent by micro-enterprises and small enterprises and sectors significantly affected by the coronavirus crisis. However, this lower level is due to the fact that the legally defined deferral of installments does not apply to large companies that have agreed on deferral of installments individually with the financing bank. From the point of view of individual economic sectors, companies from the economic sectors most affected by the crisis made the most of the possibility of postponing installments. In the case of accommodation and food services, deferred loans account for half of total loans, while in the arts, entertainment and recreation sector, these loans account for one third.

Table 3: Share of deferred loans according to the size of the enterprise (in %)

	micro	small	medium	large
Share of deferred loans	15.0	15.2	11.8	5.9
Share of loans granted to enterprises which have been granted a deferral of repayments on at least one loan	17.7	19.5	21.0	13.1

Source: Own processing according to the data of the National bank of Slovakia, data to September 2019

The deferral of repayments was just one of the measures taken by the governments to mitigate the effects of the COVID-19 pandemic and restart their economies and international trade. In general, these are measures to support:

• liquidity of companies and households (deferrals of loan repayments we mentioned, provision of loans and guarantees from public sources, relief in the area of tax burden)

• solvency of companies (capital injections from public sources, temporary stronger protection of debtors to delay restructuring-bankruptcy proceedings)

• exports (short - term export credit insurance) a

• employment policies (compensation for companies with compulsory closure, contributions to compensate for the decline in sales, contributions to job retention).

Slovakia is no exception in the use of support tools. Measures that are considered to be most effective so far include deferrals of corporate and household loan repayments and measures to support job retention.

In this context, we emphasize that the uncoordinated termination of support instruments may endanger the gradual recovery of the corporate sector. The main target group of ongoing support measures should be, in particular, promising companies with a sustainable business model that need to bridge the temporary shortfall in sales.

In a period of growing uncertainty due to future waves of the pandemic, maintaining access to finance for businesses will be crucial.

4. CONCLUSIONS

The attention of governments, professionals and ordinary people all around the world is focused on addressing the consequences of the current pandemic caused by the spread of COVID-19. However, in addition to measures to prevent the further uncontrolled spread of coronavirus and the collapse of health systems, it is important to consider the state of the economy. Worldwide, this has found itself in an unexpected and intense crisis.

Regarding the business sector, small and medium – sized enterprises are the most vulnerable and most affected group. In some cases, measures related to the saving of human lives have an existential impact to them. Due to their economic and social importance for the economies, it is necessary to monitor their access to sources of finance.

This paper surveyes the access of SMEs to bank loans in Slovakia in 2020. We can conclude that the dynamics of corporate loans recorded a stable development during the first wave of the pandemic. Compared to the countries of the region of the Central and Eastern part of the EU, the domestic banking sector achieved the most significant growth in August. Credit growth has slowed in most of these countries. The situation is the opposite in several large western EU countries, where there has been a significant acceleration in corporate lending, probably against the background of strong fiscal stimulus.

Demand from clients, especially for operating financing, continued in the market. Banks' credit conditions eased partially in summer months, i.e. at the end of the second quarter, after the tightening in the first months of the coronavirus crisis.

In terms of maturity, loans with a maturity of over 5 years contributed to the year-on-year growth most significantly. However, these were not investment loans, which continued at a subdued pace. The slowdown in investment loans was largely offset by government-guaranteed loans.

The year-on-year growth in the volume of corporate loans was relatively significantly affected by deferred loan repayments. The impact of the pandemic on the credit risk of the corporate portfolio will thus become apparent only after the end of the deferral of repayments and support measures by the state.

At the end of the third quarter of 2020, growth in corporate loans slowed to 2.9% year on year. Despite this slowdown in lending activity in September, the availability of corporate finance can be assessed relatively favorably. Uncertainty about future developments in the corporate sector remains significant.

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