

Improving SME Access to Finance in Ukraine

- Summary of results -

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1. Introduction

- Small and medium-sized enterprises (SMEs) can contribute to a more diversified and open economic structure and support employment generation in Ukraine
- However, a number of factors impedes SME development, and lack of access to finance is one of them
 - In surveys among Ukrainian SMEs, mentioned as one of the top three business constraints
- This presentation:
 - Analyses the supply and demand of SME finance, and estimates the resulting financing gap,
 - Provides a review of existing financing instruments,
 - Puts forward recommendations on how to improve the situation

2. SMEs in Ukraine and their Role in the Economy

Role of SMEs in the national economy

SME's share of	Ukraine	Slovakia	Poland	Germany	EU-28
Enterprises	99.9%	99.9%	99.8%	99.5%	99.8%
Employment	75.5%	71.2%	69.0%	60.9%	66.9%
Sales	60.4%	62.7%	51.0%	53.8%	57.9%

Source: State Statistics Service of Ukraine, Eurostat

- The number of SMEs in Ukraine (legal entities and private individuals) is with almost 2 m quite large (see Annex 1 for details)
- In a peer group comparison, roughly similar shares in terms of number of enterprises, employment and sales
- Low contribution to the state budget due to special tax regime

3. SME Finance: Demand, Supply and the Financing Gap

SME demand for financing

Economic unit	Number	Average equity (per one), EUR m	Average debt (per one), EUR m	Probability of taking SME financing	Total demand for equity, EUR m	Total demand for debt, EUR m	Total demand, EUR m
Micro company	278,922	0.01	0.03	25%	697.31	2,091.92	2,789.22
Small company	45,676	0.1	0.3	25%	1,141.90	3,425.70	4,567.60
Medium company	15,906	0.5	1.5	25%	1,988.25	5,964.75	7,953.00
Micro PEs	1,580,965	0.01	0.03	10%	1,580.97	4,742.90	6,323.86
Small PEs	9,483	0.1	0.3	15%	142.25	426.74	568.98
Medium PEs	712	0.5	1.5	20%	71.20	213.60	284.80
Farmers	38,850	0.1	0.3	25%	971.25	2,913.75	3,885.00
Other SMEs	30,165	0.01	0.03	25%	75.41	226.24	301.65
Total	2,000,679	-	-	-	6,668.53	20,005.58	26,674.11

Source: State Statistics Service of Ukraine, own estimation

- Based on a set of realistic assumptions, we estimate **significant demand for finance**, in particular for debt finance

SME supply for financing

Type of Financing	Supply of equity, EUR m	Supply of debt, EUR m
Loans from Ukrainian banks	-	10,167.26
SME credit lines by IFIs arranged through partner Ukrainian banks	-	1,000.00
Loan guarantee schemes	-	-
Leasing and factoring companies	-	392.35
Credit unions	-	25.41
Own equity	5,483.92	-
Equity funds	200.00	-
Startup financing	111.00	-
Total supply	5,794.92	11,585.02

Source: National Bank of Ukraine, National Commission for State Regulation of Financial Services Markets

- Existing debt/ equity financing sources are much more limited

Financing gap

Type of finance	Demand	Supply	Financing gap	In % of demand
Equity, EUR m	6,668.53	5,794.92	873.61	13%
Debt, EUR m	20,005.58	11,585.02	8,420.57	42%
Total, EUR m	26,674.11	17,379.93	9,294.18	35%

Source: Own estimation

- Comparing supply and demand, we see a **total financing gap of EUR 9.3 bn**
- The debt financing gap makes up the biggest part with EUR 8.4 bn

4. Strengths and weaknesses of existing SME financing instruments

Financing instruments	Strengths	Weaknesses
Loans from Ukrainian banks	Most accessible instrument, provided in local currency	Predominantly short-term, high interest rate, often require hard collateral
SME credit lines by IFIs arranged through Ukrainian partner banks	Medium and long-term loans, often accompanied by technical assistance	Hard currency loans
Leasing and factoring companies	For leasing: medium and long-term, leased object used as a security For factoring: accounts receivable used as a security, could be revolving	For leasing: Own contribution up to 50% required For factoring: short-term financing, could be recourse
Credit unions	Unsecured	Low capacity, small amount, high interest rate, individuals only
Own equity	Permanent risk capital	Difficult to raise, if urgently needed
Equity funds	Permanent or temporary risk capital, often medium or long term	Low capacity, difficult to access
Start-up financing	Good appetite for innovative projects from global companies and funds	Low capacity, mostly in IT sector, investments often made outside Ukraine

Source: Own research

- Mixed experience with existing instruments

5. Immediate priorities for improving SME access to finance

- Below are some recommendations on how to improve access to SME finance in the short term:

#	Subject	What to do	How to do
1	Loans to SMEs	Adopt legal and regulatory reforms and consider credit guarantees to improve access to finance	<p>Cooperate with IFIs and governmental agencies on further improvements in the legal and regulatory framework</p> <p>Coordinate with EU SURE a Loan Guarantee Facility of EUR 40 m</p> <p>Initiate a specialised loan guarantee scheme for farmers</p> <p>Resolve issues related to warehouse receipts</p>
2	Loans to SMEs	Address the current decline in lending to SMEs	<p>Initiate a financing package of EUR 500 m for SMEs (including EUR 109 m for SMEs of IDPs) from IFIs to channel through partner banks as identified in 3.1 above.</p>
3	Loans to SMEs	Work towards a regulatory framework that facilitates banks' access to longer term and local currency funding and promote competition in the banking sector to encourage banks to offer more competitive rates and reach out to new segments	<p>Cooperate with IFIs and governmental agencies for clearing all barriers to provide loans to partner banks for further on-lending to SMEs in Hryvnias'</p>

Source: Own research

Immediate priorities for improving SME access to finance (cont'd)

#	Subject	What to do	How to do
4	Non-bank financial products and services	Support viable alternatives to bank financing by putting in place adequate legal frameworks for the provision of non-bank financial products and services	<p>Initiate a Ukrainian SME private equity fund of EUR 25 m. Use experience of British programmes of Business Finance Partnership (BFP), Start-up Loans Scheme, Business Angel Co-Investment Fund, Enterprise Capital Funds Programme, etc.</p> <p>Cooperate with business associations representing leasing, factoring, credit unions venture capital and business angel financing to improve the legal and regulatory framework.</p>
5	Education and training	Promote financial literacy among the public and build financial management and business planning skills among small business owners	<p>Enhance financial skills of SMEs by training entrepreneurs in how to raise financing: cooperation with banks and investors, basics of finance, business planning, financial projections, etc.</p> <p>Train SME how to raise alternative financing such as leasing, factoring, credit unions, venture capital, business angel financing, etc.</p>

Source: Own research



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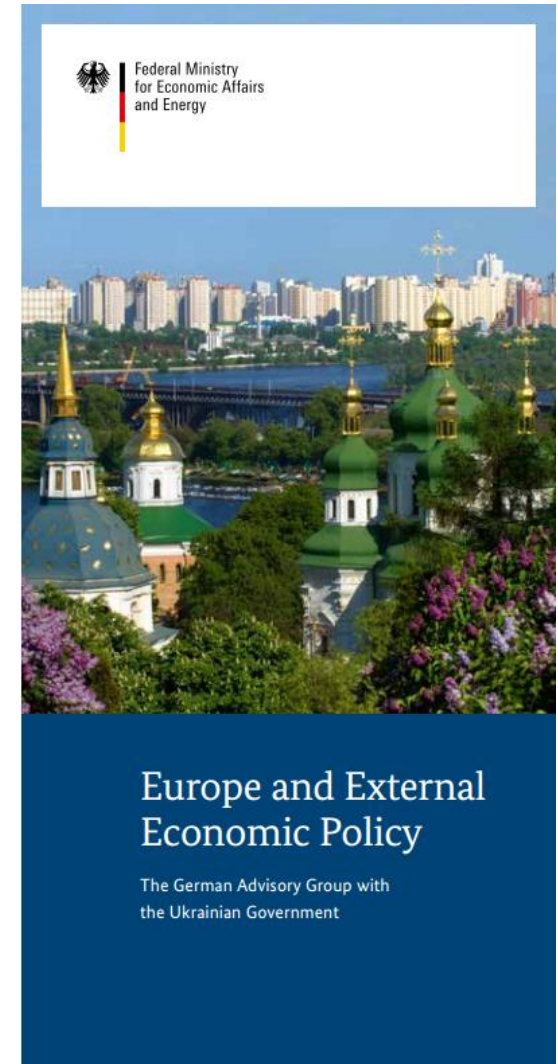
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Annex 1: SMEs in Ukraine

Number of SMEs in Ukraine

Economic unit	Number (as of 31 December 2014)*	Share of total number of companies
Micro company	278,922	81.8%
Small company	45,676	13.4%
Medium company	15,906	4.7%
Total	340,504	99.9%

Number of private entrepreneurs

Economic unit	Number (as of 31 December 2014)*	Share of total number of PEs
Micro PEs	1,580,965	99.4%
Small PEs	9,483	0.6%
Medium PEs	712	0.0%
Total	1,591,160	100%

Source: State Statistics Service of Ukraine, Eurostat

*Excluding the Autonomous Republic of Crimea, Sevastopol and the conflict area in Eastern Ukraine.

- Since 2012, identical SME definition in Ukraine and the EU
- Except optional balance sheet criterion

Annex 2: OECD SME Policy Index on Ukraine

#	Policy factor	Score	Gap to 5.00, %
1	Create an environment in which entrepreneurs and family businesses can thrive and entrepreneurship is rewarded	2.25	55%
2	Ensure that honest entrepreneurs who have faced bankruptcy quickly get a second chance	2.05	59%
3	Design rules according to the “think small first” principle	2.45	51%
4	Make public administration responsive to SMEs	3.81	24%
5	Adapt public policy tools to SME needs	2.29	54%
6	Facilitate SME access to finance and develop a legal framework and business environment supportive of timely payments in commercial transactions	3.22	36%
7	Help SMEs to benefit more from the opportunities offered by the Single Market	4.34	13%
8	Promote the upgrading of skills and all forms of innovation	2.21	56%
9	Enable SMEs to turn environmental changes into opportunities	1.22	76%
10	Encourage and support SMEs to benefit from growth markets	1.63	67%
	Overall score	2.55	49%

Source: OECD SME Policy Index

Annex 3: OECD SME Policy Index, Access to Finance component

#	Policy factor	Score	Gap to 5.00, %
6	Access to finance for SMEs	3.22	36%
6.1	Legal and regulatory framework	3.70	26%
	Creditor rights	3.85	23%
	Register	3.49	30%
	Credit information bureau	4.31	14%
	Banking regulations	3.50	30%
	Stock market	3.00	40%
6.2	Bank financing	2.06	59%
	Banking statistics	2.32	54%
	Credit guarantee schemes	1.67	67%
6.3	Non-bank financing	3.54	29%
	Microfinance	3.00	40%
	Saving and loan associations (SLAs)	3.67	27%
	Leasing	3.50	30%
	Factoring	4.00	20%
6.4	Venture capital	1.38	72%
	Legal framework	1.45	71%
	Design and implementation	1.49	70%
	Monitoring and evaluation	1.00	80%
6.5	Financial literacy	3.29	34%
	Design and implementation	3.86	23%
	Monitoring and evaluation	1.00	80%
	Overall score	3.22	36%

Source: OECD SME Policy Index

Annex 4

Potential Partner Banks for Cooperation with IFIs in SME Finance

Bank	Shareholder Structure	Market Share by Assets	Market Share by Loans	Equity, EUR m	Number of branches	Experience with IFIs (if yes - donor and product)
Group of the largest banks						
Ukreximbank	State - 100%	11.13%	7.48%	270	102	Yes (WB, IFC, KfW, EBRD, GCPF, EIB) - EE/RE loans, SME loans
Raiffeisen Bank Aval	Raiffeisen Bank International (Austria) - 96.45%	4.18%	3.37%	159	595	Yes (EBRD) – SME loans
Ukrsibbank	BNP Paribas S.A. (France) - 84.996%	3.02%	2.55%	77	455	Yes (EBRD) – SME loans
First Ukrainian International Bank	Rinat Akhmetov (Ukraine) - 99.9%	2.85%	3.37%	168	157	No
OTP Bank	OTP Bank Plc. (Hungary) - 100%	1.83%	1.98%	54	83	No
Group of large banks						
Credit Agricole	Credit Agricole S.A. (France) - 99,996%	1.74%	1.78%	61	168	No
Megabank	Victor Subbotin (Ukraine) – 60.89%, EBRD (UK) – 15.00%, KfW (Germany) – 15.00%, IFC (US) – 6.01%	0.68%	0.89%	34	170	Yes (EBRD, IFC, KfW, GGF, GUF, OPIC, NEFCO) - EE microloans, EE SME Agri loans
Kredobank	PKO Bank S.A. (Poland) – 99.57%	0.65%	0.51%	41	108	No

Annex 4 (cont'd)

Potential Partner Banks for Cooperation with IFIs in SME Finance

Bank	Shareholder Structure	Market Share by Assets	Market Share by Loans	Equity, EUR m	Number of branches	Experience with IFIs (if yes - donor and product)
Group of mid-sized banks						
ProCredit Bank	ProCredit Holding AG (Germany) – 60.87%, KfW (Germany) – 39.13%	0.54%	0.63%	26	27	Yes (EBRD, KfW, IFC, GUF) - EE microloans, SME loans
Pravex Bank	Intesa San Paolo S.p.A. (Italy) – 100%	0.34%	0.24%	50	139	No
Piraeus Bank	Piraeus Bank S.A. (Greece) – 99.99%	0.25%	0.18%	17	17	No
Idea Bank	Getin Holding S.A. (Poland) – 99.34%	0.21%	0.29%	12	82	No
Group of small banks						
Bank Lviv	Margeir Petursson (Iceland) – 99.88%	0.10%	0.12%	7	24	Yes (EBRD, NEFCO) - EE microloans

Source: National Bank of Ukraine, own research

Annex 5

Estimation of financial needs for SMEs affected by the conflict in the East and Crimea

	Whole Ukraine	Share of total population	Estimated number of IDPs and displaced SMEs	Demand for financing per one SME, EUR m	Probability of taking financing	Demand for financing, EUR m
Population	42,619,835		1,438,000			
Number of PEs	1,591,160	3.73%	53,686	0.01	15%	80.53
Number of SMEs	340,504	0.80%	11,489	0.01	25%	28.72
Total						109.25

Source: State Statistics Service of Ukraine, UNHCR, own estimation

- Similar methodology of analysis as in chapter 3 (financing gap)
- Only demand for debt estimated, for those SME that had to relocate from conflict areas to regions under government control