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ACCESS TO FINANCE IN 2022

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BOX 1: ACCESS TO FINANCE IN 2022[1]

SMEs account for most of the value added produced in the economy but face unique challenges when it comes to obtaining finance, especially in terms of access to capital markets.[2,3] The aim of this box is to analyse information collected through the Survey on Access to Finance of Enterprises (SAFE) on developments in the financial situation of enterprises in Malta and across the European Union (EU) in 2022.[4]

The SAFE was conducted by the European Commission in cooperation with the ECB between 7 September and 27 October 2022 among 15,625 enterprises across the European Union, including 101 Maltese firms. It covers the period between April and September 2022.

The financial situation of SMEs

Survey results show that between April and September 2022 – the reference period for the latest survey – 44% of SMEs in Malta reported an unchanged turnover level. Around 35% of SMEs reported an increase, while 20% reported a decline.[5] As a result, on balance, 15% of respondents assessed turnover to have increased over the 6 months preceding the survey. This is an improvement over 2021, when on balance, turnover was assessed to have remained unchanged. By contrast, between April and September 2022, a net 16% of domestic SMEs in Malta reported a decrease in profits, a marginally smaller share compared with the net 18% of domestic SMEs which reported lower profit in 2021.

In the EU, a net 18% of SMEs reported higher turnover, slightly higher than that of 14% reporting higher sales a year earlier.[6] Meanwhile, profits fell for 20% of firms in 2022 compared to 6% of firms in the preceding year. Hence, in Malta and across the EU, firms on balance reported a decline in profits despite higher turnover, with the share of SMEs' reporting a decline in profits slightly lower in Malta.

With regard to labour and other costs, on balance, 85% and 83% of Maltese SMEs respectively claimed that these have increased during the reference period. While the net share of respondents reporting higher labour costs is higher than that for the EU27 (68%), Maltese SMEs were slightly less likely to report increases in non-labour costs (including materials, energy and other costs) than those in the EU (91%). These figures mark a significant increase in the incidence of firms which report cost increases relative to 2021 – when only 44% and 58% of domestic SMEs reported higher labour and other costs, respectively. Survey results for 2022 show that the share of firms reporting such higher costs is now even above that recorded in recent years (see Chart 1).

During the period covered by the survey, on balance, the number of employees was assessed to have increased by 14% of SMEs in Malta, as opposed to 5% of SMEs in the EU. The share of domestic SMEs reporting a net increase in the number of employees in 2022 contrasts with that recorded a year earlier, when the number of employees was assessed to have remained stable. The pace of hiring seems to have moderated compared to 2019, when 22% of SMEs in Malta had reported a net

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[2] Structural Business Statistics published by the NSO indicate that in 2020, 99.7% of firms in the non-financial business economy were SMEs.

[3] SMEs account for 77.7% of all persons employed in Malta and for 65.9% of all turnover. See NSO *News Release* 116/2022 https://nso.gov.mt/en/News_Releases/Documents/2022/07/News2022_116.pdf

[4] Companies that employ less than 250 persons and make less than 50 million in turnover are classified as SMEs.

[5] Figures from SAFE are rounded, in line with the approach followed by the ECB when commenting on SAFE results.

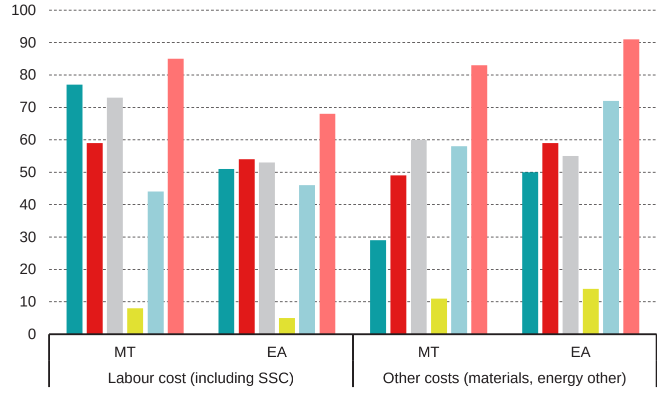
[6] Net percentages refer to the difference between the percentage of respondents reporting that a given factor has increased and those reporting that it has decreased.

increase in the number of employees, likely reflecting the increasing difficulties to find personnel with the required skills.

Meanwhile, a net 22% of firms in Malta recorded an increase in inventories and working capital, compared with 7% in the EU.

In 2022, 67% of firms reported an unchanged level of fixed investment; while a fifth of respondents reported an increase, and slightly less than a tenth reported a decrease. Hence, on balance, 13% of SMEs in Malta reported an increase in investment in plant, machinery, or equipment. This compares with 9% of SMEs in the EU. While the increase in the share of domestic SMEs that reported higher investment signals a recovery over the past two years, the net balance in Malta is still below that reported in 2019, when it stood at 35%.

Chart 1
SMEs REPORTING HIGHER LABOUR AND OTHER COSTS
(net share of respondents)



Source: SAFE, various editions.

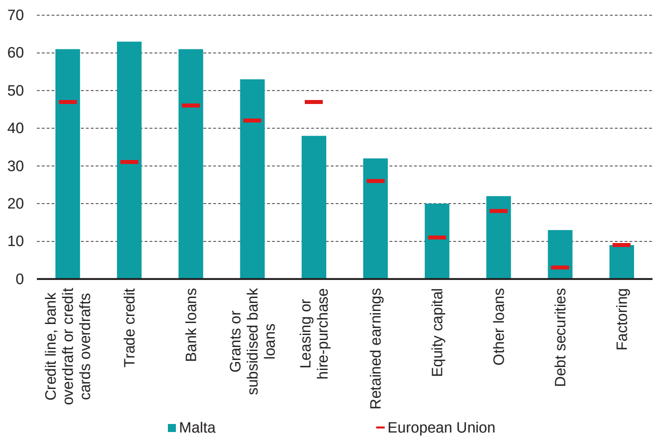
The SAFE also reveals that the share of local SMEs reporting an increase in interest rate expenses rose to 16%, from 13% a year earlier. More widespread increases were observed in the EU, where this share rose to 28%, from 10% in 2021.

Sources of finance used by SMEs

In 2022, the proportion of domestic SMEs that considered trade credit as relevant to their business rose to 63% from 56% a year earlier. This share was marginally higher than that of Maltese SMEs that deem bank-related products and bank loans as relevant (see Chart 2). The fact that trade credit was the most relevant source of finance by SMEs suggests that certain businesses might have found it easier to resort to this type of financing to fill liquidity gaps.

During the period under review, a significant share of SMEs in Malta continued to prefer bank-related products such as overdrafts and credit lines, as well as bank loans over most market-based products and other

Chart 2
SOURCES OF FINANCE DEEMED RELEVANT BY SMEs
(used in the past or consider using in the future; percentage of respondents)



Source: SAFE (2022).

sources of finance. However, the share of SMEs in Malta that used credit lines, bank overdrafts or credit cards overdraft, or that expected to use them in the future, fell to 61%. This marks the lowest rate recorded since 2016. The relevance of this type of financing has been consistently decreasing – falling gradually from 83% in 2016 to 71% in 2019 and 2020, before increasing to 78% in 2021. Similarly, the share of firms that used bank loans in the past or considered using them in the future fell to 61% from 64% in 2021.

By comparison, in the EU, just below half of the respondent SMEs used bank loans and credit lines, bank overdrafts or credit cards overdraft, or expected to use them in the future – with the share being broadly stable over recent years.

The share of SMEs in Malta that considered grants or subsidised bank loans as being relevant to their enterprise edged up to 53% in 2022, from 48% a year earlier. By contrast, the share of SMEs in the EU that mentioned this type of financing as being relevant fell marginally to 42% from 43% in 2021.

Meanwhile, the relevance of internal funds (retained earnings or asset sales) as a source of finance also fell in Malta, following a significant increase in 2021. In 2022, 32% of domestic SMEs considered this source as relevant for their business, down from 52% a year earlier, and below that of 46% recorded pre-pandemic. Nevertheless, it was still above a net 26% reported in the EU.

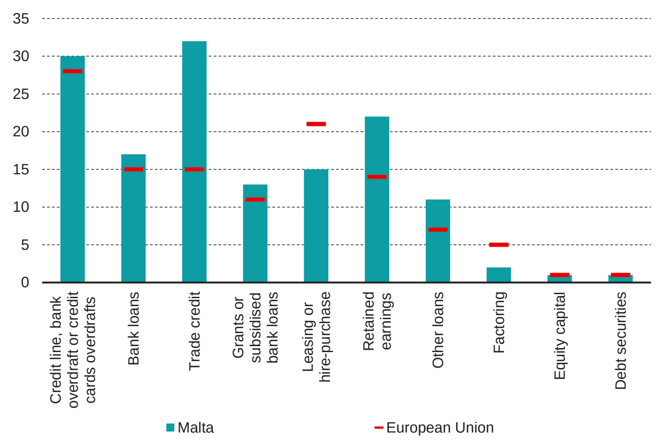
Chart 3 reports on the use of different types of funding sources used during 2022. Trade credit as well as credit lines, bank overdrafts and credit cards overdraft were used most often. However, the share of domestic SMEs using these types of financing fell.

The proportion of those that used trade credit in 2022 fell to 32% from 38% a year earlier, and stood in the same level as that recorded in 2020. Although the share of SMEs in Malta that used this type of financing was more than double that in the EU on average, the SAFE notes some heterogeneity among countries. At 42%, SMEs in Ireland were the highest users of this source of financing, followed by Cyprus (40%), and Greece as well as Poland (34%). Meanwhile, in France, Germany, Hungary, the Czech Republic, Luxembourg, Slovenia and Croatia, less than 10% of SMEs used this type of financing.

The share of domestic SMEs using credit lines, bank overdrafts and credit lines decreased to 30% from 49% in 2021, and marks the lowest rate recorded since 2015. The share of domestic SMEs that used this type of financing in 2022 was slightly above the share of EU firms reporting that they used this source of funding in recent months (28%).

Similarly, the share of firms that used bank loans in the last six months preceding the survey fell to 17%

Chart 3
SOURCES OF FINANCE USED BY SMEs IN 2022
(over the preceding six months; percentage of respondents)

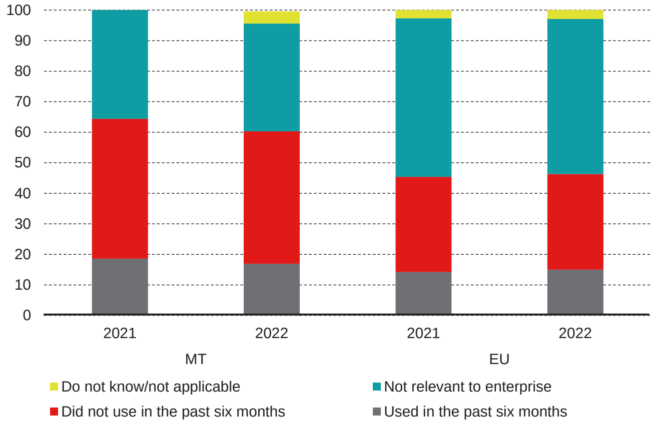


Source: SAFE (2022).

in Malta from 19% a year earlier, standing below the share of firms that had recently relied on internal funds (22%), though above that of 15% in the EU.

In general, the use of instruments of finance by Maltese firms was in line with or higher than that in the EU, with the exception of leasing, hire purchase and factoring, where the fraction of firms using such financing stood lower in Malta.

Chart 4
NEW LOANS OR LOAN RENEWALS
(percentage of respondents who took new loans or renewed the loans in the past six months)



Sources: SAFE (2021); SAFE (2022).

Less than half (43%) of domestic SMEs did not use bank loans in 2022, as opposed to 46% in 2021, while 35% replied that they considered them irrelevant for their enterprise, marginally down from 36% a year earlier. Meanwhile, in the EU, 31% of SMEs claimed that they did not use bank loans in the six months preceding the survey, while half of SAFE respondents stated that bank loans were irrelevant for their enterprise. The figures for 2022 were thus broadly similar to those reported in the preceding year, with EU firms still more likely to say that bank loans were not used or were irrelevant than Maltese firms (see Chart 4).

When asked to elaborate on why bank loans are not deemed relevant, 78% of domestic SMEs stated that they did not need this type of financing. Meanwhile, 7% reported that interest rates or prices were too high, while a further 5% of domestic SMEs claimed that no bank loans were available, while 10% cited other reasons.[7]

In the EU, 74% of firms that considered bank loans as being irrelevant replied that they do not need such financing. A further 9% mentioned too high interest rates, while only 3% reported that bank loans were unavailable. Another 14% of SMEs mentioned other reasons.

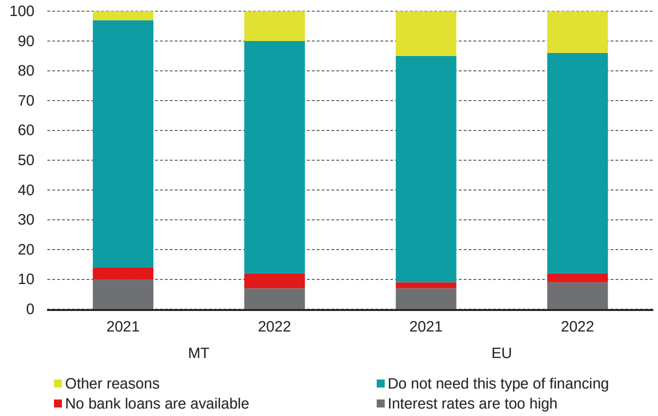
The reasons behind the irrelevance of bank loans cited by EU firms were largely unchanged from those reported in 2021. Meanwhile in Malta, the composition of responses changed slightly from that reported in 2021. The share of SMEs that cited bank loan unavailability rose marginally, while those that claimed that they do not need this type of finance fell (see Chart 5).

The share of SMEs that used retained earnings or proceeds from the sale of assets fell to 22% in 2022, from 28% a year earlier (see Chart 3). This share remained above that in the EU, which remained stable at 14%. This could explain why Maltese firms were more likely than their EU counterparts to report that they did not need bank financing. Hence, although there remains a much higher recourse to retained earnings in Malta when compared to the EU, the gap has narrowed somewhat.

[7] 'Other reasons' include insufficient collateral or guarantees, reduced control over the enterprise, too much paperwork and unspecified reasons.

The share of firms that reported using subsidised loans or grants decreased to 13% in 2022, from 15% in 2021. This share was marginally higher than that reported for the EU (11%). This suggests that the use of this type of financing is converging to that recorded in the pre-pandemic period (2019: 10%), after increasing to 20% in 2020. Following the outbreak of the pandemic, a number of SMEs benefitted from moratoria on loan repayments to ease liquidity shortage caused by the COVID-19 pandemic.

Chart 5
REASONS WHY BANK LOANS ARE DEEMED IRRELEVANT FOR BUSINESS
(percentage of respondents who replied that bank loans were irrelevant for their enterprise)



Sources: SAFE (2021); SAFE (2022).

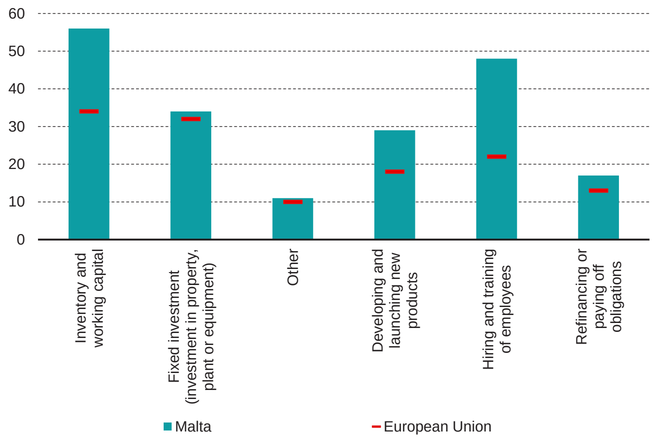
Meanwhile, the proportion of firms that used leasing or hire-purchase more than doubled and stood at 15% in 2022, up from 6% in 2021. Nevertheless, it stood below that of 21% reported in the EU. During the period under review, the use of other loans such as those from family and friends, a related enterprise or shareholders, increased slightly to 11% from 10% a year earlier. During the same period, only 1% of domestic SMEs made use of equity and debt securities. In fact, debt securities, factoring and equity capital remained the three sources of finance that were least used in Malta and across the EU.

Uses of external finance

Chart 6 shows the purpose for which SMEs in Malta and in the EU used external financing obtained during 2022. The share of SMEs that obtained external finance for inventory or working capital fell to 56% in 2022 from 59% a year earlier but remained above that of 34% in EU. In the latter case, this share also fell from 38% a year earlier.

The proportion of domestic SMEs that used external financing for fixed investment in property, plant or equipment remained unchanged at 34%, and stood marginally above that of 32% in the EU. Meanwhile, the proportion of SMEs in Malta that used external financing for the development and launching of new products rose to 29% from 24% in the preceding year and stood above that of 18% in the EU.

Chart 6
USES OF EXTERNAL FINANCE
(over the preceding six months; percentage of respondents)



Source: SAFE (2022).

During the period under review, the share of domestic SMEs that used external financing for the hiring and training of employees rose significantly to 48%, from 29% a year earlier. This share is the highest recorded since 2015 and might reflect the tight labour market conditions and broadening wage pressures. It also stood significantly above that of 22% recorded among respondent firms in the EU. A further 17% of domestic SMEs used external finance to refinance or pay off obligations, compared to 13% in the EU.

Most pressing problems facing SMEs

Chart 7 provides a breakdown of the most pressing problems that SMEs faced between 2018 and 2022. The share of respondent SMEs that cited the availability of skilled staff or experienced managers as the most pressing problem stood at 35% in 2022, up from 30% a year earlier and slightly above the shares recorded in the three years preceding the pandemic. This was also the most pressing problem for SMEs in the EU (27%).

SAFE results show that in 2022 the countries with a larger share of respondents than Malta that cited skills availability as most problematic were the Netherlands (40%), Austria (37%) and Croatia (37%).

Meanwhile, 18% of domestic SMEs have reported ‘other problems’ than those listed in the survey as the most challenging issues that they faced in 2022, as opposed to 21% in the EU.

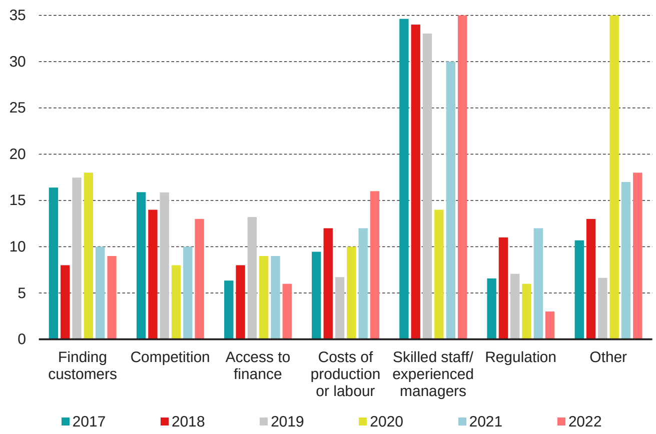
Other non-financial barriers that undermine firm growth include costs of production and labour. The share of SMEs in Malta that consider higher costs as their most pressing ones rose to 16% in 2022 from 12% a year earlier but was below that of 18% in the EU. Meanwhile, the share of SMEs that cited a burdensome regulatory framework as a most important problem in 2022 dropped to 3%, from 12% in the preceding year. The share of firms concerned with these issues in 2022 was below that of 9% reported by their EU counterparts.

During the reference period, 9% of SMEs in Malta considered the problem of finding customers for their products or services as their most pressing problem, down marginally from 10% reported a year earlier and that of 12% in the EU.

Meanwhile, 13% of domestic SMEs considered competition as the most pressing problem – above the share of 10% in 2021 but still below that of 16% reported pre-pandemic. In 2022, competition was considered as a most important problem for only 7% of SMEs across the EU.

With regard to access to finance, the share of SMEs in Malta that considered this as a most pressing problem has declined compared with recent years. It fell to 6% in 2022 – the same proportion as that in the EU. According

Chart 7
MOST PRESSING PROBLEM FACING FIRMS
(percentage of respondents)



Source: SAFE, various editions.

to SAFE 2022, access to finance remained a very pressing problem to SMEs in Greece, where it was mentioned by around 14% of participating firms, and least of a problem in Ireland, Slovenia and the Netherlands – reported by less than 5% of respondents in each country.

Availability of financing

When asked about the availability of different types of financing, a net share of 3% reported a deterioration in the availability of bank loans in Malta – an unchanged share when compared to a year earlier. By contrast, in the EU the net share reporting a deterioration stood at 8%, compared with a net share of 6% that reported an improvement a year earlier.

Furthermore, a net 2% of SMEs in Malta believed that the availability of credit lines, bank or credit card overdrafts improved in 2022, as opposed to a net share of 3% that signalled a deterioration in 2021. Meanwhile, in the EU the net share of SMEs reporting a deterioration stood at 4% in 2022 compared with a net 6% of SMEs that reported improved availability a year earlier.

On balance, a smaller net share of SMEs (1%) in Malta claimed improved availability of trade credit compared to 2021 (7%). Meanwhile, the availability of 'other loans' worsened as 4% of domestic SMEs reported a deterioration as opposed to a 7% net improvement in 2021.

By contrast, on balance, 18% of domestic respondents claimed that the availability of financing through leasing or hire-purchase improved, as opposed to a small deterioration reported in 2021.

Looking forward to the six months ahead, domestic SMEs expected a deterioration in the availability of bank loans, credit line, bank overdraft or credit cards overdraft, trade credit and 'other loans'. By contrast, they expected an improvement in equity capital, leasing or hire-purchase as well as debt securities. Meanwhile, in the EU, on balance, surveyed SMEs expected a deterioration in the availability of the various types of financing mentioned above.

Credit demand

The SAFE also provides information on the demand for finance by participating firms to complement replies on the availability of financing (supply). Table 1 shows the number of firms that applied for bank loans, trade credit, bank overdraft, credit line or credit card overdraft since 2018. The proportion of SMEs that applied for bank overdraft, credit lines or credit card overdrafts remained unchanged at 14% in 2022. During the same period, 46% did not apply because of sufficient internal funds. Internal earnings thus remained the main factor behind firms' reluctance to apply for a bank loan (EU: 42%). The share of those that did not apply because of possible rejection rose to 8% from 4% a year earlier, while the proportion of those that did not apply for other reasons increased to 32%.

Table 1
FOR EACH OF THE FOLLOWING WAYS OF FINANCING, COULD YOU PLEASE INDICATE WHETHER YOU:
Over the preceding six months; per cent of responding firms

	Bank overdraft, credit line or credit card overdrafts					Bank loans					Trade credit				
	2018	2019	2020	2021	2022	2018	2019	2020	2021	2022	2018	2019	2020	2021	2022
Applied over the past six months	42	24	26	14	14	22	16	20	21	15	48	32	29	32	26
Did not apply because of possible rejection	2	8	3	4	8	1	6	1	3	7	0	1	1	2	4
Did not apply because of sufficient internal funds	32	48	51	55	46	45	53	59	58	40	32	29	44	48	31
Did not apply for other reasons	23	14	20	28	32	25	16	19	18	38	16	28	23	18	39

Source: SAFE (2022).

During 2022, the proportion of domestic SMEs that applied for bank loans fell to 15% from 21% a year earlier and stood marginally lower than the share of 16% recorded in the pre-pandemic period. The share of respondent firms that did not apply because of possible rejection rose to 7%, while the proportion of those that did not apply for other reasons more than doubled and stood at 38%. Meanwhile 40% of firms did not seek bank loans due to sufficient internal funds – down from 58% in 2021 and less than 43% of SMEs in the EU.

The percentage of respondents that applied for trade credit fell to 26% in 2022 from 32% in the preceding year. This was marginally below that of 28% in the EU. Survey results show that a significantly lower share of respondents (31%) did not apply because of sufficient internal funds compared with 48% a year earlier. While only 4% did not apply for fear of rejection, 39% did not apply for other reasons – a considerable higher share than that reported in SAFE carried out in preceding years.

Looking forward, when asked about the type of external financing they would solicit to realise their growth ambitions, domestic SMEs expressed a strong preference for bank loans. 76% of SMEs in Malta prefer this type of financing. Only 14% of domestic SMEs showed preference to taking loans from other sources, while just 1% of respondents replied that they would seek equity investment. The preferences of domestic SMEs in Malta are largely in line with those reported by their EU counterparts, though at 63%, a smaller share of SMEs in the EU prefer bank loans, while a higher proportion of SMEs (6%) would choose equity capital.

When asked about the limiting factors for obtaining finance, 22% of domestic SMEs believed that there were no obstacles as opposed to 36% across the EU. Both in Malta and in the EU, this share fell when compared to a year earlier. The share of SMEs that considered interest rates or price as being a potential limiting factor stood at 16% in Malta, marginally lower than 17% reported in 2021. However, this share rose to 26% in the EU from 12% a year earlier. Meanwhile, 21% of local respondents said that they had insufficient collateral or guarantee, as opposed to 13% in the preceding year – more than double the share of 10% reported in the EU as whole. Furthermore, almost a fifth of domestic SMEs reported too much paperwork as a limiting factor, up from 7% in 2021 and across the EU.

Conclusion

The SAFE 2022 indicates that on balance, SMEs in Malta and in the EU signalled a recovery in business activity, with a higher net share of domestic SMEs reporting an increase in turnover in 2022 compared with a year earlier as well as with their EU counterparts. Nonetheless, profitability fell for a greater proportion of firms over a year earlier on account of higher labour and other costs, though Maltese SMEs were slightly less likely to report increasing costs of materials and energy than those in the EU. This likely reflects the fact that energy prices remained unchanged in Malta thereby limiting scope for cost increases compared to a scenario in which such prices would have responded to higher international commodity prices. On the other hand, labour shortages and labour costs seem to have become ever more challenging, with indications that funding resources might be diverted to address such issues instead of being put to more productive use.

While in large part, domestic SMEs continued to obtain external finance for inventory or working capital purposes, the proportion of those that used external financing for the hiring and training of employees rose significantly and stood well-above that recorded among respondent firms in the EU. This reflects tight domestic labour market conditions. In fact, the proportion of SMEs in Malta citing the availability of skilled staff or experienced managers as their most pressing problem rose above the level recorded in the three years preceding the pandemic.

Access to finance continued to stand among the least pressing problems during the period under review. The share of SMEs in Malta that reported a deterioration in the availability of bank loans was also unchanged from a year earlier. Respondents however, expected availability of bank related products to worsen in the months ahead – though to a lesser extent than that in the EU, where expectations of deterioration among the various types of financing are shared by a significantly larger proportion of firms. Meanwhile, collateral scarcity is still a limiting factor for some businesses.

The SAFE also reveals that a higher proportion of local SMEs reported an increase in interest rates compared to 2021. Domestically, developments were not as strong as those observed in the EU, possibly reflecting the fact that locally the transmission of tighter monetary policy across the euro area, was more limited.