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SELECTED EXTERNAL SOURCES OF THE FINANCING OF DEVELOPMENT

Abstract:

Small and medium enterprises play an important role in the development of the economy of Poland. They are characterized by rapid response capability with reference to market needs, creativity, flexibility and adaptive efficiency and relatively low costs of maintaining jobs.
SMEs are usually prepared for the initial stage of functioning while referring to their own savings, the support of the family and friends. Difficulties in access to capital frequently occur at the subsequent stage of life of the company when it is essential for its further functioning and development. The problem does not only refer to new businesses. Experienced entrepreneurs, who think about further development or expansion, also complain about difficulties in financing.
The access to external financing of Polish small and medium enterprises is dependent on many factors, among which the following should be listed: the size of the company, type of the conducted activity, its financial situation and its individual preferences and possibilities.
The aim of the paper is the evaluation of the access to external sources of the financing of activities of the SME sector in Poland based on literature studies and the information resulting from the research carried out by the Confederation of Lewiatan in the framework of the project "Monitoring the condition of the MSME sector 2014". In the included analysis, the attention has also been drawn to the availability of external sources, directions of their allocation and the achieved results or problems occurring while achieving relevant capital. Recognized the problem of the research work is valid and important because of the role played by SMEs in the development of the Polish economy.

Keywords:

Sources of financing, credits, leasing, loads, EU funds, SMEs.

JEL Classification: M21

Introduction

The sector of small and medium enterprises faces a lot of opportunities for using the forms of financial support for development. They include e.g. credits, loans, credit guarantees, leasing, factoring, franchising etc. In the paper, there are presented the selected sources of the financing of SMEs, paying attention to their availability, directions of allocation of the obtained funds and achieved results or problems occurring while achieving relevant capital.

Classification criteria of the sources of financing

The possessed capital is the condition essential for the functioning of the enterprise of the SME sector, enabling its development, improvement in competitiveness, strengthening its market position, application of new technological solutions or modernization of products and services. [1]

Availability and forms of the sources of financing, most of all, depend on the size of the company and stages of its growth[2], since this influences the potential of the specific company and assessment of its credibility by institutions providing capital.

Financial decisions directed towards the achievement of goals taken by the managers of the SME sector company requires the knowledge of basic properties and functions of capital, which are specified in accordance with different reference points. The following can be listed in here: the equity structure, i.e. the relationship between own capital and foreign capital,[3] or the period of financing with reference to which long- and medium-term capital can be discussed[4]. The processes of the financing of the SME sector activity can be considered from many points of view, which are presented in Table 1.

Table 1 Classification of the sources of financing

Classification criteria	Type of financing
ownership of capital :	• own capital • foreign capital
sources of capital origin:	• internal • external
time of disposal of the specific capital, including capitals:	• short-term • long-term
reason for financing:	• primary, • current activity, • development, or investment processes.

Source: I. Staniec, P. Malicki, *Źródła finansowania małych i średnich przedsiębiorstw w aglomeracji łódzkiej,* [in:] *Wspomaganie i finansowanie rozwoju małych i średnich przedsiębiorstw,* M. Matejun (ed.), Difin, Warszawa 2011, pp. 310–311. W. Dębski, *Teoretyczne i praktyczne aspekty zarządzania finansami przedsiębiorstwa,* PWN, Warszawa 2005, p. 57.

[1] I. Staniec, P. Malicki, *Źródła finansowania małych i średnich przedsiębiorstw w aglomeracji łódzkiej,* [in:] *Wspomaganie i finansowanie rozwoju małych i średnich przedsiębiorstw,* M. Matejun (ed.), Difin, Warszawa 2011, pp. 310–311. 412

[2] *Przetrwanie i rozwój małych i średnich przedsiębiorstw,* F. Bławat (ed.), Scientific Publishing Group, Gdańsk 2004, p. 29.

[3] D. Dziawgo, A. Zawadzki, *Finanse przedsiębiorstwa,* Wydawnictwo Stowarzyszenie Księgowych w Polsce, Warszawa 2011: p. 38.

[4] K. Sieradzka, Po*lityka innowacyjności a rozwój przedsiębiorstw w Polsce [in:] Procesy innowacyjne a rozwój regionu*, Pytlak K., Majerek D., Sieradzka K. et al, Wyd. Politechnika Lubelska, Lublin 2014: pp. 27–40

From the point of view of the company development, while selecting the sources of financing, it is important who the owner of the capital is, since this allows for its classification as own capital or foreign capital. Own capital may come from internal and external sources, whereas foreign capital is always external. It is commonly believed that the basis for the financing of the company operations should be own capital since the period for which it can be used is not specified. The company also has freedom to decide on what these funds are to be used for, they are also without time limit, they are burdened with smaller risk from the point of view of the enterprise. Unfortunately, using own funds, particularly external ones, is often associated with significant costs, which can be higher than in the case of foreign capital[5]

Depending on demands, the financing of the SME activity can be divided into:

- Financing current activities
- Purchase of equipment,
- Purchase of goods,
- Purchase of real estate,
- Fixed assets – credit or lease?
- Bank guarantee?
- Factoring[6].

It should be pinpointed that the problem of financing accompanies the enterprise as early as at the stage of organizing the activity. There arises the issue of the availability and selection of the sources of financing since the availability of the capital for the specific entrepreneur depends on many factors, among which there is the size of the company or the type of the activity conducted by specific entities and their preferences and capabilities. The SME sector in Poland, among others, is characterized by low level of own capital and simple organizational form, therefore, the scope of opportunities for financing the activity is more humble than in the case of large enterprises.[7]

The sources of the external financing of SMEs

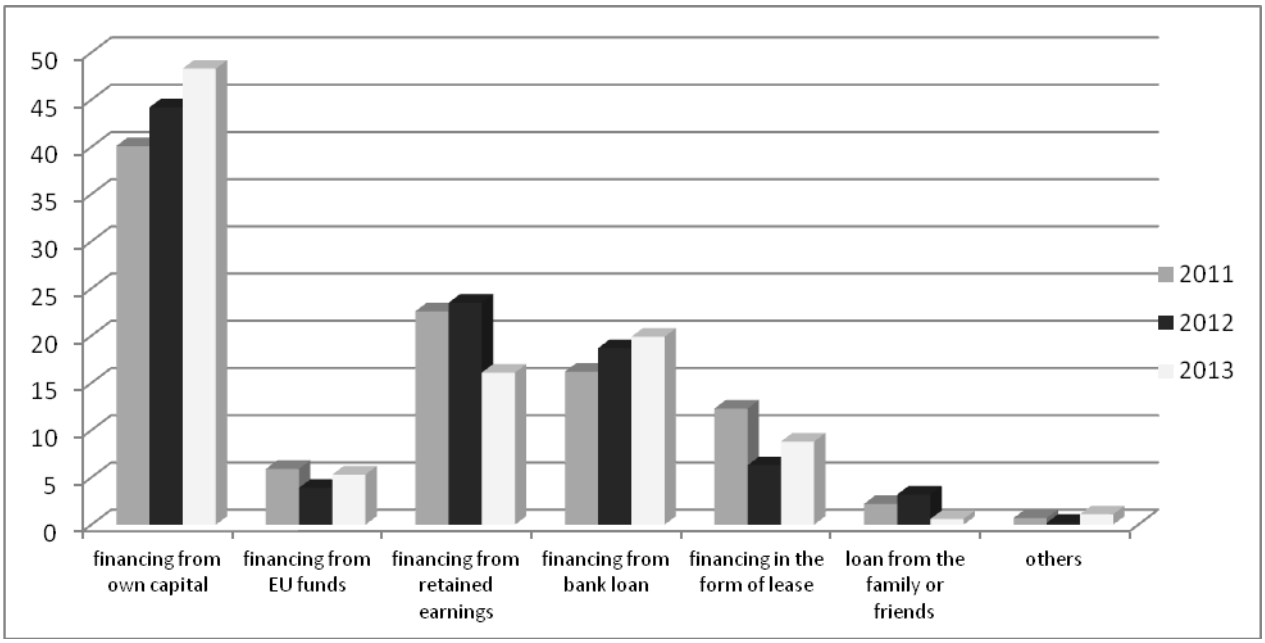
In the Polish economy, the development of an individual business activity is very important, however, for the SME sector, a serious impediment, frequently indicated as the greatest one, has been the limited access to external funding. In 2013 28% of entrepreneurs considered the conditions of the access to credit and credit-related guarantees as the factor negatively influencing the development of the company and its economic situation. Therefore, the funding from own capital was the most frequent source financing capital expenditure. Such a result was not surprising since it had been the most frequent source financing capital expenditure taken into account since as early as 2011 (see: Diagram1)

[5] A. Skowronek – Mielczarek, *Małe i średnie przedsiębiorstwa. Źródła finansowania*, C.H. Beck, Warszawa 2007, p. 20.

[6] Ł. Miernik, *Zewnętrzne źródła finansowania dla Małych i Średnich Przedsiębiorstw,* WWW.metody.eu. accessed on 17.01.2016

[7] J. Brodowska-Szewczuk, *Źródła finansowania rozwoju małych i średnich przedsiębiorstw*, Zeszyty Naukowe Akademii Podlaskiej w Siedlcach No 83 Seria: Administracja i Zarządzanie 2009, p. 136.

Diagram 1. What are the sources your company finances capital expenditure from? (%)

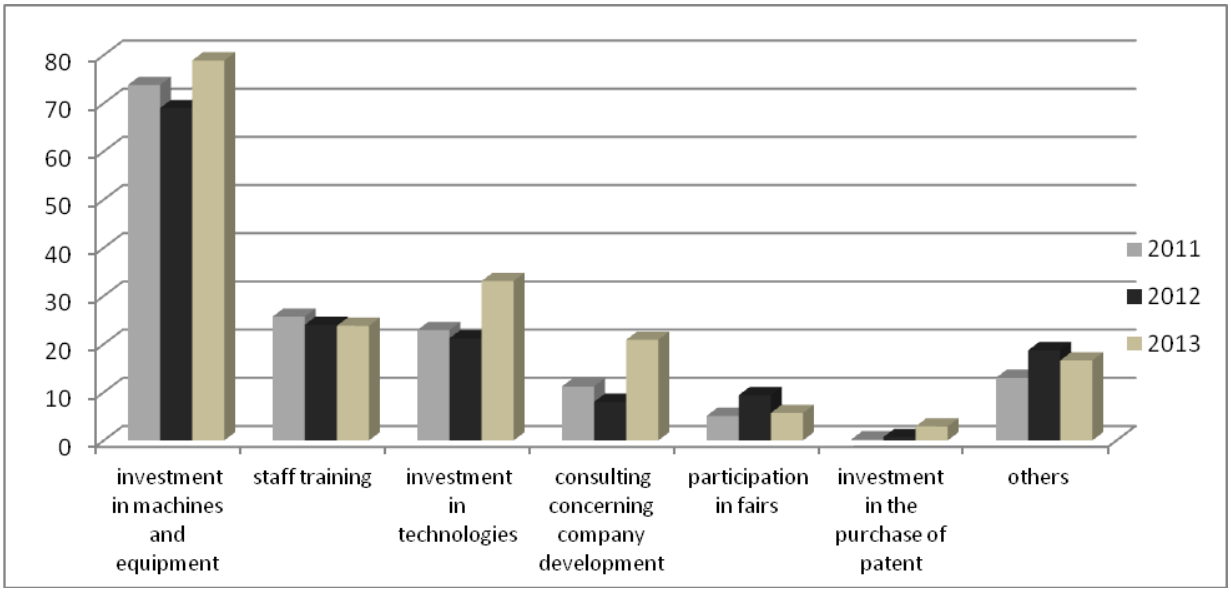


Source: B. Wyżnikiewicz, *Polskie MSP na drodze ku nowoczesności*, Instytut Badań nad Gospodarką Rynkową i Konfederacji Lewiatan, Warszawa 2013, p.53.

Another source of the financing of capital expenditure was funds from retained earnings which, in years 2011-2012, respectively amounted to 22.6% and 23.5%. In 2013 they fell to the level of 16.1% of the total capital expenditure. On the other hand, bank loans, as the source of the financing of capital expenditure, showed a systematic growth from the level of 16.2% in 2011 to 19.9% in 2013. In turn, in 2013 8.8% of the companies used the opportunity provided by lease. However, in spite of a significantly higher share of this type of funding (growth by 2.5% comparing years 2013 and 2012), the trend of 2011 was not recorded. While deciding on the financing of capital expenditure, a surprisingly small number (only 5.3% in 2013) of small and medium enterprises used EU funds, and even fewer (only 0.6% in 2013) used the loan from the family and friends and other forms amounted only to 1.1% of the available sources of financing.

While focusing on the analysis of EU funds and particularly the way of their use, it should be pinpointed that they were mostly used for investment in machines and equipment (78.9% in 2013), i.e. an increase in production capacity or modernization and exchange of old machines. Investment in new technologies was the second important allocation of EU funds: in 2013 it was as much as 33.1%, by 12% more than in the previous year. Expenditure on staff training, in spite of a slight fall in the analyzed years, still constituted an important part of realized investments (23.8% in 2013). Not much less, since 20.9% of the companies, considered the cooperation with entities providing consulting services in the field of company development as the key part, which had amounted to a small percentage in the previous years (respectively: 11.3% in 2011, 8.0% in 2012). (See: Diagram 2)

Diagram 2. What were EU funds, obtained by your company, used for? (%) – the selected items

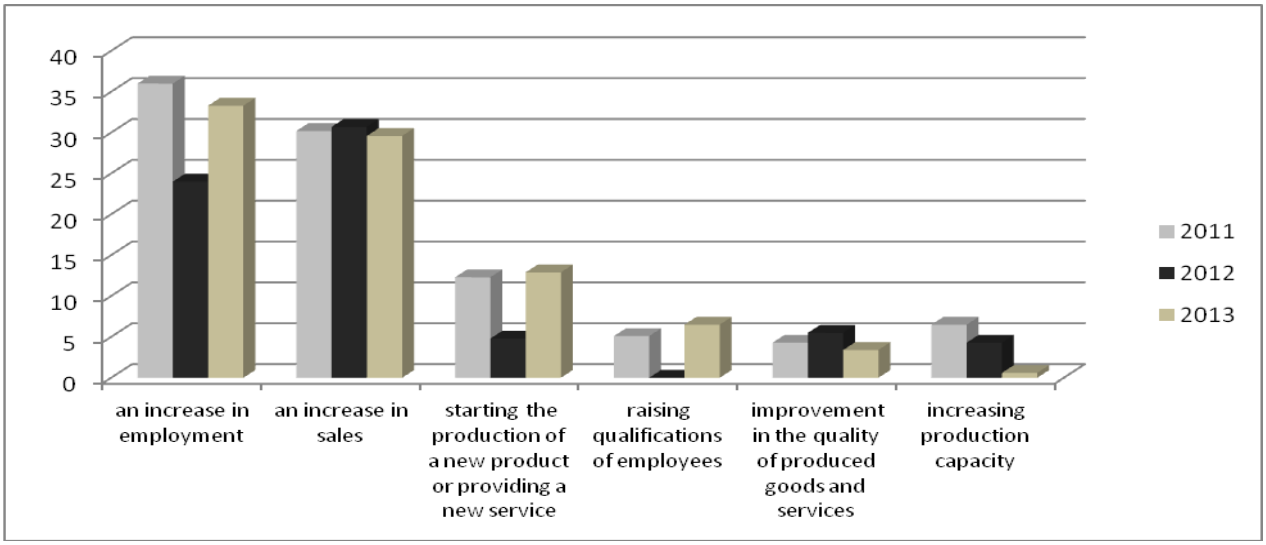


Source: B. Wyżnikiewicz, *Polskie MSP na drodze ku nowoczesności*, Instytut Badań nad Gospodarką Rynkową i Konfederacji Lewiatan, Warszawa 2013, p. 55.

While continuing the analysis of Diagram 2, it can be noticed that the items of minor importance EU funds were used for were: participation in fairs (5.7% in 2013), investment in the purchase of patent (2.9% in 2013) or cooperation with scientific units, universities on the joint project.

Proceeding to the effects achieved due to EU funds, most of all, there should be pinpointed an increase in employment, an increase in sale or beginning the production of a new product or providing a new service or raising qualifications of employees. Undoubtedly, these effects contributed to staying on the market and increasing sales – but they did not have significant impact on long-term growth opportunities of the company since such an assurance-related attitude did not influence the improvement in competitiveness of the company and weakened its power to attract new customers. It should be added that it is, however, the result of a difficult and turbulent environment and the suffered crisis. (See: Diagram 3)

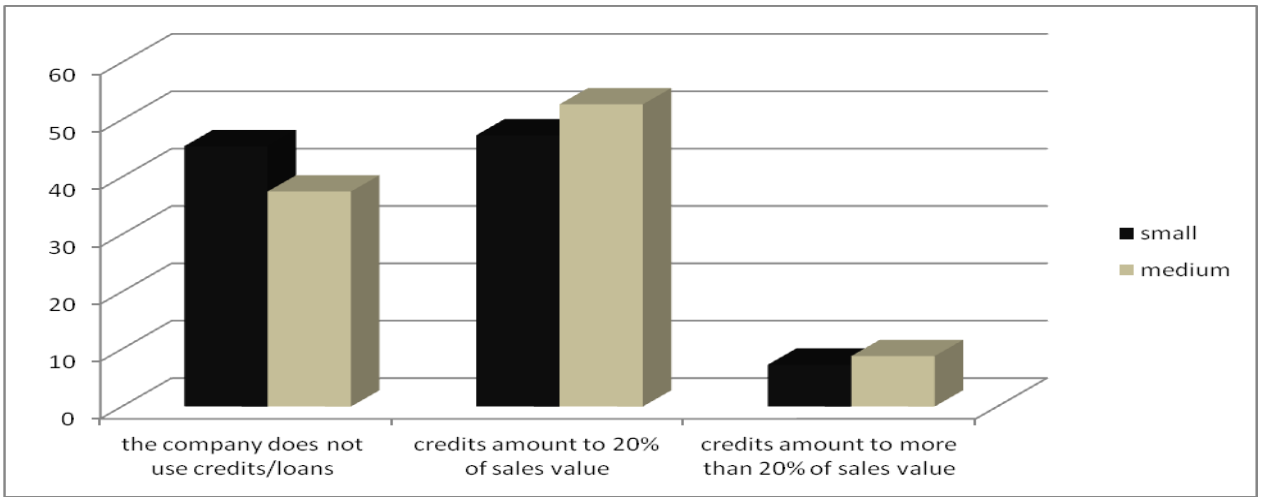
Diagram 3. What results has your company achieved using EU funds (%)?



Source: B. Wyżnikiewicz, *Polskie MSP na drodze ku nowoczesności*, Instytut Badań nad Gospodarką Rynkową i Konfederacji Lewiatan, Warszawa 2013, p. 56.

Small and medium enterprises were and still are careful in using bank loans, which results from the fact that some of them have not been creditworthy, have not had appropriate security in the form of the value of fixed assets or the cost of capital (interest rate, bank commissions) has been too high for them to be covered by revenues and income from their activity. Analyzing the willingness of SMEs to use credits and loans, it can be noticed that medium enterprises used bank financing to a larger extent than small companies. Certainly, this was the result of greater operational and development needs of these entities and their better creditworthiness and greater knowledge of financial liquidity management.

Diagram 4. What is the average percentage share of (long-term and short-term) credits in the enterprise sales value? (% of SME by size class in 2014)

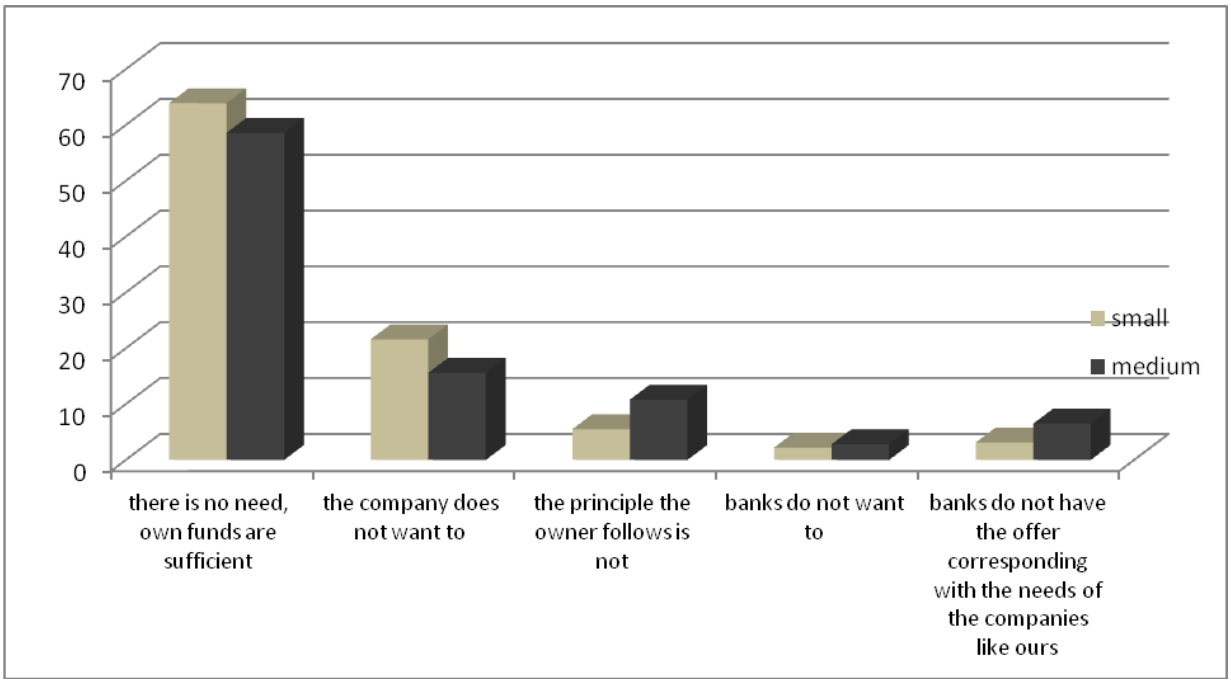


Source: M. Starczewska – Krzysztoszek, *Curriculum Vitae: mikro, małych i średnich* …., op. cit., p.58.

Little willingness of SMEs to use credits and loans was the result of the adopted goals which focused on staying on the market and providing employment and income to the owner and his or her family. Such targets assumed the adjustment of the activity to the

possessed own funds and not referring to credits and risky actions. The subsequent Diagram 5 shows the response to the question why the company does not use credits/loans.

Diagram 5. Why does the company not use credits/loans – indicating one - the most important reason? (% of SMEs by size class in 2014)



Source: M. Starczewska – Krzysztoszek, *Curriculum Vitae: mikro, małych i średnich* …., op. cit., p. 59.

The presented Diagram 5 shows that 63.9% of small and 58.6% of medium entrepreneurs indicated that there is no need since own funds are sufficient for operations and development. In turn, 21% of small and 15.6% of medium entrepreneurs do not want to take risk of borrowing money in such a changing and risky environment since they do not know if they will be able to repay the loan. Therefore, they do not use bank financing or the owner follows the principle of not using credits. It should be added that medium enterprises were more open to external funding than small companies. A small percentage of the analyzed companies talked about resentment of banks towards SMEs, which did not want to grant credits to entrepreneurs (less than 3%), and also about the lack of the offer corresponding with this group of companies. It should be pinpointed that, in the group of medium enterprises, there were more companies talking about the lack of the appropriate product range from banks than among small enterprises - as much as 6.5%.

Analyzing another source of financing – lease, it should be stated that, for investment purposes, SMEs used lease more frequently than bank loans. The reasons for such behavior should be sought in willingness to maintain financial liquidity, better conditions of funding and the fact that the subject of the lease makes money to repay installments or favorable tax regulations. SMEs also paid attention to easy access to leasing companies which not only provide the money for financing the investment in fixed assets but also, due to agreements with the producers of leasing goods, the entrepreneur gains access to these goods without the necessity to search for them on the market. Therefore, the lease allows for rapid access to essential fixed assets and business development which would not be possible from own funds.

The lease also faces the barriers that SMEs agree upon, concerning the fact that bureaucracy is a smaller barrier than high costs. While focusing on three most important barriers, SMEs listed: first, the lack of appropriate product range adjusted to their needs; secondly, the fact that the leasing company retains ownership for the period of the contract, thirdly, the problem in the assessment of the total leasing cost and its comparability to the credit.[8]

Summing up. Small and medium enterprises used different sources of the financing of their activity. The most frequently, they selected funds from own capital or funds from retained earnings, which resulted from unwillingness to take risk or additional costs. It was related to the behavior of Polish entrepreneurs who prefer the strategy of self-financing as the basis for maintaining legal and economic independence as well as the independence of their company[9]. The popularity of credits, as another source of financing,[10] has also risen. However, the lack of creditworthiness or guarantees required by financial institutions and high costs of capital have become the reason for careful credit policy. In turn, diversity of barriers encountered in acquiring the financing of the activity with leasing[11] or EU funds occupied further positions.

Conclusions

The economy of Poland is based on the development of the sector of small and medium enterprises, which play the key role, both with reference to the number of entities and the level of share in creating the national income. Therefore, the right choice of the forms of financing is a very important aspect in the finance management process in the enterprise and it may determine its long-term position on the market.

Small and medium entrepreneurs create the most jobs on the market, showing creativity and involvement, which also frequently results in the development of new advanced technologies. Finally, the companies of this sector also contribute to the global market development. However, SMEs are really prone to negative impact of the external economic and political development. Few entrepreneurs succeed in surviving on the market for more than five years. Therefore, the authorities of many countries, while perceiving the significance and economic potential of SMEs create support programs, companies and research institutes dealing with the analysis of development and activities of this sector. The support given by the State allows to maintain or even increase employment.

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