

**Bank Financing of Small and Medium-sized Enterprise's in Ireland: The Banker's  
perspective**

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Abstract

**Bank Financing of Small and Medium-sized Enterprise's in Ireland: The Banker's  
perspective**

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*This research seeks to gain an understanding of the banker's perception on lending to SMEs in Ireland. Using new and unique data generated from interviews conducted with bankers from four banks, the research seeks to provide information on bank financing of SMEs in Ireland. The study found out that perceived profitability and cross-sale opportunities are the major drivers for banks involvement with the sector. Dominance of two major banks, issues relating to Brexit and regulations are the major impediments. Due to size of the SME segment, most banks have different organizational set ups to serve the market. Activities such as Loan approval, Risk management and loan recovery function are centralized while loan origination, initial screen and sale of other products to SMEs are carried out at the branches.*

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## **DEDICATION AND ACKNOWLEDGEMENTS**

Firstly, this dissertation is dedicated to Almighty Allah, for His Inspiration and Sustenance towards me during this program. My sincere gratitude and appreciation go to Almighty Allah for his continued blessings and protection over my life. You alone we worship and You alone we ask for Help.

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## **List of Abbreviations**

CBI – CENTRAL BANK OF IRELAND

CRO – CREDIT REVIEW OFFICE

ECB – EUROPEAN CENTRAL BANK

EU – EUROPEAN UNION

OECD – ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT

SMEs - SMALL AND MEDIUM ENTERPRISES

## CHAPTER 1 INTRODUCTION

### 1.1 MOTIVATION AND SIGNIFICANCE OF STUDY

*“Access to capital is critical for small business success and crucial to our economic recovery. Without access to capital, many small companies are not able to maintain operations, let alone expand and create new jobs”.*

Sam Graves.

The importance of Small and Medium Enterprises (SMEs) to any economy cannot be overemphasized in terms of employment generation, economic growth etc. In Ireland, small and medium enterprises account for 99.7 per cent of all active business enterprises as well as employing 71.0% per cent of the workforce and they are also responsible for over half the Republic’s annual turnover (Ireland SBA Factsheet, 2016). However, a major impediment to the further growth of SMEs is finance. Because of their relative importance to any economy, the problems associated with the financing of SMEs has been a source of interest to stakeholders such as policy-makers, entrepreneurs, bankers as well as researchers. Lending to SMEs is widely considered to be fraught with risks. With their importance to any economy, it therefore, stands to reason for continuous research into bank financing of SMEs and SMEs relationship with banks. It is imperative to research on the various drivers and impediments to SMEs financing to ensure their continued growth and success. Research on how the relationship can continue to be symbiotic and mutually beneficial for all parties concerned is important.

There has been extensive research into the financing of SMEs around the world (e.g. Ramaswamy, 2014; McCarthy, Oliver and Verreyne, 2016; Liu and Wang, 2013; Yamb and Ndjek 2016); however, a common theme among the research is the fact that they mostly relate to the views of the SMEs and not the supply-side i.e. banks. This means that the results could be skewed, and action taken based on those researches might be wrong as the other party perception have not been adequately heard. This research will seek to bridge this gap by analyzing the banker’s perspective of the issues relating to financing of SMEs in the Republic of Ireland. The research also aims to provide empirical analysis that will help shape future government policies on SMEs. This is expected to be achieved by analyzing banker’s views on current government incentives and initiatives aimed at SMEs. By analyzing banker’s perception of the SMEs segment, we aim to provide information that help to have more informed prospective borrowers who are aware of the drivers and obstacles to their relationship with banks.

Also, while there have been a few empirical studies which focused on finance ‘supply side’ in various other countries such as Beck, Demirgüç-Kunt and Peria which studied bank lending to SMEs by 91 banks in 45 countries (Beck, Demirgüç-Kunt and Peria, 2008). A study into bank lending to SMEs in Serbia was carried out by a team from World Bank (World Bank 2007a) while a similar study on Latin America and the Caribbean was carried out by de la Torre, Peria and Schmukler (de la Torre, Peria and Schmukler, 2008). Quartey, Turkson, Abor and Idrissu also carried out a research on SMEs financing constraints in the Economic Community of West African States (ECOWAS). There appears to be no such study on bank relationship with the SME sector in Ireland. This research is therefore important as it helps bridge such existing gap in literature.

This study will therefore attempt to address the gaps mentioned above through the analysis of data generated from four sampled banks in Ireland. The study will conduct semi-structured interviews with bankers from the four banks. Due to access issues, convenience sampling will be used. The research focuses only on banks that have relationships with bank and will benchmark result with results from previous studies.

## 1.2 RESEARCH OBJECTIVES

- To gain an understanding of the banker's perspective on lending to the SME sector in Ireland.
- To determine the various drivers and impediments to SMEs financing in Ireland.
- To study the effect of government policies and incentives on the SMEs financing in Ireland.
- To gain an understanding of how banks engage with the SMEs segment in Ireland.

## 1.3 RESEARCH QUESTIONS

- **Objective 1** – The bankers' perspective of the SMEs sector in Ireland
  - Do bankers view SMEs as a profitable sector to finance?
  - What is the banker's definition of SMEs?
  - How does the bankers perceive the prospects of the SMEs sector?
  - Are there additional criteria set by bankers before granting of SMEs loan application?
- **Objective 2** – What are the drivers and impediments to bank financing of SMEs in Ireland
  - What collateral or security are more favored by banks?
  - To what extent does credit score or rating play a part in consideration of a loan application?
  - What effects does increased competition have on the SMEs lending environment?
  - What are the effects of the macroeconomic environment on SMEs lending?
  - To what extent does the size of the firm, cash flows, financial statements, age of the firm affects the loan application?
- **Objective 3** – The effect of government regulation and policies on the SMEs sector
  - What is banker's perception of current government policies and regulation as regards lending to SMEs?
  - How does the banks rate the current government incentives and programs?
  - What further regulatory changes can be implemented to further enhance the SMEs-Bankers 'relationship'?
- **Objective 4** – How banks engage with SMEs?
  - What operational changes have been made by banks to accommodate the SMEs sector?
  - Does the bank have specialized departments that deals with SMEs?

#### **1.4 STRUCTURE OF THE DISSERTATION**

This dissertation is divided into five chapters. Following the introduction, Chapter 2 review the relevant literature and theoretical background of the dissertation. In this chapter, capital structure is established as the relevant theoretical framework and Pecking Order theory is identified as the capital structure theory which explains SMEs decision on how to finance their assets and operations. Recent and relevant body of works which have similar theme as this dissertation are reviewed in this chapter. Chapter 3 describes the research methodology and approach used in this dissertation. Phenomenological approach was adopted as it aligns with the research objectives. The chapter also discussed the data sources, data collection and the research instruments used for the dissertation. The reasons for the choice were also enumerated in the chapter. The analysis of the data generated from the interviews are explained in Chapter 4. The chapter also elaborates of the various findings made while conducting the dissertation. The comprehensive analysis explicitly answers the research questions. The final chapter provides an opportunity to highlight the major findings of the dissertation and provide some concluding thoughts on them. Recommendations on how to foster better relationships between the banks and SMEs were given and recommendation for further research on the subject matter were also given.

## **CHAPTER 2                    LITERATURE REVIEW**

### **2.1     INTRODUCTION TO LITERATURE**

SMEs are integral to any economy, but a major source of issues is the definition of what an SMEs is. SMEs have been previously defined in terms of their annual turnover, employment and total assets. Lawless, McCann and Calder (2014) defined small firms as those whose total employees are between 10 and 49, medium firms as those with employees numbering between 50 and 249 while large firms typically have over 249 employees. The Central Bank of Ireland (CBI) and the Credit Review Office (CRO) in defining SMEs uses a combination of employment (less than 250 employees), annual turnover (less than €50million) and balance sheet (less than €43m). This definition is in tandem with the new European Union (EU) definition introduced in 2005. The EU definition further categorized SMEs into three namely: micro enterprises (less than 10 employees), small enterprises (between 10 and 49 employees) and medium enterprises (between 50 and 249 employees). Beck (2013) alludes that an important dichotomy in defining SMEs is the distinction between formal and informal enterprises. Informal enterprises are usually seen as being the same as micro-enterprises. However, it is also important to be aware that the distinction between SMEs and large enterprises goes beyond pure size. Organizational, behavioural and other dimensions differ between SMEs and large enterprises. SMEs can be found virtually in all sectors in Ireland. It is not uncommon to find SMEs in Agriculture, Manufacturing, Wholesale/Retail, Education, Transportation, Construction, Hotels and Restaurants, Education and Professional services.

This literature review will firstly discuss the supply of finance to SMEs and the importance of SMEs to economic growth and development. It will then discuss the impact of the 2008 global financial crisis on the SME lending environment. To provide a theoretical framework for the study, the research discussed the capital structure and the various capital structure theories and then relate the theories to the capital structure decisions made by SMEs.

### **2.2     SUPPLY-SIDE FINANCE TO SMES**

A large number of studies based on various surveys have shown that access to finance is one of the main challenges to the growth and development of SMES (Peachey, 2004; Beck, 2008; ECB 2012). In 2013, The European Central Bank (ECB) conducted a survey on the access to finance of SMEs in the Euro area. The survey showed that “Access to finance” (16%) was the second-ranked most important issue being faced by SMEs in the euro area. At the top echelon, 32% of those surveyed SMEs in Greece, 23% of those surveyed in Spain and 20% of those surveyed in Ireland, Italy and the Netherlands mentioned access to finance as the most important problem encountered by SMEs while SMEs in countries like Germany and Austria reported a lower degree of concern for lack of finance. Due to their inability to meet up with the exorbitant costs of listing, strict listing requirements, lack of required managerial skills, low capacity and reputation, SMEs usually have little to no direct access to the stock market and as such rely on banks for external funding.

A major source of finance for SMEs are loans from banks. Commercial banks are the primary suppliers of financial products to SMEs (Mach and Wolken, 2006). They provide a wide range of financial services to their SMEs customers such as support and advice on financial issues. However, SMEs are susceptible to failure when compared to relatively larger firms as they are characterized by a higher degree of output and profit volatility (Lawless and McCann, 2011).

Manufacturing enterprises with less than twenty employees have been found to be five times more likely to fail in a given year than larger firms (OECD, 2006). Could this be the reason for the perceived lack of finance and higher costs of finance to SMEs? In July 2011, a survey carried out by the Institute of Certified Public Accountants in Ireland (CPA) showed that 87% of its members believe banks are not “open for business”. Also, 61% of CPA members opined that viable business has had their loan applications rejected by banks which gives credence to the reduced supply of finance to SMEs as at that time. This gives credence to the reduced supply of finance to SMEs as at the time the survey was conducted. In comparing the extent, pricing and type of financing banks extend to SMEs, Beck et al (2008) observed that banks have a lower level of exposure to SMEs compared to larger firms. They also experience a higher number of defaults on these loans and charge higher fees and interest rates on loans to SMEs. Various studies have also come to show similar results: access to credit is one of the biggest constraints for SMEs in Colombia (Stephanou and Rodriguez, 2008). Previous rejection experience of loan applications by banks have led to a situation known as the discouraged finance seeker in Australia (Xiang, Worthington and Higgs, 2015). This is based on the idea that SMEs do not seek finance even if needed because they believe that a loan application will be turned down given their previous experience. Undoubtedly, this lack of finance and increased costs hamper the growth of new and existing SMES. Hutchinson (2006) found out that the inability to raise finance is a major reason for the underdevelopment of SMEs in Slovenia. Despite the costs and difficulties associated with raising finance from banks, bank loans still remain an integral part of SMEs balance sheet. A World Bank group study in 2007 shows that banks in Chile and Argentina have a significant level of exposure to SMEs in terms of loans with the exposure being higher in Argentina than Chile. This shows that banks perceive the SMES sector as being profitable and the implied costs are less than the benefits. A survey of banks in Ireland, the Bank Lending Survey carried out by the Central Bank found reports of credit standards tightening between 2008 and 2010 and remaining unchanged since July 2010. This survey also reported credit demand falling from 2008-10 and stabilizing since late 2010. This, however, had to do with lending generally in the Irish economy and not just peculiar to SMEs.

### **2.3 SMES AND ECONOMIC GROWTH AND DEVELOPMENT**

The importance of Small and Medium Enterprises (SMEs) to any economy cannot be overemphasized in terms of employment generation, economic growth, innovation, nation building etc. Management guru, Peter Drucker (2009) stated that small enterprises represent the main catalyst for economic development. SMES contribute intensely to achieving the fundamental goals of any national economy, becoming the backbone of social economic progress (Drucker, 2009). SMEs are a great example of risk-taking and initiative taking as they have a relatively small size and can easily adapt to changes in requirements (OECD, 2006). As the world moves to the knowledge-based economy, this above feature becomes important (Popescu, 2016). SMEs serves as the backbone of the EU’s economy. In 2016, 99.8% of the enterprises that operated in the EU non-financial business sector were SMEs. They have over 93 million employees representing 67% of the total employment in the business sector as well as generating 57% of the value added in the business sector (EU Annual report on European SMEs 2016/17). The non-financial sector consists of all economic sector of the member states of the EU. Exceptions to this sector are governmental activities, financial services, education, health, arts and culture. In Ireland, small and medium enterprises account for 99.7 per cent of all active business enterprises as well as employing 71.0% per cent of the workforce and they are also responsible for over half the Republic’s annual turnover

(Ireland SBA Factsheet, 2016). The United Kingdom has one of the most vibrant SMEs sectors in the EU area. As at 2015, the sector employs over 10m employees representing 53.6% of the total employees and 1.8m enterprises representing 99.7% of the total enterprises in the country (United Kingdom SBA Fact Sheet, 2016). For developed countries, there is a positive relationship between entrepreneurship and economic growth while evidence suggests a converse relationship between entrepreneurship and economic growth in developing countries (Van Stel, Carree and Thurik, 2005 and Wennekers, Van Stel, Thurik and Reynolds, 2005). SMEs are the main player in Indonesian domestic activities as they act as the substantial provider of employment opportunities and consequently provider of primary and secondary sources of income for most households (Tambunan, 2008). SMEs also plays a role in the class caste system. In Romania, the SMEs sector acts as the main source for forming the middle class as they play a decisive role in maintaining the social-political stability of the country (Neagu, 2016). After establishing the importance of SMEs to economic growth and development and identifying finance as a major inhibitor to SMEs growth, it is therefore imperative to research on the various drivers and impediments to SMEs financing to ensure their continued growth and success (Beck et al, 2008; Rupeika-Apoga, 2014; Beck, 2013). This explains and gives credence to the significance of this study.

## **2.4 GLOBAL FINANCIAL CRISIS AND SMES**

As a result of limited financial capital, size and reliance on external finance (bank loans), the 2008 global financial crisis had a global impact on SMES (Vermoesen, Deloof and Laveren, 2013). A bank lending survey conducted by the ECB upholds that the global crisis significantly reduced the availability and provision of loans to SMEs in the Euro area (including Ireland). Lack of diversification in their customer base, markets and suppliers also increase the difficulties faced by SMEs in maintaining their level of activity during the crisis (OECD, 2009). Unlike their large enterprise counterparts, their relative lack of technological, human and managerial capabilities also reduced their abilities to overcome the economic crisis (Bourletidis and Triantafyllopoulos, 2014). The finance constraints faced by the SMEs increased the likelihood that European SMEs will use informal lending (such as trade credit or leasing) or loans from other companies but not apply or use market finance (Casey and O’Toole, 2014). In periods of recession, Financial Institutions in the United Kingdom (UK) use firm size as the primary lending deciding factor with SMEs particularly restricted in their access to capital and lenders seems to ignore growth projections of SMEs (Cowling, Liu and Ledger, 2012). In Belgium, Vermoesen et al (2013) concluded that there was a statistically and economically significant reduction in investments in Belgian SMEs in 2009 caused to a large extent by the reduction in the credit supply as induced by the financial crisis. The latest bank lending survey by the ECB (covering October 2017-March 2018) indicates that the availability of skilled labor and difficulty of finding customers are the dominant concern for SMEs in the Euro area while access to finance was considered the least important obstacle. The change in SME lending environment and perspective can be attributed to the various expansionary monetary policies and governmental stimulus implemented by the ECB and the monetary authorities in various countries to tackle the financial crisis (ECB, 2017). In all, the financial crisis raised concerns about the reliance of non-financial corporations in the EU on banks for external financing especially the SMES which usually have little to no access to direct capital markets (ECB, 2015). From above we can see that during the period of economic crisis, SMEs faces multifaceted problems ranging from customers, suppliers, source of finance to sourcing of labor skills.

## 2.5 CAPITAL STRUCTURE AND CAPITAL STRUCTURE THEORIES

The literature review has focused on the supply of finance to SMEs, SMEs importance to economic growth and development and how the global financial crisis impacted the SMEs. The review will now turn to capital structure and the various academic theories that surround this topic.

Capital structure, for the most part, alludes to how an organization is being financed and there are commonly two sources of finance namely: equity and debt. An organization could be financed by either of the two or by both sources of finance. A major responsibility of a finance manager is determining the optimal mix of debt and equity to be used in financing the organization's activities (Channar, Maheshwari and Abassi, 2015). Capital structure alludes to the manner in which a company utilizes the mixture of debt, equity or hybrid obligation securities to finance its assets. (Saad, 2010). Brigham and Davies (2004) expressed that the capital structure is the manner by which a firm funds its total assets, current operations and any expected growth through the issuance of debt, equity and hybrid securities. To finance their activities, organizations use debt instruments like loan notes, bonds, equity instruments like retained earnings, common stocks or shares as well as hybrid instruments which has the characteristics of both debt and equity instrument. However, a major headache for finance managers is in determining the right or optimal capital mix to utilize (Channar et al, 2015).

Several theories have been hypothesized on the optimal capital structure. The major significant establishment for discussion on Capital structure was laid by Franco Modigliani and Merton Miller in 1958. They hypothesize that the capital structure of a firm has no impact on the value of a firm under a perfect market condition (Modigliani and Miller, 1958). The assumption of a perfect market includes, no transaction cost, no taxes, market efficiency, information symmetry, no taxes and investors are rational and faces homogeneous risks. Following Modigliani and Miller debt irrelevance theory, several researchers have advanced several debt relevance theories by relaxing the perfect market assumption inherent in Modigliani and Miller's theory. The Modigliani and Miller theory of capital structure Proposition I was laden with numerous implausible presumptions based on the idea of a perfect market. In 1963, Modigliani and Miller introduced taxes into their model. This prompted the improvement of the Modigliani and Miller Theory of Capital Structure Proposition II where tax-related benefits of debt were offset by the costs of financial distress (Bhaird and Lucey, 2010). Under Proposition II, the value of a levered firm is equivalent to the value of an unlevered firm and tax shield. Debt as a source of capital has the advantage of its interest payments being tax deductible (tax shield).

Throughout the years, researchers have extended the theory of capital structure. According to Michaelas, Chittenden and Poutziouris (1999), the theories could be extensively separated into three classifications to be specific; tax-based theories, agency cost theories, asymmetric and information signalling theories. Tax-based theories are based on the idea that tax and bankruptcy effects ought to be the essential reason affecting the capital structure decisions of an organization (Michaelas et al). As interest on debt reduces taxation paid on income, profitable firms with smaller



non-debt tax shields should utilize more debt than less profitable firms (DeAngelo and Masulis, 1980). As per these theories, firms paying taxes should substitute debt for equity as a source of finance up to the point where the costs of financial distress become significant. However, practically speaking, firms don't take after this strategy especially SMEs (Ray and Hutchinson, 1993). SMEs are expected to be less profitable and have less use for tax shields when compared to the profitable larger firms (Pettit and Singer, 1985). Agency costs theories emerge due to conflict of interest between stockholders and bondholders. The agency costs theory was progressed by Jensen and Meckling (1976). The consistent message of the theory is that such conflict creates motives for stockholders to take actions which benefit their interest at the expense of bondholders and that such actions may not necessarily maximize firm value (Micheals et al, 1999). A particular type of firm that is said to have a lower agency cost is the family-owned firm. Due to the lack of dichotomy between owners and managers as family members owning a large proportion of the firm, the belief is that the structure helps prevent agency problems from arising (Steijver and Voordeckers, 2009). The alignment of family interests, however, comes at a cost for debtholders (Niskanen and Niskanen, 2010) and also importantly, altruism and lack of self-control can lead to increase in agency costs for firms that are family-owned (Sharma, 2004 and Lubatkin, Schulze, Ling and Dino, 2005). As a result, family firms are more susceptible to the twin negative effects of altruism and lack of self-control. In a study of Australian family-owned- firms, Xiang et al (2014) concluded that altruism effect can increase agency costs in family firms as the effect is embedded in the relationships within the firm and altruism is an embedding factor in agency costs of family-run firms. Information asymmetries theories are based on the dissimilarity of information available to 'inside' managers and 'outside' investors. Managers and insiders in the firm due to their positions usually possess private information on the firm's return streams, growth trajectory and return opportunities which are not available to outsiders. These costs act as the focal point of asymmetric and information signalling theories. The major conclusion from this theory is the signalling theory (Ross, 1977) and the pecking order theory (Myers, 1984), which states that organizations should choose capital, based on the relative costs of the various sources of finance which reflects the information asymmetries. The pecking order theory is based on the idea that firms prefer to finance investment opportunities using internal equity, when the internal equity is used up, they then use debt finance before utilizing external equity as a means of last resort (Myers, 1984).

## **2.6 CAPITAL STRUCTURE AND SMES**

While there have been various studies on the capital structures, little has been done on the capital structures of SMEs (Hall, Hutchinson and Michealas 2004; Sogorb-Mira, 2005). The research on the capital structures of SMES is a neglected and much-ignored area of research (di Pietro, Palacín-sánchez and Roldán, 2018; Forte, Barros and Nakamura, 2013; Menike, 2015; Rossi, 2014; Zingales, 2000). Bhaird et al. (2009) investigates the applicability of theories of capital structure in a sample of Irish SMES by empirically testing the effect of firm characteristics on the sources of debt and equity employed. The research shows that firms source finance in the manner predicted by Myers' (1984) pecking order theory. A high level of fixed assets is financed by pledging

collateral to secure debt finance. The pecking order theory assertion of SMEs is also supported with the assumptions bothering on the age and profitability of SMEs, Berger and Udell (1998) concluded that as time goes by, SMEs uses less debt. Ang (1991) also pointed out that pecking order theory applies to SMEs except subcontracting SMEs or SMEs which are in a group arrangement. Lopez-Gracia and Sogorb-Mira (2008) in a study of a sample of Spanish SMEs spanning a 10-year period found evidence that SMEs follow a funding source hierarchy even though a greater trust is placed on SMEs that aim to reach an optimum leverage level (trade-off theory).

The pecking order theory is more relevant for the SME segment when we consider the greater information asymmetries and higher cost of external equity for SMEs (Ibbotson, Sindelar and Ritter, 2001). Some studies even go ahead to report that some firms operate under a constrained pecking order, and do not consider raising external equity (Holmes and Kent, 1991 and Howorth, 2001). Even when the owners have insufficient firm assets, they secure loans using the assets of the firm owner (Di Pietro et al, 2018; Menike, 2015). Control and managerial autonomy are also a major reason for debt finance preference by SMEs owners. Due to the desire of the SMEs owners to retain the control and maintain managerial independence, it's not uncommon that they prefer debt finance (Chittenden, 1996). Equity has the effect of diluting the stock ownership, earning and control in a firm as well as having a higher cost than debt as equity owners need to be paid a premium for the higher level of risk they have undertaken (Sogorb Mira, 2005, Ou and Haynes, 2006). Empirical evidence suggests that the ownership structure of a firm has a significant effect on the desire for control, with consequent implications for financing (Bhaird and Lucey, 2010). Family-controlled firms have a greater desire for control and exhibit an aversion to external financing (Mishra and McConaughy,1999). Empirical evidence from Italy using Amore, Minichilli and Gorbetta (2011) indicated that the appointment of non-family professional CEOs leads to a significant increase in the use of debt driven by short-term maturities.

While not necessarily a preferred source of financing, a good number of SMEs in certain sectors of the economy use external equity as a means of financing their investment opportunities (Hogan, Hutson and Drnevich 2007). Equity could be in the form of private or public equity. A public equity offering offers SMES benefits that transcend from initial capital offerings (IPO) to longer-term repeat access to financing, increased creditworthiness, transparency, visibility and larger access to finance (Nassr and Wehinger, 2016). These benefits, however, come with certain costs like high admission cost and stringent listing requirements in the stock market are usually too high for SMES. The small high-tech ventures are a good example of a sector where external equity financing is more common than debt (Hogan, et al 2017). They found out that the “greater the owner’s perception of information asymmetries in debt markets, the larger the perception of external equity in the firm’s capital structure”. Unlike the general population of SMEs, high tech small firms face a higher information asymmetry in the debt market (Bank of England, 1996; Berger and Udell, 1998; European Commission 2003). The high level of human capital involved and the information asymmetries between owner and external financiers (banks) makes it difficult to value high-technology business and to advance finance to them.

A popular means of external finance is the funds provided by Business Angels (BAs). In recent years, BAs as a form of external equity finance have gained prominence providing €6.7 billion annually for SMEs in the European Union (EBAN, 2018). The number of networks of BAs in Europe has experienced an increase of over 100% from 228 in 2005 to 474 in 2018 highlighting the tremendous growth in the use of finance provided by BAs (EBAN, 2018). BAs are particularly interesting for SMEs that not just want financial capital, but also want to benefit from the kind of mentorship, assistance, expertise and networks provided by BAs. For family businesses, private equity minority investments have become an attractive alternative means of finance. This is however not in tandem with the popular belief as regards the objective of the family business in preserving their continuous and unlimited influence on the business since such private equity will mostly lead to the partial secession of control to the private equity investor. Succession problems and lack of capital attract family firms to private equity (Upton and Petty, 2000). For Tappeiner, Howorth, Achleitner, and Schraml (2012), non-financial benefits because of cooperation with investment managers is the major driver for family firms seeking private equity minority investments. Franke (2005) concluded that private equity financing is mostly used by family firms when they are confronted with complex challenges that cannot be solved with only debt financing and they require equity capital and professional financial investor and neutrality of an external shareholder. BAs, venture capitalists and other forms of private equity are important to SMEs as they are providers of value-added finance to SMEs businesses they invest in. Private equity investors create economic value by imbuing strategic, operational and financial efficiency in their portfolio of companies (Kaplan and Stromberg, 2009). They stay involved in the business, even after the initial investment period acting as a guide and bridging the knowledge gap which can be an added advantage for the SMEs. Cumming, Siegel and Wright (2007) also suggest that better corporate governance can be associated with firms with private equity investments. They, however, aim to exit their investment profitably within a certain time horizon ranging from about three to five years (Fraser-Sampson, 2010). There are however costs associated with using business angel as a source of finance. The high risks taken by business angels mean they also demand for high annual return which could be in range of 20% or 30% (ACCA, 2018). Control issues can arise if a large amount of equity is taken by a business angel, the greater the equity taken, the greater the exit costs (Olaore and Adetoye, 2014). Crowdfunding, peer-to-peer and other similar equity financing options can also help prevent the need for debt financing (Franke, 2005).

## **2.7 DRIVERS AND IMPEDIMENTS TO FINANCE**

As a major provider of finance to SMEs, it is important to research the key factors that impact SMES lending. Such research should be able to provide answers to question such as; What factors does bankers see as driving forces for SMEs lending? What factors deter them from granting a loan application by SMEs? How does the level of profitability, non-financial indicators, financial statements, securities or collaterals affect the granting of a loan application to SMEs? Beck et al (2008) found out that 80% or more of the banks studied agreed that perceived profitability is the major driving force of the relationship with the SMEs segment. Although differences might arise between private-owned enterprise and government-owned enterprise with the profitability higher in the rank of the former, a better relationship will be expected when the banks perceive the SMEs

to have good profitability prospects. In addition to the study above, World Bank (2007a) concludes that the key driver for SMEs lending in Serbia is the perceived profitability of an enterprise. The banks studied were of the opinion that the profit potential from SMEs lending is high and in fact higher than lending to large enterprise. Other factors that drive SMEs lending in Serbia include; competition among the banks, over-exposure to retail customers and other segments and the need for diversification (World Bank, 2007a). In a study of Baltic States, Rupegia-Apoka (2014) concluded that the availability of financial funds depends on company development level, the bigger and familiar you are the broader choices you have. As such, it is quite important for new companies to seek alternative resources such as business angels, venture capitals, seed funding and take advantage of various government support programs. In Ireland, credit standards on loans to enterprises loosened slightly in 2017 Q4, across the small enterprise, medium enterprise, large enterprises, long-term loans except for short-term loans. “The drivers of this loosening were competition from other banks, expectations regarding economic activity and industry-specific outlook” (Bank Lending Survey 2018).

On the other side, certain factors act as obstacles when lending to SMEs. A uniform trend that can be noticed from the paragraph above is profitability and how it is a key driver in SMEs lending. This study will now assess if there are also uniform reasons acting as obstacles to SMEs lending. Interestingly, Beck et al (2008) found out that the major obstacles varied from developing countries to developed countries. While developed countries perceived competition in the SMEs segment as the top obstacle, the developing countries see the macroeconomic environment as the top obstacle. Like above, there was also a noticeable difference in opinion between government-owned banks who viewed regulation and macroeconomic environment as the most important obstacle, and the privately-owned banks who viewed the degree of competition in the SMEs segment and macroeconomic environment as the most important obstacles. Silva and Carreira (2010) identified that the size of a firm and its cash flows plays an important part in the firm accessing of finance while the age of the firm play no significant part. Schiffer and Weder (2001) in a cross-country study revealed that there is a negative relationship between the size of a firm and the risk it poses to the lender. Beck, Demirgüç-Kunt and Maksimovic (2004) showed that small firms benefit disproportionately from higher levels of property rights protection. Lack of collateral, low creditworthiness, minimal cash flows, lack of credit history, higher risk premium, high transaction costs and lack of proper bank-borrower relationships are major reason obstacles for SMEs accessing finance in sub-Saharan Africa (Quartey et al, 2017). World Bank (2007b) studied banks in Argentina and Chile and perceived SMES-specific factors as a major deterrent in dealing with SMEs. SME-specific factors are factors that affect only SMEs without affecting other firms that operate within the same legal, contractual and regulatory environment. These factors include lack of formality, low-quality balance sheets and lack of adequate guarantees. To circumvent the legal and contractual environment in which banks operate, banks adapt to it by offering products that bypass existing deficiencies in the system (World Bank 2007b).

## **2.8 CONCLUSION**

In the literature review, the study has sought to provide an empirical and theoretical background for our chosen area of research. The literature review started with the definition of what SMEs are. This distinction was necessary to distinguish SMEs from the large enterprise. This is paramount as large enterprises do not naturally face the same financing issues as small enterprises. The study

went on to discuss how important finance from banks is to SMEs. The focus on banks rather than other financial institutions and non-financial institutions is because studies have shown that the main source of external finance to SMEs across most countries are the banks (Beck et al,2008). The study analyzed various literature that shows the importance of SMEs to economic growth and development as well as the impact of the 2008 global financial crisis on SMEs around the world. To provide a theoretical background for our research, the research discussed capital structure and capital structure theories. Pecking order theory was highlighted as the main capital structure theory that supports SMEs decisions on how to finance their assets and operation. However, there is still a need for research in this area to fully understand the preference of the bank. There is also a need to gain an in-depth understanding of the various drivers and impediments to their relationship with SMEs in Ireland. The research also hopes to help plug the gap in the literature on banker's perspective of SMEs financing in Ireland. The research is also necessitated by the need to have an analysis of the various government initiatives and incentives to support SMEs in Ireland. This can help shape future government policies. The literature review section was concluded by exploring various literature that showed perceived profitability, competition among banks and the need for diversification as the major driving force for SME lending. The literature also showed that impediments to SMEs lending include: competition in the SME segment, the size of the firm, macroeconomic environment, SME-specific factors etc.

The study will now turn to the methodology section. This section will outline the research philosophy and approach used to gain data to answer the research questions. The section will provide insights on the study's population, sample size and sampling technique. It will also discuss the data sources, data instruments as well as ethical and access issues relating to the research.

## **CHAPTER 3: RESEARCH METHODOLOGY**

### **3.1 INTRODUCTION**

The last chapter provided an opportunity for a comprehensive review of the relevant literature and theoretical background for SMEs financing in Ireland and around the world. The chapter also helped in the pointing out the suitable research methodology and approach for this study. In this research methodology section, the discussions will center around the study's research philosophy and approach. The structure is as follows: the first section discusses the various types of research philosophy, the two main traditional research approaches and research paradigm. The section shows the importance of undertaking a study that make use of a research philosophy, approach and methods that helps to provide answers to the research questions and help in achieving the research objectives. The reasoning behind the choice of method of data collection, analysis and interpretation will be also be discussed. Further sections will outline the study's population, sample size and sampling techniques. The various data sources, data instruments as well as ethical and access issues relating to the research will also be discussed. The chapter will be concluded by discussions on the various identified limitations of the study.

### **3.2 RESEARCH PHILOSOPHY**

Research philosophy refers to the belief about the way in which data about a phenomenon should be collected, analyzed and interpreted. Research philosophy is concerned with the way in which things are viewed in the world (Saunders, Lewis and Thornhill, 2009 and Yin,2009).

A major issue with carrying out research is not just in identifying the appropriate methodology to use but also in affirming the exploration standards (Sobh and Perry, 2006). There are four types of research philosophy viz: Positivism, realism, interpretivism and pragmatism. Positivism and those that subscribe to the idea, Positivists, believe that reality is stable and can be observed and determined from an objective viewpoint without any interference with the hypothesis being considered. (Levin,1998). They are of the view that the phenomenon being studied should be treated separately and the observations should be repeatable. This will usually lead to the variations in a single independent variable and distortion of realities to identify regularities and form relations between the constituent elements. Hirschheim (1985) believes positivism is so embedded in our society that knowledge claims not grounded in positivist thought are simply dismissed as not scientific and therefore invalid. While positivism has had a particular successful association with physical and natural sciences, there has been much debate about its applicability and suitability for the social sciences (Kuhn, 1970; Bjorn-Andersen, 1985 and Remenyi and Williams, 1996). Realism relies on the idea that there is need for separation of the reality and human mind. Realist believes that there is a scientific approach to the development of knowledge and reality. Realism can be further divided into direct and critical realism. Direct realism sees the world through the lenses of personal human senses known as "*what you see is what you get*" (Saunders et al, 2009). On the other hand, Novikov and Novikov (2013) argued that critical realism is based on the idea that humans do experience sensations and images of the real world. These sensations and images can be misleading and do not necessarily depict the real world. Interpretivism maintains that only through the subjective interpretation and active intervention can reality be fully understood (Hirschheim, 1985). Interpretivists acknowledge that the study of a phenomenon in its natural

environment is important and that researchers cannot avoid intervening with the phenomenon under study. Pragmatism is based on the idea that the reality is constantly changing, debated, renegotiated and as such the ideal method is any method that solves the problem at hand with change being the underlying deciding aim or factor. Creswell and Clark (2011) and Saunders et al (2009) argued that the research questions are the major important determinant of which position to choose. Therefore, in this realm, the use of both qualitative and quantitative methods to resolve practical real-life situations are recommended.

However, before deciding on the appropriate research philosophy for our study, it is important to determine the appropriate research paradigm. A research paradigm acts as a general framework where a researcher can work i.e. the belief system or perspective that shapes the mind and works of a researcher. Guba and Lincoln (1989) held that the research paradigm can be characterized through epistemology, ontology and methodology. Patel (2015) mentioned that epistemology helps answer the question, what or how can I know the reality or knowledge? that is, it serves as the connecting point between the researcher and reality. Ontology refers to the reality and Methodology provides answer to the question, ‘what procedure can we use to acquire the reality or knowledge’? With these questions and our research objectives in mind, we adopt a research methodology that most appropriately use the methods and techniques that helps achieve our research objectives. These methods and techniques are also as used in previous related research thereby providing us with empirical backing.

### **3.3 RESEARCH APPROACH**

The two main traditional research approaches are the quantitative and qualitative approaches. Today, a mix of quantitative and qualitative approach exists and is referred to as deductive or inductive approach (Cresswell, 2009). The choice of the method used in a research is usually determined by the research objectives and the research questions (Farrugia, Petrisor, Farrokhyar and Bhandari, 2010). Cresswell (2009) defined a qualitative research approach as an investigation process into a social or human problem which focuses on reporting comprehensive views of the informants, holistically depicting the situation and the research is conducted in a normal setting. On the other side, a quantitative research approach involves *“the investigation into a social or human problem which is based on testing a theory composed of variables, measured with numbers, and analyzed with numerical procedures, in order to determine whether the prognostic generalizations of the hypothesis hold true”* (Creswell, 2009). The former technique is referred to as a constructivist or inductive or interpretative technique while the latter is referred to as a positivist or deductive technique (Saunders et al, 2009; Yin, 2009). Johnson, Onwuegbuezie and Turner (2007) defined the mixed approach as that which makes use of both quantitative and qualitative approaches in a study to ensure an in-depth understanding of a phenomenon. As a result of the issues being addressed in this study, qualitative method was chosen as the ideal research method.

Benbasat, Goldstein and Mead (1987) accurately observed that no single research methodology is by design better than other methodology with authors like Kaplan and Duchon (1988) recommending the usage of several research methods in order to improve the quality of research. In this study, the major aim is to apply a research philosophy, approach and methods that helps to

provide answers to the research questions and help in achieving the research objectives. A phenomenological approach could help in achieving these aims. *“The phenomenological approach uses qualitative and naturalistic approach to inductively and holistically understand human experience”* (Karami et al 2006). A qualitative research interview will seek to describe and give meanings to the central theme in the life world of the interviewees; unfold the meaning of people’s experience and understand the world from the interviewees’ point of view (Kvale, 1996). McNamara (1999) opined that interviews can be very useful in getting the story behind a participant’s experience and to pursue deeper information about the topic. This is in tandem with the research objective of gaining an understanding of the banker’s experience as regards SMEs financing. Interviews could be structured, semi-structured or unstructured interview (Valenzuela and Shrivastava, 2008). At the quantitative end is the structured interview while the semi-structured and unstructured interviews are mostly used in qualitative research (Bryman, 2001). Edward and Holland (2013) asserts that the semi-structured and unstructured interviews are characterized by lack of structure and an increased level of flexibility.

This study used semi-structured interview approach to gain an insight into the perspective of bankers on bank financing of SMEs in Ireland. According to Cohen (2006), semi-structured interviews as a method of interview involves covering a list of standard questions and topics but it allows the interviewer to follow topical trajectories and to stray away from these standard questions when it is appropriate. The reason for using semi-structure interview was to allow for further discussions on the subject matter and not be limited to the standard questions. It also provided an opportunity for further learning for the researcher on the topic and go ‘off limit’. The semi-structured interviews carried out aimed at ascertaining whether there are similarities and differences in experience of the loan officers about the financing of SMEs in Ireland. It aimed at establishing patterns in experience of the respondents, if any. An inductive approach was also taken in conducting the interview and the respondents were allowed to interpret their reality rather than imposing views on them. Inductive research allows the researcher to approach the research with an open mind and watch for the emergence of patterns and processes which can then be used to provide a detailed description of their experience (Gilgun, 2001). The interviews took place mostly at the bankers (interviewees) office while some took place on the phone. Due to banker’s tight schedule, some were sent the interviews questions and they replied through emails with further clarification sought through emails too. The interviewees were sent the interview theme and consent form prior to conducting the physical interviews. For the interviews that were conducted physically, through phone calls and skype, the audios were recorded using an audio recorder. The major qualification for interview participant is to be working in the SME segment of the four participating banks.

### **3.4 RESEARCH OBJECTIVES**

- To gain an understanding of the banker’s perspective on lending to the SMEs sector in Ireland.
- To determine the various drivers and impediments to SMEs financing in Ireland.
- To study the effect of government policies and incentives on the SMEs financing in Ireland.



- To gain an understanding of how banks engage with the SMEs segment in Ireland.

### **3.5 POPULATION AND SAMPLE SIZE**

The population for our study consists of all commercial banks in the Republic of Ireland. There are currently 19 commercial banks in Ireland namely:

- Allied Irish Bank
- Bank of America Merrill Lynch International
- Bank of Ireland
- Bank of Montreal Ireland
- Barclays Bank Ireland
- Citibank Europe Plc
- Dell Bank International
- Depfa Bank
- EBS
- Elavon Financial Services
- Hewlett-Packard International Bank
- Intesa Sampaolo Bank Ireland
- JP Morgan Bank (Ireland)
- KBC Bank Ireland
- Permanent TSB
- Scotiabank (Ireland)
- Ulster Bank Ireland
- UniCredit Bank Ireland
- Wells Fargo Bank International

It is a common knowledge however that most of these banks do not necessarily give loans or accept deposits or have any financial interactions with SMEs in Ireland. They mostly deal with large enterprises or are created as a special purpose vehicle like Dell Bank/Hewlett-Packard International Bank etc. Most importantly, the Central Bank makes use of data from Allied Irish Bank, Bank of Ireland, Permanent TSB Bank and Ulster Bank for collecting loan-level data on SMEs in Ireland (SME Market Report, H2 2017). The report also indicates that the SMEs lending market is highly concentrated with the market share of the three main lending currently accounting for 82% of new lending flows. (SMEs Market Report, H1 2017). Therefore, with regard to sampling, this research assumed same method as used by the Central Bank in providing the market report on SMEs in Ireland. Furthermore, it is better to concentrate on large banks that focus on SMEs in a country due to their systemic importance and their significance as potential SMEs financiers (Beck, Demirguc-Kunt and Martinez-Peria, 2008). To ensure meaningful statistical analysis, the researcher has an obligation to ensure a carefully planned sample size that is of significant size to warrant thorough analysis but however not too vast to limit results (Lenth, 2001). Lenth's (2001) opinion was motivated mainly due to financial reasons. For example, a study with a small sample size could prove to be a total waste of resources with the benefits not being fully realized. A study with a large sample size can lead to usage of more resources than necessary with the costs outweighing the benefits to be derived from the research. As such, these four banks form the sample used in our research as we believe that additional banks do not necessary increase the

efficacy of our results. The four banks form the major representation of financial institutions acting as financiers in the SME lending environment in Ireland. These four banks are Allied Irish Bank, Bank of Ireland, Permanent TSB Bank and Ulster Bank.

### **3.6 DATA SAMPLE**

The study adopted commercial banks as against other sources of external finance available to the SMES because “*previous studies have shown that banks are the main source of external finance for SMES across countries*”. (Beck, Demirguc-Kunt, and Maskimovic, 2008). Due to the time limitation and cost implications, the study used convenience sampling to select the sample. Convenience sampling is a kind of non-probability or non-random sampling where individuals of the target population that meet certain useful criteria, for example, geographical proximity, willingness to participate, easy accessibility and availability at a given time are included in the study (Dornyei, 2007). Convenience sampling places emphasis on generalizability, that is, the knowledge gained from the sample should be a representation of the population (Etikan, Musa and Alkassim, 2016). A disadvantage of convenience sampling is however that all the members of the population do not have an equal opportunity of being represented (Mackey and Gass, 2005). The sample selected will be those who are convenient for the author to interview. The interviewees sampled in this study are bankers from these banks; Allied Irish Bank, Bank of Ireland, Permanent TSB and Ulster Bank.

#### **3.7.1 DATA COLLECTION**

**3.7.2 Data Sources:** We collected new and unique data from the interviews conducted with the respondents who are credit managers at the sampled financial institutions. We also made use of secondary data on SMEs and financial institutions in Ireland available on the Central Bank of Ireland website. These include but not limited to

- a.) Trends in Business credit and Deposits (Q4 2017)
- b.) The Central Bank of Ireland Quarterly Bulletin, April 2018
- c.) SMES market report, H2 2017.

**3.7.3 Data Instruments:** To acquire the needed data on bank financing of SMEs in Ireland, we conducted semi-structured interviews that address the research objectives of the study. Because of the link between the study and previous International Finance Corporation (IFC) and the World Bank initiatives for a better understanding of banks involvement with SMES, the interviews conducted were closely-linked with those used in the previous similar research. IFC (2007) developed its own questionnaire and used this to survey 11 banks in the SMES business segment operating in countries such as Australia, the United States of America, the Netherlands, the United Kingdom, Brazil, Thailand, India and Poland. World Bank (2007b) used its own developed survey in the study of SMEs financing in Latin American countries such as Argentina, Chile and Colombia. To study SMEs financing in Serbia, World Bank (2007a) conducted both interviews and administer questionnaires. Using similar methodology with these recent studies means that the result of the research can be compared with results from other countries. However, time-lapse,

different economic conditions in the countries can limit comparability. Events after those studies such as the 2008 global financial crisis and the attendant policies and tools used to solve the crisis can also limit comparability. Interviews have been preferred to questionnaire because the questionnaires were used mostly in multi-countries study where time and constraints would have made it impossible to conduct interviews while the interview were used when studies were limited to one country. Although, the proposed interview might have elements of the questions from those previous studies, a major difference with the previous studies is that this study is Ireland-centric and focuses solely on issues affecting SMEs financing in Ireland. The research aims to provide information that could help in tailoring future government, banks and other stakeholders' policies on SMES.

The data collection involved making numerous contacts with several bankers. It was ensured that the interviewees were only bankers who has had experience in SMEs lending in Ireland. This was to ensure that enriched information on both current and past issues relating to the subject matter can be gleaned from them. Attempts were made to contact them at their physical office addresses, emails, LinkedIn, through mutual acquaintances and follows ups with phone calls outlining the research objectives and significance of study. Prior to the interviews, consent forms were also sent to their email addresses. All interviewees were subjected to same set of questions and as it was semi-structured interviews, the follow-up questions were different for each interviewee. The interviews were conducted in August 2018. The interviewer recorded the interviews using an audio recorder while also taking notes of other salient points discussed during the interview.

**3.7.4 Interview:** To acquire information on the banker's perspective of SMEs in Ireland, we conducted interviews with 6 questions focusing on collecting socio-demography data and 15 main questions focusing on the main topic. To start with, the study examines how bankers perceive the SMEs segment. Specifically, the interview focuses on the drivers and impediments to SMEs financing in Ireland. Likewise, the interviewer asked about the banker's impression on the role of government incentives and programs as well as views on regulations requirement by the Central Bank of Ireland. The interview incorporates questions related to the business models utilized by banks to serve SMEs. Specifically, the study asks whether banks have separate organizational set ups to deal with their activities with SMEs, the criteria considered while assessing SMEs loans and types of collateral most popularly used in SME financing. Due to the semi-structured nature of the interviews, the interviewer was at liberty to discuss related matters that were not captured on the main interview questions sheet.

**3.7.5 Access and Ethical Issues:** Access to data and information is an important matter that should be given adequate priority before and when carrying out research. An understanding of the organizations before contacting them as well as clarifying the advantages of the study to the respondents are also quite important (Saunders et al, 2009). Accessing the bankers for interview was strenuous as expected. This was however made harder due to the need for the banker to have had experience dealing with SMEs. Another issue on access was the delay in bankers getting necessary approval from their superior before granting the interview. To fully grasp the issues discussed during the interviews, the researcher

approached the research setting with two mental orientations: open-mindedness about where to find them and flexibility in looking for data (Stebbins, 2016 and Adegbite, 2010).

On ethical issues, the interviews conducted for this research were done in a manner that ensured the respondents anonymity by asking no questions on the identity of participating banks and staffs. This was clearly stated on the consent form. Any information that could lead to the identification of identity of any participating bank or staff were not used in the study. Codes are used to protect the anonymity of the banker and the banks they are employed. The interviews were confidential which help ensure that the banks feel no constraint in sharing their information. Also, the data is reported in percentages and aggregates without disclosing each position on issues. The interviewees were made to understand that the consent forms and original audio recordings will be retained until the researcher's university exam boards confirm the result of the dissertation. The disposal of the data will also be carried out shortly after the confirmation of the dissertation result by deleting the audio files and incinerating any paper trail.

### **3.8 RESEARCH LIMITATIONS**

The study is Irish-centric and as such the implications are only applicable to Ireland. While the general lending situation in the Euro area can be said to follow same pattern, there should be caution in applying the study to other euro area countries. Ireland is also only a small part of the Euro SME market. The banking industry is smaller when compared to other nations in the Eurozone. All the interviewees are also based in Dublin and as such there is a possibility of differences in opinion of bankers based in other counties. Time constraints was also an issue in the conduct of this study. The opinions expressed are also from the supply-side (bankers) and might be different when compared with the demand side. a study combining supply-side data with firm-level data from the demand side will offer key insights into areas not explored in this study.

### **3.9 CONCLUSION**

The research methodology and approach of this study is in order with previous studies on SMES financing (Beck, Demirguc-Kunt, and Maskimovic, 2008; Beck, Demirguc-Kunt and Martinez-Peria, 2008; World Bank, 2007a; World Bank, 2007b). The research methodology has also been intended to guarantee an adequate conceptual grounding while clinging to methodologically stable and precise strategies, keeping in mind the end goal to make noteworthy and theoretical contributions (Bartunek, Bobko and Venkatraman, 1993). The hope is that this dissertation help fills the gap caused by the dearth of literature on SMEs financing from the banker's perspective. In Chapter 1, the major themes of this study were introduced. Chapter 2 reviews the existing literature on the subject matter as well as theoretical background of the study. The research methodology and approach has been discussed in Chapter 3. The next chapter will focus on data analysis and presenting findings of the research.

## CHAPTER 4 DATA ANALYSIS AND FINDINGS

### 4.0 INTRODUCTION

This chapter will focus on data analysis and a discussion of the findings. The findings were mainly from the interviews conducted with the bankers. Other sources of information for the analysis include Trends in Business Credit and Deposits (Q4 2017), The Central Bank of Ireland Quarterly Bulletin, April 2018, SMES market report, H2 2017 and other reports from the Central Bank of Ireland. The analysis conducted is in accordance with the research approach and methodology enumerated under the methodology chapter. The chapter will start with the analysis of the socio-demographic data of the interviewees and then move on to analyze the responses from the interview questions. The banker's perception of the size and prospects of the Irish SME market as well as drivers and impediments to banks relationship with SMEs will be analyzed. The role of government programs and incentives will also be discussed. Matters relating to Central Bank of Ireland reporting requirements and documentation will also be discussed. The chapter ends with an analysis of how Irish banks engage with SMEs.

### 4.1 INTERVIEWEE'S PROFILE

The respondents were mainly credit managers at the sampled financial institutions. A total of five interviews were conducted. The semi-structured interviews address the research objectives of the study. The interviews were recorded with the interviewees consent.

#### 4.1.1 INTERVIEWEES SOCIO-DEMOGRAPHIC DATA

#### 4.1.2 INTERVIEWEES AGE RANGE DISTRIBUTION

Table 1

Age range	Frequency	Percent	Valid Percent	Cumulative Percent
18-25	0	0.0	0.0	0.0
26-35	1	20.0	20.0	20.0
36-45	2	40.0	40.0	60.0
Above 46	2	40.0	40.0	100.0
<b>Total</b>	<b>5</b>	<b>100.0</b>	<b>100.0</b>	

Source: Interview

Table 1 above shows the age range of the interviewees. It can be deduced from the table that most of the interviewees fall between the age ranges of 36-45 years and above 46 years. 80% of the interviewees fall within this range. The remaining 20% are within the 26-35 years age range.

#### 4.1.3 GENDER DISTRIBUTION OF INTERVIEWEES

Table 2

Gender	Frequency	Percent	Valid Percent	Cumulative Percent
Male	4	80.0	80.0	80.0
Female	1	20.0	20.0	100.0
<b>Total</b>	<b>5</b>	<b>100.0</b>	<b>100.0</b>	

Source: Interview

The table above considers the gender distribution of the interviewees. We can conclude from the table that the male gender makes up the highest percentage of interviewees. They constitute 80% of the interviewees while the female gender makes up the remaining 20% of the interviewees.

#### 4.1.4 JOB TITLE OF INTERVIEWEES

**Table 3**

<b>Name</b>	<b>Job Title</b>	<b>Bank Name</b>
Mr A	Business Development Manager	Bank Z
Mr B	SMES Business Manager	Bank Y
Mr C	Head of Market Risk	Bank X
Ms D	SMES Business Advisor	Bank W
Mr E	SMES Business Manager	Bank Y

*Source: Interview*

The job title of the interviewees is enumerated in Table 3 above. A system of coding has been employed to ensure the anonymity of the interviewees. Their names and the institutions have each been given a particular code which will then be used for subsequent identification in the study. Most of the interviewees have current experience or prior experience in SME banking. This put them in a good position to give valid and insightful opinion on the current state of SME lending.

#### 4.1.5 EDUCATIONAL STATUS OF INTERVIEWEES

**Table 4**

<b>Level</b>	<b>Frequency</b>	<b>Percent</b>	<b>Valid Percent</b>	<b>Cumulative Percent</b>
<b>Primary</b>	0	0.0	0.0	0.0
<b>Secondary</b>	0	0.0	0.0	0.0
<b>Degree</b>	2	40.0	40.0	40.0
<b>Masters</b>	3	60.0	60.0	100.0
<b>Others</b>	0	0.0	0.0	100.0
<b>Total</b>	<b>5</b>	<b>100.0</b>	<b>100.0</b>	

*Source: Interview*

Table 4 indicates the educational status of the interviews. According to information gathered during the interviews, 60% of the interviewees have a master's degree while 40% have a bachelor's degree.

#### 4.1.6 NUMBERS OF YEARS IN THE CURRENT FINANCIAL INSTITUTION

**Table 5**

<b>Years</b>	<b>Frequency</b>	<b>Percent</b>	<b>Valid Percent</b>	<b>Cumulative Percent</b>
<b>Less than 1 year</b>	0	0.0	0.0	0.0
<b>1-2 years</b>	0	0.0	0.0	0.0
<b>2-4 years</b>	0	0.0	0.0	0.0
<b>Greater than 4 years</b>	5	100.0	100.0	100.0
<b>Total</b>	<b>5</b>	<b>100.0</b>	<b>100.0</b>	

*Source: Interview*

A good way of determining fit for the interview purpose was to have had a sizeable number of years. Table 5 shows the numbers of years the interviewees have in their current financial institution. All the interviewees have been employed in their current financial institutions for more than four years, showing that all interviewees are experienced banker and a good fit for the interview purposes.

#### **4.1.7 NUMBERS OF YEARS IN BANKING INDUSTRY**

**Table 6**

Name	Number of Years
Mr. A	11 years
Mr. B	15 years
Mr. C	24 years
Ms. D	7 years
Mr. E	10 years

*Source: Interview*

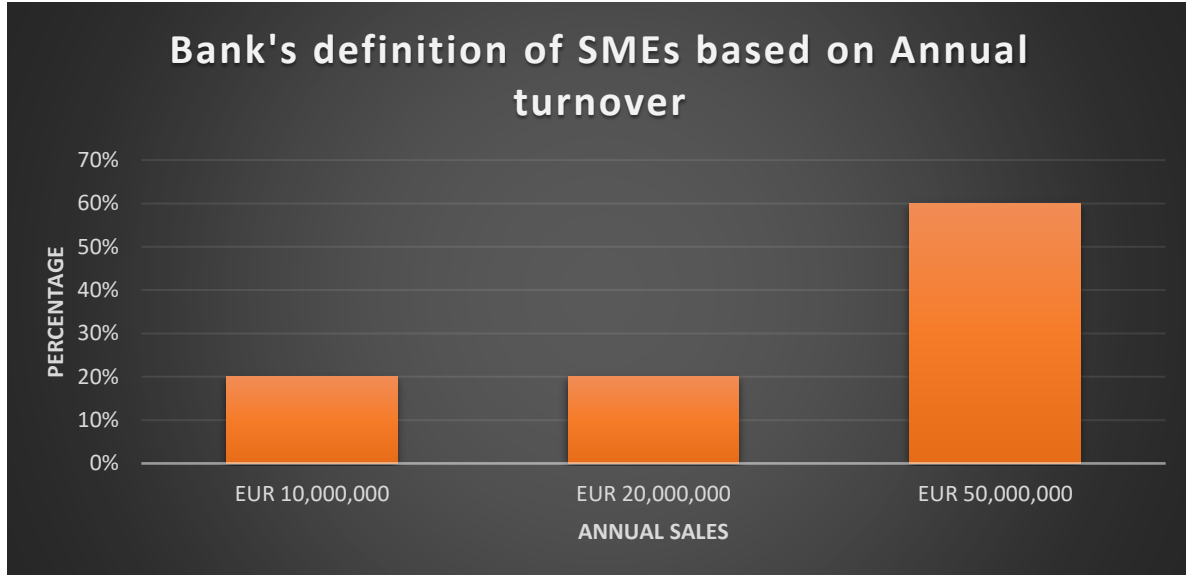
Lastly, Table 6 indicates the number of years of experience in the banking industry for each interviewee. As a corollary to the above, the interviewees also have substantial years of experience in the Irish banking industry.

### **4.2 INTERVIEW ANALYSIS**

#### **4.2.1 BANK'S DEFINITION OF SMES**

The interviewees were asked to give their definition of an SME in accordance with their individual bank policy. The definitions were to be given in relation to sales revenue, number of employees or any other criteria as used by the bank. The definition given by the banks were not significantly different from each other. In relation to number of employees, all (100%) interviewees defined a SME as a company with less than 250 employees. Figure 1 below shows the distribution of the definition of SMEs based on annual turnover. In terms of sales, 60% of the banks defined SMEs as those with annual sales of less than 50m euros. 20% of the banks defined SMEs as those with annual sales of less than 10m euros while the remaining 20% defined them as firms with annual sales of 30m euros. Most banks definitions of SMEs are in tandem with the standard EU definition of SMEs. The EU defined the category of SMEs as made up of enterprises which employ fewer than 250 employees and which have an annual turnover less than or equal to 50 million euros and or/an annual balance sheet less than or equal to 43 million euros (European Commission, 2005). In some banks, there are distinction between Micro and Small Enterprises. The micro enterprise includes enterprises which have less than 50 employees and which have an annual turnover less than or equal to 10 million euros and/or balance sheet total of less than or equal to 10 million euros. This definition is also in agreement with the guidance given by the European Commission in 2005. However, the banks do not distinguish between small and medium enterprises. In all, it can be suggested that the banks in Ireland define enterprises in a manner consistent with European Union definition.

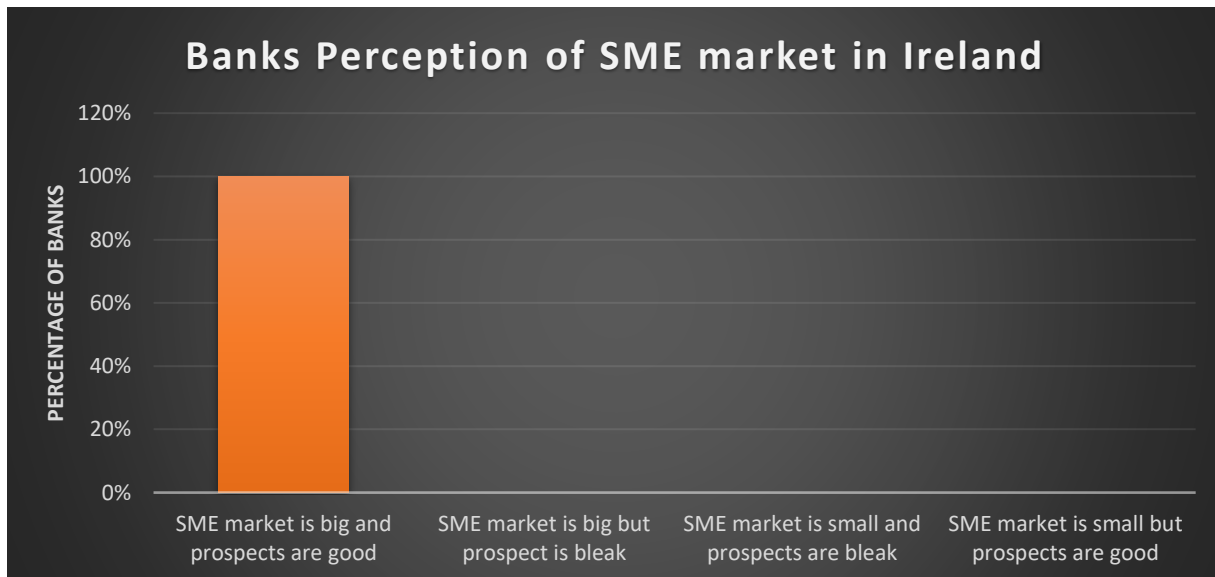
Figure 1: Bank's definition of SMEs based on Annual turnover



#### 4.3.2 HOW BANKS PERCEIVE THE SME MARKET IN IRELAND

The interviewees were asked questions to help determine their banks perception of the SMES market in Ireland. The perceptions were to be based on the size of the segment as well as the prospects of the segment.

Figure 2: Banks Perception of SME market in Ireland



As shown in Figure 2 above, all the banks perceive the SME segment as a big, fast growing segment with huge prospects. For bank Z, SME lending makes up 80% of the business part of the bank while Bank Y only established its SME division a couple of years ago. The decision indicates



that bank Y believes in the Irish SME segment and its prospects. All the banks have huge SMES business targets. They also have big investments in the various sectors of the economy in which there are SMEs. The Demand for SME lending in Ireland in 2017 increased by 14% on a year on year basis with improved conditions expected in 2018 (PTSB annual report, 2017).

### 4.3.3 DRIVERS AND IMPEDIMENTS TO SMES FINANCING IN IRELAND

To comprehend their interest in the SMEs segment, banks were requested to indicate the drivers of SMEs lending and to depict how significant these factors are in characterizing their level of involvement with the segment. The major drivers for bank's involvement in SMEs financing in Ireland include perceived profitability of the SME segment. A clear majority of the banks consider that they will accomplish elevated profits that will more than cover for the higher costs and risks of the SMES segment. The high profitability of working with SMEs does not just comes financing products but also from potential for cross-sale. Possibility to seek out SMEs through existing personal relationships (cross sale opportunity) is another major driver for SMEs financing. Once the connection with the organization is built up, banks offer SMES an assortment of services and get the larger proportion of their incomes from the fees they charge for these services. Other drivers include intense competition in the SMEs segment, perceived opportunity to service smaller owner managed SMEs, well-thought out business plan, previous cordial relationships and SMEs experience of its market. In the case of Bank Y, a major driver is its goal of being the bank of choice for Ireland's Small and Owner Managed Business Enterprises. Perceived profitability and the possibility of cross sale opportunity can be highlighted as the major driver of SMEs financing in Ireland.

To understand the obstacles to bank financing of SMEs, bankers were asked the impediments to banks involvement in SMEs financing in Ireland. There were clear agreements by the bankers on the following issues:

- i.) Dominance by two major banks: The SMEs segment in Ireland is highly dominated by two major banks. There is a major concentration with little competition. Competition is only provided by digital lending and online lending. A recent Accenture report indicates that 73% of SMEs are satisfied with the level of service they receive from their current banks and only 25% expects to switch their provider over the next year (Accenture, 2018).
- ii.) Brexit Issues: The potential negative impacts from Brexit and sterling depreciation is a source of concern for the banks. Although the risk of a 'hard' Brexit has receded recently, there is still much uncertainty about the likely outcome of the decision. The Irish SMEs sector especially the agri-food segment dependence on the UK market is a major source of concern.
- iii.) Regulations: While regulations and compliance issues offer protections to both the SMEs and banks, they can make access to finance become a long and tedious process. This is more difficult for new SMEs rather existing ones because of the former's lack of relationship with the bank.
- iv.) Financial Crisis: One of the fall-out from the recession is the high level of residual debt still unpaid by SMEs. This has led to an environment of distrust between SMEs and banks.

Other obstacles include: Lack of demand from the SMEs sector of appropriate credit quality, macroeconomic factors which have various effects on different SMEs segment. The legal and contractual environment in Ireland was given the least important obstacle to SMEs financing.

#### 4.3.4 PERCEPTION OF GOVERNMENT INCENTIVES AND PROGRAMS

The study collected information on the banker's perception of the roles of various government incentives and programs. These were limited to mainly programs that aims to support the SMEs and to promote SMEs financing in Ireland. Banks report that various government agencies programs exist to promote SMEs financing in Ireland. Consistent with Beck et al (2008) and World Bank (2007b), government credit guarantee schemes were mentioned as the most common government program used to support SMEs financing in Ireland. These programs are an important determinant of banks relationship with the SMEs. Banks are more inclined to establish a relationship with SME recommended under such schemes. The most commonly mentioned government guarantee scheme for financing SMEs is the recently revised SME Credit Guarantee Scheme 2017. The scheme was launched in July 2018 and 75% of the banks in our study participates in the scheme. The scheme assists viable SMEs who are unable to borrow under normal lending circumstances by providing 80% guarantee (previously 75%) on qualifying loans to SMEs. The typical loan size range from 10,000 euros to 1 million euros and loan term is up to 7 years. Term loans, performance bonds, demand loans and other non-traditional bank loans like factoring, invoice discounting, leasing are all covered under the scheme. Another important government program available to SMEs is the Brexit Loan Scheme. This is a 300 million euros loan scheme which aims at offering competitively priced loans to eligible Irish SMEs. 75% of the banks in our study participates in the scheme. The scheme was launched in March 2018 and is intended to run till March 2020. It provides loans from 25,000 euros to a maximum of 1.5 million euros. Loans can typically be used in financing working capital, funding innovation and adaptation of the business to mitigate against the impacts of Brexit. Bankers also provided their opinion on the role of the Microenterprises Loan Fund administered by Microfinance Ireland (MFI). The fund was established in 2012 to improve access to credit for Microenterprises and to facilitate the growth and expansion of viable businesses which have been refused credit by banks. To be eligible for a loan, applicants must submit a business plan, a commercially viable proposal and capacity to repay the loan.

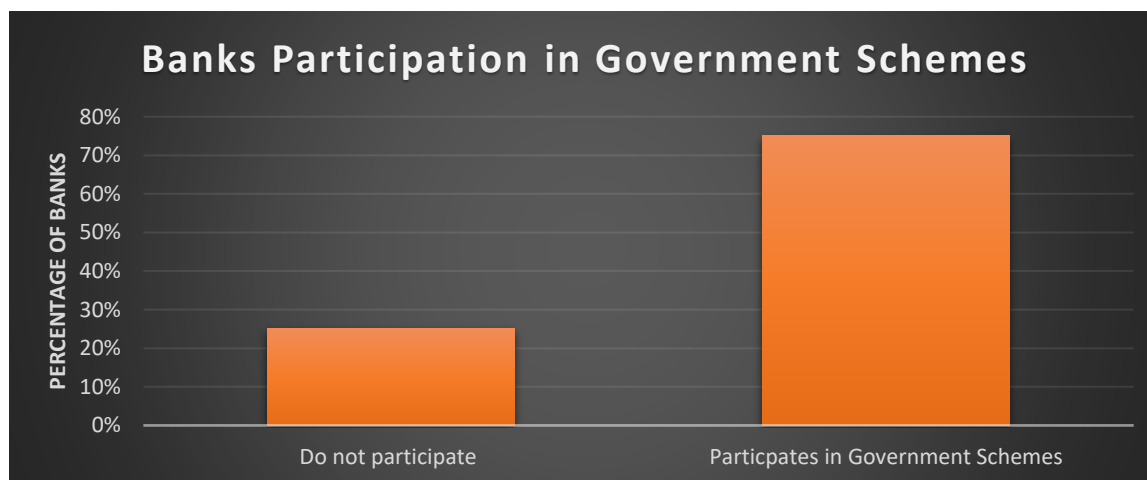


Figure 3 above illustrates bank's participation in various government credit schemes

Another role played by the Irish government in encouraging SME financing is through the Credit Review Office. The office provides a simple and effective review process for SMEs that have been refused credit by the banks used in this study. SMEs can apply for the review of their application and get information on whether their business is viable and get an independent, impartial opinion on whether business is viable. The activities of the Strategic Banking Corporation of Ireland (SBCI) in promoting access to flexible funding for Irish SMEs was also lauded by the bankers during the interviews. Among the banks, programs such as Targeted Long-Term Refinancing Operations (TLTRO) scheme has provided significant incentives to banks to increase lending, especially SMES lending. The TLTRO scheme are euro-system operations that provide financing to credit institutions for periods of up to four years. To further ease private sector credit conditions and stimulate the real economy, they offer long-term funding at attractive rates to banks. This then helps to further ease the conditions demanded by banks when granting finance to SMEs. In all, 80% of bankers have a positive perception of the various government incentives while 20% have a neutral perception of the government incentives and programs to support SMEs.

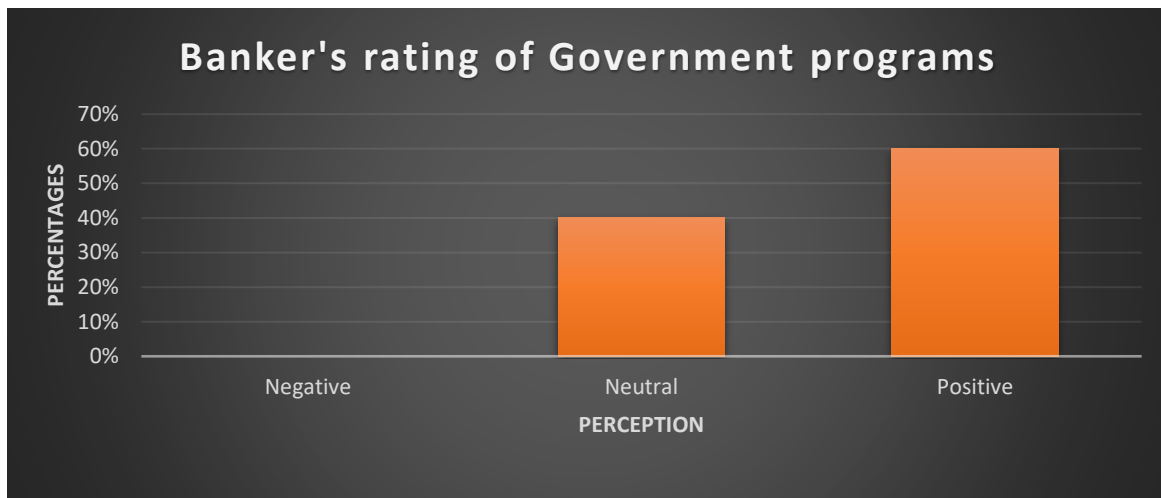


Figure 4 shows how the different bankers rate the various government programs aimed at promoting banks involvement with SMEs in Ireland.

#### **4.3.5 BANKERS PERCEPTION ON REGULATIONS AND DOCUMENTATIONS REQUIREMENTS**

A major way through which governments can influence banks involvement with SMES is through the various regulations put in place by the regulators. As a member of the European Union (EU), banks in Ireland are expected to follow both supranational and national laws on banking. Figure 5 shows the bankers' perception on documentations requirements for lending to SMEs while Figure 6 illustrates banks' perception on how regulations affect their involvement with SMEs. Unlike previous sections where there were convergent views, this section had divergent views. 60% of the bankers perceive documentation requirements for SMEs financing to be appropriate while 40% of the bankers believed that the documentation requirements for SMEs financing are excessive. The bankers on the "appropriate" side believes that the current level of required documentation

help the banks in making an informed and fair decisions on SMEs lending applications. It also helps ensure that repayment capacity (a key factor used by the bankers) can be determined.

Figure 5: How bankers perceive documentation requirements

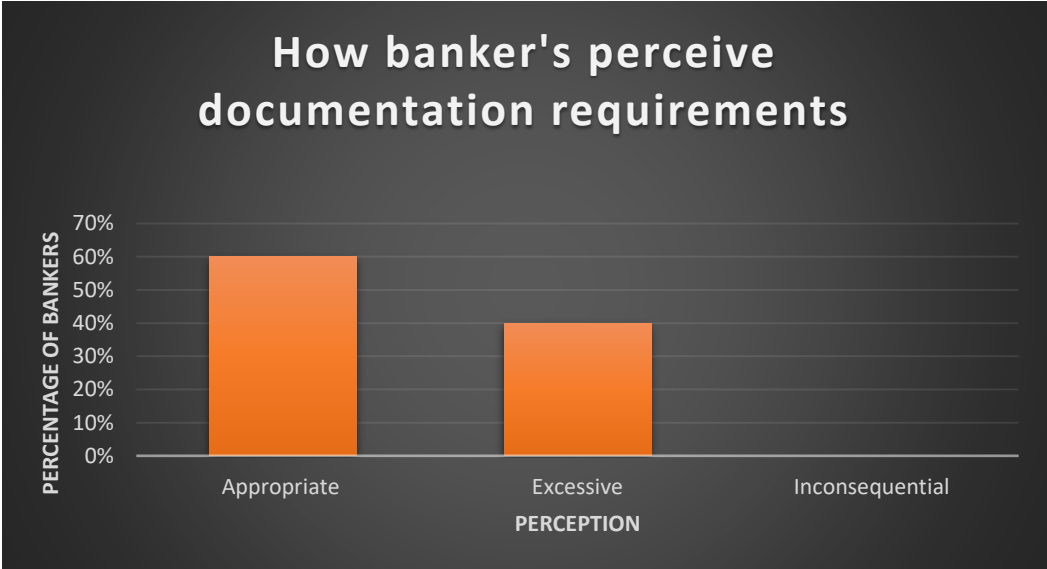
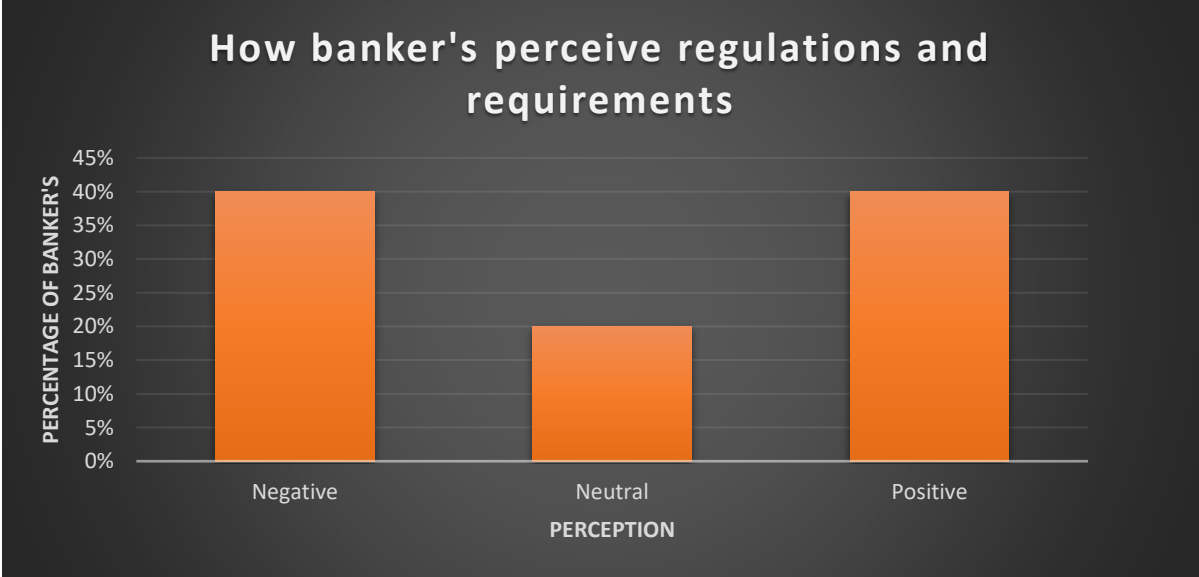


Figure 6: How bankers perceive regulations and requirements



Regulations and requirements by the Central Bank of Ireland (CBI) seem to be an important issue for bankers. 40% of the bankers interviewed believe that the regulations and requirements by CBI have negative effects on the relationship between banks and SMEs. 40% of the bankers interviewed believe that the regulations and requirements by CBI have positive effects on the relationship between banks and SMEs. 20% of the bankers interviewed believe that the regulations and requirements by CBI have neutral effects on the relationship between banks and SMEs.

Findings shows that the regulations are not tight on the SMEs but establish strenuous controls on the banks. The process of documentation and reporting of lending to CBI is *“time consuming and excessive”* as expressed by one of the interviewed bankers.

#### **4.3.6 HOW BANKS ENGAGE WITH SMES IN IRELAND**

This section deals with the business models adopted by banks in serving the SMEs. The bankers were asked to address issues such as: *“what is the extent of decentralization in serving SMEs”?* *“Does your bank have a separate organizational set up to serve SMEs”?* *“What criteria are used by banks in making loans decision”?* *“What is the importance of collateral in granting loans to SMEs”?*

Most banks (75%), have separate organizational set up to serve the SMEs segment. They have established a distinct SMEs division separate from the divisions that serve large enterprises. This is due to the fact that SMEs lending constitutes a large percent of the bank’s activities. They however do not separate between small and medium firms. The SMEs are managed through a different segment with specialists in the different sectors of the economy. This is done to facilitate cordial relationships with the SME. The relationship occurs through the branches and headquarters as varied by the different bank structures. Common patterns can however be detected among banks in Ireland.

The majority of banks (75%) operating in the SMEs segment in Ireland have a centralized structure for SMEs loan approval. The lending units are tasked with making decisions for all branches. 15% of the banks have a decentralized structure for granting loan approval to SMEs, this however depend on the size of the loan. Decisions on larger loans to SMEs will tend to be made at the headquarters. Loans above certain thresholds must also be approved by more senior approval authorities within the organizations. The initial stages like loan origination and initial processing are usually done at the branches. Risk management and non-performing loan recovery functions are centralized by all banks (100%). All banks usually have distinct departments at their headquarters responsible for risk management and recovery of non-performing loans. Sales of other products to the SMEs are decentralized by all banks (100%). They are usually carried out at the branches and through electronic means e.g. online, telephone etc.

75% of the banks make use of scoring models in SMEs lending, only 15% of the banks do not make use of score cards. Although 75% of the banks agreed that scoring is an important input in loan decision making, none of the banks grants approval solely on good score cards. Scoring is used primarily as an input in the whole financing decision process. All banks (100%) agreed that credit rating by credit agencies have a big impact on SMEs lending in Ireland. Credit history as evidenced by the Irish Credit Bureau is an important input in making financing decisions to SMEs. The credit history provides information on past repayment history and repayment capacity. For SMEs who had repayment difficulty during the 2008 global financial crisis, the banks have mechanism in play to ensure well-informed decisions are made.

In terms of specific criteria that are used by banks in evaluating and making loan decisions, the study examine various factors and asked if there are differences between such criteria for SMEs

and large enterprises. The most common criteria mentioned by the banks include financial analysis of the business, the firm's credit history and relationship with the bank, size of the loan, purpose of the loan, repayment capacity, firm's owner characteristics etc. There are majorly no differences between the criteria set for SMEs and large enterprises, only that larger loans are subject to higher level on internal scrutiny. There is a general consensus (100%) among the banks that collateral although important, it should only be seen as a secondary source of repayment. The primary source should be the cash flows from the project or business being financed. The most commonly accepted collateral by Irish banks is personal guarantee. Although frowned upon by SMEs, personal guarantee allows the bank to recoup using the company owners' assets. A way of gaining competitive advantage for the bank could be in waiving the need for a personal guarantee (in certain cases). This is because the vast of SMEs director's wealth are usually linked to the business. Other commonly mentioned collaterals include first charge over property or land, claim on deposits held with the bank, assets such as machinery and equipment, cash and other liquid assets.

#### **4.4 CONCLUSION**

In the sections above, the findings and analysis of data generated from the interviews conducted for this study were analyzed. It started with the analysis of the socio-demographic data of the interviewees. The major questions from the interviewees were then analyzed. To summarize, the major drivers for banks involvement with the SMEs segment are perceived profitability and cross-sale opportunities. The banks also see the SMEs sector in Ireland to be huge with good prospects. The banker's perception of the various government's incentives and programs are positive while there is believe that regulations and requirements by CBI could be less time-consuming and moderate. Most banks have separate organizational set up to serve SMEs, have centralized risk management, loan approval process and non-performing loan recovery system while sale of other products to SMEs are decentralized. Score cards are an important input and most banks prefer personal guarantee of SMEs owners. In the concluding chapter, the study will offer several recommendations for further research and provide concluding thoughts.

## **CHAPTER 5 RECOMMENDATIONS AND CONCLUSION**

### **5.1 DISSERTATION SUMMARY**

Chapter 1 of the dissertation gave a general introduction of the key themes of the study. It highlighted the motivation and significance of the study. The research questions and research objectives of the study were also discussed. In Chapter 2, attempts were made to carry out a comprehensive review of relevant literature of the subject matter. There were discussions on the importance of SMEs to economic growth and development as well as the impact of the 2008 global financial crisis on the SMEs lending environment. Capital structure and how its theories relate to capital financing decisions of SMEs was also discussed in the chapter. This helped to provide a theoretical framework for the study. Discussions in Chapter 2 highlighted the suitable research methodology and approach which were then discussed fully in Chapter 3. The phenomenological approach was adopted to provide answers to the research questions and achieve the research objectives. Chapter 4 focused on the analysis of the various findings from the interviews conducted for the study. The semi-structured interviews adopted provided the researcher with an ample opportunity to inductively and holistically understand the banker's experience and opinions on issues. The discussions focused on gaining an understanding of the banker's perspective; the major drivers and impediments; effect of government policies and incentives and how banks engage with the SMEs sector in Ireland. The concluding chapter provides an opportunity to make certain recommendations on how to foster better relationships between the bankers and SMEs as well as recommendations for further research.

### **5.2 CONCLUDING THOUGHTS**

The overall objective of this study was to document the state of SMEs financing by banks in Ireland. This was done from the perspective of the bankers to shed light on the relationships between the SMEs and banks. To achieve the research objectives, the researcher interviewed and collected new and unique data from five bankers in four banks in Ireland. These four banks namely: Allied Irish Bank, Bank of Ireland, Permanent TSB Bank and Ulster Bank are those used by the Central Bank of Ireland for collecting loan-level data on SMEs in Ireland (SME Market Report H2, 2017). The analysis done in this study were mainly from the information collected from the interviews. The dissertation should provide an empirical basis in analyzing the relationship between the bankers and the SMEs. Specifically, the main research objectives of the study were to gain an understanding of the banker's perception on lending to the SME sector in Ireland; to determine the various drivers and impediments to SME financing in Ireland; to study the effect of government policies and incentives on the SMEs financing in Ireland and to gain an understanding of how banks engage with the SMEs segment in Ireland. The researchers concluding thoughts on these objectives are provided below.

#### **Banker's perception of SMES sector in Ireland**

The SME sector is an important and strategic segment of bank's activities in Ireland. This was expected and is in line with previous empirical evidences (Beck et al, 2008; Rupegia- Apoka, 2014; World bank, 2007b). Most banks in Ireland define SMEs and other enterprises in accordance with guidelines provided by the European Commission in 2005. The SMEs lending market is seen by banks to be large in size with huge prospects. SMEs exist in virtually every sectors of the economy. Banks are confident of future growth of the sector and are constantly churning out innovative

products to cater for the needs of the SMEs. Digital and online lending is an excellent growth opportunity area for the banks. It provides a means for giving quicker loans to clients.

### **Drivers and impediments to SMES financing in Ireland**

Perceived profitability was identified as the major driver for SMEs financing by banks in Ireland. Banks are more inclined to grant finance to SMEs that they perceive as being profitable after thorough assessment of its financial history and future plans. Cross sale opportunities are also an important driver for banks which help ensure that the benefits of engaging with SMEs are more than the associated costs. The major obstacles to banks' relationship with SMEs in Ireland include dominance of the market by two major banks, uncertainty and issues relating to Brexit, Central Bank reporting requirements and remnants of issues stemming from the 2008 global financial crisis. The lack of cohesion and agreements on Brexit is a major concern for banks (and other industries) as activities in the Irish economy especially the SMEs sector will greatly be impacted by any agreement on Brexit.

### **Impact of government policies and programs on SMES financing**

The banks generally have excellent opinions on the activities of government policies and programs. Various government agencies have programs and schemes in place which aims at promoting banks involvement with SMEs in Ireland. The activities of the Department of Business, Enterprise and Innovation, Strategic Banking Corporation of Ireland (SBCI), Enterprise Ireland, Failte Ireland, MicroFinance Ireland were lauded by the bankers. 75% of the banks studied participates in these government schemes. Banks are more likely to establish relationship with SMEs under the various government credit guarantee scheme. Regulations and documentation requirements are however a different ball game as there are no consensus views on them. The Irish government should at a cursory look at these towards improving relationship between banks and SMEs. This should however be done in a manner consistent with ensuring a safe and sound financial system to prevent issues that lead to the last financial crisis.

### **Engagement with SMEs**

Due to SME segment taking a huge chunk of the banks activities, most banks have established different organizational set ups that aims at servicing the needs of SMEs. Activities that require specialist's knowledge such as non-performing loan recovery and risk management are usually centralized while sale of other products, initial processing. are decentralized and carried out through the branches and other various means. The use of score cards is an important input in loan decision making by the banks. Banks also use several criteria like credit history, previous relationship and financial assessment of the business in making loan decisions.

## **5.3 RECOMMENDATIONS**

To conclude this study, this section will highlight several recommendations aimed at fostering better relationships between the banks and SMEs in Ireland. Recommendations for further research on the subject will also be discussed.

**Credit Review Office:** The office was established in 2010 to provide independent and impartial review of unsuccessful loan applications by SMEs, sole traders and farm enterprises. It gives



opinion on the viability and loan repayment capacity of the business. The office however does not have regulatory or statutory powers to reverse bank lending decisions. The researcher believes that strengthening staff strength, expertise and skills of the office can go a long way in promoting the relationship between SMEs and banks in Ireland. The office could also take up a more pro-active role by being involved prior to submission and not just only post-submission of loan applications. This will also have the effect of informing government of the performance of the Irish credit systems.

**Technology:** One of the issues raised in the study is that Irish SMEs are not prone to change finance providers. Banks were therefore stuck in a system whereby the only attempt at differentiation is cost. However, the introduction of more competitive, technologically advanced products and services by traditional and non-traditional finance providers has challenged the ability of banks to attract and retain SMEs clients. To counter this, the banks must as a matter of urgency vigorously pursue advanced digital technology capabilities as a way of differentiation, attracting new customers and retaining old ones as well as enabling new revenue streams (Accenture, 2018).

**Demand and Supply-side:** For further research purposes, combining data from the supply-side (as used in this study) and demand-side data like firm-level survey (Yamb and Ndjeck, 2016) can provide a more complete picture and add further dimensions and thoughts to the current findings. It can also help in identifying others bottlenecks in SMEs financing and help the government and its agencies in developing policies that affects SMEs lending.

**Increased Sample:** For future research on same subject matter, it would be helpful to consider bankers from other counties in Ireland. This will widen the scope of the research and help determine whether there are differences in their own perception of the SMEs lending environment. Another way could be by carrying out the same research in similar and comparable euro area countries. Such research could offer learning opportunities for monetary authorities of the countries involved.

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**APPENDIX 1: INTERVIEW QUESTIONS FOR A RESEARCH ON BANK FINANCING OF SMALL AND MEDIUM ENTERPRISES IN IRELAND: THE BANKER'S PERSPECTIVES.**

**BACKGROUND:** The importance of Small and Medium Enterprises (SMES) to any economy cannot be overemphasized in terms of employment generation, economic growth etc. In Ireland, small and medium enterprises account for 99.7 per cent of all active business enterprises as well as employing 71.0% per cent of the workforce and they are also responsible for over half the Republic's annual turnover (Ireland SBA Factsheet, 2016). However, a major impediment to the further growth of SMES is finance. Because of their relative importance to any economy, the problems associated with the financing of SMES has been a source of interest to stakeholders such as policy-makers, entrepreneurs, bankers as well as researchers. Lending to SMES is widely considered to be fraught with risks. Access to finance as well as the higher cost of finance has been shown to be a problem for SMES unlike larger firms thus being an impediment to the growth of SMES.

The research will seek to gather data into the philosophy of thinking of banks as it relates to SMES financing, what factors drive and impedes the financing of SMES in Ireland. On the driving factors, how important are the SMES financial statements, credit ratings and history, owners and management reputation and characters as well as the role of competition by other banks? On the impeding factors, what regulatory factors, contractual issues and firm-specific issues affect loan application by SMES.

**SECTION A: Socio-Demography Data**

1. Age: (i) 18-25 (ii) 26-35 (iii) 36-45 (iv) Above 46
2. Gender: (i) Male (ii) Female (iii) Prefer not to disclose
3. Job Title:
4. Educational Status: (i) Primary (ii) Secondary (iii) Degree (iv) Masters (v) Others
5. Years employed in the company: (i) < 1 year (ii) 1-2 years (iii) 2-4 years (iv) > 4years
6. How many years have you been working in the banking industry?

**SECTION B:**

1. What is the definition of an SMES according to your bank? Any difference between small and medium?
2. How does your bank perceive the SMES market in Ireland? Size and Prospects?
3. What are the key drivers for your bank's involvement with SMES in Ireland? What roles does Perceived profitability in the SMES segment, Intense competition for large corporates, Intense competition for retail customers, Excessive exposure to large corporates, Excessive exposure to retail customers sector, Possibility to seek out SMES through existing relations with large clients play in the relationship?
4. What are the key obstacles to the relationship with SMES in Ireland? What roles does Macroeconomic factors, Regulations Legal and contractual environment, Bank specific

factors Nature of the lending technology to SMES Competition in the SMES segment, Lack of adequate demand play in the relationship?

5. What is the banker's perception of existing government incentives and programs to promote SMES financing in Ireland? E.g. guarantee programs, interest subsidies.
6. How do bankers rate the various government incentives?
7. What is the banker's perception on the documentation requirements for SMES lending in Ireland?
8. How do regulations and requirements by the Central Bank of Ireland affect SMES lending in Ireland?
9. Does credit rating by credit bureaus impact on SMES lending in Ireland?
10. Does your bank have separate organizational set up to serve SMES in Ireland? Any special arrangement for Small-sized enterprises separately, Medium-sized enterprises separately, Small and medium-sized enterprises combined (but separately from large firms), Small and medium-sized enterprises separately or None of the options?
11. What is the extent of decentralization in serving SMES by your bank? (e.g. loan approval, risk management, the sale of other products to SMES, non-performing loan recovery).
12. How important is the use of scoring in SMES lending?
13. What are the criteria used by your bank to make a business loans decision? Any differences with large enterprises?
14. How important is collateral in making business loans decision to SMES?
15. What are the most commonly accepted assets used collaterals by SMES granted loans by your bank?