

The Impact of Banking Finance on Financial Performance of Egyptian Small Businesses in period from 2013 to 2016

Eslam Mahmoud Saadallah

Banker, Doctoral of finance 2019 (DBA) from Arab academy for science in Egypt

Abstract: *Small business is important for economic development as it acts as an engine of employment, poverty alleviation and broad-based economic growth. This research focuses on the impact of banking finance at a normal interest rate on small business financial performance. Such a study is important in order to provide a measurement for the impact of banking finance on the financial performance of small business enterprises in Egypt and clarify the importance of banking finance for small business. It is also important as it examines the control role of firm leverage and firm age small business financial performance.*

The research approach adopted in this dissertation includes quantitative secondary data from annual reports of 90 small business firms in Egypt in the period from 2013 to 2016 (annual report in 2013 and 2014 without a loan, 2015 and 2016 with a loan). Data was collected for the research variables; loan volume, return on assets, return on equity and net profit margin. Loans volume at a normal interest rate represents the independent variable, firm leverage and firm age represent the control variable, and financial performance indicators (ROE, ROA and NPM) represent the dependent variable. Results showed that loan volume has a negative significant impact on financial performance of small business, firm leverage has a negative significant impact on financial performance of small business and firm age has insignificant impact on financial performance of small business.

Keywords: *Banking Finance, Loan Volume, Financial Performance, Return on Assets, Return on Equity, Net Profit Margins.*

INTRODUCTION

Small business becomes important for the economic development as it acts as an engine of employment, poverty alleviation, and broad-based economic growth. Small Businesses have usually been perceived as a dynamic force for economic growth and have a multiplying effect on the economy in Egypt, Socially, entrepreneurship empowers citizens, generates innovation and changes mindsets, Economically, entrepreneurship stimulates markets. The formation of new business leads to job creation. Thus, entrepreneurship is described as a potential driver to support the economic growth, have the potential to integrate developing countries into the global economy but the ability of small business access

to finance has always been considered a major obstacle facing many Small Businesses (Elsaid et al., 2011).

The developing countries perceive small business enterprises as engines of employment, poverty alleviation, and broad-based economic growth. Access to finance is a make-or-break issue for many Small Businesses in the developing world. Thus, developing access to finance allows them to capitalize on their growth opportunities, operate on a larger scale, and contribute the economic growth. Egyptian banks should benefit from the expertise of institutions responsible for financing microenterprises in other countries and to identify the tools, policies and technologies used in financing (Nasr-Esfahani et al., 2010)

Small Businesses in Egypt provide almost 60 percent of jobs and three quarters of the national value added but Access to external finance is an important barrier to small entrepreneurs development in Egypt similarly to many other countries so small business needs to provide a business environment in terms of regulations and the way they are implemented and the government needs to improve infrastructure and access to markets to open opportunities for small entrepreneurs (Selim et al., 2017).

RESEARCH PROBLEM AND QUESTIONS

The environment of small businesses in Egypt suffers from the lack of strong accounting systems, the belief that the debt financing is not the preferred method of finance, very low Profit margins, the belief that the cost of credit is too high, not seeking funding from sources other than banks, not having business plans and believing that it is more difficult to obtain financing from banks. On the other hand bankers indicated that management and financial status of small businesses is the main obstacle to banks' involvement with the sector; banks do not offer facilities that best fit the varying needs of small businesses and financing decisions depend on documents within the enterprise rather than its growth potentials (Elsaid, 2010).

Small businesses in Egypt have a number of problems that they face before obtaining funding, such as the lack of sufficient sources of financing working capital and fixed assets for small business. Owners' of small business do not have awareness of the importance of banking finance, not only that but also

the high interest rate of banking finance, the lack of a good administrative and financial structure compared to large firms and lack of collateral for borrowing. The small business in Egypt has a number of problems after obtaining funding so this was an incentive for us to studying these observations and try to measure the impact of banking finance at a normal interest rate on the financial performance of small businesses, explain the importance of bank financing for small businesses and explain the causes of problems faced by small businesses after financing. The following questions should be answered during this study:

1. To what extent could the banking finance at a normal interest rate effect the financial performance of small business enterprises in Egypt?
2. What is the role of firm leverage and firm age on the impact of the financial performance of small business enterprises in Egypt?
3. What is the role of CBE to support small business compared to other developing countries?
4. Are there any problems that faced by small businesses after obtaining bank financing?
5. What do small business enterprises in Egypt need to improve their financial performance?

RESEARCH AIM AND OBJECTIVES

Small businesses have usually been perceived as a dynamic force for economic growth and have a multiplying effect on the economy in Egypt. Socially entrepreneurship empowers citizens, generates innovation and changes mindsets. Economically entrepreneurship stimulates markets. The formation of new business leads to job creation. Thus, entrepreneurship is described as a potential engine to support economic growth, they have the potential to integrate developing countries into the global economy, but access to finance by small businesses is always a major obstacle for many small businesses. (Elsaid et al., 2011).

The overall objective of this research is to measure the impact of bank finance at a natural interest rate on the financial performance of small businesses in Egypt. In addition to explaining the importance of bank financing for small businesses, where small companies suffer from many problems, both before obtaining finance or after obtaining financing. The literature review revealed that there are different views on the impact of bank financing on the financial performance of small businesses. There are three objectives that are aimed to be achieved:

1. Measuring the impact of banking finance on the financial performance of small business enterprises in Egypt.

2. Measuring the role of loans volume and firm leverage on the financial performance.
3. Measuring the role of loans volume and firm age on the financial performance.

Research Hypotheses

Two main research hypotheses are developed. Each hypothesis is tested once against the whole sample of Small Businesses and another time against Small Businesses with loans only. Hypotheses are stated as follows:

H1: banking finance have a significant impact of small business Financial Performance

Sub H₁: banking finance have a significant impact of ROA

Sub H₁: banking finance have a significant impact of ROE

Sub H₁: banking finance have a significant impact of NPM

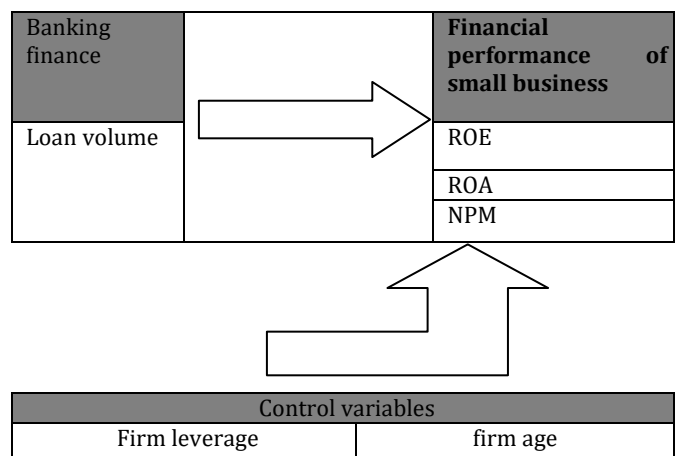
H0: banking finance have an insignificant impact of small business Financial Performance

Sub H₀: banking finance have an insignificant impact of ROA

Sub H₀: banking finance have an insignificant impact of ROE

Sub H₀: banking finance have an insignificant impact of NPM

Research Framework



EXPERIENCES OF SMALL BUSINESSES IN EGYPT

First on December 16, 2008 the Central Bank of Egypt issued decision, No. 2408 which includes the following: Banks are exempt from the 14% deposit reserve ratio that provides credit facilities to SMEs, this decision applies to companies that have sales from 1 million pounds to 20 million pounds and has a capital of 250 thousand pounds to 5 million pounds. Determine the size of the company's business by submitting audited financial statements from the

auditor; The Egyptian Banking Institute prepares studies, qualifies human cadres and establishes specialized departments that provide services to SMEs (www.cbe.eg). Second On December 3, 2015 the Central Bank of Egypt issued a decision which includes the following:

A small business is defined as follows: In medium companies, the capital ranges from LE 5 million to LE 10 million to industrial companies and from LE 3 million to LE 5 million to other companies. Manpower ranges from 10 to 200 workers and sales from 20 million to 100 million pounds. In small companies, the capital ranges from 50,000 pounds to 5 million to industrial companies and from 3 million to 5 million to other companies. Manpower ranges from 10 to 200 workers and sales of 10 million to 20 million pounds. In very small companies, the capital and manpower are the same as that of the small companies but the sales range from 1 million pounds to 10 million pounds. Amend the Central Bank of Egypt initiative issued on December, 16 2008 to include only small and very small companies and cancel the element related to the presentation of financial statements approved by the auditor, which determines the size of the business.

Third on December, 6 2015 the Central Bank of Egypt issued a decision which includes the following: Increase the loans and facilities portfolio granted to SMEs by at least 20% of the Bank's total portfolio within 4 years from the date of issuance of these instructions; targeting LE 200 billion to finance small projects within 4 years (LE 112 billion was achieved until December 2018). The lending rate for small and very small businesses does not exceed 5% (decline simple rate). In addition to nurturing small industrial companies, small labor intensive businesses, small businesses that have innovative ideas and small businesses that target export. It does not allow the approval of new credit facilities to repay existing credit facilities to take advantage of the new pricing.

Fourth On February, 2 2017 a decision was issued by the Central Bank of Egypt stating the new definition of small business as follows: Medium companies, capital ranging from 5 million pounds to 15 million, industrial companies ranging from 3 million to 5 million and other companies, the workforce ranges from 10 to 200 workers, and sales range from 50 million pounds to 200 million pounds. In small companies, the capital ranges from 50 thousand pounds to 5 million, industrial companies ranges less than 3 million and other companies, the work force ranges from 10 to 200 workers, and sales range from 1 million pounds to 50 million pounds (www.cbe.eg). Allowing banks to finance small businesses whose sales range from 1 million to 10 million without obtaining audited financial statements and the lending rate for small businesses does not exceed 5% (decline simple rate).

The Central Bank of Egypt (CBE) supports the Credit Guarantee Company. The company decided at the end of 2017 to increase credit insurance policies in return for granting credit to small companies to LE 15 million instead of LE 2 million owned by public sector banks. In July, 2017, the Central Bank of Egypt decided that agro-processing, feed, fisheries and dairy projects with sales ranging from 250,000 to 50 million pounds have the right to benefit from the 5% initiative (www.cgcegypt.com). Finally, the Central Bank decided on January, 9 2019 to limit the initiative to industrial, health and contracting projects only

Experiences of Small business in Indonesia as a developing country

Indonesian MSMEs are the main players in domestic and economic activities, accounting for more than 99 percent of all existing firms across sectors in 2008 and providing employment for over 90 percent of the country's workforce mostly women and the youth. The majority of MSMEs in Indonesia are involved in agriculture (mada2011).

The growth of especially MIEs in Indonesia is more likely a reflection of poverty distress, as poor people are "pushed" to undertake such activities, the larger GDP share of MSMEs in Indonesia is mainly because the number of these enterprises is very huge. MSMEs in Indonesia have a number of constraints which include the lack of fund to finance their working and investment capitals, Limited access to financial resources; low innovation ability, difficulties in procuring raw materials and other required inputs, marketing and distribution; high transportation costs; problems caused by cumbersome and costly bureaucratic procedures, especially in getting the required licenses; and policies and regulations that generate market distortions (mada2011).

The Government has made regulations on small and medium enterprises, namely Law no. 20, 2008, however the development of SMEs is not satisfactory, because in fact the progress of SMEs is very small compared with the progress made by large companies. The regulation number 20, 2008 about Small and Medium Enterprises define a small enterprise are assets between 50 and 500 million rupiah and earnings between 300 million and 2.5 billion rupiah. Family business is one form of small and medium businesses and a major contribution in terms of employment and economic output. Most of the SME in Indonesia is a family business, built with family funds (Ilma et al 2012).

Indonesia has several organizations which concern to the entrepreneurship; one of the organizations is SMESCO that stands for "Small and Medium Enterprises and Cooperatives" was founded in March 2007 with one overall goal to promote

Indonesian products of outstanding quality to the world (Ilma et al 2012).

The identify sources of the competitiveness of SME in Indonesia on the level of innovation, entrepreneurship, human capital, financial resources, potential market and business strategy. Our findings show that SMEs need government assistance to develop marketing networks and access to financial institutions and financial access is very important to SME's business performance (Anton et al 2015).

The government In Indonesia has already implemented some policies to ease SMEs' financial constraint such as the low tax rate for SMEs that have a gross profit below 4.8 billion rupiah, which about 12% of the gross profit per annum. This tax rate is considered very low compared to the tax rate in many developed countries, which is around 15% per annum .Beside a low tax rate, the Indonesian government also provides a low-interest loan for low risk SMEs through the national banks, hoping that by this loan the SME can achieve significant growth. Nevertheless, with these policies, the government has not achieved a significant growth in the number of entrepreneurs in Indonesia (Suryo 2015).

Only 18% of the SMEs have access to formal sector finance and the remaining 82% still rely on internal savings and borrowing from family and friends. The Indonesian Ministry of Cooperative and SMEs, which identified that in 2011 the SMEs created job opportunities for 101,722,548 people in Indonesia (97.24% of the total employment in Indonesia) the SMEs' contribution to GDP is also substantial, with 57.94% (equal to 4,303,571.5 trillion rupiah) in 2011 (Suryo 2015).

Ministry of Finance provides insurance for 70% of the loans that are given to SMEs, while banks bear 30% of the risk .Under this scheme, there are six national banks and also 26 regional banks that have already joined in order to provide loans to SMEs with a rate of 13% for retail businesses and 22% for microenterprises with a ceiling of 20 million rupiah that can be borrowed by microenterprises (Suryo 2015).

Owners face the obstacles of external factors when sales are situational, such as holiday seasons, weather and seasonal rains. The government should give a nonmaterial support by providing easiness to letters/ permission arrangement or provide mentoring in the arrangement of the business license/collaboration. The owner needs to adopt information technology in order to obtain business information since the ability of MSMEs to survive in the increasingly competitive global environment depends on the capacity of the information owned, it is necessary to the owner of MSMEs to provide a good administrative system in financial management, provide training for the worker to develop skills, adopt

a system of quality control of products and have a good relationship with suppliers. The government needs to provide support in material such as the capital as well as marketing/promotion through varieties marketing programs and help to connect supplier with business owners (Tony et al 2017).

Finally: Small businesses in Indonesia still suffer from lack of funding, lack of awareness, lack of training and lack of competitiveness despite government efforts. Such as: setting a Ministry of Small and Medium Enterprises and Cooperatives that was founded in March 2007, the low tax rate for SMEs that have a gross profit below 4.8 billion rupiah, which is about 12% of the gross profit per annum and low interest rate of 13%. The government provides insurance for 70% of the loans that are given to the SMEs, while the banks bear 30% of the risk

Research Methodology and Sampling

Philosophy	Positivism
Approach	Deductive Approach
Design	Quantitative Research Design
Population	Small Enterprise in Egypt
Sample Size	90 small business firms in Egypt in period from 2013 to 2016 (annual report in 2013 and 2014 without loan, 2015 and 2016 with a loan).
Data collection	Historical Secondary Data collected from official periodicals
Statistical Packages	SPSS
Unit of analysis	Organizations unit of analysis where the data used is that of year 2017
Time Horizon	CNPMs Sectional

RESEARCH CONCLUSION

This study focuses on three main objectives; the first objective which is measuring the impact of banking finance on the financial performance of small business in Egypt is attained by formulating the first hypothesis and three sub hypotheses. The results have shown that loan volume have a negative significant impact on financial performance of small business, firm leverage has a negative significant impact on financial performance of small business and firm age has insignificant impact on financial performance of small business. The volume of bank financing help to increase leverage and bank interest expenses reduces net profit and also reduces equity (net profit as part of equity) thus have a negative impact.

There must be a financial management within each small company that is important to help to use bank financing in a timely manner and for the appropriate purpose. To achieve a positive effects of bank financing the banking finance should help the assets turnover to increase net profit, provide the awareness of the use of short-term financing in short-term investments and the use of long-term funds in long-term investments, and the use of financing for the purpose specified for it and not for any other purpose . Finally, small projects cannot afford the costs of bank financing at the normal price and the effects will be negative. This shows the importance of the initiative of the Central Bank of Egypt issued in January 2016 at an interest rate of 5% and the MSME Development Agency initiatives issued at the end of 2014 with a 10% and in 2019 with a 13% return rate. We should not stop at interest rate only, small business do not take advantages comparing with large companies.

The government has to support small enterprises while offering tax and guarantee benefits to small enterprises and provide procedural advantages in the industrial cities of small entities related to the process of obtaining land or the extraction of licenses. The Chambers of Commerce and Small Business Development Agency must provide training programs for small businesses related to capital management, human capital management, the extraction of export card, training programs related to customs procedures, international trade agreements with the same degree of interest to senior firms, set database that includes the number of small projects in Egypt, the number of beneficiaries of initiatives and the value of funds provided.

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