



# Bank Lending to SMEs

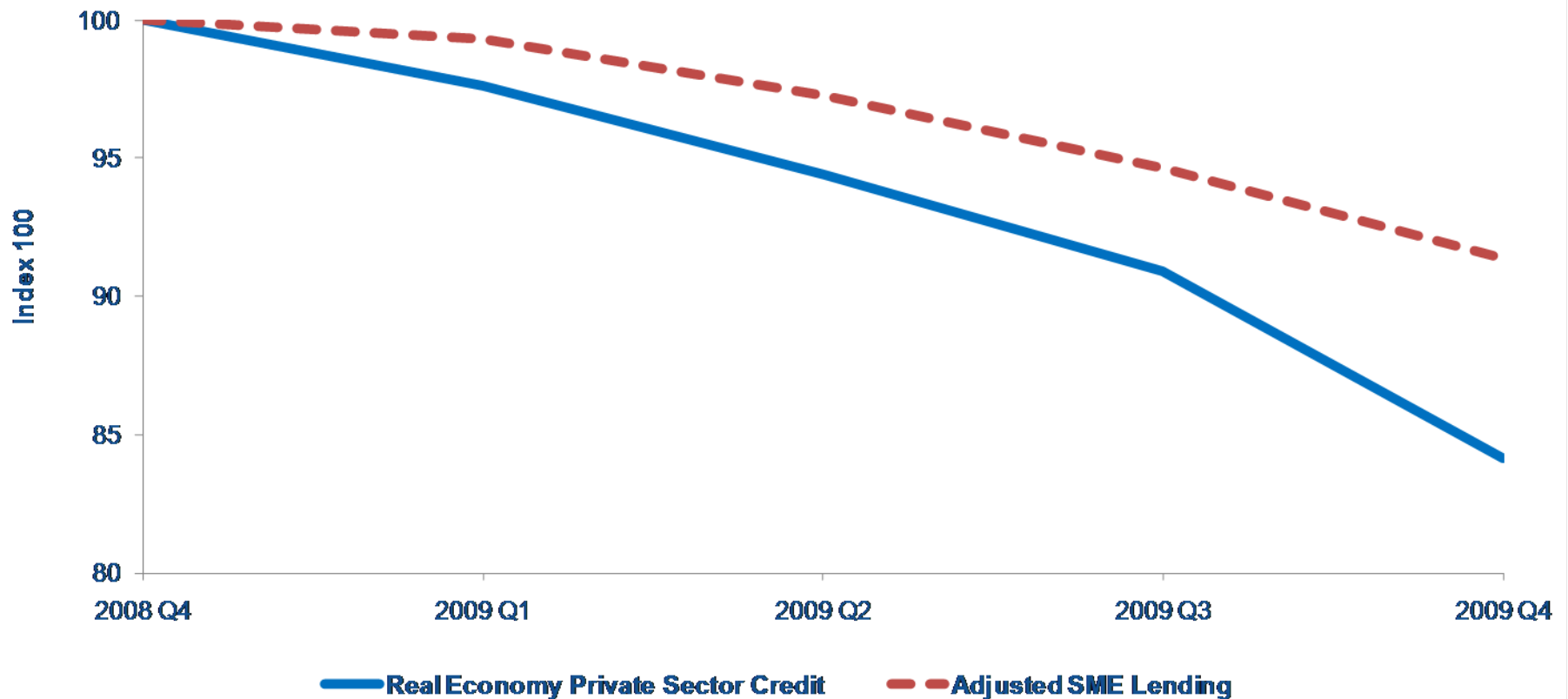
Dera McLoughlin  
Partner

- **3 Mazars Reports on Lending to SMEs to date**
  - ▶ Mazars 1            7 months            June 2008 to February 2009
  - ▶ Mazars 2            9 months            March to September 2009
  - ▶ Mazars 3            3 months            October to December 2009
- **Commissioned by Department of Finance**
- **Examined**
  - ▶ SMEs  $\leq$  250 employees,  $\leq$  €50m turnover,  $\leq$  €43m balance sheet
- **Focused on “real economy” business activity & excluded:**
  - ▶ Speculative construction
  - ▶ Charities
  - ▶ Private lending
  - ▶ Non SME financial intermediaries, credit unions, SPVs, pension schemes

# Overall Lending in the Economy

Lending to SMEs falling but more slowly than overall lending in the economy

Real Economy Private Sector Credit vs Adjusted SME Lending, Index 100 = Dec 08



SOURCE: CBFSAI; Mazars SME Lending Reports

# Total Lending to SMEs

## Small decrease in the value of lending to SMEs

1.2% – as compared to Q3 2009

3.6% – as compared to Q4 2008

	Q4 2008 €million	Q4 2009 €million	% Change Q4 2009 V Q3 2009	% Change Q4 2009 V Q4 2008
Loans	26,677	26,340	-0.5%	-1.3%
Overdrafts	2,845	2,833	-1.8%	-0.4%
Finance & leasing	3,058	2,407	-7.0%	-21.3%
Invoice discounting	907	700	-3.7%	-22.8%
<b>Total</b>	<b>33,487</b>	<b>32,280</b>	<b>-1.2%</b>	<b>-3.6%</b>

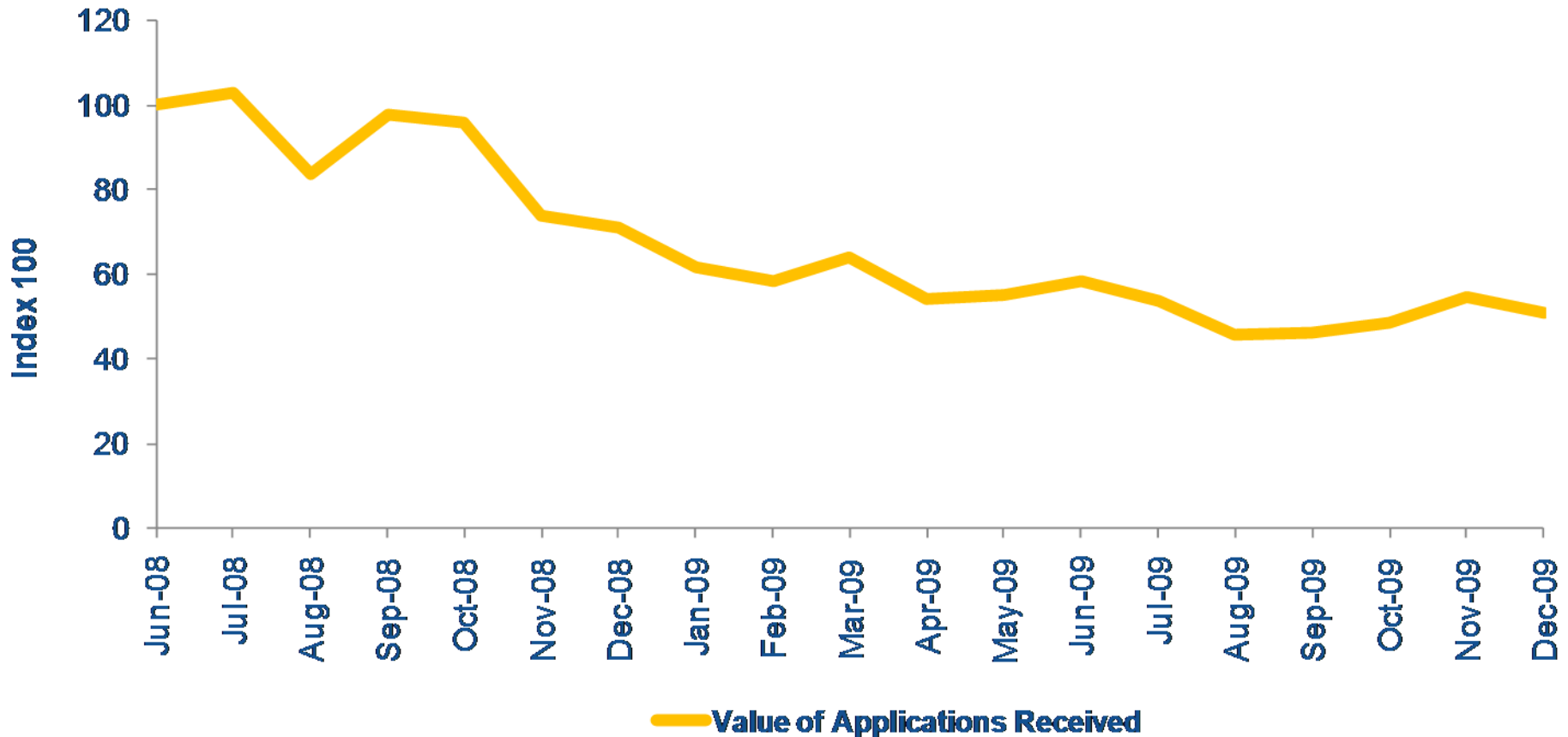
# Total Lending to SMEs – by Sector

	Q4 2008 €million	Q4 2009 €million	% Change Q4 2009 v Q4 2008
A – Agriculture, Hunting & Forestry	4,403	4,150	-5.7%
B – Fishing	345	325	-5.8%
C – Mining & Quarrying	325	303	-6.8%
D – Manufacturing	2,869	2,630	-8.3%
E – Electricity, Gas & Water Supply	292	279	-4.5%
F – Construction	1,355	1,249	-7.8%
G – Wholesale/Retail Trade & Repair	7,379	6,954	-5.8%
H – Hotels & Restaurants	7,172	7,327	+2.2%
I – Transport, Storage & Communications	1,695	1,512	-10.8%
J – Financial Intermediation	359	348	-3.1%
K – Real Estate, Renting & Business Activities	4,051	3,816	-5.8%
M – Health & Social Work	1,350	1,472	+9.0%
N – Other Community, Social & Personal Services	1,892	1,915	+1.2%
	<b>33,487</b>	<b>32,280</b>	<b>-3.6%</b>

# Applications for Credit

Credit Applications from SMEs down approximately 50% since June 2008

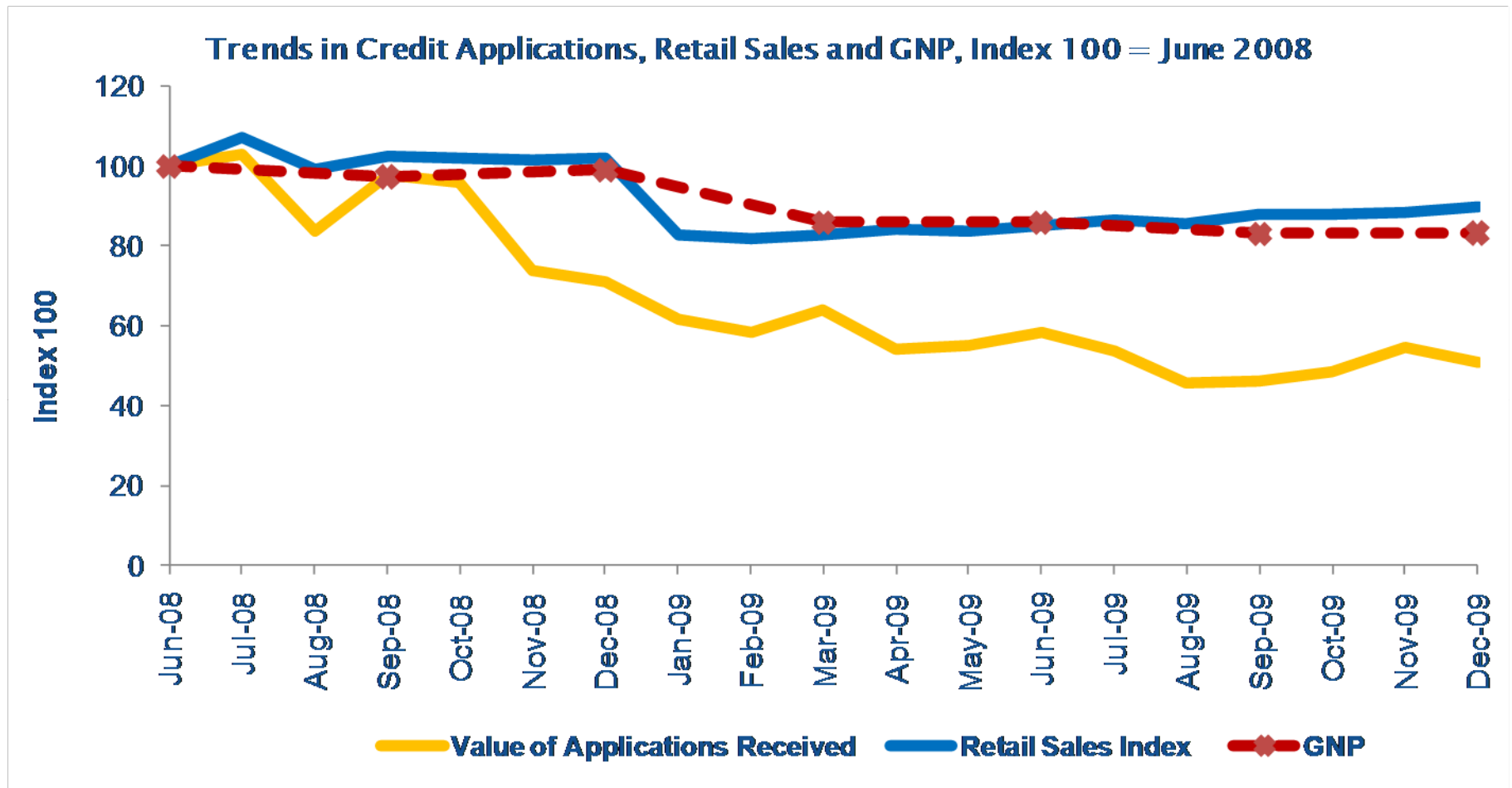
Trends in Credit Applications, Index 100 = June 2008



SOURCE: Mazars SME Lending Reports

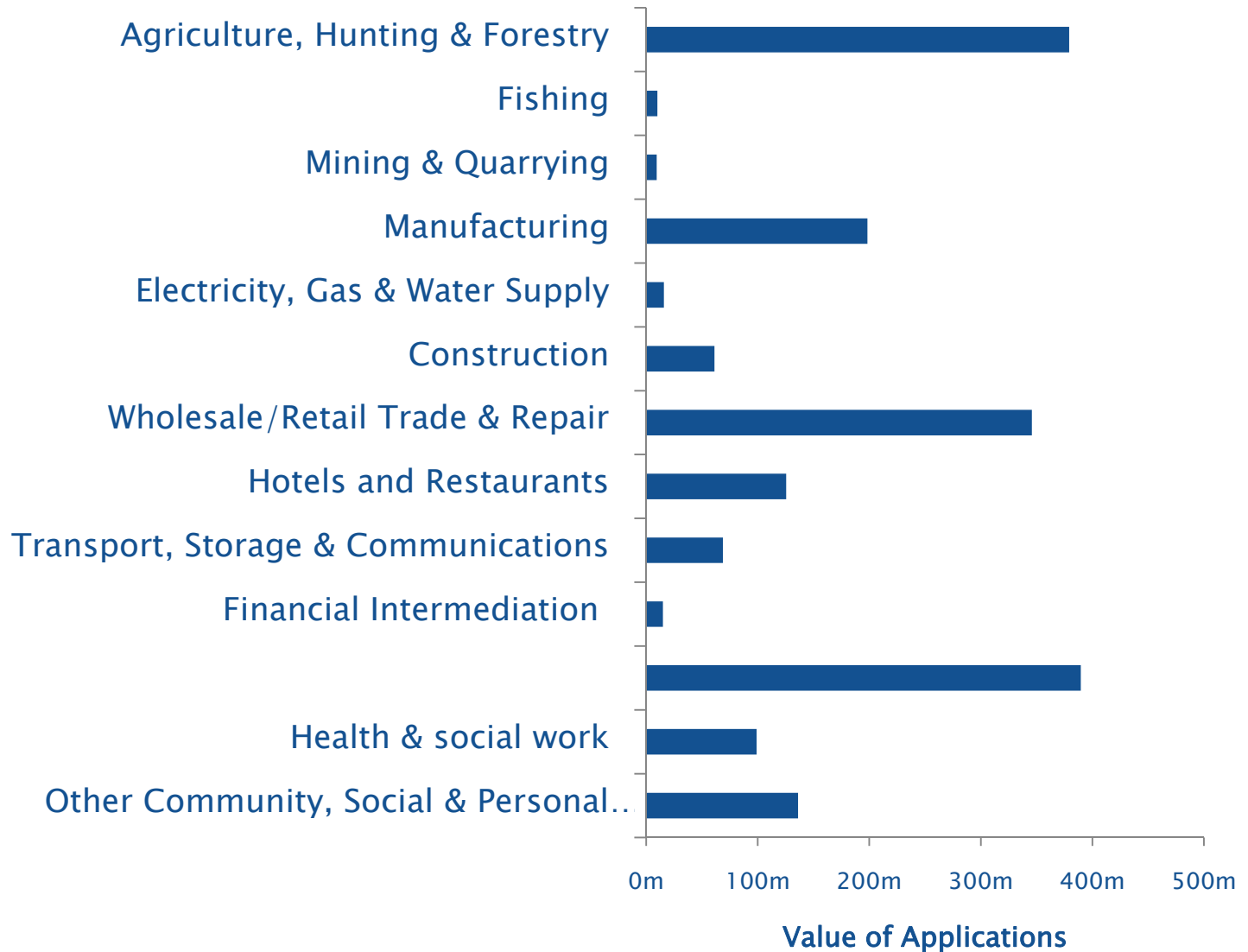
# Applications for Credit V Economic Demand

Credit applications from SMEs declining against background of shrinking economy



SOURCE: Mazars SME Lending Reports; Central Statistics Office

# Approvals



# Other Key SME Lending Indicators

## Drawdown Level

- Decrease from monthly average of €377 2008 to €356 million in quarter

## Overdraft Utilisation Levels – Working Capital Capacity

- Value of approved overdraft limits fallen by 7% since last year
- But up to €2.6billion available for working capital
- 48% of approved limits

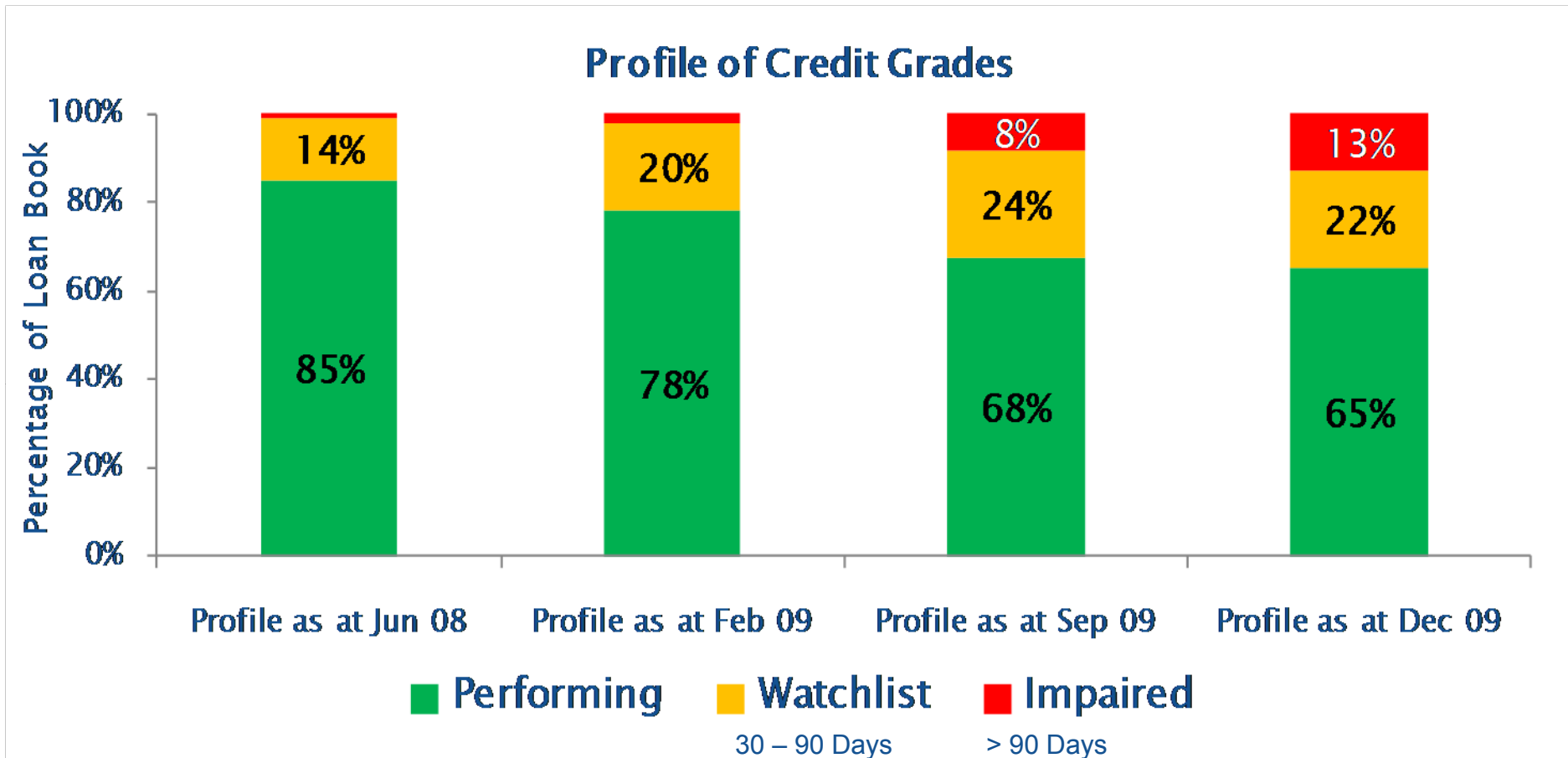
## Repayments

- At December 2009 – 5.2 years
- SMEs currently making greater repayments than credit drawdowns

# SME Distress

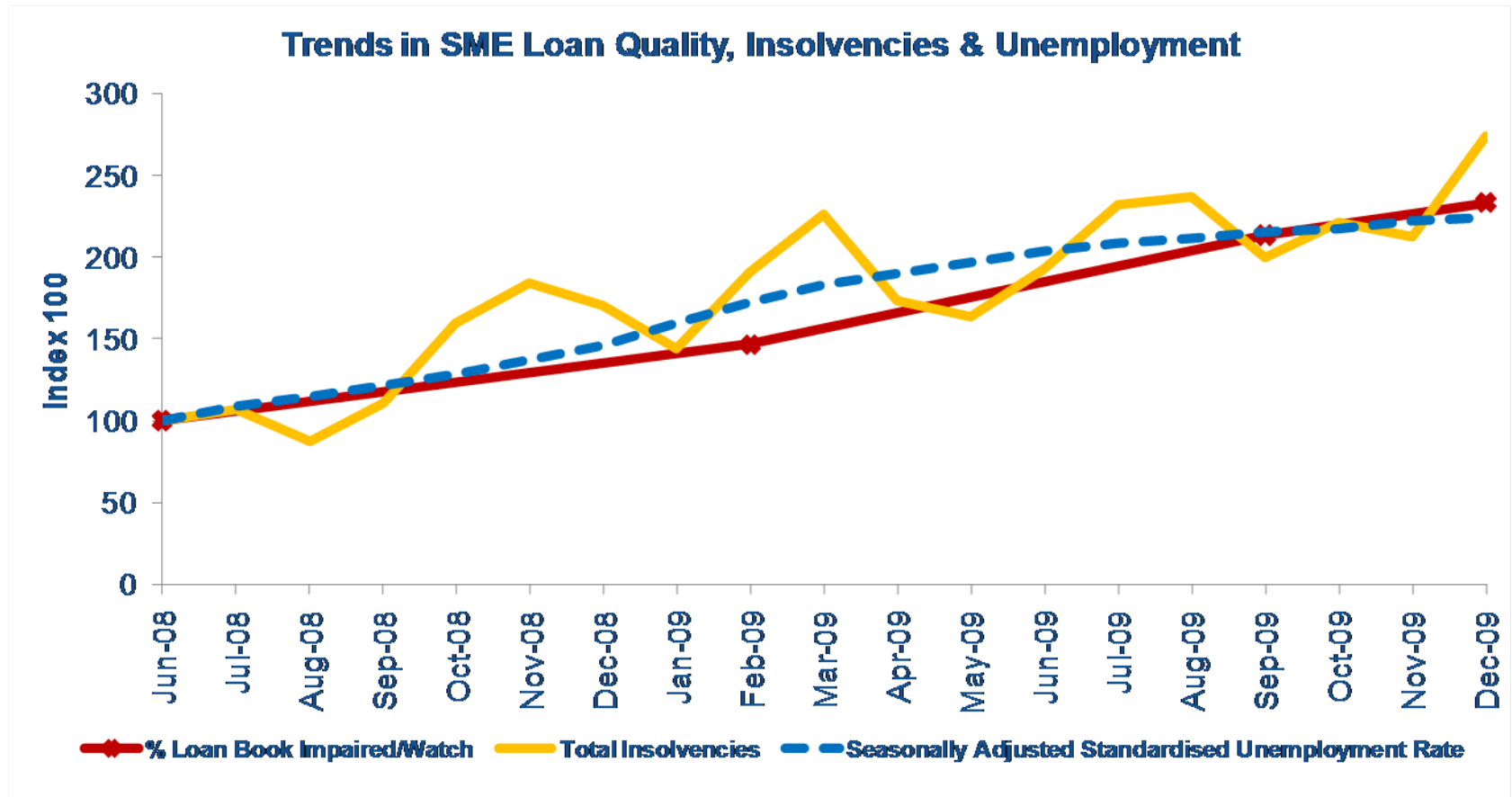
Continued distress in SME loan quality – although stabilising somewhat

35% of SME loan book – overdue



# SME Distress V Other Economic Difficulty

Level of distress in SME loan book continues in line with other indicators of economic difficulty



SOURCE: Mazars SME Lending Reports; Central Statistics Office; Insolvency Journal

# What are SMEs Saying

- 1,200 SMEs
- All sectors of the economy & sizes of business
- Truly representatives of all Irish SMEs

## Trading Conditions

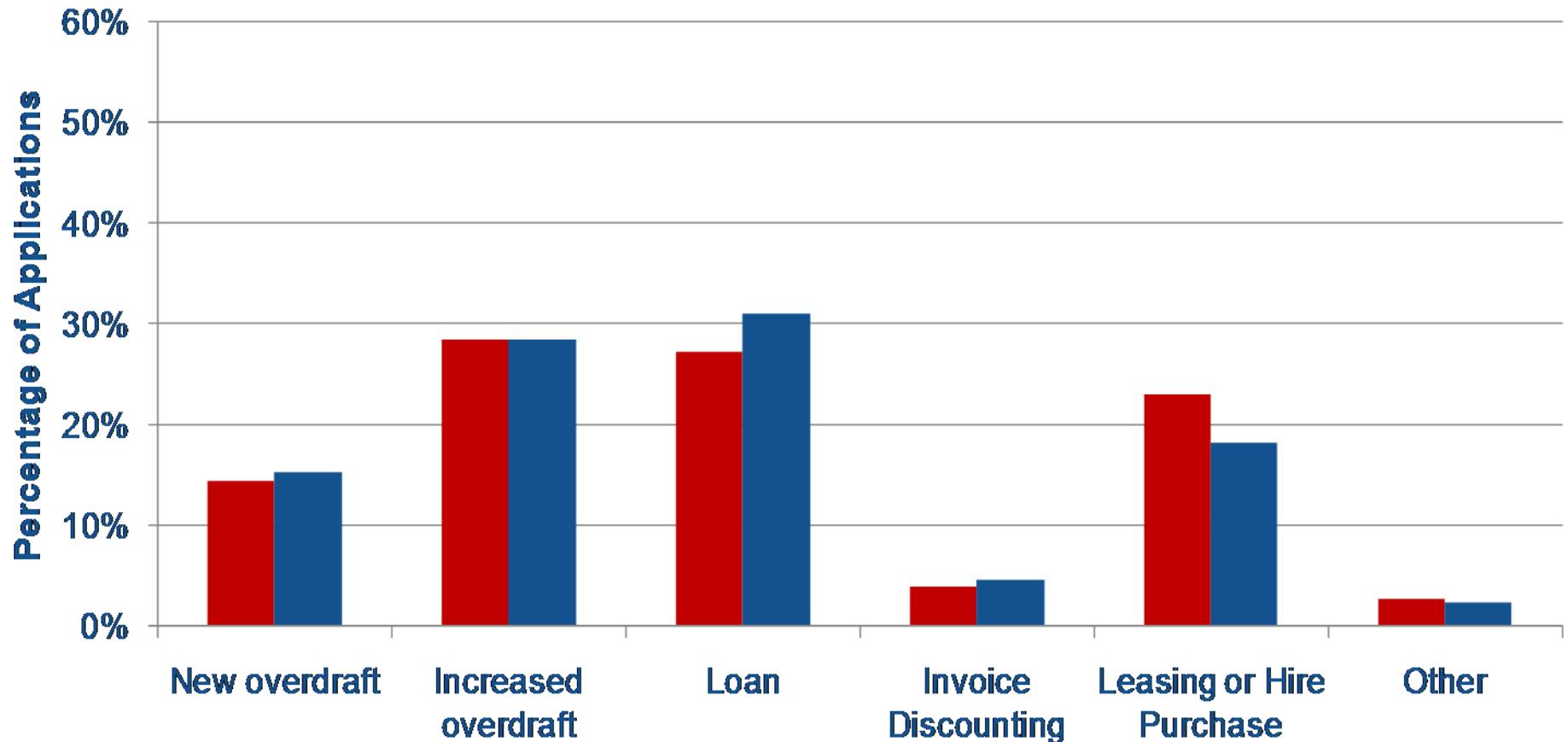
- Continued difficult trading conditions
- 78% reported a continued decrease in turnover
- 45% reported more than 20% decrease in turnover
- Levelling off in rate of decline of employee reductions

## Demand for Credit

- 46% of respondents made one or more requests for credit
- 79% of applicants made a formal request
- 11% applied for a form of non bank finance

# What are SMEs Saying

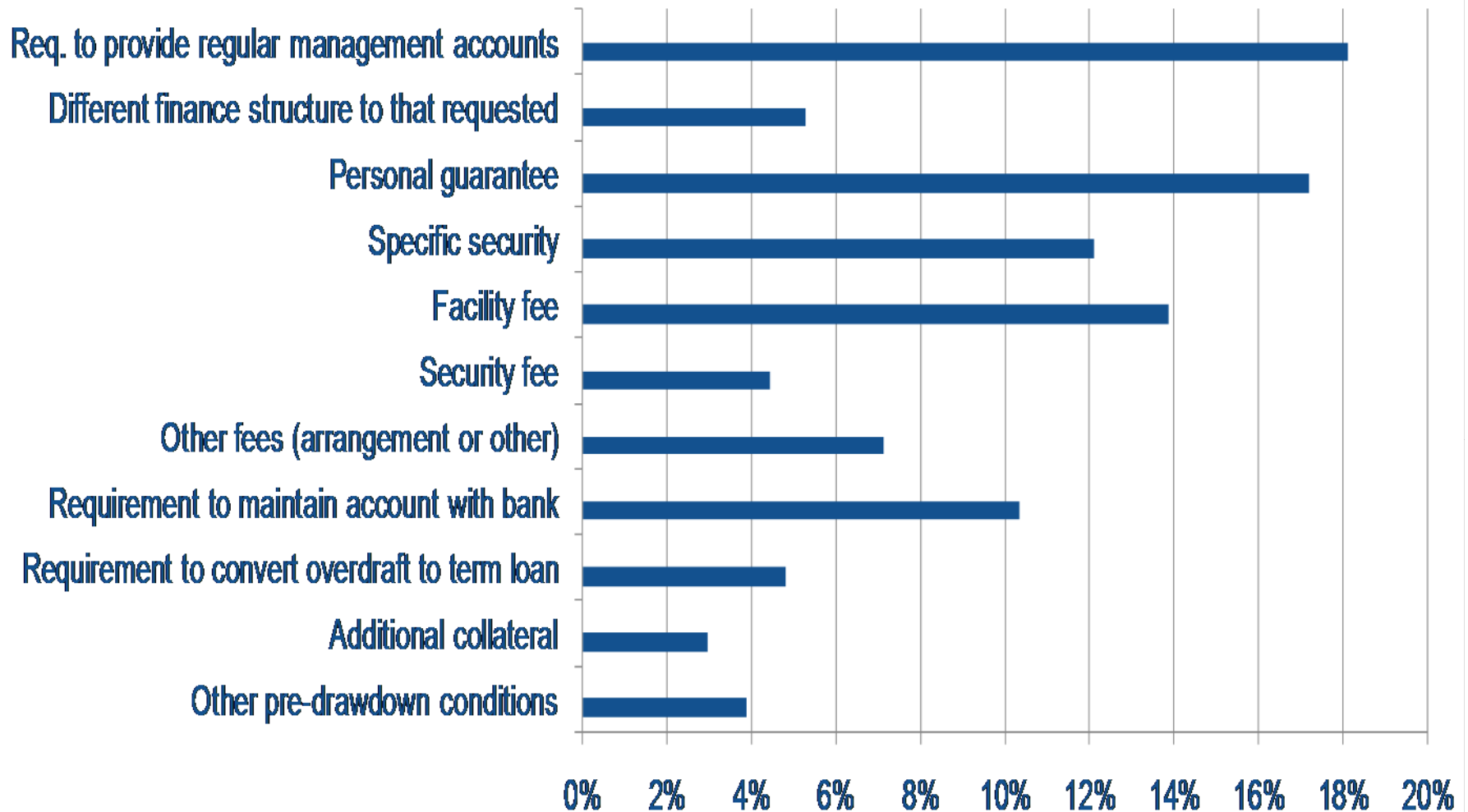
Type of Credit (Product) Requested



# What are SMEs Saying

Reason Request	
Working capital / cash flow	24%
Decline in business revenues	17%
Slow down in debtor collection	12%
Bad debts increasing	9%
Increase in supplier costs	6%
Expansion	9%
Property related loan	5%
New business venture	7%
Other	11%
	100%

# What are SMEs Saying



# What Support is Available

1. Code of Lending to SMEs
2. Credit Review Office
3. Formal application
4. Minimum level of information expected
5. SME specific credit funds & products
6. New €3billion – AIB & BOI

Credit guarantee scheme

- Mazars SME Lending Reports show fundamental shift in lending & borrowing patterns
- Lending to SMEs has declined more slowly than overall lending
- Credit applications fallen by 50% in last year
- Continued distress amongst SME's – 35%
- Support available
  1. Code of Lending to SMEs
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  5. SME specific credit funds & products
  6. New €3billion commitment – AIB & BOI



# Observations on Current Banking Trends

Tom O'Brien  
Partner – Financial Advisory Services

There are a number of factors that will impact on the lending approach adopted by banking institutions including:

- Recapitalisation/funding issues
- Impact of NAMA on loan book
- Reorganisation of internal structures
- Risk appetite v's reward
- New business targets set down

# Bank Lending – Welcome to the New World...

## ➤ Hot sectors

- Food & Agri business
- Energy
- Waste
- Primary Healthcare
- Community & leisure
- Professional services

## ➤ Change in lending dynamic

- Cash flow is key
- Less importance placed on asset backed lending
- EBITDA/debt multiples significantly lower
- Greater equity input from borrowers – maximum LTV of 70% - 80%- generally lower
- Minimum interest cover requirements
- Shorter repayment periods on term facilities
- Financial position of promoter
- Non recourse generally not available
- Increased focus on personal guarantees

# Bank lending – Welcome to the New World...

## ➤ Pricing

- Increase in margins - expect minimum margin of 2.5% over 3 month cost of funds
- Funding premiums – can be up to 1.5%
- Arrangement and exit fees
- Limited potential for negotiation

## ➤ Product specific issues

- Invoice discounting
- Asset finance
- Overdraft/term loan

# Recent Case Experience

## ➤ Increased focus on covenant compliance

- Waiver fees
- Renegotiate terms and security or
- Both!!

## ➤ Restructuring existing facilities

- Contingent fees
- Cash sweeps
- Debt/equity swaps

## ➤ Reluctance to extend exposure to fund shortfalls in working capital requirements in certain cases

- Additional commitment from promoter
- Review of invoice discounting facilities may be an option

- **Rollup of existing interest only facilities now difficult to secure**
  - Conversion to term
  - Rollup of interest only on the basis of upfront capital repayment or
  - Revision of interest rate
  
- **Increased focus on overdraft accounts**
  - Should be in credit for a minimum of 30 days in any year
  - Not to be used as core medium/long term financing
  - Conversion to term facility

# Tips for Success

- **Ensure that the bank understand your business**
  - Invite bank to place of business
  - What markets do you operate in
  - Who are your competitors
  - Differentiation/ USP
  - Customer profile
  - SWOT analysis
- **Provide accurate, relevant & timely financial information**
- **Maintain open lines of contact**
  - Early warning of potential issues
- **Quality of management team and their advisors**
- **Important that new proposals**
  - Demonstrate risk sharing ie. LTV <80%
  - Are realistic and include range of scenarios stressed for different outcomes
  - Contain contingency plans to cope with the unexpected
  - Allow flexibility should activity levels drop ie. is invoice discounting appropriate to your business in the current environment?

- **Allow flexibility when agreeing covenants**
  - Ensure base case is prudent with appropriate headroom
  - Don't overpromise and underachieve
  
- **Understand your facility agreements - Are there specific restrictions on**
  - Proprietorial remuneration/expenses
  - Related party transactions
  - Particular consents required in order to undertake certain transactions
  
- **In multi-banked situations ensure**
  - That bank that does not have current account has sufficient visibility on performance and activity
  - Do not use income from asset financed by Bank A to repay Bank B





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