The Analysis of Financing Structure Optimization Problem in Small and Medium-sized Enterprise

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Abstract. Although the contributions of small and medium-sized enterprise (SME) to economic development are more and more important in China, there are difficulties in financing which is signed the "bottle-neck" problem. Therefore, it is particularly important to optimize SME financing structure. Because optimizing the financing structure of SME can help enterprises establish the scientific financing structure, improve its own financing efficiency, and enhance the enterprises' competitiveness to meet the market. At first, this article briefly describes the status of SME in the economic development and the problems faced by it. The paper then analyzes four main issues on the presence of SME financing structure: the proportion of equity capital and debt capital is irrational, the structure of debt capital itself with equity capital is unreasonable, the ratio of internal financing in equity capital is extremely low, the method of financing is single. The paper further proposes some measures to optimize the financing structure, including: optimize the ratio of equity and liabilities, keep capital structure some flexibility and maintain a virtuous circle, establish a reasonable financing order via learning from overseas financing experience, innovate the methods of SME financing. Finally, the paper introduces the SME objectives of financing optimization in China.

Keywords: Small and Medium-sized Enterprise; Financing Structure; Financing Method; Internal Financing

1. Introduction

1.1 Status and Problems Faced by SMES in the Economic Development

Small and medium-sized enterprises are the most active power in modern social economy development. Its function and position are not allow to be ignored in any countries and regions. Smes’ development has been hot economic problems and be common concerned by various countries government and many economists in the long-term. The small and medium-sized enterprises has become an important force in building the socialist market economic system in the economic development of our country. They are playing a more and more important role in promoting rapid economic growth, maintaining market prosperity, expanding employment and increasing in taxation. The total number of Smes in China has reached to more than 4,200 million by the end of 2008, accounting for total enterprise's number 99.8 percent above. Small and medium-sized enterprises demonstrates gross industrial output a 29.79% year-on-year increase, sales revenue a 30.46% year-on-year growth, the profit 8255.39 billion yuan, an increase of 43.22%, tax payment rose by 27.43%. Growth rate is higher than the national average. Smes provide society with 75% of the urban employment opportunities.

Small and medium-sized enterprises make tremendous contributions to China's economic development in recent years. small and medium-sized enterprise external financing faces problems due to the rising prices of raw materials, labor cost increasing, bank tighter credit factors such as intensifying competition. The majority of small and medium-sized enterprises, especially small and medium-sized private enterprises by private
capital investment complete the primitive accumulation of capital. When the enterprise developing to a certain scale, especially from labor-intensive to technology-intensive transition, internal financing is hard to meet the enterprise investment demand and external finance demand will be increasingly urgent. The smes' financing channel is narrow and the shortage of capital constraints smes development has become the main bottleneck because the national finance policy limit and people shackles of traditional ideas, and small and medium enterprises’ problems.

1.2 Smes’ Financing Structure Status in Our Country

Generally speaking, enterprise's financing structure is to show enterprise various financing source the proportion between the relations, namely self-capital (equity) and borrowed funds (debt) composition condition. It is measured one country capital allocation of resources and the level of economic development important symbol.

Small and medium-sized enterprise financing mode is different from big enterprises because of its assets, small scale business uncertainty big, financial information opaque, bear external economic impact ability, such as low restraining factors, plus its operating flexibility requirement. Overall the sme financing structure in our country has the following features currently: Firstly, small and medium-sized enterprises, especially small businesses depend more on internal financing than large corporations in the financing channels. Smes’ financing structure in the proportion of internal financing is less than 20% comparing with the developed countries because of small and medium-sized enterprise ego accumulation and less profitable causing internal financing source impeded. Investigate its reason: enterprise management level is low, the ego accumulation is consciousness, internal profit distribution exists in the tendency, long-term business thought is lack. Secondly, small and medium-sized enterprises depend more on debt financing during the exogenous financing way choice, mainly depends on debts from bank loans and other financial institutions. But small and medium-sized enterprises are difficult to obtain bank credit funds support and bank loans in financing structure in proportion is less than 10%. Investigate its reason: on one hand is due to a lack of the supporting of national policy, the credit rating of small businesses and business in the development is usually lower. The bank give up sme loans support for preventing financial risks; On the other hand is due to financial accountin not real problem existing in small and medium-sized enterprise and they do not have a credit basis. Thirdly, debt financing in small and medium-sized enterprise shows small scale, high frequency characteristic. More and more small and medium-sized enterprises dependent on enterprise's commercial credit, equipment leasing from non-financial institutions of various financing channel and folk informal financing channel.

2. Problems Existing in Smes Financing Structure

2.1 Irrational Proportion Between Equity Capital and Debt Capital Amount

In theory, companies capital can be divided into own funds and borrowed money according to its nature. Own funds is investors invested into the company's capital and operating formation in the accumulation, which reflects the enterprise owners’ equity, say again equity funds. Borrowed money is absorption funds from the bank, and other financial institutions and other enterprise etc, also called debt funds. Equity funds have the vital significance for the management and development of the enterprise, which is not only the initial operation of capital enterprise foundation and is but also the basis of liability undertaken by the enterprise. Enterprise's normal operation and development is affected, enterprise financial risk increases and enterprise's survival poses a threat if an enterprise equity funds is less, debt capital is too much and unreasonable capital structure.

Most of the small and medium-sized enterprises should rely mainly on equity capital. The ratio of equity capital is less and less and the ratio of liabilities is more and more with the further development. Our smes asset-liability ratio is 70.36% compared to 54.82% of the large enterprise according to the state statistics bureau census. So high asset-liability ratio not only directly affects their financing ability and brings serious financial risk and financial crisis for enterprises.

2.2 Equity Capital and Debt Fund Itself Structural Imbalance
Internal informal equity of equity capital and listed stock fundraising proportion is very low. Corporate indebtedness mainly comes from bank loans and commercial credit from debt capital internal. Enterprise financing proportion is almost zero through issuing bonds. In bank loans fixed assets loans less and less, liquidity loan period shorter and shorter according to the relevant data shows. 53.09% enterprises made 1-3 years of long-term loans and 46.90% enterprises had no long-term loans according to 2006 provincial bureau to the province of small and medium-sized enterprises long-term loans and satisfaction survey. this shows that small and medium enterprises are difficult to get bank loans and more difficult to obtain bank long-term loans. Equity and debt capital internal structural is imbalance, making the sme financing serious is lack of flexibility.

2.3 Equity Capital in the Ratio of Internal Financing is Extremely Low

Internal financing refers to the process of enterprises' retained earnings and depreciation transferring for investment. Enterprise internal financing size dependends on profit level and net assets scale, and other factors. According to the modern western capital structure theory "the financing law", internal financing is the first enterprises' financing choice. We can save transaction costs, reduce the income tax expenses, and improve the investment returns because converting profit to investment will contribute to the enterprise assets value. The ratio of internal financing is low in small and medium-sized enterprises in China.

Smes’ financing order departs from modern capital structure and other western developed countries financing practice plainly. The study found that developed countries enterprise mode of financing arrangements for: retained earnings is preferred, followed by debt financing, the last is equity financing.

Asset-liability ratio is high in the basic capital structure, viz., the percentage of debt and equity of Small and medium-sized enterprises in China. In the capital structure of the second level, enterprise internal excessive rely on bank loans in debt. Internal financing proportion is low in the equity internal, equity financing proportion is high.

Smes' funds mainly comes from all kinds of loan according to the state bureau investigation, accounting for enterprises to acquire funding sources of total 70.65%; Internal financing proportion is very low, especially medium-sized enterprises accountes for only about 20% higher, the small business is only 2 to 3 percentage points higher.

2.4 Single Financing Mode

Through the above analysis, we can draw: Smes' financing relies mainly on all kinds of loan from the financing structure perspective, namely to exogenous financing is given priority to, a small proportion of internal financing. Bank loan is first in external financing. Smes' financing channel is unitary, the bank loan mainly of indirect financing is high proportion and direct financing in its capital structure is in marginalized status.

3. Smes Financing Structure Optimal Measures

3.1 Optimizing the Capital Structure of The Proportion Between the Rights and Liabilities

We must improve enterprise internal financing ability and enhance the competitiveness of enterprises. Improving enterprise internal financing ability can increase corporate equity financing proportion, reduce financing costs and reduce enterprise debt-repaying risk. In the long run, it can enhance the enterprise market competitiveness. On the one hand, the enterprise should carry on the modern enterprise system reform and transform the management mechanism. They should improve the production and operation of enterprises management, change market environment and constantly develop new markets. They should strengthen internal management and save various expenses., They should speed up the capital turnover, reduce the production cost, improve quality and structure, reduce profit allocation and other measures through the rational configuration of assets to promote enterprise profitability growth, continuously improve the economic benefits of the basis, continuously improve the fund and undistributed extraction proportion, expand the self-owned capital scale, improve its regulatory capital adequacy ratio and broaden the source of retained earnings. On the other hand, they should reasonably formulate and utilize plan to reduce taxes and increase enterprise
depreciation fund. In addition, the state should have a beneficial to the enterprise internal accumulation of tax system, financial system, so as to reduce business tax.

Capital market must be further developed. Perfect and multi-level securities market system must be set up. Thus different levels of the market have different financing management conditions and different style of trade and different companies such as scale, profitability requirements to meet financing and equity transaction needs of many small and medium-sized enterprises and high-tech company do not have the mainboard listing qualifications. For example, second market scale is further strong expanded and small and medium-sized enterprise bond issuance is increased.

Smes' quality is improved and smes' financing ability is continuously enhanced. We should further standardize enterprise management structure, clear definition of property rights, adjust the optimizing structure of organization, simultaneously must strengthen qualities, enhances the enterprise the management efficiency and internal cohesiveness and management to enhance the enterprise financing capability. We should establish long-term goal of enterprise development on the basis of continuously improving economic efficiency, continuous accumulating fund of extraction and undistributed, expanding the self-owned capital scale and improving its regulatory capital adequacy ratio.

3.2 Benign Circulation and be Flexible of Capital Structure

Capital structure is relationship and scale ratio between the enterprise long-term debt capital and equity capital structure. Capital structure is a kind of dynamic portfolio. New raise funds’ joint may cause the current reasonable capital structure produces too high or too much debt equity capital, etc. One of task of enterprise financial management is to adjust irrational capital structure through the financing management. Otherwise, it would form a vicious circle if we don’t strengthen beforehand prediction and planning and not execute the initiative of financial management. Therefore, the enterprise shall be paid to find a realizing capital structure a virtuous circle of the road in research capital structure problems. They should start from establishing the reasonable capital structure of enterprise, look high benefit and appropriate risk as foothold, innovate financing ways, implement new financing structure, the investment structure and assets structure combination, thus realize reasonable capital structure. Enterprise should pay attention to the capital structure be flexible in optimizing the capital structure, besides maintaining the capital structure of the benign circulation outside. Capital structure flexibility refers capital structure adjustment and the possibility of a change at any time. Enterprises’ profit level, management condition and market environment is not unalterable in producing management process, therefore, business capital structure should be in response.

3.3 Referencing Foreign Financing Experience to Establish Logical Financing Order

Theory of modern capital structure is "the financing law" in the western developed countries to be universal test and verify. According to "financing law", the reasonable financing order is: Retained earnings, debt financing, stock financing. Smes can draw lessons from the experience and combine the actual conditions and determine the reasonabl financing order in the financing decision. In various financing channels, enterprises should be preferred tendency of internal financing. The biggest advantage of internal financing is free. It includes no financing cost and no external trade, thereby avoids transactional tax cost. Also, internal financing risks is less for the enterprise. It still can increase the strength of corporate and corresponding increase enterprise's reputation, thus enhance enterprise's financing capability. Financial personnel should consider the outside financing after enterprise in excavation internal resources.

3.4 Financing Mode Innovation

The financing mode refers to small and medium-sized enterprises realize the financing specific methods and form in the financial markets. Generally speaking, small and medium-sized enterprises will be more and more multi-layered situation the financing way along with our country market economy unceasing development, financial market increasingly activity and financing channel increasing gradually. Say from big field, enterprises financing solve the question of funds from two ways of internal financing and external financing. When the internal financing cannot satisfy the requirement, external financing channels can solve. From the actual situation, the external financing is the mainly the financing channels and sources of medium
and small enterprises, which includes bank loans, bonds, financing lease and commercial credit such debts and absorption direct investment, financing, such as issuing stocks and interests form.

4. Optimization Goal of Smes Financing Structure

"Japan-German mode" and " Anglo-Saxon model" are regarded the financing structure mode internationally at present. "Japan-German mode " is a main bank mode and " Anglo-Saxon model " reflects a kind of worldwide-diversified market mode.

"Japan-German mode" is perhaps an inevitable choice If the medium and small enterprises in China want to develop from the medium term. "Japan-German mode" provides enterprises most external funding by bank comparing with "Anglo-Saxon model ". This largely replaces " Anglo-Saxon model " a series of function in securities and bond market and forms a set of special argues relationship financing system. Japanese firms can rapidly expand in this mode, which is fit for the rapid expansion of small and medium-sized enterprises at present. "Japan-German mode" can be adopted at present for China's smes’ development.

However, "Anglo-Saxon model" should be more beneficial to small and medium-sized enterprises’ long-term development with external financing ways innovation and development in the long run along, especially develop more perfect capital market, According to above analysis for smes financing ways, we should promote non-bank financial institutions development after smes achieved state-owned specialized bank commercialization share and state-owned enterprises in Japan and Germany in accordance with the "Japan-German mode". The target mode will be gradually transited into the future of target mode, namely the diversity "Anglo-Saxon model" with the perfection of the market economic system and mature financing mode of our country.

5. References


