SMEs in Europe

- Definition provided in EU recommendation 2003/361

- SMEs are around 20.7 million firms
- accounting for more than 98% of all enterprises
- of which the biggest part (92.2%) are firms with <= 10 employees.
- for 2012 it is estimated that SMEs accounted for 67% of total employment and 58% of gross value added (GVA)[1]
- But how much do they weight in the balance sheet of the banking system?
- The ECB does not provide such an info.

[1] Source: Annual report on small and medium-sized enterprises in the EU, 2011/12. ECORYS for the EC

SMEs in Europe

- how much SMEs weight in the balance sheet of the banking system? The ECB does not provide such an info.

- Based on a study of DG for Internal Policies[1] and on stock outstanding amounts of the ECB's statistical bulletin[2], we can estimate that back in 2010 SMEs (= 98% of European companies) represented approx. 14% of total outstanding of Banks - Non Financial Corporations accounting for 38%

→ relatively low exposures fragmented among a high number of counterparts: statistical approach seems reasonable in small business target

- But are we talking of an homogeneous bunch of companies on the lenders' eye?

[1] Source: Banking system soundness is the key to more SME financing. DG FOR INTERNAL POLICIES, IP/A/ECON/NT/2013-02
2 Source: ECB, Statistical Datawarehouse, Monthly Bulletin

There are SMEs and SMEs…

A major difference is on the **available data sources**.

Balance Sheets:

- are due for Corporations;
- they are not for Partnership Companies and Sole Traders (e.g. in Italy, this kind of SMEs account for the 85% of total companies: 5.1 over 6 millions).

In particular, **no way to have official data on assets** - only income data is available.

→ **Statistical approach** is not only reasonable where balance sheet is missing, but probably is mostly appropriate to take into account the major part of available info (non soft) while preserving the homogeneity principle and bear a cost which is convenient for the born risk.

Scoring on SMEs
the Scoring definition from the DG Markt EGCH

Credit Scoring = **Automated system** based on statistical procedures that uses past behavior and/or characteristics of borrowers with the objective of forecasting their repayment behavior[1]

Scoring has to be automated:

up to the lenders to decide whether a judgmental approach is applicable and appropriate in top/medium-sized SMEs

[1] Report of the Expert Group on Credit Histories, 2009. Available at the EC website, DG Internal Market

Scoring on SMEs
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Credit Scoring = Automated system based on statistical procedures that uses **past behavior and/or characteristics** of borrowers with the objective of forecasting their repayment behavior

Scoring need to have enough information:

Past = sufficient depth of information available – this is not true throughout Europe

Behavior = positive, light negative and default information – this is not true throughout Europe

Characteristics = this is more in line with terms such as *not excessive* rather than *minimum necessary*: statistics need to know in order to determine what is statistically significant

= SUFFICIENT BREADTH AND DEPTH OF DATA!

Scoring on SMEs
the Scoring definition from the DG Markt EGCH

Credit Scoring = Automated system based on statistical procedures that uses past behavior and/or characteristics of **borrowers** with the objective of **forecasting their repayment behavior**

Scoring is objective, it is not judgmental:

Borrowers = SMEs and relevant shareholders. It is demonstrated that the smaller the enterprise, the highest the correlation among the credit risk of the company and the one of the company holder(s)

Forecasting = high predictive value of scoring systems. This is already achieved, no bank uses a scoring system if it does not have a high predictive value.

If previous recommendations were achieved,

high predictive value could be always ensured

Case Study: Impacts on Expected Loss and RWA

- a leading Italian Bank was NOT using CRIF Credit Bureau data and CRIF Credit Bureau Scoring for assessing the Expected Loss and RWA over its SMALL BUSINESS Customers' portfolio;

- to improve its performances, the Bank decided to integrate the Credit Bureau data and the Credit Bureau Scoring;

- thanks to this, the more accurate risk assessment of its SMALL BUSINESS Customers' portfolio has brought savings to the Bank in terms of:

Expected Loss	**Rwa - Risk Weight Assets**
-25 %	**-20%**

Scoring on SMEs

In conclusion, what is needed:

reduction in local and pan-EU constraints in the availability and usage of credit data on SMEs and SME shareholders for credit scoring and creditworthiness evaluation purposes

(creation of a level playing field across Europe)