Contributions and Limits of the Loans Guarantee System for Small and Medium-Sized Enterprises (Smes): Case of the Central Guarantee Fund (CCG)

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Summary

SMEs have always suffered from the problem of access to finance preventing them from growing and even more from failing to play their role fully especially when it comes to their contribution to the creation of the value added which remains very timid (not exceeding 20%). The difficulty of accessing finance has become more acute with the advent of the financial crisis that has led to tightening loan conditions. To remedy this, in 2009, banks began to apply the internal rating system, which aims to treat SME loan files objectively and more fairly. To reinforce this action and increase the chances of SMEs, The Central Guarantee Fund undertook, from the same year, to support this category of companies by making available to their banks, the required guarantee.

Our research paper consists then to examine the contributions of the Central Guarantee Fund, in other words, to verify if this guarantee fund was able, through its two development plans (2009-2012 and 2013-2016), to allow for enough SMEs to easily have the loan they need.

Key words: SME financing, guarantee system, CCG contributions, CCG limits

Introduction

In Morocco, as well as internationally, SMEs has always suffered from the problem of access to finance, which they consider to be the main difficulty that prevents them from growing and sometimes even continuing to exist.

Faced with this situation, actions have been taken to simplify the introduction of the SME to the stock market and thus allow it to benefit from the diversification of its sources of financing. But practice has shown that this market remains relatively demanding and weakly attractive and cannot therefore be an alternative to the banking market.

For this, the public authorities didn't stop looking for solutions to improve the relationship between the SME and the bank. Then, they demanded, on the side of the banks, the adoption of the internal rating system which consists in evaluating the SME on the basis of a tool that takes into account its specificities, thus confirming that "beyond the prudential objectives which are the fundamental purpose of the Basel II system, its implementation taking into account the specific characteristics of SMEs, testifies to the importance of the integration of this category of companies in the financing circuits of the economy" (Bank Al Maghrib, 2007) and on the side of the SME, the respect of the rules of the code of good practices of governance in order to palliate the problem of asymmetry of information which pushes the banks to behave reluctantly in front of the requests for loans expressed by the SMEs because, as Adam, Farber and Michel (1989) and Colot and Michel (1996) argue, the banker or venture capital provider has difficulty controlling the actions of the small firm, especially because lack of transparency of the media.

To complement the actions already mentioned, which aim to facilitate SME's access to bank loans, the public authorities have set up guarantee funds, which is mainly the case with the Central Guarantee Fund (CCG) which has a main mission to support SMEs in financing. So, the question at this level is whether the CCG has been able to play its full role? More specifically, has it enabled a large number of SMEs to have the financing they need for their development?

To answer this question, we will focus on the role of the guarantee in the loan transaction, from a theoretical, practical and also empirical point of view. In a second line, we will focus on the case of the CCG as the main Moroccan guarantee fund dedicated to SMEs, we will determine its contributions through the study of effectiveness of its development plans. Regarding the third and last axis, it will be reserved for the shortcomings noted in the mission of the CCG regarding the SME.

- **The role of the guarantee in the loan operation**

The guarantee is an essential component of any loan file. It is even more so when this file is presented by an SME, generally considered a high-risk client.

- **Theoretical and practical framework**

Bankers give so much interest to guarantee because its own great usefulness both for deciding the granting of loans and for stimulating its repayment.

- **Before granting loan**

The primary role of the guarantee is to help the bank to better resolve the asymmetry of information. In this respect, it is seen as a signal because it is more costly for poor borrowers who are more likely to default, but also for who are more likely to lose the guarantee, is higher (Bester, 1985; Chan and Kanatas, 1985; Besanko and Thakor, 1987). In the case of good-quality borrowers, they are more likely to agree to provide guarantees in exchange for a lower interest rate on the loan than poor borrowers (Blazy and Weill, 2006). The guarantee serves as an instrument of separation between good and poor quality borrowers.

The SME can be considered as a poor borrower. She does not usually provide its own bank with all the information requested. To fill this gap, the bank is obliged to ask for guarantees. As Bester (1994) points out, the use of guarantee is a classic solution to the problems of adverse selection and moral hazard. It is an action that empowers the borrowing companies, it pushes them to carry out their project in order to be able to repay the loan received and subsequently recover the goods given as a guarantee.

Banks only agree to grant loans to companies that provide the guarantee to cover the risks associated with the loan transaction. This is not an easy thing for SMEs that “have fewer guarantees to offer than larger companies. They may need to provide more guarantee than the latter for the same amount of loan taking into account a low survival rate of the company”(Ngongang, 2015).

The guarantee plays a second role that relating to the determination of the interest rate. As such, it allows to determinate a better pricing of borrowers according to their quality. A bank can thus discriminate against borrowers by offering them the choice between a secured loan with a low interest rate and an unsecured loan with a high interest rate (Blazy, Weill, 2006). In other words, when the guarantee presented by the company is large, of great value and of a high level of security, the interest rate fixed by the bank is relatively low and aims to fulfill the function of “profit”. Otherwise, that is to say that the guarantee is of average quality, the bank is then obliged to apply a high interest rate in order to cover the risk of default of its client and, also, to achieve a profit.

- **After granting loans**

When the claim on a customer becomes an outstanding claim, that is, the repayment has not occurred for at least three months after the due date, the bank must comply with Bank Al Maghrib’s requirements that specifies that “pre-doubtful, doubtful and compromised debts must give rise to the constitution of provisions” (Bank Al Maghrib, 2002). These, i.e., provisions, represent the cost of counterparty risk that the bank has an interest in controlling so that it can preserve its net banking income and, subsequently, improve its profitability. Thus, and thanks to the guarantee received, the bank manages to reduce the amount of the provision, the calculation of which is based on the deduction of a guarantee, and also the reserved amounts (Bank Al Maghrib, 2002).

In the event that the receivable becomes uncollectible, the taking of guarantee allows the bank to reduce the loss incurred. The guarantee gives the bank a right to specific assets (Blazy and Weill, 2006).

Empirical Verification

Numerous studies have focused on the empirical verification of the theoretical arguments about the role of guarantees in bank loans. The majority of them proved the importance of the guarantee in reducing the loan loss. This is mainly the case of:

1. Berger and Udell (1990) fund a positive relationship between guarantee and the risk of the loan, which encourages banks to demand more guarantees from higher-risk companies and apply higher interest rates to them.
2. Jimenez and Saurina (2004) noting that the probability of default is greater for secured loans, which confirms the assumption of the observed risk that the guarantee is required to cope with the poor quality of the borrower.
3. Jimenez *et al*., (2006) stating that only companies experiencing financial difficulties are required to submit more guarantees for loans.
4. Blazy and Weill (2006) who find that banks charge higher rates and require more guarantees from risky companies.

Regarding the role of the guarantee in resolving adverse selection issues and when it was overturned by Blazy and Weill (2006) and Weill and Godlewski (2009), Berger *et al*., (2011), have succeeded in validating it by noting that riskier the borrower, the more the bank requires guarantees to mitigate the problem of moral hazard. These authors add that the guarantee can only be a signal if there is an ex-ante informational asymmetry.

Regardless of the analytical framework considered (theoretical or empirical), the guarantee is mainly used to reduce the loan loss in case of default. It is more imposed on SMEs (considered as high-risk entities) that generally fail to respond positively, hence the creation of the central fund guarantee (CCG).

Contributions from CCG Programs

The CCG is a public institution having a financial nature. As a guarantee fund, it is one of the types of guarantee schemes that can be determined according to the scope of the activity (retail guarantors, wholesale guarantors and portfolio guarantee), the guarantee (direct guarantors and indirect guarantors or guarantors) or the nature of the entity (guarantee companies and guarantee programs).

The CCG was created in 1949 with a mission to guarantee the repayment of loans granted by banks to public or private companies.

In the case of SMEs, the CCG only began to be interested in them in 2009. Such guidance is part of the government's efforts to support and promote this category of companies. Certainly, the CCG is seeking, through its offer, to allow loan files submitted by SMEs to obtain a good rating and benefit from an acceptable interest rate. From this perspective, the CCG has developed a first development plan covering the period 2009-2012 and was structured around the following three pillars:

- A generic product offering that covers the life cycle of the SME;
- A new partnership with banks based on a thorough review of processes;
- A regional deployment for greater proximity with banks and businesses (Ministry of Economy and Finance, 2013).

The CCG was able to achieve the objectives of its development plan with a completion rate of 100%.

Table 1. Achievements of the development plan 2009-2012

Synthetic economic indicators	Achievements 2009-2012	Annual average
Guarantee Commitments in MM DH	5,54	1,385
Bank loans mobilized in MM DH	9,98	2,495
Co-financing commitments in MM DH	0,74	0,185
Number of VSMEs * (2/3 of which are VSE **)	5200	1300

Source: CCG Activity Report, 2016

** VSME: Very small, Small and Medium Enterprises. ** VSE Very Small Enterprise*

The very successful results of this first plan of 2009, which prove its effectiveness, encouraged the institution to adopt a second and even more ambitious development plan in 2013, spanning four years (CCG, 2016).

Table 2. Objectives and Achievements of the 2013-2016 Development Plan

Synthetic economic indicators	Objectives 2013-2016	Achievements 2013-2016	Achievement rate
Guarantee Commitments in MM DH	10	19,43	194%
Bank loans mobilized in MM DH	18	38,87	216%
Co-financing commitments in MM DH	0,99	2,77	278%
Number of VSMEs (2/3 of which are VSEs)	8600	17968	209%

Source: CCG Activity Report, 2016

Table 2 shows that the CCG's second development plan is more effective than the first. It has managed to far exceed its forecasts by recording fairly high completion rates, between 194% and 278%.

Table 3. Comparison between the 1st and the 2nd development plan

Synthetic economic indicators	Achievements 2009-2012	Achievements 2013-2016	variation rate
Guarantee Commitments in MM DH	5,54	19,43	251%
Bank loans mobilized in MM DH	9,98	38,87	289%
Co-financing commitments in MM DH	0,74	2,77	274%
Number of VSMEs (2/3 of which are VSEs)	5200	17968	245%

Source: Made by us

Table 3 shows that the CCG's achievements in favor of the VSMEs have evolved considerably between 2009-2012 and 2013-2016, thus making it possible to favorably influence the Moroccan economy and achieve the following results:

- 2/3 of creations and ¼ of development projects registered their first access to loans thanks to the CCG guarantee;
- The control of the loss ratio at 2.6%, which proves the effectiveness of the CCG's selection mechanisms that have made it easier to access financing for only viable VSMEs;
- Guarantee SMEs have managed to improve their overall performance: Turnover up to 5%, growth of the added value by 6% and increase in the payroll by 12%;
- An average growth of 33% in the volume of loans;
- The discounted value of the benefits of the institutional guarantee shows a net benefit/cost ratio of 1.5 Dirhams for each Dirham spent over the entire economic cycle (CCG, 2016).

The CCG's Limitations on SME Financing

Many researches have revealed the inability of guarantee funds to simplify access to finance, especially for SMEs:

- "Today, more than 2,250 loans guarantee schemes exist in a wide variety of forms in nearly 100 countries, but most are small, local, weak and failing sustainability" (Davies, 2007);
- "Currently, no warranty company for micro, small or medium-sized borrowers has priced its guarantee at a price that allows it to maintain its capital level ... losses are often erased either by a donor or a flow Continuous subsidy ... SMEs and micro-entrepreneurs do not need guarantees, but rather a different appreciation of their loan and an appropriate loan monitoring technology". (Gudger, 1998)
- "... creation of guarantee funds which undertake to indemnify in case of default. In various countries, particularly in Central Africa, this did not work because the granting of a guarantee was accompanied by a less strict choice of investment projects and a lower rate of recovery of outstanding payments". (Kauffmann, 2005)

Nevertheless, a study on the Italian mutual guarantee consortia demonstrates the relevance of the Italian Public Guarantee Fund for SMEs, "in terms of widening access to the bank loan ... The empirical demonstration presented in the analysis shows that the Italian system has reached a certain level of efficiency to reduce the cost of loans for SMEs and their financial constraints ... Empirical data ... indicate that by a good selectivity of targeted SME groups, individual beneficiaries and coverage ratios ... unlike other public funds, the Italian Fund was able to manage the default rate and contain the public subsidy element that is required to maintain its sustainability" (Zecchini & Ventura, 2008).

In the case of Morocco, as we have already stated above, the CCG's production between 2013 and 2016 greatly exceeded the objectives initially set with very satisfactory achievements, which raised the guarantee fund at the head of guarantee institutions across Africa and MENA regions. But despite this, the CCG's action vis-à-vis SMEs still has shortcomings:

1st insufficiency:

It is true that the CGC's intervention in favor of the VSMEs is effective. However, if we limit ourselves to the case of SMEs, we can argue that those who have benefited from the offer of the CGC are of a very limited number, even insignificant. To show it, we must first deduce the total number of SMEs:

Table 4. Number of SMEs in Morocco between 2013 and 2016

	2016	2015		2014		2013	
		Global	SME	Global	SME	Global	SME
Companies creation	-	29563	28085	28833	27391	28504	27079
Companies failures	-	5783	5494	5010	4760	4373	4154
Number of SMEs	442 894	420303		397672		374747	

Source: Made by us based on Inforisk data

In 2016 and according to the data of the Moroccan Office of Industrial and Commercial Property (OMPIC), the number of companies was 466204, therefore, the number of SMEs can be calculated as follows: 466204 x 95% (share of SMEs in the Moroccan economic fabric) = 442 894.

For the years 2015, 2014 and 2013, we based ourselves on the following formula:

Number of SMEs in N = [number of SMEs in N + 1 - (creation of SMEs in N-failures of SMEs in N)

We must then determine the percentage of SMEs that benefited from the CCG intervention in the total number of SMEs operating in the Moroccan market:

Table 5. SMEs that benefited from the CCG's offer (in number and in %)

	2013	2014	2015	2016
VSME	2092	3133	5237	7290
Number of SMEs (1/3 of VSMEs)	697	1044	1746	2430
SMEs in % (compared to the total number of SMEs)	0,18	0,26	0,41	0,55

Source: produced by us on the basis of data from the CCG Activity Reports

It seems clear that the effort provided by the CCG is more oriented towards small businesses than SMEs. However, it's that second category of companies that needs more support from the CCG:

- First, to help it solve the problem of excessive guarantees. In this regard, the International Monetary Fund (IMF) specifies that although the value of securities in Morocco is generally lower than the MENA region countries, it remains very high for SMEs. This value represents more than twice of the amount of the loan locating Morocco above the world averages and in the MENA zone.
- Secondly, to enable it to play its full role in the national economy by increasing its contribution to GDP, this has remained stagnant at 20%.

2nd insufficiency:

Compared to the duration of the loans, the CCG's intervention during the 2013-2016 period has facilitated the access to short term (ST) and long-term and medium term (LMT) loans.

Table 6. Distribution of CCG Guarantee Loans for SMEBs by Duration (in billion DH)

	2013	2014	2015	2016
Total of guarantee bank loans	4,7	6,7	10	14,4
Loans at ST	3,2	4,9	7,9	11,4
Loans at LMT	1,5	1,8	2,1	3

Source: produced by us on the basis of data from the CCG Activity Reports

Table 6 tells us that almost all of the CCG-guarantee loans are operating loans. However, the investment loans constitute the greatest interest towards SMEs, especially those seeking to improve their situation. Indeed, many studies have shown that the low growth of SMEs is mainly due to the difficulties of these companies to obtain financing in the development phase (Becchetti and Trovato, 2002; Krasniqi, 2007; Oliveira and Fortunato, 2006; Pissarides, 1999).

3rd insufficiency:

The intervention of the CCG remains dependent on the decision taken by the bank in granting loans. It intervenes only when the latter appreciates the level of the risk of the entity to finance. "In practice, the entrepreneur first chooses the bank that will accompany him by presenting his business plan. The CCG intervenes after this stage and when the bank has conducted its study and assessed the risk. If the bank decides to go, the CCG co-finances. This is a sine qua non condition"[2].

Conclusion

The CCG's 2013-2016 activity has improved and has had an average annual growth rate of 21%.

This was happened to be more possible thanks to its new orientation, which has become more focused on financing SMEs than on individuals. But despite this, the results obtained are unsatisfactory. In fact, loans to SMEs accounted for only 33% of outstanding loans to non-financial businesses. Their weight has even decreased by three points during the years 2014, 2015 and 2016.

Faced with this situation, it was necessary to explore other avenues to help SMEs overcome this difficulty related to the guarantee, we can mention at this level the draft law 18-15 on the security

[2] The day debate jointly organized between Attijariwafa bank and the Moroccan Association for Industry and Automotive Trade, Tuesday, March 28 in Casablanca, under the theme "the automotive ecosystem and support for investors in this area".

rights that aim to allow SMEs to pledge new guarantees and expand the guarantee base to offer to banks.

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