

Small business crediting in Kazakhstan

Introduction

At the times of Soviet Union there wasn't not only small or middle business, there was not any business at all, everything was public and there were no owners; so all countries of ex-Soviet Union have to develop their small enterprises intensively. For Kazakhstan it was very difficult mainly because Kazakhstan had more mineral industry and a little of agriculture, for the most part – grain. Processing industry was very weak. When USSR broke up and young Kazakhstan had to care about itself, enterprises needed huge amounts of money to buy necessary equipment, employ qualified workers to work in mineral industry and to develop processing industry which demand, by the way, more expenses. However, firstly, government and banks did not have enough money to give credits to the enterprises, and secondly, it was much easier to create monopoly. Thus our system of supporting small business was not correct from the very beginning. But still 15 years later when it seems that Kazakhstan had grown roots and almost everything going rather well our system of supporting small business is not in a perfect condition.

There are several reasons why our small business develops very slowly. Firstly, there was not any optimal government strategy of supporting small business. Government did not reveal the appropriate branch and regional priorities for small business. Secondly, corruption. As we know officials can build huge barriers before entrepreneurs, for example, different checks, problems with registration, and others. Thirdly, a high taxes on enterprises. Lastly, banks do not want to credit a small business because there is more probability that business won't go well, also a large number of problems arise with preparing of necessary documents in order to get a credit, another problem is an enough liquid pledge. So we can see that enterprises collide with many problems when they are trying to receive a credit. Thus the aim of this work is to define the difficulties emerging when small business is trying to receive a credit.

Small business creates new workplaces, forms middle class, develops trade and production. If we do not develop small business there will be no competitive market, thus there will be no improvements in our market, in products and services. So, we should develop small business in Kazakhstan to build up our eco-

mony, particularly we should improve our crediting system of small enterprises because small firms have to develop themselves but they can not do that without money.

Small business crediting

First of all, let us define the notion of small business. According to the existing law, to small business refer new and working enterprises, including the number of employee not more than 50 and total cost of assets not more than 60 000 calculation indexes.¹ Thus, for today maximum amount for assets of small enterprises cannot exceed 46 500 000 tenge. Small and middle business – the basis of market economy, it overcomes monopoly, provide employment, provide revenues from its activity to government, provide more innovations than the other forms of business. In Kazakhstan, for example in Almaty, the average share of small-scale enterprises in total number of enterprises is about 95% (Table 1).

Most of small enterprises had to limit their activity because of lack or inaccessibility of credits. Thus, now the weakened business cannot carry out its functions, which create new workplaces, form middle class, develop trade and production, and which effect especially in the sphere of agriculture, tourism, rendering of services to the population, etc. Therefore the financing and investing support is the most important for effective development of small business.

Finance and investing support of small business can be realized in the following ways²:

- crediting by second tier banks priority projects by tender system on the preferential conditions;
- creating and development of guarantee credit system in a second tier banks, on a basis of forming pledge funds in regions;
- promotion of stimulation of second tier banks;
- continuation of budget and second tier banks financing projects;
- development of venture financing;
- encouragement of credit partnerships creation, mutual insurance societies.

Thus we can see that it is very important to develop investing and financial support of small business in Kazakhstan. Small companies need money to expand their business, buy equipment, employ more workers that is why the key in developing small business is investment in it.

¹ Law of Republic of Kazakhstan from 19 July 1997, No. 131-1 *O gosudarstvennoi podderzhke malogo predprinimatelstva* (with amendments to this law on 10.07.98 No. 283-1; on 26.07.99 No. 458-1; on 29.11.99 No. 488-1).

² Finansirovanie i kreditovanie sub"ektov malogo biznesa, 2001, <http://business.zakon.kz/fin-credit/>

Table 1. The share of small-scale enterprises in Almaty on 1.12.2000

| Activity category | The total number of enterprises in the region | The number of small-scale enterprises | The share, % |
|---|---|---------------------------------------|--------------|
| Agriculture | 217 | 208 | 96 |
| Fishery | 8 | 8 | 100 |
| Mineral resource industry | 89 | 87 | 98 |
| Processing industry | 2628 | 2476 | 94 |
| Production and supply of gas, water, energy | 86 | 79 | 92 |
| Building | 1812 | 1730 | 95 |
| Trade, car maintenance | 9464 | 9363 | 99 |
| Hotels, restaurant | 413 | 387 | 94 |
| Transportation, communication | 1821 | 1748 | 96 |
| Financing activities | 768 | 743 | 97 |
| Real estate activities | 4123 | 3935 | 95 |
| Public administration | 129 | 76 | 59 |
| Education | 946 | 665 | 70 |
| Public health | 466 | 358 | 77 |
| Other public utilities | 2163 | 2075 | 96 |
| Total | 25 133 | 23 938 | 95 |

Source: A. Dabaev, *Voprosy v tolpe vosklitsatelnykh znakov*, "Kontinent" 2001, No. 25, <http://www.continent.kz/2000/25/23.html>

There are many goals pursued by entrepreneur when he is asking for a credit but not for all purposes it is given. For example, EBRR gives credits for increasing of working capital, investments like purchase of real estate, etc.³ Kazkomertzbank offers credits for increasing turnover, increasing working capital for further growth, expansion of production or volume of services, purchase of machinery, equipment, raw materials, improvement of manufacture, purchase, construction and maintenance of real estate, and other capital investments.⁴

Thus, we can conclude, that there are many reasons for the enterprises to give an application to the bank in order to receive a credit, and one of the main reasons is investing, i.e. buying an equipment, building. However banks give credits mainly in order to increase turnover.

There are several documents which are required in order to receive a credit, as follows⁵:

³ Krediti dlya malogo biznesa, EBRR, 2001, http://www.fund.kz/ebrr_c.html

⁴ Kreditovanie, 2001, http://www.kkb.kz/banking_re/sber/service/06_credit.asp

⁵ Kreditovanie, 2001, http://www.kkb.kz/banking_re/sber/service/06_credit.asp

- application,
- constituent documents,
- registration certificate,
- statistical card,
- confirmation of RNN by RNI,
- borrower form and chief biographical data,
- financial reporting for the past 3 yearatures,
- contracts,
- cards with a sample of signatures,
- documents establishing right for an object of pledge,
- certificate about number of employee with the owner-manager's and the accountant's signatures with seal,
- marketable securities prospectus,
- marketable securities registration certificate,
- certificate from tax inspection and from extra-budget fund about absence (or presence) of debts.

These are the main documents demanded by banks but a representative of the credit department of the bank may require extra documents, depending upon financed project.

Since half of the year 2000 banks simplified the scheme for giving credits. Until year 2000 the main problem in preparing documents in order to receive a credit was a business-plan but now after simplifying of scheme, the main problem is to prepare annual financial statements, because banks intensify requirements for financial position and accounting documents. Why did they intensify? Now the majority of small enterprises and not only small conducts double accounting – one accounting for tax purposes and another for the presentation to banks and investors. In a financial statement for tax purposes, for instance, a company decreases its revenue or shows losses in order to pay lower taxes and if this company brings the same financial statement to the bank to borrow money, most probably the bank will deny giving a loan. Nowadays there are many organizations which help entrepreneurs to make up different kinds of documents like financial statements, pledge documents demanded by banks, but there is absolutely no guarantee that with these financial statements they will receive a credit, although the simultaneously services of these firms are rather high.

Another problem is getting sanction for the realization a project. This is due to the difficulties with receiving a confirmation of different state organizations. There are several supervising organs whose corroboration you have to receive but it depends on the project itself.⁶

⁶ I. Dauranov, *Maliy biznes: problemi oformleniya kredita*, “Al Pari” 2000, No. 5, p. 82.

- Ministry of Ecology and Natural Resources regional representations,
- sanitary-epidemic services,
- state Supervision of architecture and construction,
- standardization and certification organs,
- fire services,
- custom services.

Mainly because of imperfections of our institutions and especially due to corruption getting through the registration formalities takes 6 or more months.

No credit can be given until a banker and an entrepreneur meet. During this meeting a borrower should show and tell about his business, how it works, in short, he should do the best to present his business. The banker asks him questions about financial statements of the company, about revenues and losses, so the borrower should be prepared for these questions. A credit interview is often held in the bank or in the enterprise office. By the way, an entrepreneur should always invite to his office and not only because of an owner's proud to present his business but also to present the additional information about his business like first appearance of the office, other rooms and buildings; site, neatness of the office; to show employees, equipment. This information improves the representative's impression about the business. A representative in his turn has to be in connection with a borrower, keeps abreast of the needs of the company, should offer a bank in order to solve financial problems of the enterprise, and should offer to submit an application for a loan. Thus the representative has to understand how business works, risks connected with making deals with this company, keeps up that everything is legal, and looks after how a borrower spends credit.⁷

Banks have to secure their credits which are given to entrepreneurs in a case of bankruptcy. Thus all banks demand a pledge maintenance from borrowers. Banks accept as a pledge property, guarantees of other legal persons, and other types of pledges. For instance, European Bank of Reconstruction and Development accepts real estate, motor vehicles, personal property, enterprises' property and goods, which are in business.⁸

It is very difficult to receive a credit on ordinary terms offered by banks due to the fact that most enterprises are not able to provide a pledge required by banks or their pledge is not liquid enough. There are several problems arising with providing a pledge to the bank. The most important is illiquidity of the pledge that is offered by enterprises. Banks accept a movable and immovable properties owned either by enterprise or entrepreneur guaranties of other legal persons marketable securities.⁹ Another important thing is that banks usually underestimate

⁷ Osnovnie printsipi kreditovaniya MP, 2001, http://www.tacisinfo.ru/brochure/banksme/pzay-av_m.htm

⁸ Yevropeyskiy bank rekonstruktsii i razvitiya, 2001, http://www.fund.kz/ebrr_c.html

⁹ Kreditovanie, 2001, <http://www.hsbk.kz/default.asp?page=corporate&n=credit>

the value of the pledge. And the last thing is the registration of documents confirmed your ownership of the pledge. Banks demand these last two items when they are giving out a credit. Thus if the estimation of the pledge that is carried out by experts of the bank is free of charge then confirmation of ownership is carried out at the expense of the businessman.¹⁰

Therefore it is very difficult to receive a credit. You may have problems with providing a liquid pledge demanded by banks. Even if your business goes well and profitable your company could just have not enough assets to offer it to the bank. Moreover, your request for a loan to buy an equipment to increase your assets could be refused because the bank gives loans only to those, who already developed. Thus there is a situation when the rich become richer and the poor become poorer.

Now let us consider the interest rates which enterprises have to pay as a payment to the banks for lending money. For example, the interest rates of NSBK are determined in dependence with the concrete case and project¹¹:

- on credits in national currency – from 24%,
- on credits in national currency with fixation of the currency equivalent – from 17%,
- on credits in foreign currency – from 17%.

These interest rates look pretty high, but there are a lot of programs on supporting small business and many banks support this policy and offer credits to enterprise on less interest rates. For instance, Kazkommertz Bank offer 1% on foreign currency credits.¹²

Thus we can conclude that an entrepreneur has to prepare many documents, prepare the meeting with the executive of a credit department of the bank, has a liquid pledge and enough assets to give it as a pledge in order to be able to satisfy the bank's requirements. There are so high interest rates, but still there are many programs on supporting small business lending and enterprises have to discover first which bank is more suitable and then go and find out its personal specific terms.

Conclusion

So, we can see there are a lot of difficulties connecting with receiving a credit for small business. That's why the share of small-scale enterprises getting credits is not so large, for instance, in Almaty it is about 50% (Table 2). We can see that there are many difficulties arise with receiving a loan. Many problems are due to

¹⁰ I. Dauranov, *Maliy biznes: problemi oformleniya kredita*, "Al Pari" 2000, No. 5, p. 82.

¹¹ Kreditovanie, 2001, <http://www.hsbk.kz/default.asp?page=corporate&n=credit>

¹² Kreditovanie, 2001, http://www.kkb.kz/banking.re/sber/service/06_credit.asp

Table 2. The share of small-scale enterprises receiving a credit in Almaty on 1.12.2000

| Activity category | The number of small-scale enterprises | The number of small-scale enterprises receiving a credit | The share, % |
|---|---------------------------------------|--|--------------|
| Agriculture | 208 | 55 | 26.4 |
| Fishery | 8 | 2 | 25 |
| Mineral resource industry | 87 | 49 | 56.6 |
| Processing industry | 2476 | 1136 | 45.9 |
| Production and supply of gas, water, energy | 79 | 30 | 37.9 |
| Building | 1730 | 1355 | 78.3 |
| Trade, car maintenance | 9363 | 3904 | 41.7 |
| Hotels, restaurant | 387 | 80 | 20.7 |
| Transportation, communication | 1748 | 1187 | 67.9 |
| Financing activities | 743 | 538 | 72.4 |
| Real estate activities | 3935 | 2597 | 66 |
| Public administration | 76 | 17 | 21.9 |
| Education | 665 | 569 | 85.5 |
| Public health | 358 | 190 | 53.2 |
| Other public utilities | 2075 | 361 | 17.4 |
| Total | 23938 | 12070 | 50.4 |

Source: A. Dabaev, *Voprosy v tolpe vosklitsatelnykh znakov*, "Kontinent" 2001, No. 25, <http://www.continent.kz/2000/25/23.html>

that banks want to secure their loans, they want to be more safe but enterprises are not able to suit banks' requirements – there are difficulties with documents, with providing enough liquid pledge, meeting with representative of a credit department and many, many others.

Our lending system needs to be improved. First of all, banks should be more indulgent to small enterprises which are not able to meet some requirements of the banks, especially about pledge.

Secondly, there should be more programs on supporting small business like decreasing interest rates, giving credits for a longer period of time, etc.

Thirdly, banks should stop working only with "big people" with "big money" but also help small enterprises to enter into market and function freely.

There are in Kazakhstan some measures applied in order to improve our lending system and they work but small business because of its weakness should be backed to a greater extent. Some enterprises which are pretty big rather than others are gain on these programs but there should be some support to the beginners.

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