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Exploration of the Financing Dilemmas of Small and Micro Enterprises and the Paths of Financial Innovation

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Abstract: The prioritization of financial infrastructure construction serves as a crucial guarantee for the high-quality development of small and micro enterprises. However, resolving the financing challenges of small and micro enterprises is not a task to be accomplished overnight. It necessitates the establishment of a long-term mechanism, the acceleration of financial innovation, the gradual enhancement of the vitality of micro-entities, and the creation of a stable and healthy economic development environment. Therefore, the author first analyzes the current financing situation of small and micro enterprises, as well as the problems they face during the process of financial innovation enabling small and micro enterprises to access financing and solve their financing difficulties, such as insufficient technical support, an imperfect risk control system, incomplete information disclosure, and a lack of credit data. Subsequently, targeted paths for financial innovation are proposed, aiming to offer suggestions for solving the financing problems of small and micro enterprises.

Keywords: Small and micro enterprises; Financing; Dilemmas; Financial innovation; Paths

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1. Introduction

Small and micro enterprises are an important part of China's national economy. How to solve their financing problems and stimulate their development vitality has become a focus of market attention. Nevertheless, the problems of expensive and difficult financing still prevail, restricting the survival and development of small and micro enterprises. Relevant data shows that the financing problems of small and micro enterprises mainly include an insufficient scale of financing supply, limited financing channels, and generally high financing costs. Financial institutions need to accelerate financial innovation to solve the financing problems of small and micro enterprises and provide them with broader development space [1].

2. Current financing situation of small and micro enterprises

2.1. Insufficient scale of financing supply

In the current economic situation, small and micro enterprises in China generally face financial constraints, increased production costs, reduced profits, and insufficient orders. Thus, their loan demands are characterized by being "short-term, frequent, and urgent". However, small and micro enterprises often have high debts, lack stable repayment sources, have unstable cash flows, have non-standard financial statements and operation management, lack sufficient collateral, and find it difficult to prove their repayment ability and creditworthiness. As a result, they encounter many difficulties when seeking financial support from financial institutions. Under the traditional financial model, the loan support that small and micro enterprises can obtain from financial institutions is very limited, and only a small number of them can get sufficient loans [2].

2.2. Limited financing channels

At present, commercial banks are the main source of financing for small and micro enterprises. The lack of direct financing channels and the single-channel financing situation have restricted the survival and development of small and micro enterprises to a certain extent. Even though China has been striving to improve the financing environment for small and medium-sized enterprises and continuously promoting the optimization of the financial-side resource supply mode and the construction of the direct financing system, the problem of the lack of financing channels for small and micro enterprises has not been completely resolved. The financing support provided by the bond and stock markets for small and micro enterprises still fails to meet the actual demand. This is mainly because the direct financing market for small and medium-sized enterprises in China is still in the cultivation stage, and the financial support from the bond and stock markets to small and micro enterprises is relatively weak. For example, the Beijing Stock Exchange focuses its services on "specialized, sophisticated, characteristic, and new" small and medium-sized enterprises. The number of small and micro enterprises eligible for financing is small, and the scale of equity financing is relatively small [3]. Private lending highly depends on the personal relationships of business owners. Small and micro enterprises also face relatively great difficulties in obtaining financial support through this method. In extreme cases of financial shortages, they may even choose some informal channels, which poses greater potential risks to their development.

2.3. Generally high financing costs

Compared with large and medium-sized enterprises, small and micro enterprises have poorer qualifications, and financing institutions assign them a higher risk rating. Consequently, their financing costs are relatively high. Even if some financial institutions are willing to provide loan services to small and micro enterprises, due to their risk ratings, they will require additional fees such as consultation fees and loan guarantee fees as risk premiums. This leads to generally high financing costs for small and micro enterprises. Taking working-capital loans with a term of less than one year as an example, the loan interest rate for large and medium-sized enterprises is generally within 3%. Even if their qualifications are relatively poor, the loan interest rate usually does not exceed LPR + 50bps. However, it is very difficult for small and micro enterprises to obtain such low-interest loans. If they choose private lending, the loan interest rate may be as high as four times the bank's lending rate for the same period [4].

3. Paths of financial innovation to enable small and micro enterprises to access financing

3.1. Maintaining an incremental credit supply

The financing difficulties of small and micro enterprises stem from their short establishment time, poor credit records, and light assets. Under the traditional approval model, financial institutions find it difficult to assess their risks, often resulting in low loan amounts and high interest rates. To address this situation, China has implemented a series of policies in recent years. Especially after the establishment of a coordination mechanism in 2024, banks have increased their credit support for small and micro enterprises and promoted financial innovation to precisely meet their needs. The key to maintaining an incremental credit supply and expanding the development space of small and micro enterprises lies in the innovation of the credit-granting model. The traditional model relies on a single internal data source, which cannot meet the development needs. It is necessary to innovate the credit-granting model in light of the economic situation to balance the risk-aversion of financial institutions and the financing needs of small and micro enterprises. Digital technology should be utilized to enrich online credit forms, making financing more convenient, and focusing on first-time loans, loan renewals without principal repayment, and credit loans. For example, the Agricultural Bank of China has provided a new financing path for technology-based enterprises through intellectual property pledge. The Zheshang Bank, in collaboration with multiple departments, has launched products such as "Data Guarantee" and "Bank-tax Loan", which represent effective explorations in financial support for small and micro enterprise financing.

3.2. Continuously expanding financing channels

In the increasingly competitive market environment, capital is the cornerstone of the healthy development of small and micro enterprises. Whether they can obtain sufficient financing directly determines their market competitiveness, operational status, and even development potential. Currently, commercial banks remain the main financing channel for small and micro enterprises in China, and the financing channels are relatively single. To enhance the functions of the capital market, appropriately increase the proportion of direct financing, and provide small and micro enterprises with more financing options has become a problem that requires in-depth research. Financial institutions need to innovate bond services and products in line with the financing needs of small and micro enterprises to continuously expand their financing channels. For example, the financing support service for small and micro enterprise bonds developed by the Industrial Bank is the first innovative business in the market, benefiting many outstanding small and micro enterprises and providing them with financial support. Sichuan Kelun Pharmaceutical Co., Ltd. and Jiuzhoutong Pharmaceutical Group successfully registered the first batch of privately-owned enterprise asset-guaranteed bonds in the inter-bank market through the Industrial Bank, obtaining funds and creating more development space for themselves. Bond financing can provide small and micro enterprises with new financing channels, expand their financing sources, optimize their financing structure, reduce their financing costs, and help them further overcome financial constraints. However, due to the relatively small operating scale of small and micro enterprises, the capital market generally has a low recognition of them, resulting in a relatively low overall bond-financing scale. Since last year, the bond market environment has been relatively stable, providing an opportunity to promote the registration-based system reform and continuously expand the financing channels for small and micro enterprises. Moreover, with the IPO review process becoming more efficient and transparent, small and micro enterprises can obtain financing through listing. Currently, many high-quality small and micro enterprises have been given green-light access and have become the main issuers. In the future, expanding the outstanding scale of small and micro enterprise bonds, improving the convenience and availability of bond-financing for small and micro enterprises, and broadening financing channels will be one of the important directions of financial innovation [5–8].

3.3. Innovating comprehensive financial services

Information asymmetry is one of the main reasons for the difficult and costly financing of small and micro enterprises. In response to the current financing problems of small and micro enterprises, financial institutions are continuously enhancing their comprehensive financial service capabilities to provide new financing channels for small and micro enterprises and meet their diversified financial service needs. For example, they can strengthen the collection and analysis of information related to small and micro enterprises, understand their actual needs and risk characteristics, and provide customized financial solutions. This requires financial institutions to deeply integrate various financial services and explore new financial service projects based on the results of information collection and analysis, breaking through the boundaries of traditional financial services. They should provide small and micro enterprises with comprehensive, one-stop financial solutions that include financial consulting, insurance services, investment and wealth management, and banking services. Currently, some financial institutions have made beneficial attempts in comprehensive financial services for small and micro enterprises, providing references for the implementation of relevant work. For example, the Zheshang Bank has experimented with the financial advisor system for six years. By integrating cross-institutional and cross-industry financial elements, it has constructed a "1 + N" comprehensive financial service system specifically for small and medium-sized and micro enterprises. This system realizes multi-dimensional complementarity and multi-party sharing of information, making up for the shortcomings of enterprises in professional knowledge fields such as law, finance, and accounting, and providing practical experience in solving the information-asymmetry problem between financial institutions and small and micro enterprises [9–11]. Based on the financial advisor system, the Zheshang Bank has actively promoted the construction of financial advisor studios and conducted research activities relying on these studios to better understand the financing demands of small and micro enterprises and further assist them in solving problems related to enterprise listing, industrial mergers and acquisitions, the construction of supply-chain ecosystems, and liquidity management.

3.4. Improving the credit risk control system of financial institutions

The high risk rating assigned to small and micro enterprises by financing institutions is an important factor contributing to their financing difficulties. Therefore, financial innovation for small and micro enterprises should focus on improving the credit risk control system of financial institutions. For example, innovating their credit-loan system and adopting a digital risk-control model. Financial institutions can optimize the risk-control process through advanced technical means such as artificial intelligence and big data, thereby enhancing their risk-monitoring and early-warning capabilities, accurately identifying credit risks, and making rapid responses. The application of big data technology can improve the ability of financial institutions to obtain, process, and analyze enterprise risk data. Financial institutions can use big data tools to enrich the types of enterprise data collection, expand the scope of enterprise data collection, and achieve batch processing of enterprise data from different types and sources. For example, algorithms can be used to automatically evaluate the lending amount of credit loans within the limit, reducing the risk-control cost and the bad-debt rate. At the same time, financing institutions can also combine big-data analysis, intelligent control, and traditional manual operations. When it comes to issues such as medium-and long-term loans for small and micro enterprises, mortgage loans, and over-limit lending, financial services can be classified as complex and high-risk credit products, and then the manual credit-approval process can be implemented. Currently, many large and medium-sized financial institutions have started to layout digital financial products, aiming to enhance their digital capabilities and strengthen cooperation with external fintech companies to seek digital transformation. This will enable them to cover more small and micro enterprises with financing needs and provide them with more convenient and targeted financial services [12, 13].

3.5. Improving the mortgage and guarantee system for small and micro enterprises

Many small and micro enterprises have a high risk rating from financing institutions due to their small operating scale, insufficient operating stability, and lack of rich historical credit records, making it difficult for them to obtain financial support from financial institutions. To address this issue and enable small and micro enterprises to access financing more conveniently through financial institutions, it is necessary to improve the mortgage and guarantee system for small and micro enterprises. First, the government can provide financing guarantees for outstanding small and micro enterprises with financing needs by setting up special funds and establishing policy-based financial institutions. Relatively speaking, government-provided guarantees have a high degree of recognition. By introducing a market-based operation mechanism based on fiscal budget calculations and reviewing small and micro enterprises applying for financing, the government can provide policy-based guarantees for eligible small and micro enterprises, enabling them to obtain financing more smoothly. Second, diverse credit-guarantee institutions should be established. For example, financial institutions can establish cooperative relationships with local small and micro guarantee institutions, improve the joint-guarantee system, guide and encourage them to participate in the mortgage and guarantee for small and micro enterprises, and provide credit enhancement support for small and micro enterprises' financing, thereby reducing the loan risks of financial institutions and improving the financing availability of small and micro enterprises. Finally, corresponding preferential and subsidy policies should be introduced to reduce the losses of small and micro institutions, help them break through financing bottlenecks, and solve the borrowing problems of small and micro enterprises caused by the lack of collateral [14].

3.6. Implementing supply-chain finance

While continuously expanding the financing channels for small and micro enterprises and improving their mortgage and guarantee system, supply-chain finance should also be implemented, incorporating multiple entities such as core enterprises, distributors, suppliers, and financial institutions into the financial model. Different from the traditional financial model, supply-chain finance emphasizes the coordinated cooperation among all participating entities, forming a strategic alliance relationship and a solid cooperation mechanism to enhance the overall credit level of the supply chain and create conditions for small and micro enterprises to obtain financing. In this model, core enterprises need to play a leading role and guide upstream and downstream enterprises to actively participate in supply-chain finance management activities. Relatively speaking, core enterprises have high market influence and credit ratings and can provide credit guarantees for small and micro enterprises in the supply chain, enhancing the confidence of financial institutions in them. For example, core enterprises can establish a unified financial management system and an ERP business management system to transparently manage their accounts receivable and accounts payable information and share relevant data with upstream and downstream enterprises, improving the information-transfer efficiency and reducing the financing costs of small and micro enterprises [15]. At the same time, each node enterprise in the supply chain should strengthen risk control and internal management to ensure the timeliness and accuracy of information updates. This requires financial institutions to strengthen the application of advanced technologies such as blockchain and big data to achieve accurate credit assessment and comprehensive monitoring of each enterprise in the supply chain. Small and micro enterprises should also improve their internal control systems, standardize financial statements, and enhance their management levels.

4. Conclusion

In conclusion, accelerating financial innovation to address the problems faced by small and micro enterprises in financing, such as insufficient financing supply scale, limited financing channels, and generally high financing costs, is the foundation for stimulating the development vitality of small and micro enterprises and promoting the high-quality development of China's national economy. In response to the financing difficulties of small and micro enterprises, it is necessary to promote financial innovation through multiple measures, including maintaining an incremental credit supply, continuously expanding financing channels, innovating comprehensive financial services, improving the credit risk control system of financial institutions, and implementing supply-chain finance, to improve the convenience and availability of small and micro enterprise financing.

Disclosure statement

The author declares no conflict of interest.

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