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THE REGIONAL EFFICIENCY OF CREDIT GUARANTEE PROVIDED BY THE RURAL CREDIT GUARANTEE FOUNDATION: HUNGARIAN CASE STUDY

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─Abstract ─

In Hungary – as well as in other EU countries – small- and medium sized enterprises (SMEs) are not enough capitalised to make investments and their lack of capital causes difficulties in access to finance. Credit guarantee – which is one of the most effective financial instrument – helps SMEs to get external financing. Regional development is one of the core issues in Hungary nowadays, because the high proportion of agricultural production of the total GDP is not sustainable anymore. Therefore a number of Hungarian farmers have to finish its work or other rural inhabitants should diversify their activity as well to other related businesses in order to ensure or enhance their cost of living. In this study we examined the efficiency of the Rural Credit Guarantee Foundation (AVHGA) in the access to finance of rural enterprises through regional breakdowns. AVHGA issues credit guarantee for all regions in Hungary, and have been provided guarantee for more than 33 000 cases of more than 600 billion HUF credit amount from the start of its operation until the end of year 2011. The examination based on the statistical data of AVHGA (by the regional amount of guarantee, aid element and redemptions) and the regional GDP data of Hungary in the year of 2008. During the analysis we assume, that the GDP/capita index shows the degree of development by regions.

Based on the fundamental goals of AVHGA, the data show the verification of the higher subsidisation of less developed regions. The significantly low percentage of Central Hungary also fulfils the main requirement that the most developed area is not promoted too much. There are possibilities in two regions for more guarantees: Northern Hungary and Central Transdanubia.

Keywords: *credit guarantee, small- and medium sized enterprises, finance, rural development*
JEL Classification: G21, G30, O16

1. INTRODUCTION

Hungary is a Central European country, located on a 93 000 km2, with 10 million inhabitants (Official website of Hungary, 2012). Hungary is a member of the European Union from the 1st of May 2004. The country has exceptionally good capabilities for agricultural production, the 70% of the whole territory is appropriate for agricultural activity (Wikipedia Encyclopaedia, 2012). According to the EU rural definition (NUTS3) the 66,3% of Hungary falls under the rural area (Rural Development Report, 2010). There are 688 000 active small- and medium sized enterprises (Hungarian Central Statistics Office, 2012), they are the target group of the Rural Credit Guarantee Foundation (AVHGA).

There are two main participant of credit guarantee business in Hungary, and one of them is AVHGA, which has a leader role in rural guarantees.

Regional development is one of the core issues in Hungary nowadays, because the high proportion of agricultural production of the total GDP is not sustainable anymore. Therefore a number of Hungarian farmers have to finish its work or other rural inhabitants should diversify their activity as well to other related businesses in order to ensure or enhance their cost of living. In this study we examined the contribution of the Rural Credit Guarantee Foundation (AVHGA) in the access to finance of rural enterprises through regional breakdowns.

1.1. The role of guarantee societies in the EU

"The European Mutual Guarantee Association (AECM) has 37 member organisations operating in 20 EU countries, Montenegro and Turkey. Its members are mutual, private sector guarantee schemes as well as public institutions, which are either guarantee funds or Development banks with a guarantee division. They all have in common the mission of providing loan guarantees for SME who have an economically sound project but cannot provide sufficient bankable collateral. In 2010, AECM member organisations had a total guarantee volume in portfolio of € 71 billion and issued a total of € 31 billion in new guarantees." AECM pursues three main aims: the political representation of its members, the exchange of best practices and the promotion of guarantee instrument (AECM, 2012).

1.2. The activity of AVHGA

"Over one and a half centuries ago, Count István Széchenyi saw the absence of lending as the greatest obstacle preventing Hungarian enterprises from growing as fast as their Western peers. The situation is largely similar today. Even though the political changes brought about greater opportunities, the scarcity of capital remained the most serious problem facing small and medium-sized enterprises, especially in rural areas, in agriculture and the related sectors, unable to provide enough collateral to borrow from banks. Having recognised the situation, the developed part of Western Europe tried to offer help by establishing the Rural Credit Guarantee Foundation under the PHARE Programme in 1991. It was the first credit guarantee institution in Hungary, improving the access of Hungarian rural enterprises to lending.

The mission of the Rural Credit Guarantee Foundation is to increase the creditworthiness of rural small and medium-sized enterprises: improve their access to financing and ensure their financial viability by issuing guarantees." (Website of AVHGA, 2011)

The Rural Credit Guarantee Foundation (AVHGA) issues credit guarantee for all regions in Hungary, and have been provided guarantee for more than 33 000 cases of more than 600 billion HUF credit amount from the start of its operation until the end of year 2011.

The guarantee provided by AVHGA is considered as state aid, due to the 85% state counter guarantee; therefore it has to apply all EU state aid rules. Since in case of guarantees payment is made only at the time of default, not the whole amount of the guarantee is counted as an aid. Based on the EU competition rules the aid element of the guarantee is the difference between the annually discounted market price and the effectively payed guarantee fee.

2. THE METHOD OF EXAMINATION

The examination based on the statistical data of AVHGA and the regional GDP data and regional GDP/capita index (total country=100) of Hungary issued by the Hungarian Central Statistic Office in the year of 2008. During the analysis we assume, that the GDP/capita index shows the degree of development by regions. We used only data of 2008, because the previously examination of data before 2008 showed not significantly different breakdowns by regions neither in AVHGA guarantee, aid element and redemption amounts, nor in GDP data.

Therefore the examination of one year can be considered significant. The territory of Hungary was divided into seven regions in 1999.
By applying a bubble chart for the regional breakdown of issued guarantee amount, aid element and deemed amount/GDP/capita index we can divide four segments, and can analyse the data by groups.

2.1. The analysis of regional breakdowns

The Deed of Foundation of AVHGA prescribes, that the target group of credit guarantee is those rural SMEs that have not enough collateral to obtain external finance, but are creditable. As it is mentioned before we use the regional GDP as the indicator for regional development. During the examination we assume that in less developed regions the available collateral amount is less as well. If we correlate the regional guarantee and aid element amount to regional GDP we can see how efficient the guarantee in the certain region was.

Figure-1: The regions of Hungary

Source: http://hu.wikipedia.org/wiki/Magyarorsz%C3%A1g_r%C3%A9gi%C3%B3i

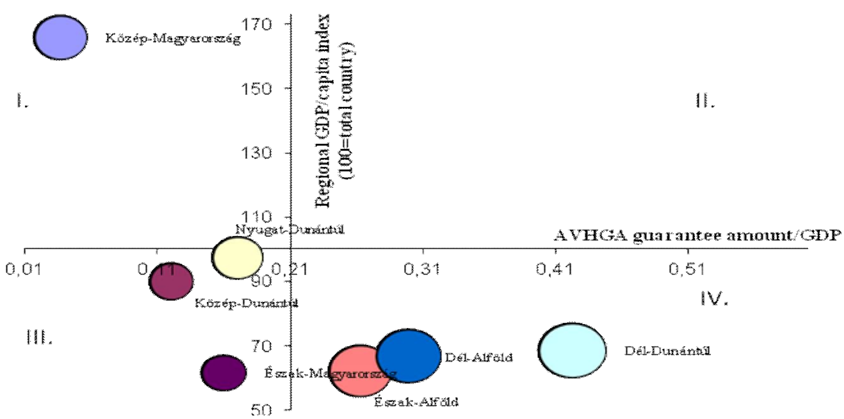
As it is shown in Table-1, the issued guarantee amount/GDP varies from 0,04% to 0,42%. The smallest proportion is in Central Hungary, and the highest is in Southern Transdanubia. In order to present all the three dimensions in one diagram, we can create the following four quadrants bubble chart. On the X axis are the guarantee/GDP data, on the Y axis is the regional GDP/capita index. The size of the bubbles shows the issued guarantee amount in the certain region. The intersection of the two axes is at the average of data.

Table-1: The regional breakdown of issued guarantee amount and GDP (2008)

Region	GDP (HUF million)	Issued guarantee amount (HUF million)	Issued guarantee/GDP (%)
Közép-Magyarország (Central Hungary)	12 809 257	4 683	0,04%
Közép-Dunántúl (Central Transdanubia)	2 648 269	3 182	0,12%
Nyugat-Dunántúl (Western Transdanubia)	2 586 048	4 393	0,17%
Észak-Alföld (Northern Great Plain)	2 508 083	6 590	0,26%
Dél-Alföld (Southern Great Plain)	2 377 752	7 102	0,30%
Észak-Magyarország (Northern Hungary)	2 028 903	3 241	0,16%
Dél-Dunántúl (Southern Transdanubia)	1 751 546	7 393	0,42%

Source: Hungarian Central Statistical Office: www.ksh.hu, AVHGA data, own calculations

Figure-2: The regional breakdown of issued guarantee amount and GDP (2008)



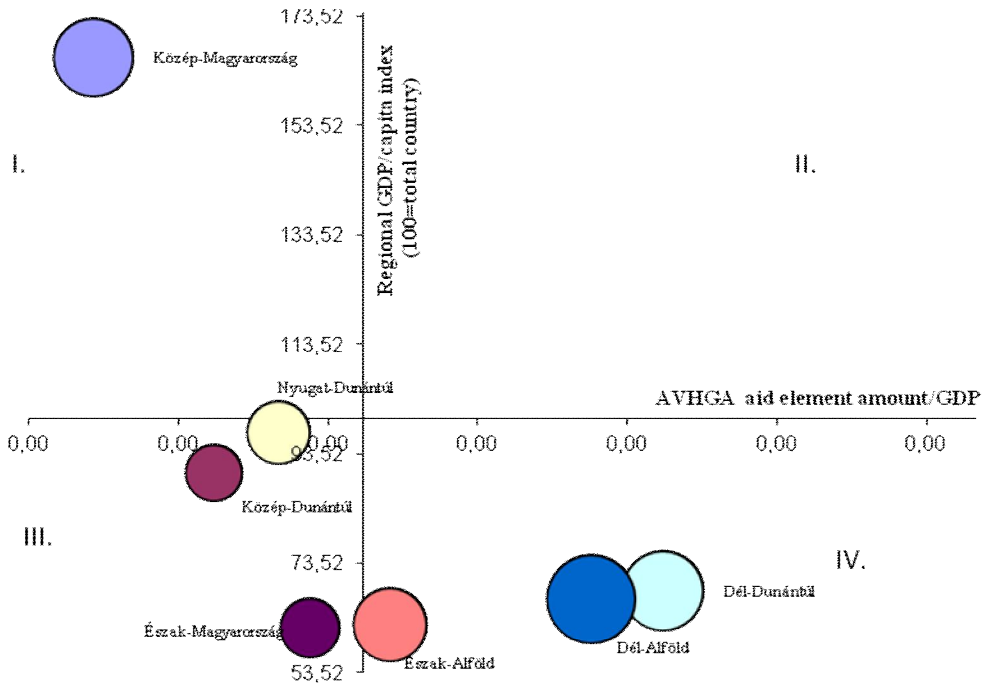
Source: Hungarian Central Statistical Office: www.ksh.hu, AVHGA data, own calculations

Using the Figure-2 chart we can divide the data into four segments. In quadrate I. there are the relatively developed regions with relatively low amount of guarantees. In quadrate II. would be the place of developed regions with high amount of guarantees. In quadrate III. we can see the less developed region with low guarantee, and quadrate IV. shows the less developed regions with more guarantees both by the amount and the percentage of the GDP.

First of all if we consider the fundamental goal of AVHGA, namely the support of less developed areas, the diagram verifies it, because three of the less developed regions dispose with more guarantees. On the other hand the most developed region (Central Hungary) has significantly the fewer guarantees, which also complies with the Deed of Foundation.

In order to see how the guarantee aid element amount influences the effectiveness of guarantee, we use the same type bubble chart. The only difference is that on the X axis there are the guarantee aid element/GDP data.

Figure-3: The regional breakdown of issued guarantee aid element and GDP (2008)



Source: Hungarian Central Statistical Office: www.ksh.hu, AVHGA data, own calculations

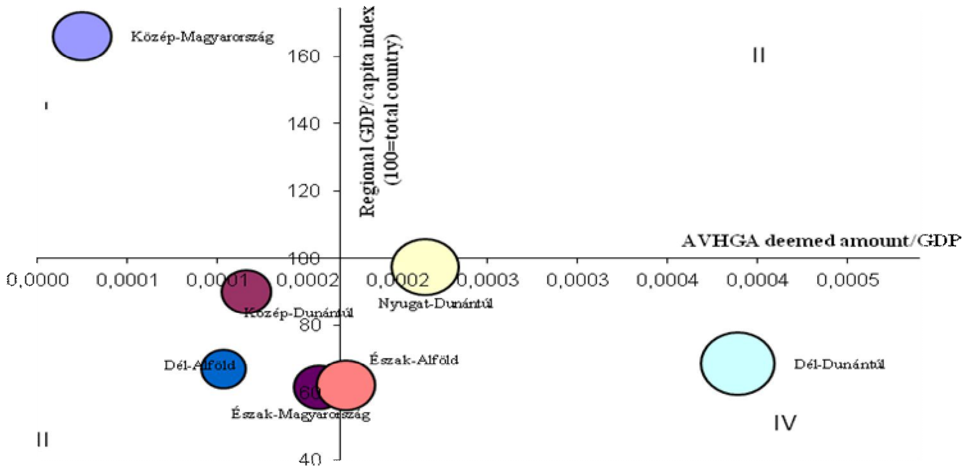
Analysing Figure-2 and Figure-3 charts, we can consider, that there are no significant difference comparing the guarantee amount and aid element amount per GDP data. All the regions are in the same quadrate as before, therefore it is validated, that the fundamental goal of AVHGA, namely the support of less developed areas, is fulfilled. One region (Western Transdanubia) has fewer guarantee amount and aid elements, but is relatively developed based on the GDP data. The two areas that would be more subsidised by AVHGA are Northern Great Plain and Central Transdanubia, because there is not too much guarantee amount and aid element although they are relatively less developed.
To see another aspect of regional effectiveness, we analysed the deemed amount of issued guarantees as well. Deemed amount means the real amount paid by AVHGA instead of the debtor (the SME) of the loan contract. Using this indicator we will see the real cost of the subsidised guarantee.

Table-2: The regional breakdown of deemed guarantee amount and GDP (2008)

Region	GDP (HUF million)	Deemed guarantee amount (HUF million)	Deemed guarantee/GDP (%)
Közép-Magyarország (Central Hungary)	12 809 257	447	0,003%
Közép-Dunántúl (Central Transdanubia)	2 648 269	333	0,013%
Nyugat-Dunántúl (Western Transdanubia)	2 586 048	583	0,023%
Észak-Alföld (Northern Great Plain)	2 508 083	454	0,018%
Dél-Alföld (Southern Great Plain)	2 377 752	269	0,011%
Észak-Magyarország (Northern Hungary)	2 028 903	337	0,017%
Dél-Dunántúl (Southern Transdanubia)	1 751 546	698	0,040%

Source: Hungarian Central Statistical Office: www.ksh.hu, AVHGA data, own calculations

Figure-4: The breakdown of redemptions by regional GDP (2008)regional breakdown of issued guarantee amount and GDP (2008)



Source: Hungarian Central Statistical Office: www.ksh.hu, AVHGA data, own calculations

Comparing the redemption bubbles (Figure-4) to the previous charts by issued guarantee amount (Figure-2) and aid element amount (Figure-3) one can observe, that three regions (Central Hungary, Central Transdanubia, Southern Transdanubia) has not moved from the original place. It means that the proportion of deemed amount equals to the proportion of guarantee and aid element amount. Two regions (Western Transdanubia, Northern Hungary) moved to the right side, in these cases the redemption was relatively higher than the average. It is interesting, that in the less developed regions (Northern Great Plain, Southern Great Plain) moved to the left side only, meaning that in these areas the guarantee was really efficient, because despite of the high level guarantee and aid element percentage the redemption amount is relatively low.

3. CONCLUSION

Based on the above analysis the activity of AVHGA is successful, because it intervenes in the execution of the EU rural development policy and helped to alleviate the impact of the global financial crisis, especially in the most endangered regions. Based on the fundamental goals of AVHGA, the data show the verification of the higher subsidisation of less developed regions. The significantly low percentage of Central Hungary also fulfils the main requirement that the most developed area is not promoted too much. There are possibilities in two regions for more guarantees: Northern Hungary and Central Transdanubia.

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