Greater access to finance as driving factor for sustainable development among tourism-related SMEs in the Philippines: An empirical framework

John Paolo R. Rivera[1]

Abstract

Access to capital funding and other forms of financing is a vital element in the sustainability and competitiveness of SMEs. It allows SMEs, particularly in the tourism industry, to partake in the global economy and seize the opportunities accompanying globalization. We propose a method to address the question of how to empower SMEs participating in the tourism industry to have easy access to financing offered by commercial and universal banks. To address this, there is a need to survey SMEs engaged in the tourism industry and discuss with financial institutions on how to liberalize their policies to provide financing. A-priori results include the need to build the capacity of SMEs to become financially sustainable. Such will allow us to craft policy recommendations on how SMEs can gain and increase their access to financing.

JEL Classifications: L20, Q20, Q56
Keywords: access to finance, development, SMEs, financial sustainability

Introduction

The global economy has been driven by the rapid growth experienced in Asia's developing world, post-Global Financial Crisis (GFC) in 2008. However, the enduring effects of the GFC characterized by economic slowdown in advanced economies, Eurozone debt crisis, and unstable capital flows introduce more complexities and risks in the global economy (Asian Development Bank [ADB], 2014). It makes the world more volatile, uncertain, complex, and ambiguous (VUCA) as coined by Bennett and Lemoine (2014).

These adverse macroeconomic shocks are being alleviated by the role of small and medium sized enterprises (SMEs) – defined as business organizations serving as one of the economic pillars of Asia-Pacific economies. That is, SME development in the region is critical for robust national economies. With globalization, economies have been characterized as VUCA calling for policymakers to design inclusive SME sector development policy frameworks to encourage enterprise growth from different perspectives (ADB, 2014).

To do this, financing SMEs is a fundamental strategy in developing this sector. From the lesson taught by the recent financial crisis, it has become essential for economies to advance innovative financing models outside conventional micro financing

[1] Associate Director, Asian Institute of Management (Philippines); Visiting Research Fellow, Ritsumeikan Asia Pacific University, Japan. E-mail: jrivera@aim.edu / rivera18@apu.ac.jp

avenues. Offering longer-term financing opportunities, such as capital market financing, for emerging enterprises is a newly incipient agenda in SME financing (ADB, 2014). Contemporary developments also demand for the amplification of policy and regulatory activities to cover newfangled areas such as crowd funding, asset-based financing, block chain technology, seed and early stage finance, and SME cluster financing. These are essential because SME financing also has to be abreast with evolving global issues such as rapid climate change, rising unemployment, and worsening poverty. Accordingly, a holistic policy framework better serving various SME financing needs is a critical component for SME development at the national economic level.

Characterized as being dynamic, SMEs are considered vital elements in advancing an economy's growth and development through the generation of meaningful employment and innovation (Aldaba, 2011). Their difficulty in accessing financing has been quoted as one of the foremost restrictions explaining their meager performance and low competitiveness. Obtaining financing from banks and other sources has always been the primary challenge for SMEs to start up, innovate, grow, and develop their enterprises.

In a survey steered by the Philippines Institute for Development Studies (PIDS) and the Economic Research Institute for ASEAN and East Asia (ERIA), cited by Aldaba (2011), results have indicated that the shortage of working capital to finance new business plans, difficulties in obtaining credit from suppliers and financial institutions, insufficient equity, and expensive cost of credit are the barriers to finance access.

As such, we have established that financing is a vital factor for SME competitiveness as well as sustainability. By making financing accessible to SMEs, most especially in the tourism industry, will allow them to "exploit and participate in the global economy" (Aldaba, 2011) and grab the opportunities that comes with the ASEAN Economic Community (AEC). In this study, we would like to address the research question of **how can SMEs participating in the tourism industry have easy access to financing offered by financial institutions**. To answer this, the following research objectives are set:

- **To pin down what is known about access to finance in the ASEAN region** in order to assess the gravity of the issue. This can be done by conducting a critical review of existing literature in order to: (1) identify what strategies are still relevant in this contemporary period; (2) identify best practices that will lead to benchmarking; and (3) update the stock of knowledge in the literature for policy implications.
- **To draw conclusions and policy recommendations** on how SMEs can gain and increase their access to finance.

When tourism enterprises operate sustainably and competitively, they contribute numerous socio-economic benefits to communities throughout the country (and the region on a macro perspective). It has been established that both private sector and local government units (LGUs) are instrumental to sustainable development since they create the infrastructure, policies, and planning measures required for tourism. They upkeep tourism businesses while adjusting practices that conserve resources and safeguard community interests.

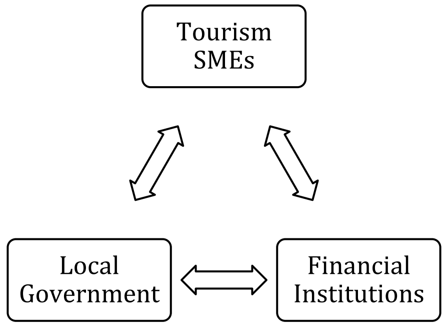

Figure 1. A tripartite relationship in tourism SME financing

Adding the role of financial institutions would make the picture more compelling a tripartite relationship amongst the players in the tourism industry (see *Figure 1*). Likewise, training those SMEs most involved in tourism can: (1) lead to improved coordination among national government agencies and among financial institutions; (2) create opportunities for local communities; and (3) ensure that the economic, financial, social, and environmental impacts of tourism are advantageous to stakeholders.

Literature Review: SME Financing

It has already been established that financial development and economic growth are coupled. That is, dependable financial systems are crucial in driving economic development (Beck et al., 2007; Levine, 2005; Wurgler, 2000 as cited by Tacneng, 2011). According to the Consultative Group to Assist the Poor [CGAP] (2010), policymakers worldwide have stressed the necessity to create inclusive financial systems to increase economic opportunities for SMEs and newly established enterprises, particularly in developing economies. They are the enterprises that most often struggle in accessing external financing. From our previous discussion, this difficulty impedes them from taking advantage of growth potentials and harnessing their productivity operations.

With globalization, financial systems in developed and developing economies have progressed through rapid technological innovation and deregulation that enhanced the openness and competition among financial markets (Tacneng, 2011). Globally, there has been an increase in the number of financial regulators with the role of increasing financial access to SMEs specifically for developing economies.

Tacneng (2011) also argued that it is critical to assess the various characteristics of banking market structures as these stimulate the obtainability of financial services to SMEs. There is a conventional view contending that competition can lead to enlarged credit supply and reduced interest rates, making credit accessible even to prospective firms and small enterprises. That is, banking competition boosts entrepreneurial activity.

Meanwhile, there is a relationship lending perspective or an information-based hypothesis that highlights the prominence of market power in aiding new enterprises to establish long-term relationships with financial institutions, subsidizing them and extracting rents in some periods (Petersen & Rajan, 2005). In other words, more concentrated banking markets result to higher availability of credit.

Furthermore, empirical studies done by DeYoung, Goldberg, and White (1999), Bonaccorsi di Patti and Dell'Ariccia (2004) and Carbo-Valverde, Rodriguez-Fernandez, and Udell (2009) provided an ambiguous relationship between bank competition and bank market structure on SME access to financing. Their results are not applicable to the developing economies of ASEAN because their studies were done in developed economies (i.e. United States, Western Europe) where SMEs are subjected to flexible institutional borrowing restrictions. This implies that access to finance is best studied at the local level. More so, the tourism industry in every economy is unique. The successes in various destinations may be likely due to the efforts of their respective local government units enabling financial institutions to relax some of its rigid policies. As such, there may be a need to let local financial institutions decide on the measures they want to employ for granting access to credit and define measures that are consistent with their organizational and institutional goals.

Aldaba (2011) conducted a study utilizing consultations with key stakeholders exposed concerns about the incapacity of enterprises to access financing due to the rigorous and voluminous requirements of financial institutions. "Firms find it hard to borrow due to the collateral requirements and the long time it takes to process their loan applications" (Adaba, 2001, p. 311). Moreover, the following reasons were disclosed: firms find that (1) the minimum loan requirement and short repayment period too restrictive; (2) loan restructuring is difficult; (3) high interest rates charged by financial institutions to firms; (4) lack of access to venture capital funds; (5) absence of financial packages; (6) and the limited access to information on fund sources.

Aldaba (2011) also underscored the viewpoint of financial institutions where they expressed their apprehensions about the bankability of SMEs and the high risks involved in SME lending due to SMEs' lack of appropriate financial management capacity.

It is also noteworthy that both SMEs and financial institutions mentioned the shortfall of the government to create policy frameworks that will address the concerns mentioned (Aldaba, 2011).

Hence, it has been apparent from the studies cited that there is a systemic and circular problem here – banks will only lend to SMEs if they are operationally sustainable and financially viable. However, SMEs will be operationally sustainable if they have access to funds. Thus, as a research gap, there is a need for an optimal strategy to break this vicious cycle without making a party worse off (see *Figure 2*). To do this, it is crucial to create a business environment with lower information asymmetry between SMEs and financial institutions.

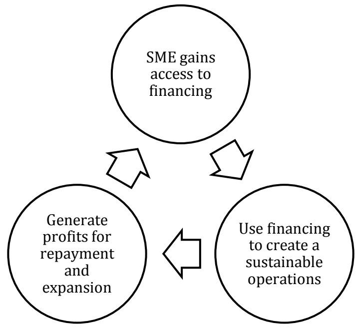

Figure 2. The cycle of SME financing.

Framework

We appeal to the framework behind LandBank of the Philippines' *Todo Unlad* Program (Total Development Options – Unified LandBank). It is LandBank's flagship program for countryside development. Through its several lending programs and support services, *Todo Unlad* connects cooperatives, LGUs, private corporations, SMEs, and non-government organizations (NGOs) in specific areas around an integrated development project. It veers away from fractional efforts in developing an area. Instead, it extends loans and other support services to all key players in a predetermined area to guarantee that all efforts lead to an integrated area development.

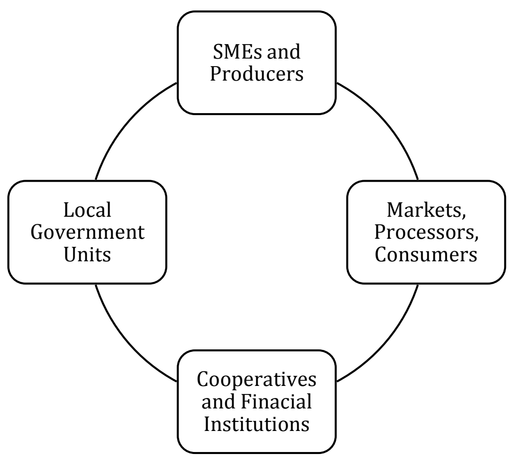

Figure 3. The value chain of SME financing.

Todo Unlad aims to achieve countryside development by linking producers to markets and processors, strengthening cooperatives, and LGUs (see *Figure 3*). Specifically, it anticipates to increase agricultural productivity, expand basic infrastructure, and eventually facilitate the way towards rural industrialization and to transfer partially or wholly, the ownership and management of productive assets to cooperatives. Its projects are composed of a combination of two or more of any of the following loans and services: (1) local government lending, (2) commercial lending, (3) cooperative lending,

(4) production or post-harvest facilities financing, (5) market matching and production, marketing and management agreements, (6) cooperative strengthening, (7) LGU advisory services, (8) trade financing, (9) and integrated loan packages for agrarian reform communities.

From our discussion above, it can be construed that there will be certain firm-level characteristics that will enhance or reduce an SMEs' access to financing such as, but is not limited to - firm's number of years of operations, leverage, financial position, financial performance, demographic characteristics of the owner (age, educational attainment), employee characteristics, credit reputation, among others. These are necessary but not sufficient factors for financial institutions. A logistic regression equation will represent this.

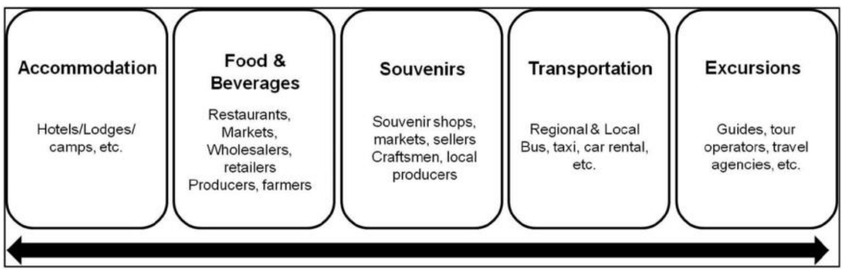

Figure 4. The tourism value chain
Source: Rivera and Gutierrez (2019)

For sufficiency conditions, we argue that for financial institutions to grant ease of access to credit, **SMEs must be an active participant of its respective value chain** (see *Figure 4*). This signals financial institutions that there is a vehicle by which a borrower SME can repay when debts come due. Being part of a lucrative value chain is becoming easier especially for tourism-related SMEs because of the growing diversity of international tourists with varied tastes and preferences, which facilitates SMEs to broaden potential offerings (Christian, Fernandez-Stark, Ahmed & Gereffi, 2011). Furthermore, according to Christian et.al (2011), the rise of digital tourism compelled enterprises to establish Internet presence by creating platforms that not only promote a destination but also include functions such as online reservation systems for local hotels and tour operators. This allowed smaller local firms direct access to the market as in *Figure 3.*

Tourism-related SMEs can take advantage of the rapidly expanding international tourism to be part of a value chain. This expansion, according to Christian et.al (2011), can be attributed to the decreasing costs of travel, developments in travel technologies that shorten travel time, and the growth of information technology (IT) allowing a traveller to easily learn about potential new destinations. SMEs may take advantage of value chains existing within the five stages of travel employed by Clawson and Knetch (1966): (1) anticipation; (2) travel to the site; (3) on-site behavior; (4) return travel; and (5) recollection.

In recent years, Google released its own version of the five stages of travel as cited by Tengco (2014): (1) dreaming, (2) planning, (3) booking, (4) experiencing, and (5) sharing.
While challenges endure due to the inherent nature of the tourism industry (i.e. seasonal nature, sensitivity to high transportation costs, concerns about safety, and fluctuating tourism preferences), the industry still provides meaningful employment opportunities for many developing economies in a wide range of services, from accommodation to transportation, food services, and guiding.

Proposed Empirical Framework

This section will describe the data requirements, sources of data, and treatment of data in various objectives of this proposal. To address the research question, there is a need to develop a survey questionnaire that will capture the firm-level characteristics (financial position, financial performance, and other relevant constructs) of tourism-related SMEs that facilitated or hindered their access to finance. By random sampling, there is a need to identifying SME-respondents who will participate in the survey. A minimum of 30 tourism-related SMEs from the Philippines will form part of the sample.
After gathering the data, an empirical model will be developed to show the relationship of the exogenous variables in the survey with the likelihood that access to finance will be granted by financial institutions. A functional form will be specified as in Equation 1.

$$ACCFIN_i = f(\mathbf{v}FINPOS_i, \mathbf{v}FINPER_i, \mathbf{v}DEMOGR_i) + \varepsilon_i \qquad (1)$$

Where:
$ACCFIN_i$ = a dummy variable indicating whether an SME was granted access to finance by a financial institution. This assumes a value of 1 if granted; and 0 otherwise. This endogeneous variable will be captured by the survey questionnaire.
$\mathbf{v}FINPOS_i$, $\mathbf{v}FINPER_i$, and $\mathbf{v}DEMOGR_i$ are vectors capturing financial position, financial performance, and demographic variables that can influence $ACCFIN_i$. Financial position variables can include assets, liabilities, and equities. Financial performance variables can include revenues and costs. Demographic variables can include age of the firm, age of the owner, educational attainment of the owner, among others. These variables will be captured by the survey questionnaire.
ε_{it} = stochastic disturbance term that captures all other variables not included in the model.
Equation 1 will be transformed into a binary logistic regression that will be estimated using Maximum Likelihood Estimation (MLE) (Gujarati & Porter, 2009).
To augment empirical results, there might be a need to conduct a focused group discussion (FGD) involving tourism-related SMEs and financial institutions. Here, it is essential to invite several SMEs who had experiences acquiring financing from banks and other formal channels. To balance the discussion, it would be necessary to include financial institutions known for having programs that cater to SME financing and development such as the Development Bank of the Philippines (DBP), LandBank of the

Philippines, Veterans Bank of the Philippines. As mentioned earlier, this will allow us to see the situation from the perspective of borrower and lender. At the same time, we would be able to validate the empirical results and add other necessary and sufficient constructs that were not captured by our empirical model. The FGD can also serve as a venue for both SMEs and banks to reduce information asymmetry between them in terms of preferences and logistical requirements.

Conclusion

At the onset, the literature and the a-priori expectations point to the necessity of building the capacity of tourism-related SMEs. Such capacity-building programs will enable SME's to learn the business techniques that are necessary in operating enterprises - a qualification that banks look for. Likewise, in the discussion table between SMEs and experts from financial institutions, there is a huge likelihood that the information asymmetry in the industry will be reconciled. Consequently, SMEs would be capable of creating a business environment in their respective enterprises that will give them the credibility to be granted access to financing. Similarly, they will be able to think strategically about their intended interventions and the key requirements for successful access to financing.

The empirical framework proposed would be able to point to policy makers and regulators areas for intervention that will allow greater access to financing especially to SMEs. However, this can only be functional with the availability of data. As such, researchers would be able to estimate the impact multipliers in order to derive causal relationships and determine specific policy frameworks to support SME through greater access to least cost financing.

References

Aldaba, R.M. (2011). SMEs access to finance: Philippines. Jakarta: Economic Research Institute for ASEAN and East Asia. Retrieved from http://www.eria.org/publications/research_project_reports/images/pdf/y2010/no14/CH_10_Philippines(291-350).pdf

Asian Development Bank (ADB). (2014). *Asia SME Finance Monitor 2013.* Manila: Asian Development Bank.

Beck, T., Demirgüç-Kunt, A., & Martinez Peria, M.S. (2007). Reaching out: Access to and use of banking services across countries. *Journal of Financial Economics*, *85*(1), 234-266.

Bennett, N., & Lemoine, G.J. (2014). What VUCA really means for you. *Harvard Business Review*. Retrieved from https://hbr.org/2014/01/what-vuca-really-means-for-you.

Bonaccorsi di Patti, E. & Dell'Ariccia, G. (2004). Bank competition and firm creation. *Journal of Money, Credit, and Banking, 36*(2), 225-251.

Carbo-Valverde, S., Rodriguez-Fernandez, F., & Udell, G. (2009). Bank market power and SME financing constraints. *Review of Finance, 13*(2), 309-340.

Christian, M., Fernandez-Stark, K., Ahmed, G., & Gereffi, G. (2011, November). The tourism global value chain: Economic upgrading and workforce development. Retrieved from http://www.cggc.duke.edu/pdfs/2011-11-11_CGGC_Tourism-Global-Value-Chain.pdf

Clawson, M., & Knetch, J. (1966). *Economics of outdoor recreation.* Baltimore: John Hopkins University Press.

Consultative Group to Assist the Poor (CGAP). (2010). *Financial Access 2010: The state of financial inclusion through the crisis.* Washington: The World Bank Group.

DeYoung, R., Goldberg, L., & White, L. (1999). Youth, adolescence, and maturity of banks: Credit availability to small business in era of banking consolidation. *Journal of Banking and Finance, 23*(2-4), 463-492.

Gonzales-Soria, J. (2011). The travel cycle. *AM-reports – Technology in Tourism, 1*, 6-8

Gujarati, D.N., & Porter, D.C. (2009). *Basic econometrics* (5th edition). Singapore: McGraw-Hill Companies, Inc.

Levine, R. (2005). Finance and growth: Theory and evidence. In P. Aghion & S. Durlauf (Eds.). *Handbook of Economic Growth* (865-934). Amsterdam: Elsevier.

Petersen, M.A., & Rajan, R.G. (1995). The effect of credit market competition on lending relationship. *Quarterly Journal of Economics, 110*(2), 407-443.

Rivera, J.P.R., & Gutierrez, E.L.M. (2019). A framework toward sustainable ecotourism value chain in the Philippines. *Journal of Quality Assurance in Hospitality & Tourism, 20*(2), 123-142.

Tacneng, R. (2011). *Local banking market structure and SME financing obstacles: Evidence from the Philippines.* Retrieved from http://economix.fr/fr/recrutement/2014/jpo-2014/papier_Tacneng.pdf

Tengco, J. (2014). It's more fun in the Philippines. A presentation for the Dr. Andrew L. Tan Center for Tourism forum on *Emerging trends in digital travel and its impact on tourism buyer behaviour*. Held 30 April 2014 in Asian Institute of Management, Makati City, Philippines.

Wurgler, J. (2000). Financial markets and the allocation of capital. *Journal of Financial Economics, 58*(1-2), 187-214.