

Chapter 1

Introduction

The small and medium-sized enterprises (SMEs) are an important part of national economy. Since the reform and opening up, China has experienced vigorous development of SMEs. By the end of 2006, there are more than 42,000,000 SMEs¹ and non-state-owned enterprises, accounting for 99.8% of the total amount of enterprises. Among them, the registered SMEs reached more than 4,300,000 and the self-employed households over 38,000,000. So, what are the small and medium-sized enterprises? Is there a worldwide standard to measure them?

The definition of SMEs is a concept which principally bases on the scale of enterprises. The SMEs in different countries are different. For instance, in Japan and in Korea, they call it SMEs- small-and-medium enterprises; in the U.S., they call them small business; and in UK and EU, the SMEs means the all types excluding those large; while in India, there is not a standard, it includes small scale service and business enterprise (SSI), ancillary industry, small scale service and business enterprise (SSSBE), and micro scale industry. Otherwise, there may be self-employed enterprises in some countries which are also included in the category of SMEs.

It is an ever changing concept too. Either in theory or in practice, it is difficult to give it an exact definition. And at present there is not a standard in the different countries of world. The reasons are: First, the economic environment is very different from each other. Second, even though in the same country, the standard is changing with the development of economy. Third, the growth of enterprises is a complex process; it is too difficult to include the all factors in a standard.

¹ *Chinese SME information report 2007*, China Statistical Press

Despite it is difficult to give a standard definition to SMEs; all countries try to make a standard in their own countries to administrate the SMEs. (*Table 1.1*) Basically there are two ways to define: the first is to define it by its economic nature: the concentration of ownership, management, the status in their profession; the second is to define them by some indicates like scale, capital, sales volume, etc. We can see the different definitions from *Table 1.1*, most countries like to use some indicates rather than the nature of enterprises. But there are a few countries use both of them.

Table 1.1 the definition standard of countries*

Countries and areas	The standard	Basis on
The U.S.	Nature: (those which have at least 2 of them are the small business): (1) the owner is the manager; (2) the capital comes from one individual or some individuals; (3) the main sale market is local place; (4) compared with other big enterprises it has a small scale Volume: Employee \leq 500	U.S. Committee for Economic Development
EU	Medium sized: employee \leq 250 and volume of business per year \leq 40 million euro; total liability \leq 27 million euro, other firms do not hold 25% share. Small: employee \leq 50 and volume of business per year \leq 7 million euro; total liability \leq 5 million euro, other firms do not hold 25% share.	European Council
UK	Nature: small scale, the owner operates the firm by himself; the managers are independent from external domination. Volume: Manufacturing employee \leq 200; Construction and Mining industry: \leq 25; retail business, business income \leq 450 thousand pound.	Bolton committee

Japan	Manufacturing: employee \leq 300 capital \leq 300 m, yin Wholesale trade: employee \leq 100 capital \leq 200 m, yin Retail business; employee \leq 50 capital \leq 50 m, yin Service industry: employee \leq 100 capital \leq 50 m, yin	Basic Law of SME (2000)
Korea	Manufacturing and transport service: employee \leq 300 capital \leq 500 m, Yuan Construction industry: employee \leq 50 capital \leq 50 million K Wholesale trade: employee \leq 50 capital \leq 100 m, Yuan Service industry and commercial industry: employee \leq 50 capital \leq 200 m, Yuan	The SME organization Law

* Collection from: Suo Jian, *The International Comparison of SME Development*, China Social Sciences Publishing House Press, 2001, p.32 and Gao Zhengping, *The New Theory of SMEs' Financing*, China finance Publishing-House press, 2004, p.39 www.cnki.com

In China, in different periods and at different development stages, the description of SME and the definition changed often. On the 1st January 2003, the first Chinese specialized Law on SMEs was put into effect--“*the Promotion Act of SME*”, in which there is the first definition in law. In the same year, the State Development Planning Commission, the Ministry of Finance and other relevant office published the “*Standard of SMEs*”. (See Table 1.2)

Table 1.2 the Standard of SME (China, 2003)*

Industries	Definition
Manufacturing	employee $<$ 2000, or the amounts of sales $<$ 300million Yuan, or total assets $<$ 400million Yuan media: employee \geq 300, or the amounts of sales \geq 30million Yuan, or total assets \geq 40million Yuan small: otherwise

Construction industry	employee <3000, or the amounts of sales<300million Yuan, or total assets<400million Yuan media: employee >=600, or the amounts of sales>=30million Yuan, or total assets>=40million Yuan small: otherwise
Wholesale trade	employee <200, or the amounts of sales<300million Yuan media: employee >=100, or the amounts of sales>=30million Yuan small: otherwise
Retail business	employee <500, or the amounts of sales<300million Yuan media: employee >=100, or the amounts of sales>=10million Yuan small: otherwise
Transport service	employee <3000, or the amounts of sales<300million Yuan media: employee >=500, or the amounts of sales>=30million Yuan small: otherwise
Postal Service	employee <1000, or the amounts of sales<300million Yuan media: employee >=400, or the amounts of sales>=30million Yuan small: otherwise
Lodgings and Catering Services	employee <8000, or the amounts of sales<150million Yuan media: employee >=400, or the amounts of sales>=30million Yuan small: otherwise

* From: Gao Zhengping, *The Theory of SMEs' Financing*, China Finance Press, 2004 p.45-46
www.cnki.com

The ultimate value of the products and services produced by SMEs accounts for 59% of GDP in China, the production of goods accounts for 60% of sales in the community and turns over to the tax accounts for 48.2% of the total. At the same time, the SMEs bear 70% of the import and export figures, and the SMEs solve the employment with the volume of more than 75% in urban and rural areas.²

² *China Statistical Yearbook 2007*, Chinese Statistical Press

According to the 2002 APEC SME Ministerial Meeting statistics, in the 21-member APEC, the amount of small and medium enterprises accounted for 97% of the total, created by the share of GDP amounted to more than half the share of exports accounted for 40% -- 60%.³

1. The SMEs are the basic force to encourage the market competition, as the natures of SMEs are very similar to the assumption of free competitive market in classical economics.

2. SMEs can enhance the national economy and raise the economic growth. In many countries, SMEs have been to become a country's economy the most dynamic growth pole. From the number of enterprises, output, exports, as well as contributions to the national economy we can see that SMEs are dominant.

3 The SMEs are important channels of solving the problem social employment. In market economy, the function in creating the employment opportunity came from SME is comprehended without no-words. Since the labor-intensive characteristic, the SMEs' workforce that the equivalent capital absorbed is far higher than that of the large enterprise. So she becomes the incoming labor force's persons who absorb mainly.

4. Small and medium-sized enterprises are positive pushers who promote international trade. In the past 20 years, it was much more important that people realized the function in international trade of SMEs is more important than the past gradually imagining. Even in the developed country, the share in exporting of SMEs is much higher than the imaginable ones.

To sum up, in countries around the world, SMEs play a more and more important role. However, it is worth noting that in the ever-changing information technologies and conditions of system, the different industries under the conditions of system, show different characteristics of the economies of scale; some sectors trend at the same

³ *APEC Statistics 2002*, APEC Database, <http://www.apectariff.org/>

time to smaller ones; while other industries have emerged of the scale. As a result, there are no absolute advantages or disadvantages between large enterprises and SMEs.

As a fact, China's economy has been growing about 10% per year in real terms over the last decade. Considering that this rapid growth may be largely contributed to the globalization of trade, we need to recognize that the SMEs play a great role in this development. The SMEs are not only China's economic lifeblood, but also the rapid economic development's "booster". The SMEs push the economy to increase day by day; they become the new dynamics of technological and systematical innovation; they provide a main channel for employment; and the SMEs play a more and more role in blooming national economy, increasing the revenue, optimizing the economic structure, enhancing economic vitality, and promoting social stability.

Regarding to the important influence of SMEs on the economic development, to study the SMEs is the hot topic. And as we know, the capital is one of the most important instruments for enterprises' economical activities. Without this instrument the enterprises can not run continually. Compared to the western developed countries, the development of SMEs in China is still relatively backward. Therefore, it is an ideal view to analyze financing problems of SMEs in China by using the western financing theories and comparative method from a historical respect.

This article is designed and written according to two purposes: first, on the base of the presentation of the relevant western financing theories, to provide a theoretical structure for discussing the Chinese case; second, by examining the successful experience of developed countries, especially the Italian case, to search a possible way for the SMEs in China.

After the introduction of Chapter 1, the Chapter 2 analyzes mainly the background, the theme of the study, the basic concepts and fundamental ways, as well as the theoretical basis of this thesis. The financing problem of SMEs is the superposition of enterprise's financing problem and SMEs problem. This thesis is mainly based on credit theory, capital structure theory, financing structure theory and so on. Financing theories developed from the "savings" theory of classical economics, Keynesian economics to the modern theories have reflected the generality of enterprise's financing system under the market economy condition. In some sense, these theories are very helpful to us to study the financing problems of SMEs.

The chapter 3 mainly introduces the development of the policies and financing channels of SMEs in China. After introducing the background of the development of SMEs in China and the Chinese banking industry, we try to reveal the status quo and problems of Chinese SMEs, specially the problems of financing, with the analysis of Chinese scholars who study the Chinese SMEs' situation with the western financing theories

The chapter 4 aims at introduce the model of industrial districts and the Italian financial system. The Italian industrial model is known worldwide as a successful example of endogenous development based on SMEs strongly rooted in their communities. A lot of SMEs make up the industrial districts which have a lot of numbers, locate dispersedly all over the country but concentrate highly in regions. After the Second World War, the government and some intermediate commercial institutions carried on many policies to support the development of SMEs and to solve their financing problems that enhance the competition power of industrial districts in the world. Among them, the medium and small banks play an important role in promoting the development of SMEs. By analyzing Italian model, I try to find some useful ideas to solve the financing problems of SMEs in China.

In Chapter 5, I try to discuss some countermeasures to solve the financing problems of SMEs in China. On one hand side, China must build and improve the Credit Guarantee Schemes (CGSs); on the other hand side, some informal finance can be took and developed, such as pawnshops and ROSCA (Rotating Savings and Credit

Association). And China can learn some lessons from the experiences of Italian: the relative policies of government and the development of industrial districts.