

Small and medium enterprises' financing and network models
Research project

The core analysis performed by the research unit will be the relationship between the governance structure of firms and their modality of financing. Within the governance structure the different types of networks of enterprises will be particularly considered.

In the research a network of enterprises is meant to be a series of relationships, legally relevant and basically steady, among two or more enterprises that are formally and legally distinct, even competing, in whose activity a significant interdependence exists or is generated. Examples can be subcontracting and franchising networks, consortia, non-consortium companies with a coordination function, joint ventures, networks consisting in cross ownership among two or more companies or characterised by interlocks regarding directors or auditors.

At least in sociological and economic debate, the literature upholds that governance is evolving from a vertically integrated system to coordination systems in which nodes-firms are more autonomous, systems that may be defined by and large as networks. It appears to be less clear instead whether this organisational change reflects upon the enterprises' financial structure and, symmetrically, how the latter may influence networks.

From this point of view, the nature of the network may be relevant under two aspects:

a) that of financing of single enterprises in network-like contexts. Networks are a system for the governance of interdependencies that bind an enterprise to other enterprises, combining cooperation and competition, and, because in many cases these interdependencies influence deeply the enterprise's value, its growth or crisis perspectives, then mapping of network systems to whom enterprises belong seems a useful step (if not a necessary step) in deciding on whether or not to finance it (with bank credit, private equity or by other means);

b) that of financing of networks, or by networks of firms belonging to them. Since networks are a mean of coordination among enterprises that can exploit complementary resources in a flexible way and, at the same time, produce public (or semi-public) goods in the interest of participants to the network, networks themselves may become a mean of financing of enterprises that belong to it (node-enterprises):

b1) as recipient of financing provided by others;

b2) as a collector of financial resources among the belonging enterprises

i. for the financing of a common project or

ii. so that these resources are distributed among enterprises (as financing, financial consulting, guarantee supplying or other kinds of financial support).

(A) ENTERPRISE FINANCING IN NETWORKS

Under the first profile, the research is intended to distinguish different types of networks which each firm belongs to and in particular:

- contractual networks, i.e. networks in which interdependencies among enterprises are regulated through contracts, bilateral (such as subcontracting networks and franchising networks) functionally

connected or multilateral (such as contractual consortia or many cooperation agreements, contractual joint ventures, etc.);

- organisational networks, i.e. networks in which coordination is accomplished through the institution of a complex entity (associations of enterprises, foundations, consortium companies, 'normal' companies);
- proprietary networks, i.e. networks in which coordination is given by sharing proprietary rights on the enterprise (such as cross ownership in various companies);
- governance networks, where coordination runs among individual and discrete organisational structures, as occurs, for example, with interlocking directorates.

These networks may be distinguished also for their finality:

- some address coordination of the whole production and distribution cycle or some phases of it (such as networks for raw material acquisition; subcontracting, franchising and distributing networks);
- others address production of goods or services for the enterprises or of positive externalities for the (local) entrepreneurial community as a whole (e.g. networks for pre-competitive research, for environmental impact control, for product safety).

The research hypothesis regards the relevance of these types of networks (in their various structural and functional kinds) in defining financial strategies of enterprises.

In particular it seems relevant to consider the impact driven from the existence of such networks (and of interdependencies they regulate, but sometimes produce) on

- the ability of enterprises to finance themselves;
- the ability of enterprises to access a plurality of diverse financing forms (not particularly from the bank's point of view – multiple simultaneous bank relationships – but rather from the point of view of the various kinds of financiers – e.g.: public, non-banking private financiers – and of forms – e.g.: securitisation, private equity, leasing);
- the ability of financier (banking and non-banking) to assess ex ante the merit of credit of the financed person and of the financed project;
- the ability of financier (banking and non-banking) to direct and then monitor the financed person's condition and the state of financing;
- the possibility that a convenient complementarity of financial resources and critical resources of different kind (such as, in particular, know-how) is exploited, so that financing may be devoted to innovative projects;
- the possibility that the entrepreneurial project to which financing is given acquires international dimension (and, in particular, may support delocalisation strategies);
- the ability of the parties to prevent and govern crisis.

In this perspective, a very relevant theme deserves particular attention: trade credit. Peculiarity of this type of credit is that it stems from a series of relationships that the enterprise (supposed creditor) has with other enterprises (supposed debtors; such as, in particular, but not only, credit for supplies).

In a more general framework, the research questions in which circumstances trade credit may be considered as a proper mean of financing for enterprises and which relationship should run between trade and bank credit: are they alternative? Or does one make up for the other? Are they integrated? In all cases, the question may have a different answer depending on whether one considers the liquidity function of certain banking contracts regarding trade credits (such as bank advances) or, rather, their function as collateral (as is in credit liens or assignments in secured transactions). In the Basel II Accord's perspective, the perspectives of development of these intersections between trade and bank credit are not granted, given constraints concerning credit risk concentration in assessing the clients' exposure.

Contiguous phenomenon, likewise worth investigation, is that of overdue payment of such credits. In a perspective that is in part new as compared with that investigated up to now, this phenomenon is worth investigating with an attention to governance structure of the relationship in which the credit originates and is governed by the parties. In particular, if one studies this phenomenon in a network context, one can wonder whether, if there is a network, trade credit may work as an instrument for cooperation among enterprises: in other terms, the extension (rather than delay) in payment could originate from the accession of enterprises to a project of common interest that needs flexibility, also in payment terms. If this is the adopted perspective, the application of regulations borne by Legislative Decree n. 231/02 on overdue payments in trade transactions may have different stresses and give new thrift to self-regulation of relationships among enterprises.

(B) NETWORK'S FINANCING

On this side, a network assumes a more important role in the financing relationship, since either it becomes a party in this relationship (as financed or financing party) or it plays a supportive role for the financing relationship (not only the banking one).

B.1: Networks as financed parties.

It could be possible to define the research hypothesis in this way: whether and, if so, on which conditions networks could be designed as financed parties.

The analysis will be divided according to the fact that the network could assume a contractual form or an organizational form, as explained above.

Contractual networks. Regarding contractual networks, it could be observed that, from a legal point of view, nothing prevents to conceive a contractual relationship in which a party is composed by multiple subjects. However, on the substantial basis, this raises problems concerning the complexity of patrimonial liability schemes and the ex ante and the ex post checks, including monitoring. In these situations, it is asked whether it could be possible to overcome these problems either by identifying a lead subject as unique or main responsible in the contract or by introducing guarantee systems (unilateral or network systems) supporting financing.

It could be possible to find out some applications of these hypotheses relating to franchising networks or supply networks: thus, financing could be direct to the supplier or to the customer and then re-allocated throughout the network or, apart from outside financing (e.g. banking financing), situations of intra-network financing occur.

One particular hypothesis, which will be specifically considered, is the securitisation of a pool of credits supplied in favour of multiple firms on an individual basis (and therefore conceived for the specific patrimonial condition of the single financed party); but in the meantime the credits are directed to converge on an aggregated pool for securitisation and placing of bonds in the market: this is the case of the so called "district bond" carried out recently by a big Italian bank.

Organizational networks. Regarding to the organizational networks, it is asked whether some network forms promote the financing of firms (e.g. limited companies taking the form of network could be better than foundations taking the form of network) or whether the supply could change according to the financing type (e.g. banking financing vs. equity investment). In fact, the choice of a specific legal form of the network affects on the patrimonial liability systems as much as internal systems that are in charge of the resources allocation and management.

B.2: Networks as financing devices.

A different issue arises when a network is built up in order to realize or facilitate the financing process of the participant firms. Many types of structured financing could be understood in this way: the venture capital, for example, or some forms of private equity could be viewed as financing networks set up by (operating) firms and (also not banking) brokers. According to the specific purposes to which financing is direct (e.g. the start-up of a firm or the restructuring of a declining firm), networks could properly manage the interdependencies between financial resources and

managerial abilities: a structure based upon a centralised control could hardly realize this coordination.

Moreover, with respect to the issue of networks as devices direct to favour access to finance by SMEs, a particular attention should be paid to Mutual Guarantee Societies as collective guarantee bodies, as recently defined and reformed by art. 13 of d.l. 269/03, converted into the law 326/03. Indeed, nowadays mutual guarantee societies may represent the most important example of SMEs network constituted for access to (mainly banking) financing.

Mutual guarantee societies' reform and organizational structure In order to face the transition linked with the ongoing reform process, which requires a rising of patrimonial levels as much as an improvement of the operating structure, mutual guarantee societies could adopt growth strategies based upon the concentration (by means of merger) of different consortia. From the point of view of this research, it could be interesting to look at the use of networks of networks as models that govern new mutual guarantee societies. These models could help consortia to reach an optimal dimension both for the patrimonial structure and for the availability of adequate managerial skills.

Mutual guarantee societies reform and modes of activity. According to the regulatory scheme introduced by Basle II agreements, it is widely diffused the opinion that the methods of selecting guarantees and collateral securities should be deeply revised. Moreover these changes could be connected with a normative scheme regarding guarantees that is facing a deep transformation both at a National and at a European level which mutual guarantees societies should take into account of (d.lgs. 170/04; dir. 2002/47/CE).

From these standpoints, the research tries to answer to some questions in a legal perspective.

- Is it useful to think about an organizational restructuring of mutual guarantee societies? What kind of opportunities does the new corporate law offer?
- Which legal model could be suggested for the Mutual Guarantees Societies which aim to upgrade further functions or different ones compared to the function of supplying guarantees (e.g. consulting, rating, monitoring, firms' assistance in distress)?
- Which legal forms can be proposed for establishing mutual guarantee societies' networks?
- Which guarantees forms could be promoted because of the new statutory provisions? Which could be more suitable for district or network contexts?

From a methodological point of view, the research unit will carry out an in-depth analysis of questions as drawn above and, although not extensively, will adopt a comparative approach, with a special attention to the English and Spanish contexts. In order to verify the research hypotheses, the unit will run a series of case studies, interviewing firms, banks, mutual guarantee societies and other relevant actors (trade and industry associations, chambers of commerce, ...). The case studies will allow to collect important information (not available in literature) with respect to the structure and the function of networks and to their impact on the financing of SMEs.

Collection and elaboration of information regarding network models structure and function raises the problem of representing and elaborating explicit knowledge using natural language. Given the intrinsic vagueness of predicates, this generates a kind of uncertainty which is not easily approached using probability measures. Under this profile, the research group, with the scientific support of other disciplines, intends to elaborate a model/system apt for representing linguistic information derived from multiple sources, aggregating it considering multiple criteria, and creating a support for decision-making by experts and operators.

This analysis should allow to work out some proposals regarding the regulation (through law or self regulation) either of networks or of some forms of network, that could be interesting for the financing of SMEs.