

22 March 2011

Managing Credit & Financial Performance of **SMEs**

Ong Siew Kim



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AGENDA

- Outlook of the SMEs Sector
- Credit Management
- Financial Management
- Credit Rating Solution



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Outlook of the SMEs Sector



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Outlook and the Credit Risk Environment

- Singapore SMEs numbered over 150,000
- >90% of total business establishments
- Employs approx 50% of total workforce
- Generated 40% of country's GDP
- Singapore SMEs survival rate (Whole Population)
 - 94% - 96% in first year
 - 62% - 75% in third year
 - 48% to 55% in fifth year

What are SMEs?

- Enterprises having at least 30% local equity ownership
- Employs no more than 200 people (applicable only non-mfg SMEs)
- Fixed Assets not exceeding SGD 15 mil



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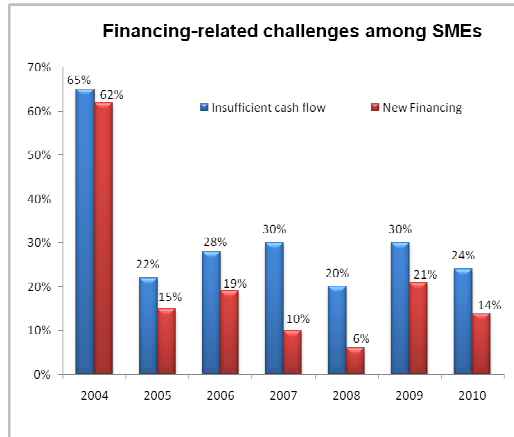


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Survey Findings of SMEs : SMEs Development Survey 2010 (Financials and Funding)

SME financing landscape has evolved over the past 7 years

- Access to financing was very challenging for SMEs in 2004
- With banks' shifting focus towards serving the SME



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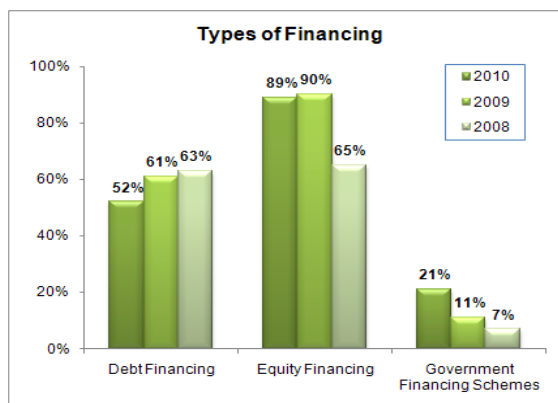


Survey Findings of SMEs : SMEs Development Survey 2010 (Financials and Funding)

SMEs shift towards tapping on Government Funding Schemes; Resulting in decline in take up of Debt financing

Debt Financing dropped by 9%

Venture Capital Funding only 1%



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Survey Findings of SMEs : SMEs Development Survey 2010 (Financials and Funding)

- New Bridging Loan Programme (BLP) and Micro Loan Programme (MLP) top the list
- Negligible take-up of Business Angels Funds (BAF) **most popular**

Top 5 Government Funding Schemes	2006	2007	2008	2009	2010
New Bridging Loan Programme (BLP)	-	-	-	11%	13%
Micro Loan Programme (MLP)	2%	3%	2%	6%	9%
Local Enterprise Finance Scheme (LEFS)	4%	6%	4%	9%	7%
Loan Insurance Scheme / Loan Insurance Scheme Plus (LIS / LIS+)	0%	1%	1%	3%	4%
Internationalization Finance Scheme (IFS)	0%	1%	1%	1%	3%

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Survey Findings on SMEs : SMEs Development Survey 2010 (Financials and Funding)

Competitive Interest Rates (81%) remains the top request by SMEs

- SMEs wants longer term loans
- More Credit facilities / Factoring / Receivable Financing (29%) emerged as a new area of needs

Top 3 areas where financial institutions can better serve SMEs	2008	2009	2010
Competitive interest rate pricing	60%	73%	81%
Longer term loans	19%	37%	41%
Simplify loan documentation	24%	39%	30%
More credit facilities / factoring / receivable financing	-	-	29%
Introduction of industry specialist	-	20%	27%
Introduction of financial specialist	-	16%	24%
Faster turnaround for loan application	18%	31%	19%
More investment plans	-	-	17%

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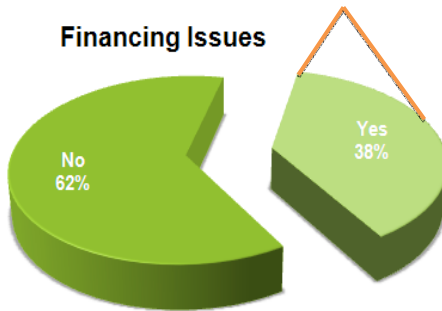


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Challenges faced by SMEs

Financing related issues	2010
Cash flow problem	63%
Bank financing difficulties	37%
Lack of funds to build internal competencies	18%
Do not meet criteria Government Schemes	7%



Lesser SMEs citing financing issues

- Percentage fell from 57% in 2009 to 38% this year
- Government financing programmes have helped

Retail SMEs (26.9%) most hit by Cash Flow Problems

- Likely to be due to poor inventory management

Infocomm SMEs find it more challenging to access Financing

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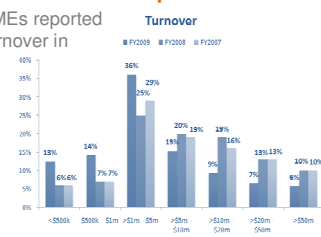


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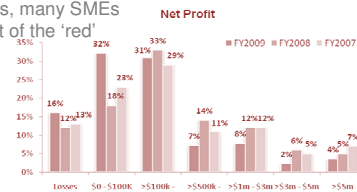
Characteristics of Respondents

More SMEs reported lower turnover in FY2009



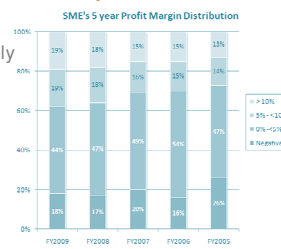
Characteristics of Respondents

Despite deterioration in profits, many SMEs stay out of the 'red'



Characteristics of Respondents

Profit Margin remains relatively stable despite recession year



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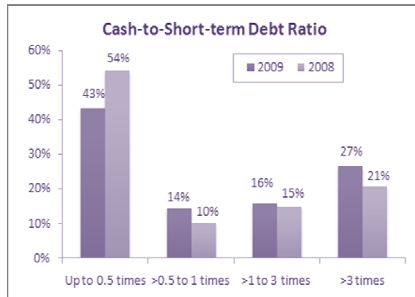
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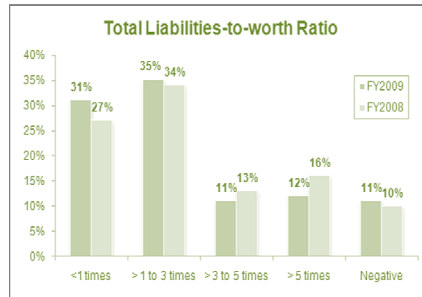
SME Liquidity



SMEs are reporting higher cash-to-short-term debt ratio

- SMEs reporting more than 0.5 times rose from 47% (FY08) to 57% (FY09)
- Average Cash Reserve increases for most sectors, except for Infocomm (-16%)
- Service Sector has the highest increase in Average Cash Reserve (34%)

SME Leverage



SMEs reporting better Debt Management

- SMEs reporting less than 1 times of Total Liabilities-to-worth ratio improves from 27% (FY2008) to 31% (FY2009)
- SMEs posting Negative Total Liabilities-to-worth ratio continue to hover around a tenth (11%)

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Credit Management - SMEs Sector



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Credit Risk Profile


Get yourself "INFORMED"!

5 'C's of Credit Check

- Determines the creditworthiness and repayment ability of a borrower.
- Analyzes cash flow streams, borrower's financial discipline, health, and other qualitative factors.

<p style="text-align: center;">Character</p> <p style="text-align: center;">Indicates borrower's "Ability to Pay" versus "Willingness to Pay"</p> <p style="text-align: center;">Capacity</p> <p style="text-align: center;">Indicates sources of repayment and borrower's ability to meet all his financial obligations on the due dates</p> <p style="text-align: center;">Capital</p> <p style="text-align: center;">Indicates the degree of commitment and the ability to sustain this commitment during bad times</p> <p style="text-align: center;">Conditions</p> <p style="text-align: center;">Refers to macro-economic environment conditions</p> <p style="text-align: center;">Collateral</p> <p style="text-align: center;">Refers to the lender's second line of defense in the occurrence of payment default.</p>	
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Credit Risk Profile

Get yourself "INFORMED"!

Information Availability Map

Pre-Credit Checks ◀

(PUBLIC INFO)

Questnet
Litigation
Directorship/Shareholder
Past Financial Info

(PRIVATE)

Investigation Banker's Report
Third's Party Report
Credit Bureau

On-Going Credit Checks ◀

(PUBLIC INFO)

Credit Monitoring
Litigation Monitoring
Industry Outlook Study

(PRIVATE)

Credit Limit / Growth
Payment Pattern
Credit Pattern
Credit Rating Pattern

Post Credit Checks ▶


(PUBLIC INFO)

Questnet
ROC
Litigation
Enhanced Individual

(PRIVATE)

Investigation
Credit Bureau
Skip Tracing / Assets Trace

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Credit Information Solutions



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Credit Information Solutions

Enhanced Corporate Search

- Detailed information on Business Profile
- Subsidiary / Associated Companies
- Key Financials
- Winding Up
- Judicial Management
- Litigation Trace
- Search Count.



Benefits:

- Establish the credentials and provide value-added information on a company / business.
- Quickly establish the business profile, subsidiary / associated companies, litigation background and credit grading of both your existing and potential business partners.

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Individual Business Search

- Name of Current & Previous Business(es) / Company(es).
- Position held
- Appointment date
- Cessation date
- 10 Year of Bankruptcy & Litigation suits (High/ Subordinate courts)
- Snapshot of the Company / Business



Benefits:

- Establish the credentials and assess the potential value of a company / business
- Increase your awareness in litigation suits filed against your clients and their company / business.
- Provide a more accurate assessment of the individual.

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Credit Information Solutions

Credit Monitoring Service

- Periodic monitoring (monthly, weekly or daily) a portfolio of clients & suppliers on litigation filed against them.
- Plaintiff & Defendant names.
- Suit number and amount .



Benefits:

- Establish the credentials and assess the potential value of a company / business
- Increase your awareness in litigation suits filed against your clients and their company / business.
- Provide a more accurate assessment of the individual.

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Credit Information Solutions

Business Watch Service

- Periodic alert on a portfolio of clients for any changes in business (ie, paid-up capital, shareholders/directors, address, status, etc)
- Market alert when there are any new players or new competitors



Benefits:

- Gain an insight into Character & Capital & Condition of the Company

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Credit Report

- Investigations
- Site Visits
- Surveys
- Details of Financial Performance
- Grading of Company versus other industry compatriots & industry performance as a whole



Benefit:

- In-depth understanding of the company relative to the external environment in which they operate.

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Financial Risk Overview

Liquidity

Working Capital / Total Assets

Measures the net liquid assets of the company relative to total capitalisation
A company with insufficient liquidity tends to have a higher probability of default

Growth

Growth: Retained Earnings / Total Assets

Measures total amount of reinvested earnings and / or losses of company over its entire life.
A company with higher growth tends to correspond to a lower probability of default

Leverage

Leverage: Total Equity / Total Liabilities

Measures how much of the company's assets can decline in value before its liabilities exceed its assets and becomes insolvent
A company that relies on higher equity than debts corresponds to a lower probability of default

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Financial Risk Overview

Profitability

Profitability: EBIT / Total Assets

Measures true productivity of company's assets independent of any tax or leverage factors.
A company with low profitability tends to have a higher probability of default.

Activity

Activity: Sales / Total Assets

Also known as Capital Turnover ratio
A company with lower activity tends to have a higher probability of default

Size

Activity: Sales

Sales is related to volatility – smaller size relates to less diversification and less depth in management.
Size is also related to market position.
A company size is inversely related to default probability

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The Seven Shenanigans

- Recording Revenue Too Soon
- Recording Bogus Revenue
- Boosting Income with One-Time Gain
- Shifting Current Expenses to Later or Earlier Period
- Failing to Record or Improperly Reducing Liabilities
- Shifting Current Revenue to a Later Period
- Shifting Future Expenses to the Current Period as a Special Change



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Techniques for Detecting Shenanigans

Database Searching

- Qualitative Screening
- Quantitative Screening

Analyze Finance Reports

- Create & analyze the **common-size** Balance Sheet & Statement of Operation
- Carefully read the footnote & other qualitative information
- Compare Cash Flow for Operation & Net Income

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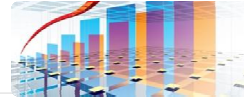
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Financial Information

Provides Information like past-year's financial performance to determine trends.

- Turnover, Profit, Assets, Liabilities, Outstanding Shareholders' Funds
- Set of Financial Ratios to access for profitability, debt management, assets, liquidity of company



Benefits:

- Gain insight into the Capacity, Capital and Collateral of the company

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Credit Rating Solution

DP Credit Rating

- Designed for SMEs in Singapore using the Altman's Z- Score model, a logic regression model to derive a default probability score
- Uses 6 broad categories of risk to determine a company's credit worthiness viz. Profitability, Capital Structure, Liquidity, Activity, Growth & Size
- Ranges from DP1 to DP8, with DP1 giving the lowest probability of default & DP8 with the high probability of default

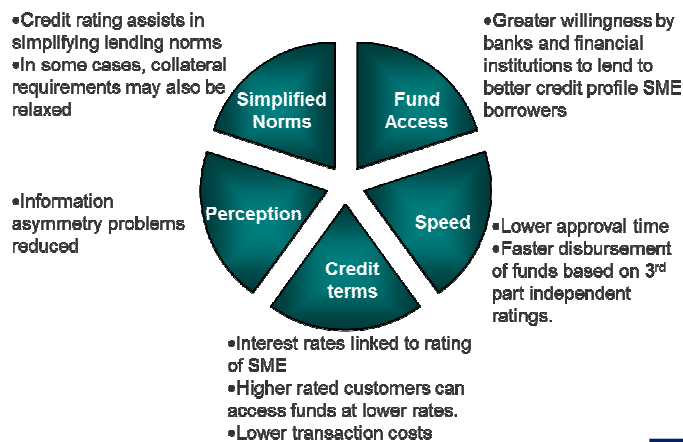
Why SMEs need to understand DP Credit Ratings ?

- All Construction firms under BCA's graded A1, A2 & B1 require annual ratings
- Private Education Institutions require bi-annual ratings for Edu-Trust Certification
- More industry sectors adopting credit ratings as a wholistic approach to measure the credit risk of a SME

DP Credit Rating & Its Benefits



Benefits of rating to SMEs



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Key Rating Insights



DP Credit Rating	Probability of Default (%)	Grading
DP1	<= 0.10	Investment Grade
DP2	> 0.10 - 0.20	
DP3+	> 0.20 - 0.30	
DP3	> 0.30 - 0.40	
DP4+	> 0.40 - 0.60	
DP4	> 0.60 - 0.85	High Yield
DP4-	> 0.85 - 1.00	
DP5+	> 1.00 - 1.55	
DP5	> 1.55 - 2.15	
DP5-	> 2.15 - 3.00	
DP6+	> 3.00 - 4.00	High Risk
DP6	> 4.00 - 5.45	
DP6-	> 5.45 - 8.00	
DP7+	> 8.00 - 10.15	
DP7	> 10.15 - 11.85	
DP7-	> 11.85 - 14.00	
DP8+	> 14.00 - 16.15	
DP8	> 16.15	

- The PD is then mapped into the respective DP Credit Rating Scale (DP1 to DP8)
- Introduced granularity in ratings between DP3 and DP8 by introducing the (+) and (-) signs to narrow down the PD range within each rating
- Each rating coincide with a probability of default (PD)
 DP1 - lowest PD;
 DP8 – highest PD

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Survey Findings on SMEs :

SMEs Development Survey 2010

Most SMEs have maintained a healthy risk profile by managing their debts & liquidity well despite the downturn

DP Credit Rating	2010	2009	2008	2007	2006
Investment Grade	23%	22%	17%	14%	20%
High Yield	47%	49%	58%	55%	49%
High Risk	30%	29%	25%	31%	31%
Total	100%	100%	100%	100%	100%



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Survey Findings on SMEs :

SMEs Development Survey 2010

- SMEs in Infocomm and Retail with at least two-fifth in High Risk Category
- While the Transport / Storage (30%) sector has higher percentage of High risk companies, it also has 31% of Investment Grade companies

Business Class	DP Credit Rating					
	Investment Grade (FY2009)	Investment Grade (FY2008)	High Yield (FY2009)	High Yield (FY2008)	High Risk (FY2009)	High Risk (FY2008)
Retail	14%	9%	43%	57%	43%	34%
Wholesale	23%	20%	51%	48%	25%	32%
Construction	16%	24%	56%	45%	27%	31%
Infocomm	18%	24%	34%	57%	49%	19%
Manufacturing	27%	26%	44%	45%	29%	29%
Services	21%	21%	42%	49%	37%	30%
Transport / Storage	31%	28%	39%	48%	30%	24%
Overall	22%	23%	47%	49%	30%	29%

Survey Findings on SMEs :

SMEs Development Survey 2010

Positive correlation between SMEs' profitability and credit Risk

- 47.2% of SMEs with high profit margin of more than 10% are in the Investment grade
- SMEs (73.4%) with Negative profit margin are in the High Risk category

Profit margin	DP Credit Rating		
	Investment Grade	High Yield	High Risk
Negative	2.3%	24.3%	73.4%
0% - <5%	16.4%	60.3%	23.3%
5% - <10%	33.2%	50.0%	16.8%
10% or more	47.2%	36.0%	16.8%
Overall	22.7%	47.1%	30.2%

Survey Findings on SMEs : SMEs Development Survey 2010

- 63.5% of SMEs with more than \$100M of turnover are in the Investment grade
- Of SMEs with less than \$5m in turnover, 65.3% are in the High risk category

Turnover	DP Credit Rating		
	Investment Grade	High Yield	High Risk
<\$5 M	4.1%	30.6%	65.3%
\$5 M - \$10 M	15.7%	55.6%	28.7%
>\$10 M - \$20 M	27.2%	57.1%	15.7%
>\$20 M - \$50 M	29.9%	66.2%	3.9%
>\$50 M - \$100 M	62.2%	36.5%	1.4%
> \$100 M	63.5%	36.5%	0.0%
Overall	22.7%	46.8%	30.5%

Survey Findings on SMEs : SMEs Development Survey 2010

- SMEs with less than \$100,000 of cash reserves are High risk
- 63.9% of SMEs with more than \$3M of Cash are in the Investment grade

Cash Reserves	DP Credit Rating		
	Investment Grade	High Yield	High Risk
<\$100,000	2.8%	33.8%	63.3%
>\$100,000 - \$300,000	10.3%	43.9%	45.7%
>\$300,000 - \$500,000	10.0%	63.1%	26.9%
>\$500,000 - \$1m	23.0%	62.2%	14.9%
>\$1m - \$3m	37.0%	56.4%	6.6%
>\$3m	63.9%	34.3%	1.8%
Overall	22.7%	46.8%	30.5%

22 March 2011

Survey Findings on SMEs : SMEs Development Survey 2010

- Seven in ten SMEs with current ratio of less than 1 times are classified as High Risk
- 64.2% of the SMEs with current ratio of more than 3 times are rated Investment Grade

Current Ratio	DP Credit Rating		
	Investment Grade	High Yield	High Risk
< 1 time	0.8%	28.2%	71.0%
1 - 1.5 times	12.2%	62.7%	25.1%
>1.5 - 2 times	23.3%	57.0%	19.7%
>2 - 3 times	45.8%	46.5%	7.7%
>3 times	64.2%	21.9%	13.9%
Overall	22.7%	46.8%	30.5%

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DP Information Group

- **30 years** of experience in the business & credit information space.
- Singapore's **leading & preferred** credit & business information Bureau by financial institutions, legal firms, MNCs, & SMEs
- Our Collaborations with Government Agencies
 - Appointed Service Bureau for BizFILE by ACRA (since 2002)
 - Appointed Service Provider for Information Services by ACRA
 - Appointed Government Supplier Registration Services by MOF
 - MOE Appointed Credit Rating Agency for PEIs
 - Appointed Credit Rating Agency for the Construction Industry by BCA
 - MAS-gazetted Credit Bureau for Banks



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- Annual nation-wide **SME Development Survey** since 2003
- Annual nation-wide Start-up Enterprise Survey since 2006
- **Ranking** Singapore 1000 and **SME 500** Companies for 23 years to recognize top performing companies.
- **Credit Rating** of non-listed companies/SMEs – key clients include Financial Institutions, Government Agencies
- **DP SME Credit Bureau** initiated since May 2002 to share payment history among non-bank members.
- **Other SME Surveys**: commission by IDA-SITF, SBF, IE Singapore, Chambers and Associations etc.



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DP Information Group

- **Our 3 Key Services**
 - SME Advisory and Bureau Services
 - Credit Management Services
 - Information Services
- **We are ISO/IEC 27001-Certified, a globally recognized information security standard.**
- **Experian is our institutional investor**
 - Credit Analysis, Decision Analytics, Marketing Services



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