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Small shop survival – The financial response to a global financial crisis

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ABSTRACT

Small and medium-sized enterprises (SMEs), many of which are small retail shops, remain the largest employer in the western world. Yet the financing of their fixed and working capital investments remains under-researched. This study focuses on this topic by examining Eurozone wholesale and retail SMEs enterprises at the peak of the 2008 financial credit crisis. In order to do this, an innovative analysis of existing theories in retail finance and policy research using generalised multilevel structural equation modelling is performed to establish how retail SMEs sourced capital during this period. This analysis, a first of its kind in wholesale and retail SME research, finds that pecking order theory, the independence of investment and financing, as well as the contest for financial resources between fixed and working capital do not hold for wholesale and retail SMEs. Moreover, it is found that government grants and subsidised loans were not used by SMEs in this sector of the Eurozone as primary sources of finance during the aftermath of the 2008 global credit crisis. Crucially, it is posited that a business environment characterized by stronger legal rights and deeper credit information did not improve SMEs' access to external finance. The authors recommend that further research should be pursued in this field in order to improve current understanding of the resilience of retail SMEs for future global financial crises.

1. Introduction

Here we consider the financial adjustments made by Small and Medium-sized Enterprises (SMEs) after the global financial downturn commencing in 2008 – hereinafter financial crisis. The latter initiated a period of policy-making centered on austerity throughout our study area, the European Union (EU), particularly the Eurozone. One response by the financial sector, as experienced in every recession of the last 80 years, was one of much closer examination of loans requested by weaker sectors of the economy. For most countries in our sample, retail SMEs constituted just such a sector. Nor was the financial crisis the sole pressure on retail SMEs (of which more below). A move to larger store formats from the 1960s, led by the French hypermarché restructured retailing to the detriment of these smaller, especially independent, rivals. That said, as Howe (1992) demonstrated, tens of thousands of retail SMEs had already been lost since World War Two. Whilst a number of European countries enacted protective (Planning) regulations these too, have become less effective (Hallsworth and Evers, 2002; Hallsworth, 2010; Hallsworth and Coca-Stefaniak, 2018). Furthermore, trade lost to the Internet and often to larger rivals with home delivery systems) has further eroded trade in a sector where available statistics are notably poor. Accordingly, one of the first sectors to suffer financially from this economic downturn was retailing, as consumer confidence and spending entered a downward spiral of decline. What we can be sure about is that the above trading pressures will continue and that there will be future recessions. What the financial crisis of 2008 onwards has offered is the chance to look at financing in a recession in order to learn lessons for future recessions. This study focuses on the financial mechanisms adopted by Wholesale and Retail (W&R) SMEs as they sought to remain in business during economic recession. This at a time when they were already under severe pressure from larger rivals. The findings of this study illustrate how public policy affects the financing of SMEs during a major financial crisis. Indeed, it may also carry implications for the present state of the world's economy, particularly given recent concerns voiced about the possibility of further financial turmoil (Wolf, 2018; Elliott, 2018).

The following research objectives were established for this study:

1. To analyze the investment and financing of SMEs in W&R during the most algid period of the global financial crisis in the Eurozone.

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2. To evaluate the role of public entities and the existing regulatory framework (including key business regulations) in the financing of fixed and working capital among SMEs during this period in this region, and consequently,
3. To comprehend the influence of country-level differences on the financing of fixed and working capital among SMEs in W&R within the Eurozone.

2. Literature review

2.1. Evolution in retail research

Over past decades the dominant agenda for many retail researchers has been store format evolution and change (Hallsworth et al., 2006) and attendant policy agendas (e.g. Guy, 1998). The rise of larger store formats such as the hypermarket, superstore or supercenter is also often linked to vastly increased market concentration in western retail markets. Indeed, Serpkenci and Tigert (2010; p61) have suggested that "'there will be but just two retailers remaining in many product-market spaces in North America". Such a duopoly already exists in the Australian grocery retail market, for example. Much large format growth, into which all the then leading operators had rushed (Hallsworth, 1996), has stalled post-2008 and, as a measure to scale back its operations in Britain, WalMart announced in 2018 a proposed merger with rival Sainsburys, which was refused by UK Competition Authorities in 2019. Recent change can also be explained, as noted above, by the rise of the internet retailers and their highly cost-efficient operations. Indeed, a vast range of technology-related innovations, together with their implications, are listed by Grewal et al. (2017).

However, we focus on that 2008 - onwards sub-prime crisis because innovation in retailing carries a basic requirement - to still be in business. Indeed, not all formats have suffered – a climate of austerity has benefited price-focused 'hard discounters' such as Aldi and Lidl. The financial crisis highlighted the fact that many previously-efficient retail corporations struggled for a variety of financial rather than operational reasons. One classic victim of format change has been the smaller (typically sole-proprietor, possibly "mom & pop") retail store – as evidenced by vacancy rates on many traditional shopping streets. We cannot further pursue wider retail change at this point but instead focus on: how has the smaller format retailer survived financial pressures?

We approach this question by examining various competing theories on how retail SME financing might be obtained. Reliable data on small retail enterprises is, however, extremely difficult to find – and more so when comparing cross-nationally as we do here. Indeed, a UK investigation into the groceries market was seen by many to have elided into a study of supermarkets precisely because data on smaller shops were so poor (Hallsworth, 2010).

2.2. Retail and wholesale in the EU

We study W&R SMEs in the Eurozone with the European Union as its wider context. Transparently, the SME sector has developed differently in different parts of the EU. In most EU countries the small shop has for many decades been the most familiar format in fixed-store/non-peripatetic retailing. The dominance of the format, by sheer numbers at least, was largely unchallenged until the 1960s. However, we should note the rise of the *multiple* small shop retailer, in Britain the archetype being J. Sainsbury, founded in the nineteenth century. Multiples came to own many small shops in the UK a pattern repeated across much of the EU. That said, outcomes vary noticeably in different parts of the EU; including the history of support for the small shops that found both multiples and large formats to be powerful competitors. Contextually, discounters such as Aldi and Lidl were nurtured by a German home base that actively sought to promote its SME sector (Wortmann, 2004). Concomitantly, Burt and Sparks asserted (2003; p. 148) "there is insufficient understanding of (…) national differences (…) it would seem that the cultural dimension in company operation is very important in explaining margin and profitability levels (…) market norms (…) condition the capabilities of firms (…) to remain in business". Other studies have contrasted retailing systems cross-nationally (see, for example, Hallsworth and Evers (2002) and Reynolds and Howard (1993)). Coca-Stefaniak et al. (2005) explicitly focused on retail SMEs in a comparative analysis with Spain suggesting that many problems, including poor quality of official data, have been common across Europe. Yet, although employment dropped dramatically between 2008 and 2013, SMEs today still employ 67 in every 100 employees in non-financial economic activities, accounting for 70 per cent of 'retail and wholesale trade' employment (European Commission, 2017).

As noted, Germany has a longstanding pro-SME philosophy that also aided smaller retail firms. In Italy, a strong tradition of support for local shops has only in recent years been eroded. However, where does Brussels fit in this puzzle? The EC's 2017 report seeks a "more efficient and fairer" EU, setting the tone and, unsurprisingly, reflecting Brussels' over-riding desire for integration, with a particular protagonist role for the Eurozone. Yet, the traditional single-unit retailer SME could do little to assist, since it often serves local markets with local products only; reflecting the fact that, for many, retail remains inherently local (Clarke et al., 2006).

France, Germany, Italy and Spain share a common trait in the EU: They belong to the common currency area – the Eurozone. As shown in Fig. 1, between 2009 and 2013 wholesale and retail predominated when compared to other relevant sectors in the industrial fabric of the Eurozone. Nonetheless, the larger the turnover, the fewer firms were found to operate in wholesale and retail sector. In fact, 83.56% of companies in the Eurozone in this period had an annual turnover lower than 50 million. Of these, 32.96% were in the wholesale and retail sector, which was central to the economy of the Eurozone region during the financial crisis – a key rationale for this study.

2.3. The financing of Eurozone W&R SMEs

Against this background, nonetheless, this study focuses on how W&R SMEs in the Eurozone financed their activities to survive one the most significant and global financial downturns in recent history, with a legacy that still lingers today. This research compares the use of internal funds by Eurozone W&R SMEs against a range of external finance possibilities as well as government lending, and their interplay with financial regulations affecting the business environment, including the Strength of Legal Rights and the Depth of Credit Information. We also analyze how fixed capital was financed by Eurozone W&R SMEs in comparison with working capital and inventories (working capital, for short). The time period chosen for this analysis corresponds to a critical stage of the global financial crisis – from the first half of 2009 to the end of 2013. Generalised Multilevel Structural Equation models were developed as part of this analysis drawing from a sample of 21,212 companies grouped at country level. The originality of this study in terms of its contribution to current knowledge in SME financing stems from the analysis carried out of internal versus external financing and investment.

Historically, SMEs have been regarded as drivers of economic development in the EU. Today, 98 out of every 100 non-financial businesses in the EU's twenty eight states (EU28) are SMEs, of which the majority - 93 per cent - are microenterprises. Not surprisingly, the financial crisis created a myriad of problems for the sector. Though many SMEs survived despite limited resources, one of the biggest pressures they faced was access to finance. Scholarly inquiry on the financing of economic activity in the retail SMEs sector has been rather sparse in comparison with research focusing on large companies (though see Beck and Demirgüç-Kunt, 2006).

The general literature on retail change through time is too extensive to cover here. Nevertheless, we have outlined briefly earlier some familiar general trends and influences. Hence, our analysis of published